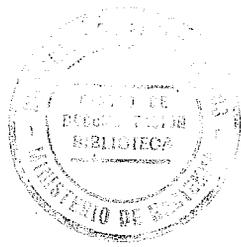


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CHILEAN ECONOMIC POLICY



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edited by Juan Carlos Méndez,
translated by Ann M. Gain de González,
designed and produced by Matte y Méndez.
It was set in Helvetica and printed by
Imprenta Calderón y Cía. Ltda. with the
financial cooperation of
the Central Bank of Chile.

Printed in Chile
November, 1979

In Memory of
Vice-Admiral
Lorenzo Gotuzzo Borlando



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Foreword

The Government has labored extensively and productively on many fronts—in economic affairs, among others. During these years, numerous obstacles have been overcome, ranging from the sound reasonable doubt and the natural sensation of discouragement felt when confronted with the very magnitude of the problems, to criticisms and positions adopted in virtue of prejudices and dogmatic concepts which, unfortunately, have long formed an important part of national life.

This book has been prepared in the hope of preserving the emphasis events gave to each problem as it arose. A careful reading of its pages will reveal a serene analysis of reality, unquestionable coherence and an accurate anticipation of events, some of which although now part of the past, at the time of analysis still belonged to the future.

To a certain extent, the economic history of this Government has already been written; this book is simply a selection of some of its chapters.

Introduction

**Chilean Economic Policy:
Dogmatism or Realism**

Juan Carlos Méndez
Director of the Budget

Let us suppose that in Chile every Government, independent of its doctrinary conceptions, and therefore, of the institutional configuration that it may have aspired to impose upon the political, social and economic framework of the country, has sought the achievement of three fundamental objectives in the economic field: stability, growth and development. At least this is the conclusion one reaches from a consideration of the explicit postulations of the various economic programs that have been presented. The crucial question is what is the most expeditious way to achieve the goals established.

Before undertaking the analysis of this subject, we must define what is understood by economic stability, growth and development. Let us define economic stability as that set of conditions which produces a minimum of macro and micro-economic alterations in the face of combined imbalance in the areas of foreign trade, money, investment, saving and specific imbalance in the micro-economic units as such.

By growth, we mean the increase in the Gross Domestic Product of the country as a result of the increase in the quantity of productive factors. Development is understood, first, as that part of the increase in the GDP generated by an improvement in the quality of the productive factors, and secondly, by a socially acceptable personal distribution of income ¹. The three objectives cited here are part of a whole and, of course, are interdependent.

For many years and until recently, Chile had chosen a certain path to development and an economic structure based on increasing intervention of the State. The economic program of the present government assigns a subsidiary role to the State. Both approaches are different and have different meaning from the economic point of view and, therefore, their effectiveness varies with respect to the achievement of stability, growth and development.

This can be seen more clearly by comparing the present economic program with another one in which the means of production are controlled by the State (centralized economies).

In the case of a centralized economy, the functions of government obviously increase, since it not only has direct control of macroeconomic man-

¹ It means that changes in the personal distribution of income, as a product of the economic system and of the distributive action of the State, approach the social welfare function.

agement, but of microeconomic management as well. From the point of view of macroeconomics, the primary objectives will be: price stability, equilibrium in foreign trade, growth and employment, and the achievement of acceptable personal distribution of income. On the other hand, we must also consider the objectives of the function of management in a productive unit which is to produce the maximum possible in goods of the greatest value at a minimum cost. In this dual function, which the Government must carry out as leader of the general economic policy and as manager of each one of the productive units, the macroeconomic interests will inevitably impose themselves as additional restrictions on productive activity, either by price fixing in order to encourage general price "stability" or by imposing numerous factors over and above what is advisable for the survival of the enterprise itself, and all this, perhaps, in an attempt to achieve the employment goals established by the authorities. Likewise, microeconomic considerations will frequently impose themselves as additional restrictions on the macroeconomic task of Government as it is in the case of the preferential exchange rate or special lines of credit which permit the fulfillment of the production plans determined by the Government itself.

In other words, in a centralized economy (or one with fixed prices), as opposed to a free market economy, additional restrictions are imposed on the macro and microeconomic functions. It is well known that, when an additional restriction is imposed on a function, the new maximum of that function will not be able to surpass the one obtained before the application of the new restriction. Consequently, the growth target is curtailed in some significant points.

This dual function produces other effects which are equally or more important than the one mentioned above. Given that within the Government itself there will be innumerable occasions on which the preponderance of one or other position will be questioned—that of those who manage the economic aggregates, and that of those who manage the productive units—instability will be generated, at least in the additional restrictions on either or both functions and, therefore, the rate of discount of those who make decisions (macro and microeconomic) will be high, and so the present will become the general rule.

The tendency will be to take advantage of the fact that a certain restriction has been eliminated because it will soon be reinstated. The result is that the best time to make decisions no longer has any meaning (which is very clear in the field of investment in public enterprise). Given that the present

is the norm, very often the Government itself becomes involved in this attitude and by sacrificing future governments it constructs stability, growth and development that are just as ephemeral as the men who make up that particular Government. This is one more reason to think that in such a scheme the goals for growth, as well as those for development and stability, are more difficult to achieve than in a free market system.²

As a result of the positions, at times unbalanced, between those who manage the macro and the microeconomic areas, it can be inferred that, step by step, the case of the productive activity will gradually be imposed, to the detriment of overall economic management, and the need to place the macroeconomic point of view in its proper place will only appear when the components of the system show clear signs of approaching crisis, and even having overcome crisis, the permanent remedy will consist in overall management with important restrictions. There is no country with a centralized economy or socialist ideology which does not impose heavy restrictions on the instrumental management of the Balance of Payments—thus losing the degree of freedom required for maximization—a loss of instrumental flexibility which, as has been pointed out by Jan Tinbergen himself, prevents maximum achievement.

Thus far we have analyzed the additional restrictions and the curtailments on achievement which they generate. Not only are there additional limitations, but also the Government as productive agent is not restricted by the same factors as its counterpart in the private sector,³ nor does it have the same variables nor the same functions of behavior.

As a matter of fact, the value of the marginal product of the factors is, in a given activity, different for the state productive agent than it is for an economic unit in the private sector. Moreover, the value of the marginal product of the factors, for the same activity, of the private sector is closer to their social value of the marginal product, than that of the same factors assigned by the state productive agent. Apart from assumptions, let us consider certain facts. One of these is that the possibility of bankruptcy in the private sector is greater than it is in the fiscal sector, which means that for the same activity with an equal production function and identical factors, in quality and quantity, at determined ("minimum") prices for the product

² A free market economy is that which allows the free and direct expression of consumer and producers, the result of which automatically determines prices and quantities.

³ In a free market economy the distortions between private and social benefits and between the social and private costs are corrected by taxes and/or subsidies.



and ("maximum") for factors, the private businessman enters losses and therefore his expected income is the weighted result of the expected profit and loss situations. The state agent, however, does not take into account fully (or perhaps not at all?) the possibility of loss and, therefore, his expected income is necessarily higher than that of the private businessman. This means that the expected value of marginal product from capital and for the rest of the factors is greater than it really should be, if the possibility of bankruptcy or of the total impact of the alternatives for loss are taken fully into account. Consequently, in a socialist economy there will be a clear tendency toward overinvestment and to overemployment. Overinvestment and overemployment occur at the expense of other functions which the State must carry out, among these being distribution, and since this is not optimum, it threatens growth and development and diverts resources from the distribution function.

These differences are produced not only in the microeconomic function of state and private productive agents. For the private businessman —given the quantity of factors in the production function and competition of products and factors in the market— the allocation of resources becomes the management variable and he must assign resources so as to produce at the minimum cost. The State as "entrepreneur" has the alternatives of the political pressure it will exert and of the allocation of resources, in order to obtain a good price for the product and low prices for inputs, and..., in so far as it allows somewhat more or somewhat less than the price that would have prevailed in the market,⁴ from the point of view of general economic equilibrium, poor allocation of resources is necessarily maintained. Thus once again growth and development potential are diverted from the country, less potential development, since there is less to distribute than there would have been in a free market economy.

But the most serious aspect of all this is that additional distortions are generated in the economic system, since there is an attempt to eliminate the foreign sector which is the only source of competition, since there is no private businessman nor fiscal productive agent who does not dream of becoming a monopolist, since this is the situation which in any case maximizes its benefits. In that way, pressure from all the productive state agents will virtually close the doors to foreign trade. A look at the countries with centralized economies will ratify this statement. The worst is that in those countries technology and progress are centered basically on the sectors in which, for other reasons, they are faced with competition. In this

⁴ A market which has been corrected by taxes or subsidies in the case of distortions.

way they develop the most advanced infrastructure in arms, and on a national level they postpone productive functions in which these giants are mere underdeveloped dwarfs. Obviously, this is not exactly an outlook that maximizes growth and the economic and social development of the countries.⁵

The "As if" of Lange and Lerner has more restrictions, different variables and behavior functions than the "If" of a free market economy. In short, the dual function of Government, orienting the economic aggregates and as productive agent, does not lead to a maximization of stability, growth and development. This brings to mind the proverb, "No man can serve two masters."

What then are the functions of the State in the perspective of the present analysis?

The putting aside of the production of private goods and services by the State leaves the following functions:

- a. The provision of public goods and services such as justice, foreign relations, defense and certain services and public infrastructure.
- b. The regulation and controlling functions such as the control of the monopoly factor and product markets not subject to external or internal competition; to avoid monopolistic practices in order to guarantee and to promote competition in all markets; to dictate and to implement norms with regard to the care and preservation of the environment and of the individual.

⁵ In the case in which the means of production belong to the private sector and the State fixes prices, the tendency not to take risks fully into account will be even greater than in the case in which both the means of production and the fixing of prices are the function of the State. This is perhaps the worst possible situation, since it is an unconscious path toward statism. The micro and macroeconomic conflicts will be felt in the national social body with greater strength. At least in the Chilean case, these led to a macroeconomic management completely dependent on the national business community with voice and power. The doors were closed to foreign trade, suppressing all effective competition. The situation became so extreme as to allow the absurd practice of having representatives of the national productive sector on the Board of Directors of the Central Bank. Legal bodies accumulated in which the lack of non discriminatory norms was supplemented by complex and varied arbitrary attributions. Obviously, all of this produced the necessary friction in the social body to motivate the final attempt to achieve a statist economy.

- c. The function of distribution so as to create equal opportunities and to solve situations of extreme poverty; and finally
- d. The macroeconomic management functions in the monetary, foreign trade and budget areas, which fulfilled by means of the proper organizations are few, clear and precise.

In the monetary sector, if the exchange rate is free, only the amount of money is managed; if the exchange rate is fixed in nominal terms, total credit is the only tool of management.

In the foreign sector there are two functions: to keep the economy open and to provide the country (not the Central Bank) with the reserve level indicated as reasonable. Eventually, there is a third function, that of fixing the exchange rate, if macroeconomic adjustments are to be made in this sector, once again being careful to maintain the established reserve levels.

The disaggregate components of the budget function are basically related to providing public goods, to the establishment of norms and to distribution.

The aggregate or macroeconomic budget function is related to defining the level and the growth of revenue and expenditure in the public sector as well as the deficit in the sector.

What is the role of public finance in this context, whose objectives are stability, growth and development?

Above all, it is necessary to determine the amount of total resources required in order to fulfill the functions proper to the State. While this statement is so broad that it scarcely has meaning, in the national context it means to discover whether or not to increase the tax and welfare burden imposed on the community.⁶ The present economic system bases its goals for growth on a State which reasonably fulfills each one of its functions and on a private sector with an increased productive capacity.

After over forty years of uninterrupted statism we find it advisable that growth in total outlay should not exceed growth in the gross domestic product, which would freeze, in a certain way, the present structure of

⁶ That is, how closely marginal movements approach the Paretian optimum.

participation (private sector versus public sector). This is not the ideal and there should be, if not a reduction in the present level of revenue and public spending, then a reduction of public spending and income as a percentage of the Gross Domestic Product.

This requires, for practical reasons rather than theoretical ones, a zero deficit in the public sector. Budgetary imbalances manifested as deficit signify rigidities difficult to overcome, which are translated in sporadic periods of inflation resulting in instability and a decline in growth and development.

Having defined the level and the tendency of public expenditure, revenue and deficit, we must now identify the source of revenue and allocation of funds that will guarantee the achievement of the three objectives. First, the revenue structure should safeguard vertical and horizontal equity, and in the second place, once distortions have been detected and corrected by means of taxes and subsidies, it should be neutral if possible with respect to the social allocation of resources. The present tax system was developed and implemented for this purpose. Likewise, the foreign trade sector is the most effective channel for competition, which should, therefore, be preserved; it is only a source of income in so far as reasonable protection is given to import substituting activities and according to the extent to which the present and potential export sectors remain reasonably unprotected. This, and only this, has been the purpose of the tariff reforms and the elimination of tariff-related barriers. Social security deductions comprise the third source of public revenue. A portion of this constitutes a tax, given that what is put into the system is less than what is obtained from it. This is a tax which discriminates against the most abundant factor in Chile, namely, manpower. The spirit of the Social Security reform is guided by a desire to eliminate this distortion, to generate a clear incentive to individual capitalization and to improve pensions.

In short, the modification of the structure of public revenues has put us on the sure path to the stability, growth and development of the country.

With regard to public expenditure, the reallocation and growth of this factor should be centered on those functions which have been most postponed. Once again, our analysis of the Chilean situation reveals that the distribution function and the provision of public goods has been postponed for forty years in favor of the public entrepreneurial activity and the regulatory (the word should really be controlling) function of the State. It is obvious that the growth in budget outlay should be generated essentially in the distribution function, accompanied by significant efforts to

achieve more efficient distribution. The new regulatory function of the State means more precise responsibilities, fewer in number and more general in nature; therefore, in comparison with former periods, the amount of resources required should be less. The "entrepreneurial" activity of the State (entrepreneurial in quotation marks because businessmen assume risks), should undoubtedly be less than they were in the past. These are and have been the priorities and have accordingly formed part of the public budget.

The great project which we are carrying out in Chile includes the objectives set forth at the beginning. One of the fundamental aims of this project is to release the economy from state control, thereby creating a truly mixed economy in which the public and private sectors complement each other. Consistency in the subsidiary role of the State is one of the most difficult things to achieve. In the measure in which the country continues the present rhythm of growth, the alternatives for allocation of resources and consequently investment alternatives will increase, and it is highly probable that these factors will grow at a rhythm superior to the availability of resources. And we will not have to face the Keynesian specter of a lack of investment opportunities. In this environment our consistency will be put to the test once again. It will be another of the many confrontations between the strength of reason and the strength of statism.

Undoubtedly, centering action on the achievement of the fundamental tasks of the State means greater development, growth and stability. Greater development because the distribution function of the State is, for the most part, an investment in human capital, which at present means an improvement of the income levels of the most dispossessed and in the future, giving them the tools with which to obtain on a steady basis, levels of well-being superior to the present ones. Greater growth, because human capital increases, and at the same time the State, having withdrawn from the productive function and handed it over to the private sector, provides the alternative of producing more than what had been produced before with the same resources. Greater stability, because the function of the State will become more and more unified and therefore the impact on the national economy of disequilibria in the "macro" or "micro" sectors will not be so strong. This is the realism which guides the actions of the present Government.

Part I

Bases for The Economic Policy

**Declaration of Principles
of the Chilean Government**

Introduction

The Junta, which came into Government in Chile on September 11, 1973, has stated on many occasions that it wishes to inaugurate a new era in our history by planning a creative and stable political system for the future. It will be the task of the new institutions arising in the country to gradually provide a juridical framework for this great collective undertaking to which the nation is committed.

For this reason, six months having elapsed since Chile's liberation from Marxism and since the initiation of the new government, it considers the moment opportune to make known its Declaration of Principles. Within this declaration is contained the essence of the philosophy which has inspired the action of the Junta. An understanding, analysis, and diffusion of these principles is of fundamental importance to every Chilean so that he may actively participate in the reconstruction of the nation.

Santiago, March 1974.

CHILE IN THE WORLD TODAY: BASIS FOR A DEFINITION

National reconstruction begins in Chile at a time when the whole world is undergoing a severe upheaval. Because of an economic crisis, which is itself a latent threat to world peace, we are faced by an even graver problem threatening the values and way of life of many societies in today's world.

A large sector of the human race, the so-called underdeveloped or developing nations, are overburdened by millions struggling in poverty and misery. Although not in the worst position, Chile belongs to this group. In our attempts to rise above our place among these nations, we observe two antagonistic types of society as possible models towards which we should aim. Some look toward the socialist and Marxist-Leninist inspired societies, while others hope for economic development compatible with the social justice and political freedom reached by the most advanced western nations.

Chile must reject the alternative of the Marxist inspired society, because of its totalitarian characteristics and its devaluation of the human being which are diametrically opposed to our Christian and Hispanic traditions. Furthermore, experience shows that Marxism does not create well-being, and its socialist and statist nature renders it incapable of achieving the economic development we require.

On the other hand, although the developed western societies may offer an infinitely preferable appearance, they have fallen into a suffocating materialism which has enslaved man's spirit. The so-called "consumer societies" have established a situation in which the dynamics of development seem to control man himself, leaving an inner feeling of emptiness and dissatisfaction, and producing a nostalgic desire for a more peaceful and humane existence. This condition favors that revolt of youth which periodically erupts in different forms. As a result of the September 11, 1973 action, we in Chile have been able to see only too clearly that all this has been aggravated by the success of Marxist penetration into these seriously weakened societies.

While others are just setting out, naïvely, on the path of "dialogue" with an understanding of communism, Chile is on her way back. Having undergone the experience of allowing Marxism within its democratic fold, having watched many democrats attempt to find common ground,

in doctrine or in practice, with Marxist sectors, and having witnessed with its own eyes the fallacy and failure of the so-called "Chilean road to socialism", our country has decided to fight openly international communism and the Marxist ideology it upholds. In doing so it has inflicted on communism the greatest defeat it has suffered in the past thirty years. The government of Chile makes no pretense of assuming any leadership beyond its own frontiers, but is aware, nevertheless, that the outcome of all that is taking place in Chile is being watched with interest by many peoples to whom our experiences may, in various ways, be useful.

While it is no concern of our country to put forward ideas of imagined world-wide scope or application, it is necessary for Chile to find its own, particular way to try to overcome the various critical factors which today affect other countries.

Chile must, therefore, work towards attaining, balancing and knitting together freedom as a way of life with the accelerated development of our economy and fair social progress.

To this task, already a challenge of the first order, must be added the necessity of accomplishing it while satisfying the spiritual restlessness of the individual, by building a nation, day by day, which reaches toward a condition worthy of man's dignity. To hope for the full attainment of such a concept would be to aspire to a factual utopia, an occurrence beyond the abilities of human nature. Therefore this cannot be presented as a "model" to be achieved by means of an ideological recipe, but only as an end toward which, together we may gradually and in the best possible way, approach.

With this in mind, the concept of the relationship between the individual and society must be established and defined; but beyond this, all else must be derived from our national makeup, past and present.

THE CONCEPT OF THE INDIVIDUAL IN RELATION TO SOCIETY

Chile's government, in tune with national tradition and with the outlook of the vast majority of its citizens, respects the Christian concept of the individual in relation to society. It was this relationship which shaped the western civilization of which we form a part, and it is the loss or distortion of this concept which, to a great extent, has provoked the moral disintegration endangering that very civilization.

In keeping with this statement, we hold that the individual is a being endowed with a soul. This is the springhead of the true basis of man's dignity, as we shall establish in the following principles.

The individual holds rights which are preferential to and above the state

These rights spring from the very nature of man himself and have their origin in his Creator. The State must acknowledge them and regulate their use, but it is not the State that concedes them, nor must it ever deny them.

The state must serve the individual, and not the reverse

Both from the point of view of his existence and his purpose, man is superior to the State. From man's standpoint, while he is a substantial being, society and the State are originally only accidental relationships. Thus it is possible to imagine man's temporal existence as independent from any form of society. On the other hand, not for one moment could the existence of a society or a state be conceived without the presence of man. Further, viewed objectively, man is primary, for while societies or the State exhaust themselves in the course of time and history, man survives them. He lives in history but is not consumed by it.

The purpose of the state is the general common good

Without contradicting ideas already expressed, since man cannot realize his full development without living within a society, he must group himself with other human beings.

The general common good, which is the goal of the State, was recently defined by the Government in a public document as "that set of social conditions which enables each and every Chilean to reach his absolute personal fulfillment." (See statement on abstention from politics in public administration, December 1973).

This definition explains a concept of the common good that is as different from that held by liberal individualism as from totalitarian collectivism. Liberal individualism sees the common good as simply the sum of the individual's welfare, which all try to attain with almost total disregard for others. Collectivism, at the other extreme, understands the common

good to be determined by the needs of the State, before which individual welfare as such completely disappears. Because of this, our century has witnessed fearful massacres staged by communism or national socialism, which were justified by its perpetrators in the name of so-called "collective welfare or necessity." These philosophies thus may lay bare an abysmal ignorance of the concepts that the individual as such exists as an entity, possessing an ultimate purpose which grants him rights no human authority may lawfully violate.

The true idea of common good avoids both extremes and transcends them. It defines the common good as arising from the attainment of individual well-being through restraint, poise, consideration, and the positive and genuine respect for the well-being of others; in this the liberal concept is rejected. But at the same time, this concept springs from acceptance of the inherent rights of the individual and refuses to allow their possible infringement in the name of any false "common welfare."

Common good does not mean, then, the welfare of the State, nor does it mean the welfare of the majority and much less, the welfare of a minority. It is the sum of those conditions by which each and every member of society may attain true individual welfare. Common good aims at enabling the individual to obtain fulfillment—not merely some individuals, be they majority or minority, but all and every one. It follows, then, that common good, as an objective, can never be entirely reached, just as absolute personal perfection can never be attained. Nevertheless, it points a goal to which the State must come as close as circumstances allow; it represents a permanent challenge to the State to always strive for although, due to man's imperfection, complete achievement will always escape.

Law, then, emerges as the principal instrument of authority to promote the general common good, that is to say, to shape, in keeping with continually changing circumstances, the most adequate social structure so all and every member of the community may achieve personal satisfaction.

Common good demands respect for the principle of conditional supervision

Since every society has its origin in man, and the individual is its justification, it follows that the more complex groups come into being to fulfill tasks the smaller groups are unable to handle on their own. The lone individual forms a family group to reach objectives which by himself he

cannot; in the next phase of human development a variety of more sophisticated groups come into being to obtain that which the family by itself cannot. Finally, the need to create a justly coordinated communal order impels all these intermediate groups to form themselves into a State, which undertakes those tasks none of them could manage directly.

This fact places a limit on the scope of activity to be undertaken by the larger social group. If the justification for the existence of the larger unit is the ability to act where the smaller one cannot, then it is evidently not right that the larger society should absorb the field that belongs to the smaller one, and over which the latter should exercise adequate autonomy. The area of influence of the larger society begins where the possibilities of effective action by the smaller one ends.

Such is the basic idea from which the principle of conditional supervision springs. By virtue of this principle no major social group may assume initiatives which the smaller group, especially the family, is able to manage, just as the family may not invade that which is personal and intimate to the individual conscience.

The conclusion to be reached from applying this principle to the State must be that the State should only assume direct responsibility for those functions which the intermediate or minor social groups are unable to deal with adequately, either because they are beyond their possibilities to do so, as in the case of national security, police work or foreign relations, or because, due to their importance to the community, it is inadvisable to hand them over to limited private groups, as in the case of services or enterprises of strategic or prime importance to the nation, or finally, because, due to their nature, they require over all State coordination. For all other social tasks, the State can only intervene directly when an intermediate social group which should on its own be capable of handling a given situation, through neglect or fault, does not do so, even after the State has taken collaborative steps to overcome the deficiency. In this case the State acts as the supervisor for the common good.

Respect for the principle of conditional supervision is the key to the existence of a truly free society, and could almost be called a barometer for measuring the degree of liberty in a social structure. By contrast, the greater the State interference in a society, the less is its true liberty, regardless of how widespread may be the exercise of political rights. The fountainhead through which liberty offers personal and creative effort a margin of alternatives of sufficient variety is to be found in a private life,

and in those activities which are independent from the State, and only subject to its control for the common good. Statism, on the other hand, produces a society that is grey, uniform, submissive, and without horizons.

Respect for the principle of conditional supervision implies acceptance of the right to private property and free initiative in economic activities

It is not difficult to see that the principle of conditional supervision presupposes the right to freedom of initiative in the economic field. Apart from being a right, the participation of private enterprise in production offers the only road to effective economic development, and the State, in keeping with the principles outlined, neither can nor should eliminate or absorb such participation. A centralized monopoly by the State of all economic activity not only leads to a statist society which, in the end, pragmatically denies personal freedom, but it also eliminates the creative capacity of private enterprise, whose replacement by the bureaucrat is detrimental to the emergence of new sources of production and labor.

The acceptance of free enterprise, as described, must, in no case, be taken as disregard for the active and very important role given to the State in the economic field. The State's mission is not limited to ensuring healthy competition and exercising control over private enterprise to avoid abuse or monopoly. A modern economy also requires the State to participate in comprehensive economic planning. However, State planning should not grow so extensive as to block private enterprise, but rather it should complement it.

Further, it would be pointless to allow private enterprise in economic activities if at the same time the right to private property, in the form of consumer goods as well as production potential, is not recognized.

This right to private property follows inevitably from the concept of man in relation to society, and also from the principle of conditional supervision, which is derived from that concept. The simplest form of this right is individual property, but communal property, when freely agreed to and maintained, may also be included. The State should only keep for itself that property which is strategic or vital to the country, and cannot be left, prudently, in limited private hands; all else should be left open to the right of private ownership. When determining the limits of the juridical State's economic power, requirement that ownership must be exercised in keeping with the social function inherent in the property, must also be established. Within this concept, the means must be devised whereby the right

to private property becomes a reality for all Chileans, whatever may be their social level. Chile must become a land of property owners, not a country of proletarians. The right to private property requires legal guarantees against arbitrary dispossession. To this end it must be established that the State may only expropriate in cases of real necessity for the common good, and must pay just and timely compensation to the affected party.

Over and above the ideological reasons which favor acceptance of private ownership of goods, including production, it is essential to add that whenever the State lays hands on all sources of production, it becomes the only entity distributing the necessities of life to the citizen. Obviously, in such a case, political liberty disappears, for he who opposes the regime stands to see his family and himself starve. However, on the other hand, when the social function of property or its effective distribution among all social classes is neglected, morally unjust situations can occur which will create tension, strain, and pressure in society.

AN INSPIRATION THAT IS NATIONALISTIC, REALISTIC AND PURPOSEFUL

While stating these principles whose validity is universal, the Government is seeking those factors within Chile today that will support its philosophical and ideological outlook. This demands a fusion of the important values implicit in our history and tradition with the new qualities of the contemporary world in which Chile exists. This leads us to the following conclusions:

The fundamental purpose of reconstruction: to build Chile into a great nation

Emerging from a long period of ideological messianism preaching petty hatreds, the Government of Chile, from an emphatically nationalistic point of view, invites its fellow countrymen to overcome mediocrity and internal division to build Chile into a great nation. With this objective in view, it has proclaimed repeatedly that it holds national unity as its most cherished objective, and rejects any outlook that may accept or encourage irreconcilable antagonism between social classes.

The spiritual integration of the country will be the basis upon which it will progress in economic development, justice and peace, and recover the leading position which the creators of our republic gave it within the

continent. The strongest inducement to awaken patriotism —that deep love of a united and great country— in the heart of every Chilean is surely the resolve to vindicate again the examples presented by our history with its leaders, heroes, teachers, and statesmen. Foreign creeds, a foreign cultural invasion, party interests, selfishness, and antagonisms deliberately fostered between social classes are conspiring against this unity.

National planning system and national project

To build Chile into a great nation, it will be the duty of the State to draft a "National Project," creating a feasible and desirable image for the republic, contemplating its long-term development and taking into account the efficient use of our real potentialities.

For this purpose, and without going beyond the limits of state action, as outlined when discussing the principle of conditional supervision, the State will draft a National Planning System which, starting from a National Project, will integrate procedures, institutions, and organizations to ensure reaching national goals within the framework of governmental policy. This system will coordinate and implement the plans of the various elements within it, taking into consideration both medium and short-term objectives.

Such a national planning system will overcome the traditional lack of coordination between development, planning, and national security, incorporating the latter as a vital part of the broad-based and integrated scheme of global national development.

An authoritarian, impersonal and just government

Guided by the inspiration of Portales, the Government of Chile will energetically apply the principle of authority and drastically punish any outburst of disorder or anarchy. It will exercise power impersonally and avoid every type of petty sectarian interest. From its position above all private groups of any type, it will ban the use of influence, protect the weak from abuse, and will act as an honest arbitrator without favoritism for justice and the common good.

The values and style of the nationalist government

Chilean nationalism, rather than being an ideology, is a code of living, the genuine expression of the nation and of the soul of its people. In keeping with this idea, Chile's government will always prize the broad principle over sectarian doctrine, achievement over programs, the spirit of morality over the letter of the law, shrewdness over ideology, and reality over the deceitful words. The nationalist government recognizes and proclaims the following as fundamental values of the national spirit:

a) **justice and equality before the law.** Without privilege or exception all must comply with the law, and all who transgress will receive equal and impartial punishment. Furthermore, it is an urgent necessity to expand this equality before the law into a true equality of opportunity in life, where the only inequalities to be tolerated are those placed on an individual by his Creator, and the limits of his individual merit.

b) **the restoration of pride in wholehearted effort,** the only true road to progress and the personal fulfillment of the human being. For decades political demagogues have preached to the people that doctrinal formulas could substitute for work as a means of economic development. Furthermore, longstanding abuses in compensating thousands of Chileans for their efforts have blurred the inherent dignity of work in the national conscience. Both faults must be corrected, and it must be understood that since the welfare of Chile is a collective responsibility, there is no excuse for parasitism or idleness.

c) **the creation of a morality based on merit and personal effort.** National politics, lately characterized by low standards and mediocrity, has developed an outlook where personal success has frequently been considered as something negative, to be hidden, something for which an individual must "apologize." To lead the country towards national greatness we must conceive a new outlook which will recognize the merit of public distinction and reward those who deserve it, be it for labor output, production, study, or intellectual creation. The State thus stresses that the fulfillment of one's duty is the true way in which each individual may serve society, and that national solidarity, far from excluding the healthy spirit of competition among those similarly employed, must stimulate it as a valuable instrument for collective effort. We seek a morality based on effort and reward, not only for individual work, but also for outstanding efficiency and civic spirit among groups and trade unions.

d) sobriety and austerity among those who govern as a symbol of the best in our national traditions. Chile has always demanded that authority set an example, and has respected in spite of political differences those rulers whose lives have been personal evidence of civic virtue. Fully aware of this, the Government is setting that example of self-denial so necessary for national reconstruction, for only thus can they expect that every Chilean will absolutely fulfill his duty, including the acceptance of his own and his family's share of the inevitable collective sacrifice.

e) the restoration of non-political status to the public administration. The custom of infusing party politics into public administration resulted in political favoritism, inefficiency, and the absence of a national state policy. As the Government has announced, any public employee who uses his position to further party interest will be dismissed, whatever branch of the public administration or related services he belongs to. For the same motive, a radical reform of the public administration will take place making it a reputable, important career or school for public service, subject to the general rules of absolute political non-involvement just as members of our judiciary must function.

**A code of justice respectful of human rights:
a guide for the present government**

Chile has always lived within a juridical order. The majesty of the law has been an inevitable force in our social development. Furthermore, legal order has always been the reflection of the deep regard Chileans feel for the spiritual dignity of the human being and for his rights. The heart of Chilean democracy is to be found in that respect for human rights.

Another important characteristic of our legal tradition has been respect for freedom of thought and the right to dissent. Both must be preserved in the legal state which the September 11th movement intends to reestablish, and which, basically, have been preserved within the scope of the emergency measures presently governing this State. Human rights must be strengthened, so they may be effectively enjoyed by all, and all may truly have an equal chance. The right to dissent must be preserved, but the experience of recent years shows the need to subject it to acceptable limits. Never again must a naïve democracy allow within its midst organized groups acting under the guise of misunderstood pluralism, to foster guerrilla violence to attain power or, feigning a respect for democracy, to further a doctrine or morality whose objective is the construction of a totalitarian state. For this reason, Marxist parties and movements will no longer be admitted into our civic life.

It should be clear, then, that Chile is not neutral in her relationship to Marxism. Her concept of the individual in relation to society, fundamentally opposed to that of Marxism, makes this impossible. The present Government neither fears nor hesitates to declare itself anti-Marxist. This is no negative attitude; it is, in fact, Marxism which denies the most fundamental values of true civilization. In politics or morality, just as in mathematics, the denial of a negative implies an affirmative. Anti-Marxism implies, therefore, the positive affirmation of the freedom and dignity of the human being.

A new and modern institutionalism: the task of the present government

Within the framework outlined above, the Government of Chile has taken upon itself the historic mission of giving Chile new governmental institutions that will embody the profound changes occurring in modern times. Only thus will it be possible to provide our democracy with solid stability, cleansing our democratic system of the vices which made its destruction easy. This, far from being a mere corrective task, will open the gate to new, creative fields. The most important factor of that new instrumentality will be the decentralization of power, both functionally and territorially, thereby enabling the country to advance toward a technocratic society with true social participation.

Functional decentralization: political and social power

The new unit, which is now being created, will distinguish between social and political power, clearly discriminating between those who hold the power and the manner in which it is exercised.

Political power or the power to make decisions in matters of general interest to the nation is, properly speaking, the function of governing the country.

Social power, on the other hand, must be understood as the power of the intermediate groups of society to develop with legitimate autonomy toward their specific goals as a means of influence to delimit or to enrich the activities of political power.

Because of the continuous erosion produced in our country by demagogues over many years, and because of systematic destruction of all aspects of our national life inflicted by Marxism since 1970, the Armed Forces, in keeping with their classical doctrine and in fulfillment of their duty toward our survival as a nation, were obliged to take over complete

political power on September 11, 1973. In so doing, they overthrew an unlawful and immoral government which had failed. They did this in response to nationwide urgings which are today expressed in the support granted to the new regime by the majority of the population.

The Armed Forces have set no time limit on their stay in government; the task of morally, institutionally, and materially rebuilding the country requires a prolonged and profound effort. Even further, and most categorically, this government has no intention of limiting itself to a merely administrative role, providing a breathing space between two party governments. In other words, Chile is not going through a period of truce, prior to restoring power to those same politicians who were so responsible, by act or omission, for the virtual destruction of the country. It is the hope of the Government to inaugurate a new stage in our national destiny, breaking ground for new generations of Chileans raised in a school of sound civic habits.

Nevertheless, although the Government sets no date, it will, in due time, hand over political power to whomever the people may elect by a universal, free, secret, and informed vote.

Do not take this to mean that the Armed Forces will disassociate themselves from whichever government follows them, just to watch the outcome as mere spectators. On the contrary, the President of the Government has said that he considers part of its mission to inspire a new and great movement; this is already emerging as a result of the present situation, and it will carry forward into the future, solidly and permanently, the efforts of this government.

The Government calls upon all Chileans who wish to participate in the era of national reconstruction to surmount former divisions and factions, and become part of that great national unity movement which is being born, and which will usher in the future.

Social power must now be considered; it is expected to develop into the most important organic channel of public expression. Chile has a long tradition of social organization going back to its Hispanic origin. The community councils, the autonomous municipalities, the labor unions and trade guilds at all levels are proof showing the Chileans have had a continuous commitment to their social organizations, as required by their historic and social development. It is essential that the municipalities recover their highly important role in local political and social organizations for which

only they are equipped, being at the immediate service of the family and the individual, and which is incompatible with the political influences to which they have been subjected.

To improve and develop genuine social power it is necessary to assure the independence and freedom from politics of all intermediate groups between the individual and the State, especially of the various federations formed by labor, employers, professionals, or students. Since the principle of conditional supervision, already stated, demands that such entities act autonomously for their specific purposes without the State absorbing their control, it is unacceptable that their objectives should be distorted by turning them or their boards into instruments to further political party interests. Therefore, all political party interference, direct or indirect, shall be expressly forbidden in the election or activities of union leadership. It is vitally important to understand that this depoliticization is the only possible manner in which unions and other intermediate organizations may become authentic means of social participation, and thus fulfill a hope which is truly in keeping with our times. Social participation cannot be discussed if the entities which should serve as the channels for the true expression of the feelings of the organized population are turned into docile spokesmen at the instruction of some political party, and are often inspired by the latter's petty electoral interests. These same requirements are applicable to the municipalities.

It is necessary to open the way for a new concept of trade unionism. Designed to gather together individuals linked by common interests and activities, the protection of its members, has been, and still is, the primary reason for the existence of these unions. Without disregarding this major function which is justified and natural, two other ideas, so far overlooked by Chilean unionism, have recently begun to demand recognition and must receive attention. First, those union activities undertaken to obtain rights and privileges must be exercised responsibly and thoughtfully, with the understanding that the State must harmonize the natural aspirations of each sector of society with the national interest according to the real possibilities of our economy. Second, this recovery of rights and privileges must not mark the limit of the unions' task. In a modern society the unions are expected to become vehicles, contributing technically to a wide understanding of political or governmental decisions. Advantage must be taken of the fact that, within a given union, persons are to be found who perform with specialized knowledge and identical activities. In a world where problems are becoming increasingly more technical and less ideological, cooperation in technical matters emerges with new and wide importance for Chilean labor and union movements.

When creating the necessary mechanism to harness this social power to our civic life, it will be the task of the new governmental apparatus to ensure that means of expression shall no longer be by threat or arbitrary action. The institutionalization and consolidation of an authentic social power, as described above, must be considered the most efficient means of transforming Chile into a technocratic society where informed opinion shall prevail over slogans, a society with a real participation where the voice of the organized population will emerge without political distortions and free from impoverishing pettiness. Our democracy will then be organic, social, and with fair participation.

Territorial decentralization; the division of the country into regions

A territorial decentralization, whose scope will be far more than simply administrative, follows naturally from the principles analyzed above.

The government has already defined effective geographic zones for a regionalization in keeping with Chile's modern requirements, which will replace an artificial and outdated division into provinces and departments.

In the planning of each region, its population, security, geography, productivity, and services have been taken into account thus allowing the various zones ample initiative and reasonable autonomy within the social and economic development of the region. The union federations, which already exist in most parts of the country, must appreciate the important role open to them to play in facilitating the application of the concepts of social participation and technical development in the regional or territorial plan. They must do this by assisting and coordinating the similar tasks which fall to the unions to undertake within their own areas in a strictly functional way.

**The basic objectives of national reconstruction:
an accelerated economic development, effective
social progress and a scale of moral values which
ensures every individual his due**

After reorganizing its economy, destroyed to its very roots by the Marxist regime, Chile has to advance rapidly and decisively for without this it will be impossible to satisfy the hopes for security of our countrymen, especially the poor. This demands a clear understanding that the only realistic way to reach these objectives lies in a large increase of mining, agricultural, and industrial production, which requires national and foreign investments.

With regard to foreign investments, the present Government reaffirms "It is not a true nationalism to reject foreign investment, but to subject it to conditions which ensure primarily that it is beneficial to Chile." (Speech by General Pinochet. November 10, 1973).

Economic development is a challenge requiring authority and discipline in production and labor customs. In turn, this demands practical methods suited to our character. Chile must guide its production towards those areas in which it is most efficient and competitive with other nations. This is specially urgent on a continent in which projects for increased economic integration are continually being proposed. With this in view, the present Government considers the reactivation of Chilean agriculture, for so long in a state of depression, a task requiring the highest priority.

The increase in mining production, since September 11, 1973, is another favorable symptom of a trend, which is important to strengthen.

A country, which intends to base its economic development on a recognition of the rights of private property up to the level of but excluding strategic and essential products, and also aware of the State planning that this area requires, must promote an economic policy which grants the consumer active participation. It must recognize the value of competition between producers and distributors within limits clearly established and guaranteed by authority.

The achievement of rapid economic development must not, however, be considered an end in itself. The accumulation of a national fortune only provides the means for the well-being of the inhabitants of the country, and it must be enjoyed fairly by all. The indices of economic growth, national production, and per capita income growth must all be accompanied by the constant efforts of the State to transform these increases into social progress. As expressed by General Pinochet in his speech on October 11, 1973, the present Government reiterates:

"Economic development and social progress are inseparable. When the demagogues sacrifice the first, the social benefits they grant become a mere illusion for they are only distributing poverty. On the other hand, when social progress is held back, economic development is not translated into justice, but stirs up undesirable tensions."

Social development must distinguish between true social improvements for the workers, because they imply greater progress for the country and

greater justice, for themselves and those ill-named "conquests" which merely conceal excuses for idleness and privilege which a country like Chile cannot accept. For example, among the first improvements which the present government intends to strengthen, may be mentioned those benefits received for uninterrupted work attendance, and the family allowance for manual workers which, for the first time in our history, the Government of Chile has equalized with the allowance received by white-collar workers. Among the "conquests" is to be found legislation which allows some people to retire on pension at thirty-five years of age, while still others receive up to four pensions simultaneously. These so-called improvements will be pruned without mercy.



On this subject, the present government gives great importance to a legal project at present awaiting approval: "The statute governing the organization of enterprises, the development and integration of labor, the promotion and management of investments". This will establish methods of effective participation of workers in the enterprises in which they serve, while also maintaining the flexibility that such a complex plan requires and including necessary guarantees for the investor.

Nevertheless, the deep moral and economic crisis, which today shakes the developed West, is a warning bell to us to take note that material security is not the only factor in achieving a balanced society in which man may develop all his potential. As we have said, the materialism which corrodes consumer societies illustrates the sort of security which does not assist man's search for perfection, but forces him into a race seeking a wealth which dominates him and, in the end, leaves his spirit empty. It enslaves man rather than liberates him.

It would be presumptuous of us to claim that Chile has a solution for such a complex and dramatic problem. But at the moment, when it sets in motion the economic reconstruction of the country, the present government recognizes its responsibility to take this problem into account. Any realistic effort to overcome it must be based primarily on an education which stimulates a set of moral and spiritual values in keeping with our Chilean and Christian tradition, and which retains a perspective about man's final destiny.

With this in view, we believe that education within the grasp of all, respecting freedom of teaching and one's innermost feelings, will strengthen the understanding of every Chilean toward his country, its geography, its history, and its people. From this rediscovery of the roots of our nation-

ality, values and virtues will emerge which will have much to contribute when we face this difficult challenge.

Chile: a nationalism which looks towards universality

In an increasingly interdependent world, Chile's government maintains that its character is nationalistic, confident in the knowledge that, in spite of its varied geography, our country is historically, ethnically, and culturally a homogeneous unit. We do not claim Chile to be superior or inferior to other nations. We maintain it is different, insofar as it has a clearcut image of its own. But this search for a rebirth, from the very depths of our national soul, does not imply that the present government expounds a nationalism belittling that universal point of view demanded by the contemporary world.

Chile's government will seek improved relations and international understanding, especially with friendly nations, in keeping with strict adherence to international treaties, non-intervention in the affairs of other nations, and the right to self-determination of every nation, as traditionally accepted by our Foreign Office. Given this feeling, the present government repeats its wish to maintain international relations with all nations whose governments do not take it upon themselves to intervene, without warrant, in our internal affairs.

With a responsible outlook debarring us from any absurd idea of leadership beyond our own frontiers, Chile's international policy is directed towards the development of "national growth," the effective ability and strength of the State to defend and promote its interests before all nations. For this task, it is indispensable to restore our national dignity in all areas, to restore to our country the worldwide prestige it traditionally enjoyed, and which the Marxist government did so much to weaken.

An outward-looking Chilean nationalism must combine the western historic and cultural tradition which binds us to European civilizations with the geo-economic fact that places our country within the New World, and specifically within Hispanic America, while at the same time opening untapped perspectives toward other civilizations and cultures across the Pacific, whose possibilities and wealth must be harnessed to Chile's advantage.

The family, womanhood and youth: pillars of national reconstruction

Finally, the present government feels the whole task it has outlined must rest solidly on the family as a school for moral upbringing, of self-sacrifice and generosity to others, and of untarnished love of country.

Within the family, womanhood finds fulfillment in the greatness of her mission, and thus becomes the spiritual rock of the nation. It is from her that youth is born who, today more than ever, must contribute its generosity and idealism to Chile's task. The courage shown by women and the young during the past few years, as bastions of the civic government, which found its climax in the military pronouncement of September 11th, must now be turned into a patriotic fiber to face the hard sacrifice ahead, and be transformed into a creative force to change a deep national hope into reality.

**Report on the State
of Public Finance**

**Vice-Admiral
Lorenzo Gotuzzo Borlando
Minister of Finance**

October, 1973

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Introduction

As Minister of Finance and at the request of the Government, it is my duty to report on the present state of Public Finance and on the current economic situation in general.

All citizens know from their daily experience, that the general economic situation is chaotic, that the country is now facing one of the worst economic crises in its history, and that the future of the country has been seriously compromised by the irresponsible and demagogical policies of the Marxist government.

Every one of us has suffered in the flesh from the problems of supply, the long lines, black market, galloping inflation, lack of job security, unjust persecution, sectarianism, all sorts of arbitrary treatment and lawlessness.

On this occasion, I would prefer to present you with a different situation, but it would only be a deception.

It will be difficult to overcome this stage in the life of our nation; to do so will require great sacrifices and the patriotic participation of all citizens.

The moment has come to put an end to the monumental dissipation into which the country was induced by the Marxist regime and during which the Nation's resources have been irresponsibly squandered.

The information I shall give you today is irrefutable and I trust that you will take seriously the terrible crisis we are experiencing. We are not surprised that, faced with this tremendous disaster, the ones truly responsible for this chaos, have attempted in one last insane attempt to drag the people into a confrontation, the consequences of which would be incalculable. The errors of a group that wanted to impose its own convictions at any price would have been bathed with the blood of many innocent men and women.

The task we now face is very difficult —we must restore the Nation's productive capacity, recover the lost years, correct existing distortions, increase investments and savings and restore morality to a corrupt system. It is not the task of one day, nor of a group of men, but rather of an entire people. The task belongs to each one of us.

We are living in a time of sacrifice, but it is also a time of great hope. Chile has found its way again, and we shall spare no effort so that the new phase

of history which opens before us today is as fruitful as the phase that witnessed the birth of the Republic.

The tasks of reconstruction shall require tremendous effort. To overcome the present crisis we must remember that the greatest effort and the greatest sacrifices must be made now, in the short term, so that once the present adversity has been overcome, the economy may be directed along the road to rapid growth.

It is urgent that we begin a process of reordering the economy so that resources may be allocated efficiently, so that exports may expand rapidly and so that numerous investment projects may be carried out.

In order to accomplish all this, we must have a realistic exchange rate policy and a system of prices in relation to international price levels. The public deficit must be solved in order to defeat inflation, and in order to eliminate exorbitant increases in the amount of money which exceed the rate required for the current level of growth.

Fiscal financing should be assured by the revenue system. We shall fight tax evasion by means of drastic sanctions, including imprisonment, for these crimes.

The civil service sector shall be reorganized in order to end unnecessary spending, but at the same time, we shall respect the careers of experienced functionaries, and we shall demand efficiency. A wage and salary policy compatible with the anti-inflationary plans shall be designed and I want to tell you quite honestly that it is impossible to continue with the massive and exaggerated readjustment policies. They are momentary solutions which in turn generate new increases in costs and prices that reduce the purchasing power of wages to levels even lower than those which existed before the readjustment. However, since uncontrolled inflationary pressures inherited from the former regime still persist, the Government will grant a bonus to compensate for the indispensable price increases which we must authorize in order to avoid worse problems for the economy. I wish to make it very clear that the Government is particularly concerned with the most needy sectors of our society. We shall establish adequate measures so that their already low standard of life may not continue to deteriorate.

Short Term Measures

In order to achieve the necessary economic reorganization and to overcome the present crisis, we have decided to modify the policies in force regarding the exchange rate, prices and income.

With regard to the exchange rate, the following norms have already been established:

- 1) There shall be only one basic exchange rate for imports and exports, which has been established at E.°280 per dollar.
- A special provisional rate of 110 escudos per dollar will apply to the small and medium copper mines.
- 2) A rate of 850 escudos per dollar has been established for tourists, subject to a 53.15% tax for those who travel outside the country.
- 3) There shall be periodic moderate devaluations to prevent erosion of the real exchange rate by inflation.

The price policy which follows complements these measures:

- 1) Prices must reflect real production costs.
- 2) The prices in the monopoly sector shall be strictly controlled. A price list shall be modified in order to transform this legal instrument into a truly operative mechanism.
- 3) With regard to articles for which sufficient home competition does not exist, the producers will set the sales prices but they must justify the costs with Commerce and Industrial Bureau DIRINCO. If abusive pricing should result, it shall be drastically sanctioned. In such a case, DIRINCO will fix the prices of these products and foreign trade mechanisms shall be used to insure adequate supply.
- 4) Agricultural prices shall be regulated according to the average international market price in recent years. This will motivate domestic production. However, temporary subsidies shall be granted to some necessary products such as tea, bread, pastas, sugar and oil in order to safeguard the level of consumption in the low income sectors.

The measures enumerated, while very difficult, are indispensable. They are the inevitable result of the truly chaotic economic situation of this nation. It is impossible to elude this responsibility if we want Chile to return to its status as a worthy progressive country respected by our sister nations.

As we have already said, "The party is over," the consequences are plainly visible. We must face them. The Marxist demagoguery maintained artificial prices, and these were converted into wealth for the administrators, black markets, long lines and a decline in production. Today, in order to rectify that situation effectively and in order to increase production, prices must reflect real production costs.

We are aware of the fact that the impact of these measures, which shall be translated into a generalized increase in prices, and which in some cases will be very great, will mainly affect the low income sectors. For this reason, the effect that these measures will have on the standard of living of the population will be compensated for by the income policy to be applied generally to the public and private sectors and to liabilities in general as detailed below:

- 1) During the next three months five complete salaries, subject to taxation, shall be paid. The base for the two additional salaries shall be the readjusted salaries for the month of April.

The payment schedule for the remainder of the year is as follows:

- a) The October salary shall be paid between the 11th and 15th of this month (October).
 - b) The November salary shall be moved forward to the first week of the month.
 - c) The first bonus shall be paid in the third week of November.
 - d) The December salary shall be moved forward to the first week of the month.
 - e) The second bonus shall be paid before Christmas.
- 2) A third bonus, equivalent to the salary for the month of April with a maximum of five basic salary units, shall be paid during the third week of the month of November.

- 3) A transportation allowance up to 720 escudos per month shall be paid to each worker.
- 4) The family allowance shall be leveled off at 900 escudos per dependent and those allowances which exceed this limit shall be frozen.
- 5) An Unemployment Subsidy shall be established for all those workers whose contracts have expired. This will be paid monthly for a period of six months. The subsidy, to be paid monthly, shall consist of the equivalent of one month's salary, with a maximum of six times the base salary for the first month, and decreasing thereafter by one salary monthly over a period of six months until its expiration.

The Government also has deemed it necessary to establish a wage policy that contemplates a uniform wage scale for the public sector, and that will put an end to the irritating differences which exist for positions of equal responsibility. The uniform wage scale for the public sector shall go into effect beginning next year together with the application of a new general policy on wages, salaries and benefits. The corresponding studies of these projects have already begun.

The income policy described above is destined to palliate to some extent the effects on purchasing power of the exchange rate and price policies. This will not, however, spare us the sacrifice that the despicable Marxist action and crude reality impose upon us.

We wish to demonstrate in figures the true magnitude of the catastrophe we must face and which justifies the measures I have just pointed out.

State of the Public Treasury

According to the report presented by the Comptroller General of the Republic, the state of Public Finance at June 30, 1973, was and still is, extremely critical. The following are some of the points which the Comptroller General's Office cites to demonstrate the seriousness of the situation:

1. Current Assets are 15.900 million escudos whereas the Current Liabilities have reached 25.300 million escudos. Therefore, short term liquidity is non-existent to meet this sort of debt and part of the national wealth will have to be liquidated.

2. The public wealth is 75.300 million escudos and the Public Debt is 90.100 million escudos, which means that there is no backing for it since the assets of the State are insufficient to meet the Debt.
3. The Total Assets do not cover Total Liabilities. This situation in any business means that, if by liquidating the current assets and the capital the short and longer term debts are not met, bankruptcy occurs.

This is the opinion of the highest controlling organization of the Republic with regard to the state of the Public Treasury.

I do not wish to tire you with figures, but the state of Government finances as well as the financial situation of public enterprises at the time when we took over the economic direction of this country must be made known to the public.

Fiscal Situation

An analysis of the information on fiscal income and spending allows us to draw the following conclusions:

Table N.º 1
Government Expenditure and Fiscal Deficit
(In Millions of E.º)

	Government Expenditure	Fiscal Deficit	Fiscal Deficit as Percent of Government Spending
1970	22.117,4	2.882,2	13,0
1971	36.506,2	12.532,2	34,3
1972	64.950,5	26.575,4	40,9
1973	277.922,0	148.434,0	52,8

1. Total fiscal spending between 1970 and 1973 increased more than 10 times, from 22.100 million escudos in 1970 to 277.900 million escudos in 1973. Since there is no tax system which permits the sound financing of such an exorbitant increase in spending, there is clearly a deficit in the financial activity of the fiscal sector.

2. The tendency which we can perceive over the last three years indicates that the magnitude of the fiscal deficit is growing. As you can see in Table N.º 1, from 1970 to 1971 the fiscal deficit quadruples. Then it doubled from 1971 to 1972, and in 1973 it will quintuple.
3. The fiscal deficit as a percentage of the total of government spending grew from year to year. This means that of every 100 escudos which the Government spent in 1970, 13 were financed by money creation. In 1971, of every 100 escudos spent by the Government, 34 were financed by printing money. In 1972 the figures rises to 40, reaching an incredible situation in 1973 in which, according to the projections made, of every 100 escudos spent by the Government, 53 escudos were financed by the printing press. In other words, by 1973 we had arrived at an untenable financial situation in the fiscal sector, since less than half of Government spending was financed by the tax system.

This situation cannot go on and the primary objective of this Ministry is to correct government finances.

The gravity of the situation described in Table N.º 1 resulted in a phenomenon of even greater proportions.

By studying Table N.º 2 we arrive at the following conclusions:

1. The Government spending budgeted yearly and proposed to the National Congress for discussion and approval has not been in proportion to the actual spending during the same period. This phenomenon tended to worsen during the last three years. Thus, in 1972 the expenditures according to the budget were to be 51.700 million escudos, but they actually reached 64.900 million. This proportion doubles in 1973, when the budget figure was 138.400 million and an estimate of the actual spending in 1973 is 277.900 million escudos.
2. In the second place, the magnitude of the Planned Deficit in each fiscal budget is not in keeping with the Actual Fiscal Deficit at the end of each year.

Thus we have, for example, that the Actual Deficit for 1971 was more than double the Planned Deficit. In 1972 the same thing occurred, as the Actual Deficit was 26.500 million escudos, while the Planned Deficit was to have been only 12.300 million escudos.

Table N.º 2

**Fiscal Spending and Deficit:
Budgeted and Actual
(Millions of E.º)**

	1971		1972		1973	
	Budgeted	Actual	Budgeted	Actual	Budgeted	Actual
Public Spending	36.004,4	36.506,2	51.758,2	64.950,5	138.465,1	277.922,0
Public Deficit	6.026,0	12.532,2	12.310,4	26.575,4	49.572,1	148.434,0

The situation for 1973 is even more serious, since the Actual Deficit for this year indicates that the Planned Deficit will be tripled, rising from 49.500 million escudos to 148.400 million escudos.

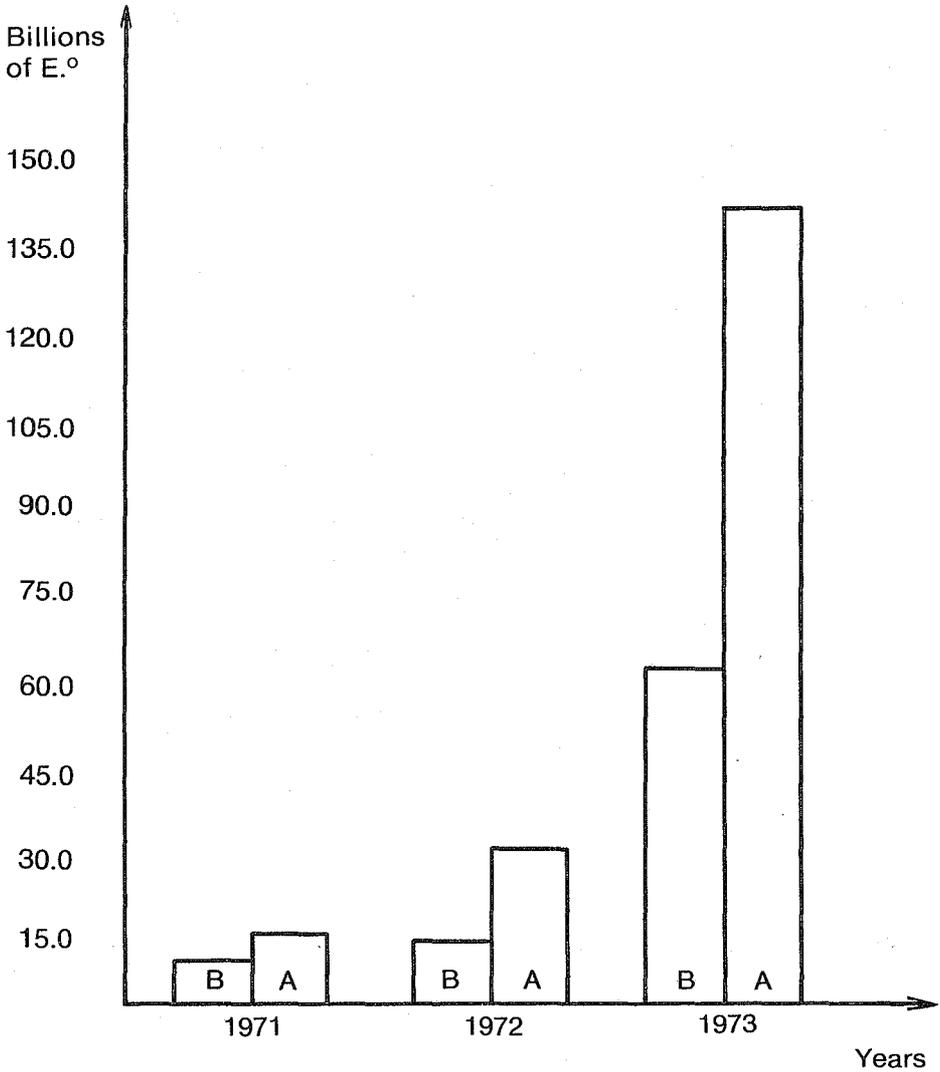
The chaos of this situation is evident from the fact that the actual deficit will exceed the total of public expenditure initially approved by the Congress.

3. The information published here indicates that the faculties of the Congress were gradually being bypassed, not only in matters of government spending, but also through the decentralized public sector.

The increase in the fiscal deficit is one of the most important causes of emissions of money by the Central Bank, and as we shall see further on, this is one of fundamental causes of a sharp increase in the inflationary spiral that is troubling every home in the country.

The deficit financing of the extraordinary increase in public spending is a result of an irresponsible economic policy intended to maintain an artificially a false sensation of prosperity. However, as we shall see further on, the real sectors of the economy were deteriorating rapidly, thereby generating the economic imbalance that caused the galloping inflation we all witnessed and that has brought our country to the deplorable situation of possessing the world record for inflation in recent years.

Graph N.º 1
Fiscal Deficit
Budgeted and Actual



B = Budgeted
A = Actual

The serious fiscal deficit problem that we are facing has been exposed. It is our intention to reduce the money creation on the Government's account and to reform the tax system, so that the revenues are in direct relation to Government spending in order to achieve sound financing of the national budget.

However, this is not all. There are important financial debts which must be solved as soon as possible. In the first place are the deficits of decentralized public institutions such as Agricultural Trade Corporation (ECA), The Agrarian Reform Corporation (CORA), the Development Corporation (CORFO), Railroads, etc., the financing of which is subject to Government transfers and credit from the banking sector, particularly the Central Bank.

Situation of the Public Sector

There is also the deficit in the companies that from what is known as the Social Area and which at present are dependent on the State. We discovered with deep surprise and indignation, the true extent of the bankruptcy of these companies.

So that you may form some idea of the economic setback to which the formerly vigorous industrial sector had been dragged, I present here a concise synthesis of the information we have been able to compile and which corroborates the opinions stated above.

A study of Table N.º 3 demonstrates the following conclusions which expose the demagogical and irresponsible management of the former administrators.

In the first place you can appreciate the situation of this economic sector which it was assumed would produce a surplus to help finance the country's economic and social plans. The Social Area did not leave a surplus in 1972, nor will it do so in 1973, according to the estimates existing before we assumed the management of the country.

Secondly, the deficit in the Social Area is multiplied nine times, increasing from 21,800 million escudos in 1972 to the incredible figure estimated to be 175,800 million escudos for 1973.

Table N.º 3

Financial Situation of Companies in the Social and Mixed Area
(In millions of E.º)

	1972	1973
Operations Income	59.144,2	254.593,9
Operations Expenses	73.803,6	346.535,8
Operating Deficit	14.659,4	91.941,9
Capital Spending	7.212,4	83.867,5
Total Deficit	21.871,8	175.809,4

In the third place, it is wise for the public to meditate for a moment on what these figures represent. The Deficit in the Social Area in 1973 is superior to the Deficit in the Fiscal Sector which as we already saw, will reach 148,408 million escudos. However, in spite of the strategic importance of this key sector in national activity, its management was not subject to inspection by the Congress or by the Comptroller General, but depended rather on the arbitrary and irresponsible decisions of bureaucrats at the service of an alienating ideology.

It is my duty to inform the citizenry, and especially the workers who loyally and honestly contributed their share of work in the Social Area, of the catastrophic financial state in which these companies have been left by their former administrators, many of whom today are fugitives accused of the crimes of fraud and robbery to the detriment of all Chileans.

For this reason, a few companies have been extracted from the long list of Social Area enterprises as examples to put before the nation.

Table N.º 4

Deficit of Some Companies in the Social and Mixed Area

(Millions of E.º)

	1972 Actual Figures	1973 Figures Budgeted in January
Cía. Cervecerias Unidas	330,8	1.816,8
Fensa	—	287,9
Ferriloza	—	115,5
Sindelen	—	100,1
Indugas	—	140,7
Yarur	219,6	434,2
Caupolican	165,1	234,7
Sumar	147,9	453,8
Oveja Tome	—	255,4
Fiap	76,4	180,8
Fabrilana	44,0	268,7
Rayonil	57,3	176,4
Continental	—	145,6
Cap	2.982,5	6.791,5
Enami	1.217,7	7.834,6
Soquimich	1.294,2	4.588,3

These figures reflect the crude reality of the condition of these and of all the companies in the Social Area after the sad and painful Marxist experiment which our people had to bear for almost three years.

I would like to take this opportunity to point out to the workers that they should have confidence in us, because the economic policy now being developed, although truly difficult, will allow them to participate in the near future in the surplus that shall be generated. The situation described above, in which you were in debt together with the whole of society because of the deficits obtained and that were financed by inflation-causing money creation, will not recur.

Monetary Situation

The situation in the fiscal sector and the Social Area which we have outlined here affects and conditions the monetary policy, because the Central Bank must finance the increase in Government expenditures and the losses in the Public Sector by means of money emission.

Table N.º 5 shows the monetary situation from 1970 on.

Table N.º 5

Total Amount of Money

	Money	% Increase Yearly	% Variation in Relation to 1970
December 1970	12.094		
December 1971	25.838	113,6%	113,6%
December 1972	70.484	172,7%	482,8%
December 1973	406.000	477,0%	3.255,3%

As you can see, money will increase from 12.094 million escudos in 1970 to 406.000 million escudos in December, 1973. Money increased at a yearly rate of 113% in 1971, 172% in 1972 and will rise to 477% in December 1973, according to figures estimated by technicians of the former Government.

This means that the rate of increase of money was accelerating progressively and that if this policy were continued, the amount of money would have multiplied 33 times in three years.

Indiscriminate increases in money were creating month-by-month increases in purchasing power under circumstances in which production did not argument at the same rhythm and had even diminished, as occurred in nearly all sectors beginning in the second semester of 1972.

In this way the increase in money became a source of uncontrollable inflationary pressures, since an ever increasing purchase power existed together with static production.

Graph N.º 2

Real Production and Amount of Money

1971	1972	1973
Production	Production	Production
8.5%	0%	-10%
E.º	E.º	E.º
113%	172%	477%

Graph N.º 2 is a full portrait of the origin of the uncontrollable inflationary pressures which exist in our economy. In that graph you can see two groups of circles. The first group, in the upper part of the chart, represents the physical volume of goods and services which the economy was capable of producing during the years 1971, 1972 and the estimate for 1973. In other words, each circle in the upper part of Graph N.º 2 represents the total of washers, televisions, refrigerators, wheat, potatoes, etc. that were produced in the respective year.

If you now examine the second sequence of circles which is located in the lower part of Graph N.º 2, you will get an idea of how the quantity of bills and coins increased year by year. For example, in 1971 the quantity of goods and services grew about 8%, while the quantity of money increased 113% in the same year. In 1972 production of goods and services experienced no growth at all. However, the amount of money grew 172%.

According to estimates made by technicians of the former regime, the situation for 1973 was so grave that the difference between the increase in production and the increase in bills made economic collapse imminent and inevitable.

If you observe Graph N.º 2 carefully, you will see that the production of goods and services for 1973 drops about 10%, while the amount of bills and coins in circulation in the economy increases 477%.

To explain this concept better, permit me to refer to a non-economic example. Let us suppose that for a hypothetical soccer game between

Chile and Russia to be played in the National Stadium, the authorities involved were to sell 300,000 tickets, when the stadium can accommodate no more than 80,000 people. Imagine what would happen. Of course, there would be a long line to get in, there would inevitably be innumerable disorders and pressures from those who were justifiably indignant for having been cheated. Finally, the pressure from those who wanted to get in would make the crowds teem on to the playing field thus destroying all possibilities of seeing the game and perhaps the very stability of the stadium building would be endangered.

To increase indiscriminately the amount of money beyond the real possibilities of production is like over-selling tickets to a soccer game. There will be long lines and many will definitely feel cheated. So the economic structure which the prices represent will collapse. Prices will then begin to rise rapidly until they reach the rhythm of the increases in money and they can even surpass these when people lose confidence in the value of monetary signs, that is to say, in the value of the currency.

I have dwelled on the monetary problems, because I want the citizenry to understand that the apparently easy solutions to the problems which cause a deficit in the public sector, in the long run cause even more serious problems. In economics there is no magic formula which allows a person or a nation to spend more than it has without this eventually causing an inevitable bankruptcy. And when the public sector spends in an exaggerated manner beyond what its resources permit and beyond what the economy is capable of financing, then a problem of inflation is produced. The effect of inflation is equivalent to a tax which directly affects those who live on a fixed income, on a salary or a wage. This is terribly unjust, because it affects workers proportionately more, as they see how the purchasing power of their income diminishes month by month. On the other hand, the sectors which derive their income from varied sources and which are in general the more comfortable groups of society, can, to a great extent, avoid the effects of inflation. There are even those who, thanks to cheap credit and speculation, profit from it.

The basic objective of the Government is to correct public finance, to reestablish order and productivity in decentralized sectors and in the companies in the social area, in order to end the financial imbalances which force exaggerated increases in money and which lead to inevitable inflationary pressures.

The public will understand that this is not an easy task, nor can it be ac-

complished over night. It is necessary to rationalize public administration in order to diminish unnecessary expenditure, and to modify substantial aspects of the tax systems so as to assure timely financing of the fiscal budget, which will permit us to shorten the lag that exists in the receipt of some taxes. It is also necessary to establish effective taxation in order to generate revenues which make it possible for the social development programs to be paid for by the high income sectors of the community. It will be important as well to modify the nature of some of the taxes which distort the efficient use of resources or that discriminate unnecessarily against some sectors.

Foreign Trade

Another task which is of particular interest to the new Government is that which concerns the foreign sector of the economy.

In the 1971-1973 period, imports in this country out-numbered by far the exports, creating a commercial deficit with the rest of the world, which provoked first the loss of the reserves of the Central Bank and then increasing foreign debt, besides making the country incapable of fulfilling its financial commitments. This led the former Government to call a unilateral halt to the payments and to renegotiate the totality of the foreign debt.

In the first place, I wish to analyze the situation of foreign trade. Then I would like to refer to the debt with foreign countries.

Imports rose from 916 million in 1969 to approximately 1.500 billion dollars in 1973.

The increase in imports has its origin in the first place in the increased number of purchases of agricultural products which increased from 173 million dollars in 1969 nearly to 600 million dollars in 1973. In comparing these figures, I wish to point out certain facts:

1. In the 1969-1970 period imports of beer were very significant but beginning with the second semester of 1972, they were almost totally suspended. If they were included in agricultural imports, these would exceed 700 million dollars.
2. The former figures include agricultural products besides foodstuffs, such as wool, leather, animal feed, etc. which traditionally had been produced by our own agriculture.

3. International prices have increased, thereby making the import of food considerably more expensive. This information shows the strategic importance of solving the existing agricultural problems. In any case, it should be pointed out that, although the estimated level of food imports is the highest ever reached, it will be insufficient to satisfy the internal need for food. In order to achieve this objective, we need a total of 700 million dollars in agricultural imports, including those raw materials produced on farms and which have industrial application.

Exports in this period have fluctuated considerably. Copper, our main export product, has declined from 920 million dollars in 1969 to 657 million in 1972. This was caused in part by international variations in the price of copper and also in a decline in the quality of our exports since the proportion of electrolytic copper, which brings higher prices, declined and metal concentrate production increased, even though it has a lower commercial value as it is semi-processed. In 1973 there was significant improvement in the price of copper which improved the value of exports, even while physical production has decreased considerably in the first semester of this year.

With regard to other minerals, especially nitrate, iron, iodine and molybdenum, there was a significant drop in 1972, which will be recuperated this year.

With respect to the remainder of agricultural and industrial products, there was a significant decline in 1972 which will continue throughout 1973. We wish to point out that, in general, the prices of all of these exports products have risen in the international market, so that the drop in production is an important indication of our loss of export capacity.

The disastrous results in foreign trade are a result of the erroneous policies which cannot continue without seriously compromising our possibilities for development. The increases in imports are, to a great extent, the fruit of an internal decline in production which must be recovered, especially in the agricultural sector. But it appears fundamental and basic to us to increase exports. Chile is a small country with a limited internal market. In order to accelerate our rate of development, it is urgent to design a bold export policy, principally in non traditional products, which will allow us to grow outward in order to take better advantage of our internal resources and our labor force. Economists, technicians and the basic productive sectors are generally aware that growth based on a rigid import-substitution model is no longer effective in Chile. Our best prospects for growth

are in an opening to international trade, in the development of export industries and in the intensification of the process of integration of Latin America from which we have been excluded during the last three years.

We are aware that rapid development of exports is possible as long as certain minimum basic guarantees are granted to exporters. The first and most fundamental of these is a realistic exchange rate which will not deteriorate because of internal inflation. Unfortunately this has not occurred in recent years and the country has returned to the practice of multiple exchange rates which discriminate seriously against the basic export sectors.

The multiple exchange rate system has been used to maintain artificially low prices for the numerous products consumed by the population. In order to do this exporters, especially of copper, have been obliged to sell foreign currency obtained at a price which does not even cover production cost. The result is that companies which export produce at a loss which they then finance by means of credit from the Central Bank. On the other hand, the low prices of imported goods discourage local production in these lines, since the national producer receives prices inferior to the real ones.

A second factor of great importance is continuity in foreign trade policy. Market formation is a difficult and slow process which requires years of effort. International competition is tough and many risks are involved, so that investments in this sector must have minimum guarantees that the conditions under which they are going to operate are stable and will not vary because of short term political whims or pressures. A third element almost as fundamental as the first two is the creation of internal economic conditions equal to those which other competitor countries grant to their own exporting sectors.

We have begun the economic reorganization by establishing new exchange rates and we shall maintain temporarily a lower exchange rate for the Large Mining Companies in order to have a subsidiary fund for necessary articles. This is a provisional measure, taking into consideration that a rise in the exchange rate will affect considerably the value of some foods, which, at the same time, will have a strong impact on the low income sectors.

The development of the export sector is also basic for the solving of our serious international finance problem related to the payment of the foreign debt.

Foreign Debt

The foreign debt situation which we have inherited will be a heavy burden for all Chileans. However, I wish to make quite clear that our country will recognize all of the international financial commitments legitimately contracted in the past.

According to preliminary figures from CORFO, the net foreign debt was 2,632 million dollars in 1970 and will reach 3,454 million dollars in 1973. This represents an increase of more than 800 million dollars in three years.

Over 75% of this greater indebtedness has been financed by countries in the Western Area and Latin America and only a small fraction with credit from the Socialist Area.

I wish to emphasize these figures because they refute the insensate declaration to the effect that the problems in this country were caused by the pressure of foreign powers and the highly publicized invisible blockade. This also demonstrates irrefutably that the solidarity of Socialist countries is another one of the innumerable myths which the former regime tried to create. When it is a question of financial affairs, those countries forget about solidarity and charge extremely high interest rates for the few loans they extend.

The Marxist Government indebted itself in a yearly amount superior to that of any of the preceding Governments. Furthermore, these credits were not used in important development projects, but rather to augment internal consumption, thereby creating a false image of prosperity by which they avoided publicizing the disastrous consequences of their policy. Thus, by deceiving the people of Chile, they squandered fabulous resources which should have been used to foment the economic development of our country.

To considerable indebtedness we must also add the loss of nearly all of the hard currency reserves in the Central Bank. The funds available were reduced from 331 million dollars in 1970 to 41 million dollars in September of 1973.

With the existing reserves it is practically impossible to end this year normally and we will only be able to meet the most urgent commitments for this month.

In the lapse of three years, the country lost 290 million dollars in reserves and was indebted in 822 million dollars. **That means that part of the cost of the experience we underwent which can easily be measured is the financial deterioration of US\$1.112 billion, which is an average of more than one million dollars per day.**

With those funds we could have built 140 houses a day, or a total of 151,200 houses in three years.

Fellow Citizens:

We have referred in depth to the serious financial problems of the country which are reflected in the deficits in the fiscal sector, in the decentralized sector, in the social area, in the monetary imbalance, in the foreign trade crisis and in the difficult foreign debt situation.

The Nation's problems however, are not only financial. There is a generalized crisis in all of the productive sectors which we must analyze thoroughly if we wish to have a correct diagnosis of the present situation.

The former Government carried out an economic policy whose main objective was to guarantee to a marxist minority the political and economic control of the Nation in the phase prior to taking full power. The purpose of this policy was not to serve the great national interests, but rather to create the short-term political conditions in order to establish the famous favorable set of forces which would facilitate the final blow to the legal and moral concepts governing the traditional Chilean way of life. That is why they were not too concerned with the growing deterioration in the productive sector and all the problems were explained with political slogans, such as "That is what the process costs," "Sabotage from the opposition," "The invisible blockade," etc.

In the first stage of the Marxist Government a "populist" policy was established with high increases in salaries and tight price controls which created an artificial economic situation nourished by the expenditure of reserves in foreign currency and large-scale imports. In this period investment levels declined notoriously and the country began to eat its own productive capital and operating stocks. All this caused internal consumption levels to rise considerably.

At the beginning, unheard of levels of apparent prosperity were reached. It seemed that Mr. Vuskovic had discovered "Colombus' egg" and em-

minent economists announced that the moment had come to burn the old text books because the new policy challenged even the laws of gravity.

However, the Marxist Government knew that the Indian Summer it was creating would not last long and that later on serious problems would arise. Meanwhile they were busy deceiving vast sectors of workers. This provided them with a bold offensive for entering into direct control of all sources of work, taking over a wide variety of companies in the name of the State and forming what became known as the Social Area. Behind the façade of the apparent participation of the workers, the entire productive system of the country was politicized, technical norms were ignored, and sectarianism extended to all areas. When it became obvious that production was insufficient to maintain the standard of living which had been artificially created, they resorted to the Supplies and Prices Committees (JAP) whose distribution policy established the most opprobrious method of discrimination among Chileans.

It would be time consuming to enter into more detailed considerations of this regrettable process. The most important thing is that the public become aware of its results and that all Chileans know the truth with regard to national production. For this purpose I will review the main sectors.

Mining

This year the production of copper has declined considerably as a result of continuous conflicts in labor and technical problems, since Chile has lost many worthy and capable professionals.

In Table N.º 6, you can see how in the first seven months of this year, production in the Large Copper Companies and Andina has dropped 12,5%. This is truly a national catastrophe, especially considering the high price of copper in the last few months. Production problems affect all of the mines, except El Salvador which increased production by 5,7%, but in the rest production declined as follows: Chuquicamata 12.4%, Exótica 26.8%, El Teniente 18.2% and Andina 12.7%.

There have also been considerable declines in the production of nitrate, iodine, iron, coal and petroleum.

One of the fundamental objectives of this Government is to reactivate mining and to recover rapidly the production levels in that sector. In order to do this we trust in the patriotic support of the mine workers. I wish to

take this opportunity to thank publicly the workers in Chuquicamata who in three days since this Government assumed command, achieved the highest level of production in the last three years. It is also urgent that we organize the working systems, with efficient non-political administration of the large mining companies, the application of adequate technology and a general economic policy which through the application of a realistic exchange rate, will solve the financial problems of these companies.

Table N.º 6
Variation in Production in Large Mining
Companies and Andina

January-July 1973/January-July 1972

Chuquicamata	- 12,4%
Exotica	- 26,8%
El Teniente	- 18,2%
Andina	- 12,7%
El Salvador	+ 5,7%
<hr/>	
Total Large Mining and Andina	- 12,5%

Industry

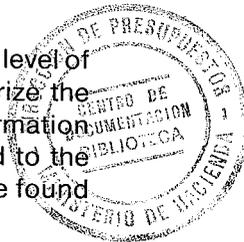
The industrial sector has also suffered enormous deterioration which worsened during the second semester of last year and which has reached very serious proportions so far this year.

In the first period of the Popular Unity Government production increased considerably thanks to the installed capacity of the industrial sector. The maximum growth with respect to the same month of the previous year was reached in November of 1971 with an increase of 30.8%. From this time on, the growth rate begins a progressive decline until November of last year when production dropped sharply by 8.8% as compared to the same month of the preceding year. This situation became more aggravated during 1973, and by the month of July production had declined 9.3%.

This very grave situation is the result of the lack of raw materials and parts, labor problems and the anarchy that existed in the area of ownership of industry.

Agriculture

The gravity of the situation in agriculture, which directly affects the level of supply for the population, is well known. I would like to summarize the case of agriculture, not in my own words, but rather with the information which the Minister of Agriculture of the Marxist regime delivered to the Ministerial Economic Committee in a confidential report which we found here in the Ministry.



“The last year shows an alarming decline in agricultural production only equal to the 19% drop during the 1968-1969 drought.”

As the saying goes: confession eliminates the need for proof.

The information on mining, industry and agriculture are of tremendous importance. The behavior of the real sectors indicates that in the economic sphere the process of destruction has generated a situation of crisis hitherto unknown in our history. The economic stagnation of last year will be followed by increasing deterioration which leads us to estimate a decline of at least 10% in the National Product.

Employment

The employment situation is, no less dramatic than that of the other productive sectors. The former Government produced an abundant flow of propaganda with regard to unemployment which, according to official figures, had diminished from about 8% to less than 3%. This was just one more lie. Political hiring and payment of activists and political favors with public resources were labeled as lower unemployment by the Marxist demagogy.

The best proof of this is that, since 1972, there is a definite general decline in productivity per worker. The magnitude of this phenomenon is easy to appreciate from a study of Table N.º 7. In practically all of the directly productive sectors, productivity per worker diminished. For 1973 the situation is still more serious.

This state of affairs cannot go on. No country can progress if the production per worker is declining. To increase employment under these conditions is only a means of cheating the laborers themselves, since this position cannot long be maintained. “Eat, drink and be merry, for tomorrow we die.”

The only way to guarantee a sure and stable source of work for all is to begin a rapid process of economic growth. And this is exactly what we are trying to do.

Table N.º 7

Gross Domestic Product, Employment and Productivity by Sectors of Economic Activity 1970-1973

GDP in millions of 1970 escudos.

Employment in thousands of persons.

Productivity in escudos per person employed.

	1970	1971	1972	1973	% Growth 71-70	% Growth 72-71	% Growth 73-72
Goods Sector ¹ GDP...	45,667	49,803	49,606	45,607	+ 9.1	- 0.4	- 8.1
Employment	1,577.6	1,651.6	1,668.7	1,690.0	+ 4.7	+ 1.0	+ 1.3
Productivity	28,947	30,154	29,727	26,986	+ 4.2	- 1.4	- 9.1
Services Sector ² GDP.	43,254	46,657	48,343	47,062	+ 7.9	+ 3.6	- 2.6
Employment	1,416.6	1,485.5	1,511.0	1,525.3	+ 4.9	+ 1.7	+ 0.9
Productivity	30,534	31,408	31,994	30,854	+ 2.8	+ 1.9	- 3.6
TOTAL GDP	88,921	96,301	97,649	92,669	+ 8.3	+ 1.4	- 5.1
Employment	2,994.2	3,137.1	3,180.3	3,215.3	+ 4.8	+ 1.4	+ 1.1
Productivity	29,698	30,697	30,704	28,821	+ 3.4	0	- 6.1

1. Includes: Agriculture, Mining, Industry and Construction.

2. Includes: Utilities, Transportation, Commerce and Services in general.

Sources: Figures for the 1970 and 1971 product are based on official Planning Office estimates.

Figures for 1972 and 1973, estimates of the Economics Department, University of Chile, Western Division.

Figures on employment, estimates of the Economics Department, University of Chile.

Prices

Another serious problem we have to face is the sharp inflation, to which we must add an irrational price structure which has contributed to the formation of a black market and which in the past allowed unscrupulous individuals of all social classes to gain from the products of the Social Area, food, and other essential articles. Worse yet, the state companies and parasite organizations at the service of the former regime hoarded many basic articles and thereby worsened the already existing scarcity and contributed to the anxiety of thousands and thousands of Chileans. Proof of this is in the numerous caches of supplies found by the Armed Forces since September 11.

The price structure and the value of the dollar must be corrected in order to organize the production process, to eliminate the deficits in the social area, to promote exports, to reactivate agriculture and, in general reorganize the economic system.

So that you can form some idea of the terrible distortions existing in the economy, I would like to point out some examples.

The president of the Communist Party, Mr. Corvalán, at a Plenary session of his party dedicated to agriculture, commented that, because of the distortion of prices at that time, it was more profitable for farmers to use their wheat for raising pigs or their milk for fattening calves instead of leaving them for human consumption.

There are many similar cases in other activities. In construction, for example, a bag of cement at the official price cost less than the sand, so it was more profitable to use exaggerated amounts of cement in the building of a house. In this way basic materials were wasted. Cement became scarce and prevented the construction of a greater number of houses.

Another significant distortion was in the value of the dollar which had been established at an artificially low price. In this way, a shirt cost US\$60, if you take the lowest exchange rate, while it cost US\$1 at the black market price of the dollar. The distortion is obvious if you consider that the real price of a shirt fluctuated between 6 and 8 dollars in the international market. This phenomenon created the conditions which permitted unscrupulous people to engage in contraband, smuggling essential goods such as food, medicine and spare parts to export in bordering countries.

Unfortunately, because of the demagogical practices of the former Government, these situations were not corrected and the problem persisted and has become worse in the last few months. All this favored the black market and helped speculators. It affected production by causing the elimination of products which could not finance production costs and in other cases was an important cause of deficit in enterprises of the State and Social Area.

Even these extreme distortions have not been sufficient to put a brake on inflation. The economic chaos is so great, the increases in money so exaggerated and the decline in production so pronounced that, the process of inflation has exceeded all previous levels and in spite of controls and of deceptions, the official rate of inflation which we inherited from the former regime exceeds 320%. The Popular Unity Government was aware of all of this. I have confidential documents here from the Central Bank which admit to inflationary pressures in the order of 500% for the end of 1973 and in which mention is made of monthly rates of inflation of 20% for the fourth quarter of this year, which would imply inflation of over 1,000% in 1974 if this rate were to be maintained.

In these same documents the need was established to increase prices in the social area in order to avoid even greater financial imbalance. For political reasons these raises were not approved, creating an untenable financial situation which must be corrected immediately.

The inflationary pressures which we have denounced are entirely the responsibility of the Marxist Government and we want all Chileans to know that, because of a huge deficit in the fiscal sector and the social area, together with the irresponsible increases in money on the part of the Central Bank, we are faced with a dramatic situation in which there is no alternative.

It is my duty to inform you that it is impossible in the present circumstances to detain the process of inflation immediately. The economic reorganization which we have undertaken requires the correction of the distortions in the price system so that during the period of economic adjustment it will be technically impossible to restrain inflation. However, once this adjustment has been accomplished and the present chaos has been overcome, we shall have eradicated the fundamental causes of economic imbalance and in 1974 we shall see a definite decline in the inflationary spiral.

The facts that I have exposed to the country speak for themselves. They

fully justify the emergency measures which I announced at the beginning of this speech.

Compatriots:

This report would be incomplete without a reference to the legitimate conquests made for the workers and to the problem of income distribution.

The main concern of this Government is not so much a wage and salary policy as the formulation of an income policy which guarantees new and permanent conditions for the workers. Among these, mechanisms will be studied which make it possible for workers to have access to the means of production and thereby guarantee better income distribution. The policies of income redistribution by means of wage readjustment in practice in the past, have proved inefficient and have finally become incorporated into the economy as a constant inflationary pressure, which in the long run does not alter existing distribution significantly and only improves it temporarily, converting the hopes of the workers into mere illusions. On the other hand, a policy designed to broaden the base of ownership in the productive sectors will not only incorporate the workers into real and effective participation, but will also guarantee permanence to the redistribution process which the Government will promote.

There are in this country groups of citizens who live in conditions of dire poverty. We want to eradicate misery from our country for ever. To this end we think it is indispensable to initiate specific, definitive actions to improve the conditions of life of the marginal sectors. These objectives will only be attained if direct steps are taken, such as assigning definitive housing to those who live in the camps on the outskirts of our cities.

We must likewise broaden access to education, especially technical training, and guarantee the development of opportunities for permanent employment.

It is, therefore, necessary to achieve accelerated economic growth. To this end we shall put special emphasis on agriculture. The Government has already announced its intention to grant land ownership to the workers in the reformed sector and we are sure that this measure, together with and adequate policy on technical assistance and prices, will bring about a real "revolution in agriculture." Once more Chilean fields will be provid-

ing generous harvests, thus eliminating the dangerous dependence on other countries for food.

Mining must recover its dynamic role in foreign trade. Once the work has been reorganized, production levels will rise in a short time to the production goals established in the plans for development begun over six years ago. Copper will again become the basic lever for economic development and the new policies on the exchange rate and technological reorganization will allow for the generation of excess to finance productive investments in other sectors of the economy. Chile's resources shall be properly spent; we shall invest them carefully in works conducive to national progress.

Industry shall play a new role in Chilean economy; it will be the basis of our policy of diversification of exports. We expect the sort of boldness, efficiency and tenacity on the part of businessmen and workers alike that is implied in the challenge of foreign competition and the opening of new horizons in national development.

We shall promote Latin American integration and the Andean Pact as efficacious mechanisms in the process of broadening our economic horizons, which will permit us to participate rapidly in the advance of modern science and technology.

Fellow, citizens, only a few days ago the Armed Forces had to take charge of the management of public affairs. This was not our desire, but in doing so, we understood that it was the best way in which to serve Chile. This is our one true objective.

We wish to open new paths to internal peace, prosperity and true solidarity within the Chilean family. In the midst of the economic chaos which we inherited, we have to design a short-term plan of action. When this difficult phase is over, we shall continue to clarify the permanent development policies which the country so urgently needs. We cannot work miracles and we want everyone to understand that only by means of a great effort, great patriotism and enormous tenacity will we be able to move forward. Three years of demolition require many years of effort.

We have great hope in the future and we have great hope in our people. It is in difficult moments that a Nation proves its worth, and this nation has proven, on numerous occasions, that it is capable of incredible feats. I am sure that this generation will write a brilliant page in the history of Chile and that the reconstruction of our Country will be crowned with success.

**Three Years to End Protection:
New Tariff Schedule Under Study**

Vice-Admiral
Lorenzo Gotuzzo Borlando
Minister of Finance

January 7, 1974

The following is an official statement of Minister of Finance, Vice-Admiral Lorenzo Gotuzzo, to disclose the government decision to end indiscriminate protection by means of customs duties, and to modify substantially the tariff policy in order to improve efficiency in the Chilean productive system and to make it compete internationally within three years.

The following is the text of the official statement of Minister of Finance, Vice-Admiral Gotuzzo:

In accordance with the Government view on matters of economic policy, we will continue to inform the public with regard to those aspects of this policy which we consider should be clearly understood in advance. On previous occasions, we have said that the foreign trade policy which the Government proposes to follow includes a thorough revision of the current tariff structure. Furthermore, we have insisted that the new economic system being put into practice, including the free-price policy, would have no meaning and could be tremendously unfair if it were not accompanied by an adequate tariff policy. This is the subject that we wish to discuss on this occasion and to which we attach the greatest importance.

It seems suitable to begin with a brief commentary on the effects of the tariff policy which has been in practice in this country practically since the 1940's. This policy originated in part as a means of satisfying the legitimate aspirations to promote industrialization by means of protection for locally manufactured goods which until then had been imported. However, various factors contributed to an accumulation of errors in the structure of the tariff system, so that it has become one of the most distorted elements in the nation's economy. Just as an example, the following are some of the principal consequences of this policy:

- 1) The tariff structure has been a significant cause of the deterioration experienced in key sectors of the economy. As a matter of fact, the very high degree of protection granted and maintained indefinitely for the greater part of the Chilean industrial sector has had the effect of discouraging development in other sectors, particularly agriculture and mining. This means, in general terms, that the scarce resources of the country have not been adequately exploited, for while some goods were produced in an extremely inefficient way, others have not been manufactured and the country was not in a condition to produce them at all.
- 2) On the other hand, within the industrial sector itself, there are many cases in which an erroneous policy has been followed for the purpose of

diminishing the importation of certain products considered as luxury items by means of high customs duties, without realizing that the effect of such a policy would be rather an incentive to produce these same items locally. A quick review of the present structure of Chilean manufacturing will bear out what we are saying.

3) Another result of this policy has been that the high degree of protection some activities enjoy has permitted the creation and subsistence of national and foreign monopolies that produce locally at a cost several times that of the international market. This causes a chain reaction, as some companies, which are in fact efficient, suffer from apparent inefficiency because they are obliged to buy locally produced material at high cost and, at the same time, must sell their products at higher prices. From this point of view, the erroneous policy of import substitution has resulted in a clear disadvantage for the local consumer.

4) Finally, the current structure of customs duties has also been the cause of stagnation and limited diversification of our exports. Based on an erroneous concept of "saving foreign currency," the tendency has been to produce locally goods which perhaps we should not have produced. At the same time, motivation was lacking for the production of other goods with which we are in a condition to compete in the international market, and which, of course, provide better possibilities than those of the limited home market. In this way, the tariff policy has put a brake on the growth of the industrial sector, since the production of goods that have no growth potential other than the home market has been artificially stimulated.

These brief reflections give us an idea of the importance for the Government to undertake a solution to this problem with realistic criteria. Basically, the problem is to make more efficient use of our scarce economic resources, which would mean a substantial increase in the availability of goods and services for all Chileans as well as the attainment of an accelerated rate of economic development. Naturally, the tariff policy which shall be put in practice is an integral part of any set of economic policies and shall be especially related to the exchange rate policy which has already been adopted.

Based on these ideas, we wish to present a succinct report on the objectives and the criteria which shall be applied in the new tariff policy:

1) The tariff structure that is being established shall be determined basically according to the degree of protection which it is deemed appropriate to

grant to the home productive sector. This means that customs duties shall not be used for purposes other than the ones stated, such as, for example, to restrict imports which are considered unnecessary, to obtain higher revenues, or to solve momentary balance-of-payment problems. For these purposes other instruments of the economic policy shall be used, such as taxes on the consumption of luxury items, or the exchange rate policy in order to maintain stability in the balance of payments. This also means that in the future other restrictions that have been in effect until now in Chilean foreign trade and that have greatly influenced the degree of protection afforded to local production shall be avoided. We refer specifically to import quotas, prohibitions, discriminatory prior deposits, etc. Finally, so that the tariff fulfills its fundamental objective to the utmost, it must be applied to all imports. The policy in this respect shall be that every importation will be subject to the corresponding duty, regardless of whether it pertains to the public or private sector. Besides this, the Government shall conduct a thorough analysis of all the existing special schedules and, as a general norm, shall tend to eliminate the discriminations which have their origins in duty exemptions.

2) The protection that the new tariff structure shall give to the various productive sectors may not exceed the reasonable limits compatible with the goals of efficiency established for the nation's economy. This system will produce substantial reductions in tariffs together with the corresponding adjustments in the exchange rate, so that they become a powerful incentive for all of those activities that have been traditionally unprotected and in which the country may be equipped to compete in the world market. In this way, the new policy will bring about some significant adjustments in the domestic production structure.

Some companies, for example, especially in the industrial sector, should already be studying the transformation of their production lines if they do not consider themselves capable of making drastic reductions in the cost of some products which they manufacture at this time. In this respect, it must be thoroughly understood that Chilean industrial development shall not be based on the maintenance of the production of goods with a value added in the internal manufacturing process that exceeds two, three or more times the same value added measured by international prices. But at the same time, it should be emphasized that this tariff policy will permit an accelerated expansion in other companies, lines of production and/or sectors of activity which shall yield high incomes when they are able to acquire materials at lower cost and when they can count on relatively better prices for their products.

On the other hand, we also wish to point out two additional aspects related to the effects of this policy. The Government expects the tariff reform to be in effect within a period of no more than three years. Therefore, it is basic to keep in mind that the transformation of productive activity which shall begin to take place immediately shall produce significant benefits for workers in general, as more jobs will be created in the expanding sector than those which could disappear in some sectors that report high inefficiency. The second aspect that must be emphasized refers to the close interdependence which exists between this tariff policy and the free price policy the Government has already put in practice. High customs duties favor the existence of inefficient monopolies which are incompatible with the free competition which should characterize a market-oriented economy. On the other hand, reduced tariffs will oblige local monopolies to face international competition, with the obvious advantage to the Chilean consumer.

3) Finally, with respect to the criteria for the guidelines of the tariff policy, it should be recalled that our country is a member of both the Latin American Free Trade Association (LAFTA) and the Andean Pact. Therefore, certain international commitments have been made which, of course, will influence the definitive structure of Chilean tariffs. Actually, the time is approaching when it will be necessary to establish a single tariff schedule in several Latin American countries, including our own. In this respect, it should be kept in mind that Chile has lost nearly three years in the process of adapting the economy to the new conditions of competition which are developing. One of the primary objectives of the tariff policy to be implemented will therefore be to put pressure on the most inefficient sectors of the economy so that they proceed rapidly to transform their production. In this way Chile will be in a position to insist on her points of view in the formation and negotiation of policies in common with other Latin American countries.

In conclusion, we wish to announce some of the measures the Government has assigned for immediate action. As we have already stated, the new tariff structure is expected to be fully in effect within three years. However, we consider it appropriate to adopt as of now, certain measures that imply the initial correction of some of the most obvious distortions in the existing tariff structure. These measures are as follows:

a) All ad-valorem tariff duties above 220% shall be reduced immediately to 200%.

b) The ad-valorem tariff duties between 50% and 220% shall be reduced, as a general norm, by 10% of the present value, subject to the following restrictions:

- 1) The ad-valorem tariff duties scale shall contain only those tariffs which are multiples of 5%, so that all tariff duties shall be rounded off to the nearest multiple of 5%.
- 2) If the resulting ad-valorem tariff duty is lower than the Minimum Common External Tariff, the latter will be imposed.

c) The existing prohibitions on the import of certain types of goods shall remain in effect temporarily. However, as a general norm, these prohibitions shall be lifted when their purpose is to restrict local consumption of the respective products, and they shall be replaced by adjusted tributary mechanisms that tax consumption without discriminating between the local or foreign origin of these products.

d) The public or mixed enterprises shall receive the same treatment in these matters as enterprises of the private sector. Likewise, as a general norm, the Government shall order that no new petitions for tariff duty exemptions shall be filed for specific import operations.

e) Within a short time specific duties shall be replaced by ad-valorem tariff duties and shall be adjusted to the new levels. Certain specific tariffs shall be maintained only in cases of absolute necessity.

f) The revision of the values shall be encouraged and supported according to the norms established by the Brussels Appraisal Committee in a coordinated effort on the part of the Central Bank and the Customs Office. This revision shall be extended to include the quality of the merchandise to be imported.

g) Finally, the Government declares that the study of a complete reform of the tariff schedule requires the collaboration of various groups within the productive sector. For this reason, the Commission in charge of this project will contact the different organizations of the private sector which could make suggestions and provide information that is indispensable for the proper preparation of a new tariff structure.



the 1970 rate by 1973. This limited economic growth and the creation of new sources of work.*

All of the production indices showed a sharp drop. Overall production in the agricultural sector declined more than 23% between the 1970/71 and 1972/73 agricultural years. In mining, production had dropped almost 20% as compared to 1970 and in industry, more than 10%. In construction, the index declined nearly 40% and thus, while in the 1960/70 decade the country constructed an average of 35,600 habitational units per year, during the Popular Unity regime the average dropped to 19,000 per year. The decline in production is synthesized in the reduction of income per capita which is estimated at approximately 6% for 1973.*

The situation of the foreign sector was very serious. The successive heavy deficits in the Balance of Payments descended to totally unacceptable limits, requiring increasing foreign debt in order to meet the minimum necessities of imports of food and raw materials, many of which had traditionally been produced within the country. The foreign trade situation became critical as a result of the decline in internal production and a discriminatory and absolutely unrealistic exchange rate policy. The net foreign debt which was US\$2,668 million in 1970, rose to US\$3,729 million in 1973. In a period of three years, the country acquired a debt of US\$1,060 million. On the other hand, the balance of freely usable foreign currency, which in October of 1970 reached US\$331 million, by the end of September of 1973 was only US\$37 million. That is to say, that part of the price of the experience we went through that can easily be measured, was the financial deterioration of an average of over one million dollars per day. Even more serious is the fact that the additional indebtedness was spent almost entirely on current consumption.

Economic and Financial Policy of the Last Twelve Months

At the beginning of this Administration it was necessary to apply drastic corrective measures in order to detain the process of chaos in the economy and to create conditions adequate for the long term measures which were to be adopted later on. These measures have been oriented toward the normalization of productive activities, the reallocation of resources to more productive activities, the deceleration of the rate of inflation and the creation of conditions for future growth.

*Source: Planning Office.

**Report on the State of
Public Finance**

Jorge Cauas Lama
Minister of Finance

October, 1974



Introduction

It is my duty as Minister of Finance to report on the present state of Public Finances and on the economic and financial situation of the country, as well as to present, in the name of the Government, the short and medium run economic programs which we propose to carry out as part of the commitment to the country. In this report emphasis will be given to the financial aspects, pointing out their relation to the Government's economic and social policies. This document should serve as the working basis for the Technical Commissions which will analyze the budget draft for 1975.

Historical Review

Before analyzing the economic policy applied by the government, as well as the results obtained and prospects for the future, we think it necessary to synthesize briefly the magnitude of the economic crisis which the country faced in September of 1973.

At the beginning of 1973, the early symptoms of hyperinflation were already obvious. Even though the Consumer Price Index was manipulated so as to dissimulate inflation, prices had begun to increase faster than money. The discrepancy between these two indices increased, so that toward the end of 1973 an inflationary explosion that would have put an end to money as a means of exchange would have become inevitable. The excessive supply of money was generated in Central Bank money creation intended to finance the growing fiscal deficit and the tremendous losses in the enterprises of the public area. These inflationary pressures, which had already become untenable, were generated in a controlled-price economy, so that the citizenry not only had to face rising prices, but also had to bear a generalized lack of supplies, characterized by the proliferation of black markets and corruption. Social discontent was manifested in strikes and a rhythm of work that was far below normal.

The erroneous economic policy of the Popular Unity Government was reflected in the negative effects manifested in practically every sector of the economy.

By October of 1973, purchasing power of workers' wages, before the bonuses were applied, had fallen to a level equivalent to 52% of what it was in 1970.

Beginning in 1971, total gross investment fell to approximately 12% below

the 1970 rate by 1973. This limited economic growth and the creation of new sources of work.*

All of the production indices showed a sharp drop. Overall production in the agricultural sector declined more than 23% between the 1970/71 and 1972/73 agricultural years. In mining, production had dropped almost 20% as compared to 1970 and in industry, more than 10%. In construction, the index declined nearly 40% and thus, while in the 1960/70 decade the country constructed an average of 35,600 habitational units per year, during the Popular Unity regime the average dropped to 19,000 per year. The decline in production is synthesized in the reduction of income per capita which is estimated at approximately 6% for 1973.*

The situation of the foreign sector was very serious. The successive heavy deficits in the Balance of Payments descended to totally unacceptable limits, requiring increasing foreign debt in order to meet the minimum necessities of imports of food and raw materials, many of which had traditionally been produced within the country. The foreign trade situation became critical as a result of the decline in internal production and a discriminatory and absolutely unrealistic exchange rate policy. The net foreign debt which was US\$2,668 million in 1970, rose to US\$3,729 million in 1973. In a period of three years, the country acquired a debt of US\$1,060 million. On the other hand, the balance of freely usable foreign currency, which in October of 1970 reached US\$331 million, by the end of September of 1973 was only US\$37 million. That is to say, that part of the price of the experience we went through that can easily be measured, was the financial deterioration of an average of over one million dollars per day. Even more serious is the fact that the additional indebtedness was spent almost entirely on current consumption.

Economic and Financial Policy of the Last Twelve Months

At the beginning of this Administration it was necessary to apply drastic corrective measures in order to detain the process of chaos in the economy and to create conditions adequate for the long term measures which were to be adopted later on. These measures have been oriented toward the normalization of productive activities, the reallocation of resources to more productive activities, the deceleration of the rate of inflation and the creation of conditions for future growth.

*Source: Planning Office.

Outline of the short run economic program

Foreign Trade

a) Exchange Rate Policy

One of the first corrective measures adopted consisted in a drastic devaluation of the exchange rate. The inadequate valuation of the exchange rate had very serious effects on the balance of payments and on the allocation of resources. At the same time, the structure was simplified, reducing the multiple exchange rate to only two: one for export-import operations and one for tourism and invisible trade.

The policy of periodic and moderate devaluations has been reinstated to avoid the deterioration of the real exchange rate when modifications occur in the relations between internal and external prices. This will encourage exports and will automatically regulate the demand for imports so that within a reasonable period of time, we may achieve equilibrium in the balance of payments.

b) Commercial Policy

A policy has been defined to prepare national producers gradually to face international competition in order to guarantee a substantial improvement in efficiency in internal production and at the same time to develop more sectors in which our country has natural advantage in foreign competition. For these purposes, a total reform of customs duties has been announced and a generalized reduction in tariffs has been undertaken. This has permitted to a certain degree the reduction of the excessive protection enjoyed by certain domestic activities.

The principle measures adopted in this field have been the following:

— Freedom of imports: the automatic exemption from a deposit of 10,000% on an increasing number of items has been authorized. At the present time the vast majority of products on the permitted import list enjoy this exemption with the exception of markedly luxurious items and of a group of agricultural items which may only be imported by the State. Although this policy is not yet the ideal one, it represents a significant advance in relation to the previous one (it

should be recalled that there were over 2,000 items subject to the 10,000% and from which the Central Bank had the power to exempt at its discretion). The Government intends to continue with the liberalization policy and to approach as much as possible a regime in which the regulation of imports becomes automatic, using the tools of exchange, tariff, fiscal and monetary policies.

— Tariff Reductions: in 1974 the first tariff reductions were put in force. The highest tariff at the present time is 140% and the Government has already made known its decision to continue to lower gradually the taxes on imports so that in 1977 no tariff will exceed 60%. In this way, the tariff policy to be followed in the future has been clearly defined. Home industry may now make the necessary adjustments and be prepared to face foreign competition.

c) Foreign financing

It is impossible for the corrective measures adopted to produce immediate and sufficient results. This means that a series of measures have been taken to obtain the foreign financial resources required for the adjustment period. In this sense, there has been favorable response in international financial circles. With respect to this matter, the following considerations should be pointed out:

— A Credit Agreement has been worked out with the International Monetary Fund to obtain assistance with the balance of payments.

— Considerable resources have been obtained or are in the process of being obtained in the form of development loans from important financial agencies such as the World Bank and the Inter-American Development Bank.

— An agreement has been reached with the creditors in the Paris Club to renegotiate the service on the foreign debt for 1973 and 1974. The general terms of the agreement are as follows: 20% is to be paid in the first three years (5% in 1974, 5% in 1975 and 10% in 1976) and the remaining 80% will be paid in 14 semi-annual installments beginning in 1977; the rate of interest will be according to bi-lateral agreement and is estimated at about 6% per annum.

— It should be noted that special care has been taken to obtain a debt structure which is compatible with the payment capacity of this country in the coming years and that the new indebtedness should basically be for the purpose of improving the country's productive capacity.

d) Other measures

— The time period for forward sale of foreign currency in the Central Bank has been reduced from 150 to 120 days.

— The banking market has begun to issue payment certificates which permit the importer who acquires them to establish the exchange rate ahead of time.

— The tariffs on imports of capital goods paid in cash until December 31 of this year have been reduced to 10%.

— Commercial Banks are authorized to carry out certain operations in the brokers' markets, such as purchase of medicines, subscriptions to magazines, purchase of books not for commercial use, etc., without previously consulting the Central Bank.

— Service to foreign banks on financial debts pending until December 31, 1973, has been normalized.

— Measures have been adopted to permit the acquisition of foreign currency from other sources. Between November of 1973 and July of 1974, private individuals have liquidated approximately US\$110 million in foreign currency in the Central Bank. Likewise, the clearance of foreign currency according to D.L. N.º 110 has produced US\$45 million in additional income.*

Monetary and Credit Policies

The purpose of the monetary policy has been to reduce the excessive supply of money in the economy, so that the rate of monetary expansion will be compatible with the goals of the stabilization program. For this purpose, measures have been taken to reduce the fiscal deficit, to control the expansion of deposits in the banking system, and to permit the self-financing of enterprises which belong to the so-called social area. In spite of the efforts made, the rate of increase in money continued high in relation to the initial goals of the stabilization program. In part, the extraordinary improvement in the balance of payments situation, explained mainly by the high price of copper in the first few months of the year, contributed to this expansion. However, there are some favorable facts: during the first semester of this year, money creation increased less than in the same period of the previous year; likewise the quarterly evolution of

* Source: Central Bank of Chile.

this indicator shows a decreasing rate of expansion. On the other hand, while in the first five months of this year, was increasing at a rate of 400% per annum, it has been reduced to a rate of nearly 290% during the last few months.

Table N.º 1

MONEY (M₁)

**Rate of Increase in 12 months
1970 - 1974
(in percentages)**

MONTHS	1970	1971	1972	1973	1974
January	37,9	71,0	108,2	169,1	402,3
February	37,6	80,4	98,6	180,6	399,8
March	44,4	84,9	88,2	193,2	398,8
April	45,3	100,2	75,9	200,7	398,5
May	45,8	97,6	84,8	225,1	395,1
June	46,5	99,3	85,0	258,7	333,4
July	52,6	105,6	77,6	313,5	277,9
August	58,9	103,5	78,9	341,5	288,6
September	64,9	102,6	81,2	354,7	289,9
October	67,1	105,8	99,0	348,0	
Novembér	63,5	119,2	128,3	348,1	
December	66,2	113,4	151,8	362,9	

Source: Central Bank of Chile.

Among the measures adopted in this period with regard to monetary policy, an important one is the reform of the legal reserve requirement established by the Executive Committee of the Central Bank at Session N.º 70 (2438) on September 27, 1974.

This reform should be interpreted as an additional manifestation of the efforts of the economic authorities to extend to the financial sector the re-

organization process which we have been applying to the economy in general. In more specific terms, this reform substitutes a direct quantitative control on the monthly expansion of credit in each bank by a legal reserve mechanism which tends to stimulate competition among the banks and permits them to exercise more freely their faculties as institutions in the capital market. The new system permits each bank to expand freely the value of loans in accordance with its own availability of resources and the new legal reserve requirement rates. The expansion of total credit in the banking system will be controlled through the legal reserve rates—which shall be uniform throughout the system—established within the context of the monetary program, so that the expansion of the credit of each bank considered separately will be the result of free competition within the banking sector itself.

The credit policy has been readjusted to the new economic situation in which the market must carry out the basic role in the orientation of productive resources. Thus a great number of selective credits characterized by direct controls on the clients by means of the various institutions which controlled the destination and the use of the credit extended have been eliminated. The few remaining special credits still in force have been formulated so as to diminish all forms of direct control and bureaucratic handling.

In order to permit the rate of interest to fulfill its role of channeling credit resources toward the most productive activities, it must reach positive values in real terms. This principle has been applied, modifying the rate of interest in light of the inflation hypothesis with which we have been working. Besides this, a set of interest rates which vary according to the time limit of the loan and the method of charging interest, has been established. This has provided a uniform cost for short term bank credit, which is presently at 20%.

Financial Market

Studies and projects have been made this year for the purpose of creating the legal framework required for the organization and the functioning of an efficient capital market. The first steps toward this end were taken with the approval of Decree Law N.º 455 on interest, readjustments and taxes on loans. This has permitted the charging of real positive rates of interest and has established as a general norm, the readjustability of loans for over one year. It is also important to point out that in a few days, a Decree Law will be promulgated

which will dictate the norms that facilitate the merger and the regionalization of commercial banks and that, at the same time, modify certain norms related to the Development Banks in order to facilitate the initiation of their operations. On the other hand, the Government has worked out a decree law project to transfer the property of banks which had been taken over by the State during the Popular Unity Government to the private sector. The project contemplates norms to prevent restricted groups of persons from controlling the property of these banks. This measure fully coincides with the Government policy which refers to the sphere of activity of the State.

The development of the capital market has special importance in increasing the rate of saving and channeling these funds toward more profitable activities. This is achieved through financial intermediaries by means of a process which should be flexible, dynamic and with a minimum operational cost. The necessity to increase substantially the rate of internal savings and to guarantee the best use of investment resources are indispensable requirements for the acceleration of economic growth. For this reason special emphasis has been placed on the development of the capital market.

Price and Income Policies

The generalized control of prices had created two very serious problems. On the one hand, fixing the maximum prices far below the real costs, as we pointed out at the beginning of this report, had created a generalized lack of supply which was reflected in the proliferation of black markets, in lines, and in the creation of various rationing mechanisms. On the other hand, the controls had created a totally arbitrary price structure which had extremely negative results on the correct allocation of resources. The strategy used to correct these disequilibria consisted in creating a free price system. Controls were maintained only in the case of some products essential for consumption and for those produced in monopoly sectors. This measure permitted the markets to normalize rapidly. Wages had fallen sharply in real terms as a result of the acceleration of the inflationary spiral. In order to palliate the deterioration of remunerations, the new Government established a bonus system for the public and private sectors for the last quarter of 1973. This consisted in the payment of two bonuses, each equivalent to the income for the month of April, 1973, and of one bonus for a maximum of E.^o10,000. The family allowance was fixed in all cases at E.^o900 per dependent

and a transportation allowance of E.°720 was also established. Besides this, no worker could receive less than E.°36,000 during the quarter, including the usual remunerations and the bonuses.

In 1974 the purpose of wage policy has been to maintain the 1973 average purchasing power. To achieve this, the following measures have been applied:

— In January, mechanisms which meant a readjustment in remunerations for the public and private sectors equal to approximately five times those of January, 1973. The minimum income for workers in the private sector was established at E.°18,000, not counting benefits.

— In February, the lowest income sector received an advance as a compensation for family expenses. The amount of the advance was determined according to the number of dependents and the amount of the remunerations.

— As of May 1, a readjustment was authorized for the remunerations and allowances of active and passive workers in the public and private sectors. The readjustment was 30%, with a minimum of E.°9,000 for the public sector and E.°11,000 for the private sector. The allowances for transportation, lunch and dependents were also readjusted. At the same time, seniority allowance of 1.5% for every two years of service in Public Administration and a special allowance for professional titles.

— In June a E.°10,000 bonus was granted to workers in the public sector as an advance of future readjustment.

— As of July 1, a general readjustment of 20%, with a minimum of E.°10,000, was authorized. The Minimum wage was adjusted at E.°35,000 in the public sector and E.°39,000 in the private sector. At the same time, the family and lunch allowances were also readjusted.

— Finally, in October the readjustment policy to be followed in the future was clearly defined, as published in Decree Law N.° 670. This decree establishes that the remunerations for October shall be readjusted 24% (which corresponds to the rise in the CPI for the months of July and August) and that the remunerations for December shall be readjusted according to the rise in the CPI in September and

October. The same automatic readjustment system will be applied in the months of March, June, September and December of 1975.

As can be seen from the preceding account, the Government has been trying to avoid large fluctuations in real remunerations and to protect the purchasing power of the lowest income groups, by means of periodic readjustments, important increases in the family allowances, proportionately higher readjustments in the minimum wage and the authorization of special monetary compensations each time there is an increase in the prices of basic consumer products.

Description of Principle Measures Adopted in the Fiscal Sector

When the new administration took charge, the fiscal situation was untenable. Income in real terms showed a tendency to decline, the product of the profound distortions in all levels of the economy. Actually, the transactions carried out in the black market as well as the profits made remained outside of the sphere of the tax system. The pressures of expenditure had accumulated for the month of October, since the readjustment in wages derived from the high rate of inflation which had occurred between May and September was due to be paid then. This meant that in September the projected fiscal deficit for 1973 was over 50% of the total expenditure. The corrective measures adopted by the new Government permitted an extraordinary increase in revenues during the first quarter of the year, bringing the deficit to only 35% of expenditure. The fiscal situation had become so grave that current income was insufficient even to finance current expenditure, which meant that a significant portion of these expenses and all capital expenditure were financed by loans from the Central Bank, that is, by money creation. As for the composition of expenditure, investment had been reduced to 23% of the total. To this must be added the extensive extra-budgetary financing granted to cover deficits in The Agricultural Trading Corporation (ECA), The Development Corporation (CORFO) and the enterprises in the Social Area, which amounted to E.^o142,000 million, or 61% of budget spending, bringing the fiscal deficit to 55% of total expenditure.

The seriousness of the situation obliged the new authorities to take immediate measures in order to lessen the magnitude of the deficit, to increase revenues, and to reduce the rate of expansion of outlays.

Fiscal Budget for 1974

The Fiscal Budget for this year established a deficit estimated at 21% of total expenditure. The notable decline in the deficit is explained principally by a strong increase in revenues and in non tax income which grow at a much higher rate than that of expenditure. The higher income from revenues is the result of the freedom of prices granted for the great majority of goods and services whose transactions are subject to the sales tax, to the various norms formulated to correct taxes and to the recovery of economic activity. The basic orientation of the 1974 budget correspond to the basic economic policies of the Government. These policies reserve for the State a supportive and organizational role with regard to the activities in which the private sector is engaged, and concentrates the direct action of the State on the implementation of social development programs. In this way, the Fiscal budget was oriented toward financing public works and housing in order to recover the levels of investment and to improve employment, on the one hand, and on the other, provided for strong growth in social development programs, by financing more outlays in health and education. We think it is important to point out that approximately 34% of Fiscal Spending in 1974 corresponds to investment. The three main objectives of the Budget were the reduction of the rate of inflation, improved efficiency in the use of resources in order to contribute to economic growth and a redistribution of income and a fairer tax system.

Measures Related to Reduction in Public Spending

— The elimination of subsidies: by allowing prices to adjust freely, it was possible to eliminate a large number of subsidies which had become an excessively heavy burden for the Government. Because of the need to guarantee a minimum level of consumption, it was not possible to eliminate them all at once. We have been eliminating them gradually throughout the year, while at the same time direct monetary compensations have been authorized to families in the low income sector.

— The reduction of the number of functionaries who work in the Public Sector: Articles N.º 24 of Decree Law N.º 534 disposes a 20% reduction of the personnel hired before September 30, 1973 in all of the Services, enterprises and institutions subject to articles 1 and 2 of Decree with Force of Law N.º 249. This disposition does not apply

to the Judicial System, the Comptroller General's Office, teaching personnel dependent on the Ministry of Education, personnel subject to Law N.º 15,076 (doctors, dentists and pharmacologists) and other professionals and technicians expressly mentioned in article 22 of D.L. N.º 534.

The personnel subject to reduction on September 30, 1973, included 235,972 persons, implying a reduction of 47,198 functionaries. By the end of May of this year the reduction of personnel had affected 16,012 persons, the additional reduction between that time and December of 1975 will affect 31,186 persons. Any personnel who withdraw before December 31, 1975 may enroll in the "Small Businessman" Program. The main purpose of this program is to provide these people with a substitute source of income, thereby facilitating the process of reduction and reorganization of the administration of the State. It will also stimulate the development of private initiative, and encourage small and medium size businesses. For this purpose, the State will assign up to US\$100 million in foreign currency which may be invested to import capital goods and equipment. Credit and special terms will also be extended through the banking system for the acquisition of the vehicles, machinery and other fiscal goods which will have to be sold as a result of the reduction in public spending.

— To decrease the number of official vehicles, which not only eliminates a spending factor, but also produces additional funds.

— To dictate norms for the elimination of spending on non-essential items.

— The sale of enterprises belonging to the State and that are administered by CORFO: This permits the reduction of expenditure and provides a source of greater income.

Tax Measures

The main purpose of the intensive work in this field has been to reorganize the administration of taxes and of the tax system in general. Part of this effort has been directed principally to reorganize and to regulate the chaotic situation in which this Government found the Government finances and the abnormal tax situation of the majority of tax payers. The formulation of these norms permitted the timely fulfillment and correction of various tax obligations. Special time periods and conditions for this purpose were authorized.

At the same time, more profound changes were also made in the tax system itself. These changes were the result of various studies, subsequently promulgated as Decree Laws, for the purpose of correcting certain defects in the legislation in force and to prepare the system for future reforms. In general, these measures have tended to simplify the system, to coordinate the rates and to eliminate exemptions.

Remunerations in the Public Sector

The Uniform Wage Scale has basically two objectives:

- a) To eliminate the differences in remunerations of personnel who have the same position, office or profession in the various institutions in the Public Sector.
- b) To define clearly and explicitly the relation that should exist between remunerations for the different positions or grades in the Civil Service.

The process of reorganizing the remuneration system of the Civil Service will continue throughout the next year in a study to identify the positions, which will facilitate the initiation of training courses in Civil Service.

Administration and Financial Control

The reform of the Financial Administration of the State required several measures to solve problems which had existed for many years, and which bureaucratized the overall conduct of finance. Significant progress has been made in rationalizing the systems of budget administration, government accounting, supply, and public credit. During 1974, a series of projects have been executed to reorganize the management of finance in the Public Sector. The Municipalities have been incorporated in the financial regime of the Fiscal Sector, Extrabudgetary Accounts and income for special purposes which posed obstacles for the efficient central management of State finances have been eliminated. The banking system is now in use as a method of collecting public income to facilitate the fulfillment of the obligations of those indebted to the State. The budget formula has been simplified, reducing the number of programs and eliminating or combining some items in the Classification of Expenditure. With regard to public credit, the existing internal

debt of the Public Sector was consolidated, and a series of studies and practical measures have been undertaken to reorganize the administration and the accounting of external debt.

These measures constitute the principal achievements in the process of reorganization of the Administration of Finance, carried out in 1974. They are the result of a coordinated action in the Office of the Comptroller General and the Ministry of Finance.

Emission of Treasury Bonds

The issuing of these securities permits the Government to resort to an alternative source of finance and provides the State with an additional tool for managing fiscal policy. The total emission of bonds programmed for this year is E.°60,000 million. At the same time, these operations have given an initial impulse to the development of the capital market, stimulating the activity of financial intermediaries.

Reform of Benefits

The Ministry of Labor has continued with studies of the modification of the Social Security System. The basic objective of this reform is to reduce the costs and to improve the efficiency of the system in order to motivate the hiring of more workers.

The present method of financing indemnization for years of service and retirement pensions will be replaced by a program of capitalization under the control of labor. These funds will eventually constitute a significant portion of national savings and the investment of these funds in economic development will produce a substantial change in the distribution of goods, with the resulting redistribution of wealth and of income.

Evaluation of Results

Economic Activity

There has been a notable increase in economic activity comprising nearly all areas of production. The estimated growth in the Gross National Product for this year is 5%. The growth by sectors is most significant in the fields of mining and agriculture. Present estimates of growth in these areas are of 16.5% in mining and 17% in agricul-

ture. Progress in mining has been achieved thanks to an increase in productivity in labor and the stimulation felt in this sector because of the application of a realistic exchange rate. The notable recovery in agriculture is the result of a return to normal in productive activities and a new price policy that improves the conditions of exchange for agricultural products in relation to those of other sectors. Another sector that has shown notable improvement is construction, with an estimated growth rate for this year of 10%.* The industrial sector shows more modest improvements: according to the National Bureau of Statistics index, there has been a 1.9% reduction for January-July of 1974, as compared to the same period of 1973. According to the National Manufacturers' Association (SOFOFA), production has increased 4.2% in that period. Both indices show similar behavior in the evolution of production by groups for the same period: heavy increases in the production of intermediate goods and construction materials, significant growth in the production of foods and durable goods, and a decline in the production of other consumer goods. It is estimated that production in the industrial sector will increase 2% during 1974.* Various problems have prevented a more rapid recovery in industrial production. Among them we must point out the initial lack of supply of raw materials, the need to renew equipment and the loss of a significant percentage of working capital.

The difficult employment situation is basically the result of two phenomena. On the one hand, during the previous regime many workers were hired in the Public Sector and in the Social Area enterprises. Since production did not increase, the productivity of these workers was extremely low and, therefore, represented disguised unemployment, which is now openly apparent. If the level of productivity corresponding to the year 1970 had been maintained in 1973, the rate of unemployment implied in the level of production for 1973 would equal 15% of the labor force.

On the other hand, the lack of investment during the last three years prevented the creation of new sources of work. The rate of unemployment in August of 1974 was 8.7% according to the National Bureau of Statistics, and 9.4% according to the last survey made in September, 1974, by the University of Chile. As a means of palliating in part the negative effects of this situation, the Government has improved the unemployment subsidy system.

(*) Source: Planning Office.

Table N.º 2
Rates of Unemployment in Greater Santiago
(In percents)

YEAR		Source: University of Chile	Source: National Bureau of Statistics	
1970	March	6,8%	January-August	3,9%
	June	7,0%	September-December	4,3%
	September	6,4%		
	December	8,3		
	Average	7,1	Average	4,0
1971	March	8,2	January-June	5,2
	June	5,2	July-December	3,3
	September	4,8		
	December	3,8		
	Average	5,5	Average	4,3
1972	March	4,8	January-August	3,2
	June	3,7	September-December	*
	September	3,0		
	December	3,6		
	Average	3,8		
1973			January	*
	March	3,8	February-April	5,5
	June	3,1	May-July	4,2
	September	*	August-September	4,1
	December	7,0	October-December	5,5
1974	March	9,2	January-March	6,6
	June	10,3	April	*
	September	9,4	May-July	8,2
			August-September	8,4

NOTE:

* No information available for this period. Beginning in February of 1973, the quarterly survey carried out by the National Bureau of Statistics in Greater Santiago has been divided in three panel-type subsamples, each of which is made monthly, in order to obtain the information more quickly. The figures that appear in this table are the averages of the sub-sample for each quarter.

Foreign Trade

In foreign trade there has been a notable recovery. Freely disposable foreign currency of the Central Bank showed a balance of US\$387 million at the end of September of this year, as compared to US\$37 million on the same date of last year. To a great extent, the improvement in the Balance of Payments situation is a result of the increase in copper exports. The increase in the production of copper is no less significant than the increase in price. It is therefore safe to estimate that the production of the Large Copper Mines will increase by approximately 100,000 metric tons as compared to 1973. On the other hand, the success of the exchange rate policy is reflected in the extraordinary increase in non traditional exports. As compared to 1973, the exports of industrial products increased from US\$111 million to US\$253 million and agricultural and seafood products from US\$24.3 million to US\$48 million.

The recovery in internal productive activities has brought about significant increases in imports of inputs (from US\$1.047 million) and of capital (US\$285 to US\$400 million). The increased internal agricultural production has permitted a reduction in the import of food from US\$595 million to US\$480 million. The significant incidence of the rise in the price of petroleum in the international market is reflected in the increase in the value of imports of fuel and lubricants which rose from US\$120 million in 1973, to US\$410 million for this year.

Table N.º 3

Remainder Balance of Payments - International Reserves Foreign Debt 1970 - 1974⁵
(Millions of Dollars)

	1970	1971	1972	1973	1974
Overall Balance of Payments Result	98,5	-309,0	-323,2	-253,2	-197,7
Net Intern. Res. ¹⁻⁴	343,2	34,2	-442,6	-724,9	-512,0 ²
Foreign Debt ⁴	2.668,2	2.696,7	3.337,8	3.728,8	4.000,0 ³

¹Includes Renegotiation of Foreign Debt.

²Information at 7/31/74.

³Preliminary estimate 1974.

⁴Net Balance at December.

⁵These figures have since been revised. The final figures appear in the appendix.

As a result of these developments, the Balance of Payments deficit is estimated at approximately US\$200 million for 1974.

Prices and Income

Even though the rate of inflation is still high, the results obtained so far permit the forecast of a substantial decline in inflation in 1974 as compared to the previous year. Indeed, if we analyze the 12 month variation in the CPI, we will observe a growing rate of inflation beginning in October of 1971, that continued throughout 1972 and 1973. Beginning in May of this year, the figures show a decreasing rate of inflation, reflecting the first beneficial results of the measures taken to control inflation. It is important to point out that the rises in prices of several items which previously had been subsidized had a strong influence on the rise in the Consumer Price Index. The elimination of these subsidies constitutes an important advance in the anti-inflation policy since they permit a reduction in the fiscal deficit financed by emissions from the Central Bank, and thereby eliminates a permanent source of inflationary pressures in the future. However, the rises in the prices of imported products, especially of wheat and petroleum, have had an unfavorable effect on the evolution of the Consumer Price Index.

As we had pointed out before, the Government policy on wages has tended to maintain the real average level of wages for 1973. At the same time, the Government has been particularly concerned about the low income sectors, as can be seen from the significant readjustments in the family allowances, and in the issuing of bonuses, which has resulted in a readjustment of the minimum wages that is far superior to the general average. If we analyze the income of a civil service employee with three dependents who receives the minimum wage, we observe that his real income has increased 57% between September of 1973 and September of 1974. Likewise, his real average income during the first nine months of this year exceeds his real income of September of last year by 44%.

Meaning of the Economic Policy

It does not seem necessary to insist here on the priority the Government gives to the anti-inflationary policy within the context of the general economic policy. It is sufficient to point out that it is impossible, for example, to obtain and to maintain an acceptable redistribution of income without attaining a minimum degree of stability. However, we believe it appropriate

Table N° 4
Real Index of Minimum Income
September 73 - September 74

	Minimum Income 1	Index of Minimum Income Sept. 73 _ 100	Consumer Price Index Sept. 73 _ 100	Index of Real Minimum Income Sept. 73 _ 100
September 1973	7,290	100.0	100.0	100.0
January 1974	25,320	347.3	237.0	146.5
February	32,900	451.3	295.0	153.0
March	32,900	451.3	336.9	134.0
April	32,900	451.3	388.4	116.2
May	47,200	647.5	422.2	153.4
June	57,200	784.6	510.1	153.8
July	61,240	840.1	568.7	147.7
August	61,240	840.1	630.7	133.2
September	81,240	1,114.4	711.4	156.6
Average September 1974				143.8

¹For September, 1973, the minimum wage was considered as two base salary units readjusted 60.8% (advance readjustments for April of 1973), plus the equivalent of three dependents. For 1974, the minimum income includes: minimum wage for civil service employees, three dependents, lunch and transportation allowances, other authorized allocations.

to clarify the meaning of the policy which we have been applying during the last year. The first decision in the anti-inflationary policy consisted in adopting a gradualist point of view instead of one of violent containment. In order to understand the reasons for such a choice, it is necessary to recall that the immediate origin of our high rate of inflation stems from the high rate of monetary expansion which was fed to a large extent by a permanent fiscal deficit. To detain inflation suddenly would imply the immediate elimination of the fiscal deficit, and the reduction of credit to the Private Sector, or the generation of an unrestrained deficit in the balance of payments in order to absorb the money in circulation. A simple analysis of these measures gives us an idea of the catastrophic consequences this type of policy would have. The elimination of the deficit is practically impossible to carry out by creating new taxes because the

average tax burden is already too high. This means that there must be a violent reduction in current as well as capital public spending. In practice, this means unemployment for hundreds of thousands of civil service employees, not initiating new public investment projects and paralyzing those already begun. This would undoubtedly have repercussions in the Private Sector as it would affect an important source of demand for their products, with the resultant decline in activity and the use of fewer resources. To this we must add the direct impact on employment and production of a drastic reduction in credit to the Private Sector.

As an alternative to generating a deficit in the balance of payments, so as to absorb the excess money in circulation, there would necessarily be heavy foreign debt and a sudden and immediate liberation of imports. The consequences of this policy would be disastrous for future growth, unless we could live forever on charity.

To summarize, the social cost, in terms of loss of production, employment and income from an economic policy such as we mentioned, would be very high and we are sure that the majority of Chilean would not be willing to accept it.

Having rejected the sudden detention of inflation as an alternative, we have chosen the gradual process. This means that the same problems mentioned previously as the causes of inflation will be dealt with, but instead of eliminating these sources of inflation all at once, it will be done over a more prolonged period of time, which could be two or three years. The goal is still to arrive at a reasonable rate of inflation, but over a longer period.

Once the gradual point of view has been chosen, it is necessary to accept the implications of this policy. One of the serious problems that accompanies every inflationary process, is that not all of the prices are adjusted at the same speed. While this is going on, distortions occur in the relative prices of products and of factors that have harmful effects on the efficient allocation of productive resources and on the distribution of income. Let us consider some examples:

— If the prices of consumer goods rise more rapidly than wages, the real income (or purchasing power) of workers diminishes.

— If the rate of interest remains fixed while the prices of all products rise, credit is extremely cheap, everyone will try to use it and few will want to

lend, creating unbearable pressure for more bank credit. If the exchange rate remains fixed while all other prices rise, the purchase of imported products will be encouraged and incentive to export will decrease, generating in the short term a crisis in the balance of payments.

A particularly inappropriate tool for restraining inflation or for avoiding the distortions in relative prices that accompany every inflationary process is massive price controls. As long as the inflationary pressures generated by fiscal deficit and excessive monetary expansion are not eliminated, it is impossible to prevent price levels from increasing. Price fixing only produces greater distortions in relative prices, creating additional problems of supply, lines, black markets, in other words, results which all Chileans already know too well.

In order to avoid the damaging effects already mentioned, the prices which the Government still controls, such as the exchange rate, the interest rate, an important part of wages, and some products, such as wheat, petroleum, etc., should be periodically readjusted. It is inevitable that this should occur, and it is preferable that the readjustments be frequent and moderate.

Not to readjust these prices would be to close our eyes to reality and to create even more serious problems. In the case of certain products, the problem is aggravated by increases in international prices. Take petroleum as an example. The country imports nearly 70% of the total it consumes. The price in the international market has risen and so the cost of importing it rises, obliging the Government to readjust the internal price. The deficit generated in this way must be financed. Since the possibilities of higher taxes are exhausted, we would have to resort to printing money, which in turn would cause the prices of other products to rise. We could also establish a special exchange rate for petroleum imports. The results would be the same: the Central Bank would collect less local currency for the dollars it sells to import petroleum, creating inflationary pressures in all the markets.

To summarize, a gradual policy necessarily implies that, during the period of adjustment and while the reduction of the inflationary process generated by high deficit and excessive emission is in progress, prices will continue to rise.

The prices of products that are not controlled will also rise. However, neither all of the increases nor their amounts are justified. On this point it

would be well to emphasize the importance of businessmen's expectations with respect to inflation. It is common to observe significant increases in the prices of products that have obvious problems in sales. Even though above normal stocks of some products are accumulating, there are substantial readjustments in the prices. The arguments used to justify these increases are that, according to the projections for the exchange rate and remunerations, replacement costs have increased and therefore, the sale price of the articles has to be adjusted. In part, the problems of a decline in sales and accumulation of stocks arise because the Government economic policy is aimed at a rate of inflation which is lower than that expected by businessmen. The financial problems which this situation creates for the companies produces pressures to increase credit and money. In other words, businessmen expect the Government to validate these exaggerated increases through monetary policy.

We wish to be emphatic in pointing out that this will not occur. The policy will be maintained, and businessmen will have to adjust to it. There is no doubt that the adjustment will be much easier if businessmen adapt their expectations and their conduct to the Government economic policy. A significant part of the recession that accompanies the periods of reduction in the rates of inflation could be avoided.

We think this explanation is very important because we hope to have convinced the workers, businessmen and the public in general, that the cause of inflation is not in the readjustments of the exchange rate, nor in the readjustments of wages, nor in the readjustments in the prices of bread or of gasoline. The causes of inflation are excessive increases in the fiscal deficit and in money. Therefore, the adoption of policies such as the periodic readjustment of the exchange rate and the periodic and automatic readjustment of wages do not mean that the stabilization policy is being abandoned or that the Government shows weakness in its attack on inflation. On the contrary, these measures are necessary to make the inflation adjustment period easier, and to avoid distortions in the relative prices that we mentioned earlier. The discipline and the conduct of the Government should be analyzed in the area of fiscal and monetary management, since they are the factors that will determine the future course of inflation. However, it is fundamental that businessmen adapt their expectations rapidly to a decreasing rhythm of inflation if we are to avoid the problems of reduction in the levels of activity and unemployment.

The policy adopted by the Government consists then in a gradual reduction in the fiscal deficit and in the excessive monetary expansion. The fig-

ures given previously show the degree of progress attained and are a sign that the path chosen is the correct one. This policy embraces nearly every area of the economy: specialization and efficiency, as well as rapid economic growth are basic goals toward which the policies on exchange, on tariffs and on taxes are aimed. A necessary change is being brought about in the economy, opening to the exterior, in order to make use of our comparative advantages and to base our future growth on an efficient and competitive production structure.

In the short term, this implies favoring sectors that are traditionally unprotected, such as agriculture, mining and in general activities with export potential. It also signifies a decline in sectors which had traditionally been protected. It does not mean that we are against industrialization, but rather that we are against indiscriminate industrialization at any cost. We are in favor of gradually adapting our industry to a more specialized and more efficient structure.

We could not end this explanation of the meaning of the policy without pointing out that the confidence of the people in the Government and in its conduct of economic affairs is vital for the success of any economic policy. Undoubtedly it is that confidence in the Government which has permitted the most spectacular advances in the normalization of productive work and in the increase of productivity and efficiency.

Economic Program for 1975

General Objectives

Economic activity and allocation of resources.

The program contemplates a growth in the GNP in the order of 6%. The recovery of the levels of investment as well as the new foreign investments will permit a reduction in unemployment. The goal for growth will require a significant effort to save internally since a level of investment of approximately 18% of the GNP is expected. The accelerated development of our economy depends basically on internal effort. However, foreign investment undoubtedly constitutes an indispensable contribution toward reaching our goal. For this reason, the Foreign Investment Statutes were promulgated, which while safeguarding national interests, also establish the basic rights and the duties of investors who wish to bring money into Chile.

Distribution of Income

Besides wage policy, emphasis will be given to a policy to improve equal opportunity and to grant access to education and health to the low income sectors. At the same time, social development programs, such as child nutrition and the construction of low-cost housing will continue to receive support. The studies of poverty will permit us to design more efficient mechanisms for direct assistance for the poorest sectors.

Stabilization

Emphasis will be given to the gradual reduction of inflation based on the reduction of the fiscal deficit and of the rate of expansion in the media of payments. In this regard, it is possible to predict substantial progress since the drastic price adjustments which used to be subsidized and which have had a great deal of influence on inflation this year will not influence the evolution of prices.

Prospects for 1975

The prospects for exports, and especially from the point of view of the internal productive effort are quite favorable. We expect improved participation of non traditional exports, especially those products which come from the forestry sector. However, the fall in the price of copper will affect the entry of foreign currency in 1975.

As for imports, a considerable reduction in imports in food products is expected, especially wheat, corn and sugar, because of satisfactory levels of national production.

A deficit in the Current Account for 1975 is expected because of the high prices of some raw materials and fuel, and of the lower price of copper. If we add to this the service on the foreign debt, a deficit can also be expected in the balance of payment. This analysis demonstrates the need to renegotiate the payments of the foreign debt for next year, so that the balance of payment situation does not constitute an obstacle for the achievement of the goals for economic growth.

Monetary and Credit Policies

The monetary policy that we have been applying recognizes that

there is a close relation between the rhythm of growth in the level of prices and the rate of expansion of the money supply. Thus recognition is not based on the unconditional acceptance of a theory or school of economic thought, but rather grows directly out of observation of the dramatic Chilean experience with inflation. We are also aware that there is a definite relation between the growth of the supply of money and the level of employment that can be attained in the economy in the very short run. To combine these two central ideas, we must reiterate that the Central Bank policy will be oriented to an energetic control of the rhythm of growth in the money wage compatible with the minimum possible cost relative to levels of employment. The high degree of sensitivity of the money supply to the variations in the fiscal deficit necessarily imply that the success of this policy is intimately bound to the maintenance of solid discipline in fiscal matters.

The Financial Market

Decree Law N.º 455, which establishes new regulations for the interest rates, permits establishment of readjustability for more than one year and gives greater flexibility to credit operations, constituted the first step toward the creation of a modern and efficient capital market.

In this way, financial activity has entered a new phase. However, the totality of the legal system which governs this area is still insufficient for the degree of development that is required in the financial sector and also lacks certain important elements which will have to be corrected. During this year, a great deal of work has been done to analyze the role to be played in the future by each one of the financial institutions, as well as to determine any deficiency in the existing legislation. This study and analysis are the basis of a proposed law on the financial credit institutions which defines the legal and institutional framework for the entire sector and that at the present time is under discussion by Government authorities. These reforms are expected to go into operation in the course of next year.

Income and Prices

Wage policy for next year has been clearly defined. The quarterly readjustment for amounts equivalent to the inflation for the two previous months will permit a gradual increase in workers' pur-

chasing power. Indeed, as the rate of inflation decreases, the average real value of wages will increase. The use of indirect subsidies will be avoided as much as possible, as this is an inefficient and not very equitable means of income redistribution. As has been pointed out on other occasions, the basic income redistribution mechanisms which the Government will use will be the tax system, especially indirect taxes, direct transfers to the lowest income groups and social programs, such as education, health and housing.

Measures in the Fiscal Sector

Reduction of the Public Sector

The fiscal budget for next year contemplates a deficit that will not be superior to 15% of expenditure. This reduction in the percent of deficit is basic for the success of the stabilization program. In order to guarantee the attainment of this goal, special emphasis will be put on reduction of the level of spending in the public sectors. Present estimates indicate that fiscal expenditure compatible with this program cannot differ in nominal terms from approximately double that of the previous period. The reason for using the control of spending as a means of reducing the deficit is based on the need to restrict the direct economic activity of the State. The level of activity and the degree of direct intervention by the public sector at this time is incompatible with the efficient functioning of a decentralized economy. The excessive participation of the State is clearly demonstrated if we notice that, in spite of all efforts to reduce it this year, it is estimated that Fiscal Expenditure alone will reach approximately 32% of the 1974 Gross National Product. In the present framework of economic policy, the State formulates general plans and establishes policy, restricting direct action to a limited number of strategic activities and to the implementation of social programs. As a result, it is absolutely necessary to reaffirm the policy to reduce the size of the public sector. In order to do this, the public sector will have to dissociate itself from activities that are not proper to it.

Policy on taxes and exemptions

Beginning next year, new dispositions on taxes and exemptions will be in force. The tax reform will affect direct and indirect taxes as well as the reorganization and the modification of the laws on regional and sectorial development.

Table N.º 5
Expenditure, Income and Fiscal Deficit as
a Percent of Outlay of Gross National Product¹

	1970	1971	1972	1973	1974
Total Expenditure ²	23.9	29.9	28.8	34.5	31.7
— Current Expenditure	16.0	20.8	22.1	27.7	19.6
— Capital Expenditure	5.8	6.6	5.6	5.6	9.1
— Service On Public Debt	2.1	2.5	1.0	1.2	3.0
Total Receipts	20.8	19.4	16.9	15.5	24.9
— Taxes ³	19.7	18.4	15.8	14.0	23.6
— Other	1.1	1.0	1.1	1.5	1.3
Deficit	3.1	10.5	11.9	19.0	6.8

¹These figures have since been revised. The final figures appear in the appendix.

²Corresponds to expenditures in Fiscal Budget in local and foreign currencies. For 1973 extrabudgetary expenditures are included.

³Includes taxes on Large Mining Companies.

NOTES:

- The figures for Expenditure of Gross National Product for 1973 and 1974 are preliminary estimates of the Planning Office. The percents in the table could undergo substantial changes when the final figures are known.
- In the 71-73 period a very high percent of Fiscal Expenditure was extrabudgetary (financing the loss in enterprises of the State and of the Social Area). For this reason the percents of Expenditure and Deficit relative to the Product for those years are not comparable to those of 1974 in which the total of Fiscal Spending was channeled through the Budget. For 1973, for which the extrabudgetary figures are available, they have been included within the expenditure in the previous table.

a) Direct Taxes. The existing distortions in the general regime of the law on Income will be eliminated and a greater number of tax-payers will be included in the general system, thereby diminishing the present coverage of special regimes. There will be a grouping of incomes in a single base to which the Work Tax or the General Complementary Tax or the Additional Tax will be applied, according to the respective categories. The definition of the tax base will avoid problems of double or triple taxation and will permit the preservation of a progressive system, by means of the grouping of real as well as imputed income.

The Government proposes the modification of article 35 of the Income Law, so that enterprises are taxed on their real profits, which must be reflected in their financial statements. This implies a correction of the tax base, in which the companies will not pay for two nominal increases in capital which are the equivalent of a devaluation in money for the period.

b) Indirect Taxes. The present sales tax basically concentrates the tax in the production stage. One disadvantage to this system consists in the difficulty and arbitrariness in the definition of the subject of the tax, since many times it is difficult to determine exactly the final use of an item in the manufacturing process. Besides this, the great variety of exemptions prevent organized management of the system and create distortions which prevent sound competition. To these problems we must also add the difficulty in harmonizing the present sales tax with the tariff policy and the new export policy. Even though the tax rate is the same for a domestic product as for its imported equivalent, when there is a different number of transactions in the processing of both articles, the result will be a different tax for each. In practice this means the operation of a tariff structure other than the one established. On the other hand, the present system does not permit organized calculation and a sound draw-back policy, which would require subsidizing imports in the amount equivalent to the total of indirect taxes on the final export item. From all of these arguments is born the need to construct a new indirect tax system. The value added tax, essential for the indirect taxation to be implemented in 1975, will be the tool which leads to coordination and harmony of the tax system with the other tools of economic policy announced in other areas. This tax system will not permit exemptions based on the legal conformation of the producing units or of con-

sumers, nor will there be exemptions based on the geographical location of the taxpayers.

c) Laws of Development by Region and by Sector

In the past, the tax exemptions have been used for the most varied reasons, and have created an enormous amount of legislation which was difficult to implement and which led to complete disorder in the tax system. On the one hand, the allocation of the country's scarce resources had been altered to such an extent that there was no longer any guarantee that the productive resources were being used for the benefit of the country. On the other hand, the varied range of exemptions has created a tax structure that puts the burden on a few who do not enjoy preferential treatment, and whose real taxes have been increased constantly, in order to maintain fiscal receipts at a minimum level required for the normal development of State activity. All this has seriously limited the possibility of using the tax policy, one of the most powerful tools for the country's social and economic development. It can be said without exaggeration that, today the general tax regime is the exception and the exceptions in the tax regime make up the general rule. The Government has, therefore, decided to modify the present exemption regime, repealing some that are unjustified, and to modify others for the purpose of adjusting them to the context of the present economic policy.

The new policy on development law will be based on the following principles:

- The regional development laws shall be applied without exception to all the activities of the region.
- The exemptions by sector shall be applied without exception within the respective sector, and shall therefore be independent of the region in which they take place.
- The programs and incentives for the various sectors are under the direct control of the Government. Therefore, the regions will have no jurisdiction over the use of taxes to promote programs within the sectors other than those established by the Government.

— The structure and the level of the exemptions will not continue indefinitely.

— No principles other than those mentioned here will be binding in tax matters as related to development laws. This means that no exemption shall be authorized and any exemption that implies a direct reduction in the various income taxes shall be eliminated.

— All discretion and all arbitrary decisions shall be eliminated from the administrative handling of these laws. In this way, only the forces of the market and the orientation on the part of the Government will determine the allocation of resources in the country.

Public Enterprises

The immense amount of resources handled by enterprises in the public sector requires measures that guarantee the efficient use of these resources. The only way to evaluate this efficiency is to end discriminatory treatment which favors different aspects and in that way force a development similar to that of the enterprises in the private sector. This implies that these companies will not enjoy special tariff or tax exemptions and that they will have to pay the cost of capital they receive, and they will have to make the corresponding depreciation charges. They will be established according to international standards and so as not to reward inefficiency. If these companies are unable to finance themselves, the losses must appear as subsidies.

Public Investment Policy

The magnitude of the effort involved and its importance for national economic development, in view of the limited capacity to mobilize the country's resources, makes it indispensable that investment on the part of the State be carried out in the most efficient way possible, and for clearly defined purposes and priorities. The objectives, priorities and restrictions applicable to public investment can be summarized as follows:

a) Level of Investment and Stabilization

Restriction in public spending is a key factor in containing the

inflationary spiral. In these conditions, the scarce resources available should be administered in the most efficient way possible and should be directed toward those investment projects which appear to be the most profitable and most urgent.

- b) Employment. The Government is especially interested in the creation of new sources of work. As a result, one of the main objectives of public investment is the direct and indirect generation of new jobs that are truly productive.
- c) Redistribution. On various occasions we have said that one of the essential objectives of this Government is to achieve a more fair distribution of income, to establish equality of opportunity and to eradicate extreme poverty permanently. Priority should be given to carefully selected projects in education, health and housing and to efforts in the fields of housing and collective transportation.
- d) Increasing the efficiency of the productive system
Inefficiency in the allocation of resources and in the evolution of the productive structure have been prevalent for over thirty years in this country. For the first time a serious effort is being made to open the country to the outside and to permit the development of those activities in which comparative advantage exists or could be developed. This will oblige us to become accustomed to an effective market regime and to open foreign competition.

In these conditions, special care should be taken not to support projects in which the cost of generating a unit of foreign currency would be superior to the social cost. Public investment should preferably be concentrated in those activities which permit the use of the basic infrastructure in order to favor rapid adaptation of the productive structure and of those sectors that generate additional foreign currency at low cost.

- e) Investments initiated. There are still some projects already in progress and for which it seems that the need will inevitably arise for investing further funds. If these projects had been thoroughly analyzed from the beginning, the decision would be clear. However, if there is any doubt about whether the additional resources required were excessive, they should be thoroughly studied to determine whether the project should be continued or suspended.
- f) Regional Development. The Government has given a great deal of

importance to regional development. This means that the various possibilities of location should be taken into consideration when decisions are made with respect to investment. The allocation of investment resources should be in keeping with well balanced development, due consideration being given to the geographical distribution of natural resources and the topographical and climatic difficulties of the different regions.

Financing of Universities

The financing of the universities has become a very heavy burden for the State. For this reason, studies have been undertaken to impose concrete measures for the purpose of reducing fiscal spending in higher education on the one hand, and to improve the use of the resources assigned to Education in general, from the point of view of efficiency as well as of distribution of income. A proposal for the solution of the problem is being studied. Meanwhile certain criteria have been established to plan the financing of higher education in 1975. They are as follows:

- In 1975, the government contribution to the current budget of the universities within the total spending on education, cannot exceed the percent historically considered as normal.
- The distribution among the Universities of the government contribution that results from the application of the preceding criterion shall correspond to the historical distribution.
- The capital budget shall be discussed separately and it shall be considered as a project.
- The State will study the means to guarantee loans for tuition and board for those students who require it. In this way, all who meet the admission requirements will be guaranteed access to the university regardless of the economic situation of their families.
- If as a result of the application of these norms, one or any of the universities deem it necessary to obtain additional financing by means of raising the tuition, they may do so without affecting the possibilities of all qualified students to enter.

Administration and Financial Control

The organization and efficiency of the financial process in the public

sector will find its fundamental expression in the law on the financial administration of the State. This brings together in one single text a large number of provisions which at the present time either do not exist or are found dispersed throughout various legal documents, to give a sense of unity and coherence to the functioning of State financial administration.

The law under analysis tends toward the formulation of a basic legal framework, structuring the bases of the financial administration system and creating the links which should make it compatible with and bind it to the central program of objectives for general reform in the public sector being carried out by the National Commission for Administrative Reform.

Once the law on financial administration has been formally sanctioned, it shall be implemented, creating and/or correcting the instruments necessary for the practical application of the general precepts.

Beginning in 1975, the following measures will be in force, in the spirit of the law:

- The broadening of the fiscal budget, in terms of structuring a single budget for the public sector.
- Financing of a fund for regional development and a fund for municipal financing, changing the traditional allocation of resources which was based exclusively on distribution by sector.
- A system for controlling investment at the project level, in order to achieve a clear perspective of the development of investment in the public sector.
- Uniform accounting systems and administrative control mechanisms will be applied.

Final Comments

At the end of this exposition, it would be wise to reiterate the fact that the Government is giving high priority to the anti-inflation policy. It is not an exaggeration to point out that the success of the entire economic policy of this Government is conditional to the advances achieved in the accomplishment of the goals of stabilization. The year 1974 will end with a

rate of inflation which although high, signifies an extraordinary reduction with respect to the level reached the previous year.

However, we have very good reasons to believe that in 1975 the results of the anti-inflationary policy will be even more encouraging. The first of these reasons is the enormous confidence in the Government and management of the economic policy. This confidence is backed by the great progress in the reorganization process and by the increased efficiency in the economic system. This is a fundamental factor, since the dynamics of inflation are such that, the success of the economic authorities in reducing the rhythm of inflation depends to a great extent on the public's expectations with respect to the future course of prices.

In the second place, the year 1975 will not only begin with a rate of inflation substantially lower than that of 1974, but the significant distortions in prices will have been eliminated. We must recall once more that the elimination of subsidies for certain products had a significant influence on the rises in prices during 1974. This phenomenon will not be repeated in 1975.

On the other hand, it is not too bold to assert that our economy has already absorbed the greater part of the enormous variations in prices of certain products observed at the beginning of 1974 in the world markets.

The progress in the stabilization program will be subject then to the degree of discipline we can maintain in fiscal and monetary matters.

**The Role of Tax Policy in
National Economic Development**

Jorge Cauas Lama
Minister of Finance

November, 1974

Introduction

It is an honor for me to inaugurate these sessions on the analysis of the Tax Reform, a significant occasion for the Ministry under my direction, given the importance of this subject for the country.

There is no doubt that the implementation of the regulations contained in the tax reform project is not only a milestone in the application of Government policy in order to correct the economic situation, but also a decisive step in the attainment of increased and sustained development. The Government has decided to disclose the entire project, and to stimulate serious discussion of the various topics involved, so as to allow all sectors to participate in the common task of searching for the optimum economic policies which will provide justice and well-being for all of the inhabitants of this nation without exception.

Beginning next year, new provisions will go into effect with regard to taxation and to tax exemption laws. The tax reform will affect direct and indirect taxation as well as the reorganization and modification of regional and sectorial development laws.

With regard to direct taxes, the existing distortions in the general tax regime of the income law will be eliminated and the tendency will be to incorporate the maximum number of taxpayers into the general system, thereby diminishing the scope of the system of the substitute regimes. There will be a single base for a grouping of income to which the Single Wage Tax, or the Global Complementary or the Additional tax will be applied, according to the respective categories.* The definition of the tax base will avoid the problem of double or triple taxation and will permit preservation of the progressiveness of the system by means of income regrouping, both real as well as presumed.

The Government proposes the modification of article 35 of the Income Law, so that enterprises will be taxed on the basis of real profits as reflected by their financial statements. This implies a correction of the tax base according to which the companies will not pay for the nominal increases in their capital that are the equivalent of the devaluation of currency during the period.

From the study of a series of arguments which we will analyze further on, we deduce the urgent need to construct a new indirect tax system. The value added tax, the essence of indirect taxation to be implemented in

*Today there is only one scale for all categories.

1975, will be the tool for coordinating the taxation system with the other tools of the economic policy which have been disclosed for the different areas. The purpose of this tax system is to improve the organization of the indirect tax system in order to eliminate present distortions that encumber sound competition and, therefore, exemptions based on the legal conformation of productive or consumer entities, or the geographical location of the taxpayers will no longer be permitted.

The third area of reform deals with the regional and sectorial development laws.

Perhaps, this is one of the fields which requires the greatest speed in the action of corrective policies. In the past, tax exemptions have been used for the most varied reasons thereby generating cumbersome legislation which is difficult to implement and which has led to complete anarchy in matters of taxation. All this has seriously limited the possibility of using the tax policy as one of the most powerful tools in the economic and social development of the country. We can say without exaggerating that today the general tax regime is the exception, and that the exception regimes constitute the general rule. For this reason the Government has decided to modify the present exemption regimes, eliminating unjustified exemptions and modifying others, within the context of the economic policy.

Finally, we have also worked on a series of administrative aspects, which although secondary, are essential for the success of the implementation and the operation of the new regulations, to permit greater efficiency and agility in the public institutions charged with the correct functioning of the tax system, especially in the Internal Revenue Service and the Treasury Department.

As can be seen, the field of action of the reform will be nearly total, consisting of a harmonious set of modifications, rather than simply partial changes. Thus, it is wise to examine briefly the general principles which every tax system should have, in order to obtain a normative pattern with which to compare the diagnosis of the present system with the goals established for the total reform. This exercise will also serve to clarify the essential contents of the new modifications proposed.

The Basic Elements of a Tax System

In general, the tax system acts on four main levels: equity, allocation of resources, growth and stability. Naturally, the effects in all these areas are

simultaneous and interrelated, but without disregarding this, they also have characteristics proper to each one.

Equity in the Tax System

Perhaps the best way to characterize an optimum tax system is to say that it should be fair, simple and efficient. Fair, in that it should be as equitable as possible, simple, in that it should not hamper initiative in productive and social activity; efficient, in that it should encourage the maximum use of productive resources in the way which is most conducive to the well-being of the population. In any case, the maxim begins with the equity aspect.

This is so because taxation is the corner stone of any system designed to achieve greater economic justice. It is the basic mechanism for attaining equal opportunities required for the inhabitants of a country. This role of the taxation policy is exclusively and unavoidably the duty of the State, and should, therefore, become the guarantee of the common good. The norm for economic justice is not founded on a vacuum or on ambiguity, but rather is firmly based on what are known as the vertical and horizontal equity principles.

By vertical equity we understand the attainment of optimum distribution of income and of wealth in the fairest way possible, and consequently, the need for equitable allocation of charges and obligations. Normally this principle is founded on the principle that each taxpayer contribute according to his economic capacity. This capacity is measured in terms of the distribution of income and wealth of the various inhabitants of the country.

On this level, the tax system exercises the redistribution function, a role which must be more or less accentuated, depending on the initial distributive state in society, on the level of economic development the society attains, and on the productive function which the various economic agents in the nation fulfill. In any case, it can be stated that the work of redistribution always exists and will exist, in all countries and for all time. What changes are its rhythm and its character.

Some aspects which automatically arise from the preceding analysis, reside in the fact that on the one hand, income taxation should be an essential pillar of any tax system, that it should be very broad in its general regime, and should be as progressive as the task of redistribution requires. It is impossible to affirm whether a tax system is just, if it contemplates a

series of different subdivided tax bases, with the proliferation of substitutive regimes, since the progressive aspect of the system as well as the equity, will be uncertain.

On the contrary, the ideal is that the system concentrate on a single general regime, centered on the basis of a precise well defined scheme of direct taxes on personal income.

The former considerations are also quite valid with respect to the horizontal equity principle, that is, the equal treatment for equals. The idea is that different persons, groups or sectors which are in equivalent positions, should be subject to similar tax regulations. Whether their income is similar, or the productive activity is the same, it is only just that they receive equal treatment with respect to taxation, bearing similar burdens, or having similar obligations. The essential is to avoid arbitrary discriminations, such as unjustified exemptions, thus seeking to level the taxes for groups with equal paying capacity.

The ideal tax system, from the point of view of equity would consist of a single progressive tax scheme, with a broad homogeneous base which would include each and every one of the increases in income of private individuals, practically without distinguishing the treatment of the various causes or sources of these increases. The main issue is the net total, effect that the taxes produce at the income or paying capacity level of the inhabitants of the country. Therefore, the final result will be better known and better defined when the various tax systems can be grouped in a common pattern. It is an extremely complex and difficult task to construct a fair tax system on the basis of the addition and imposition of partial and limited taxes. Often the result is a series of ambiguous effects, which frequently violate both the gradual or progressive principle as well as horizontal equity. For this reason, within the limitations which every empirical situation introduces and according to what can feasibly be implemented, we have tried to guide the reform toward a grouping of income on a single base, to which either the Single Work Tax or the Global Complementary, or Additional will be applied. We think that this is the only practical way to approach the ideal proposed.

To close this section, it is well to emphasize once again the importance of justice within a tax system. We should remember that the quality of a social system is not measured only by its economic efficiency, but also basically, by the pattern of social efficiency, the norm on which true national equity among all inhabitants is based.

An Efficient Tax System

As the tax system constitutes a means of orienting the allocation of resources available to society, it would be well to describe briefly some of its characteristics. Thus, a few initial words are necessary on the role of the State in the economic system.

The tax system should depend directly on the function which society grants to the State. Different societies have different concepts of this role. Ours has elected a mixed economy based primarily on private initiative and effort. The idea is to allow the greater share of responsibility to the community and to its citizens, limiting the State to definition of overall policies and the supervision of their execution and the generation of the conditions which permit individuals to know their problems and to seek solutions, assuming direct responsibility for their achievement. State responsibility is conceived as one which should inform on existing conditions, program by defining goals and general lines of action, facilitate legal channels to the maximum and preserve the general national interest, and should watch over the application and respect of the norms which proceed from the general policies adopted. When these functions have been fulfilled, each sector has the responsibility to seek and to apply the solution for its respective problems.

Thus in the economic field, the State must elaborate general programs and establish policies, centering its direct action on the implementation of social development programs and participating in a limited number of strategic activities. In other fields, the State must fill a supportive role, regulating activities which the private sector must carry out. The basis of this consists in decentralizing functions related to the economy. For these reasons, the tax system must be neutral, and must not interfere in the process of allocation of resources except in very specific and limited cases, directed according to explicit norms which are the result of social programs.

One of the clearest patterns for achieving efficiency in the economic process resides in the assignment of productive resources by the market, within the overall framework determined by the State in order to increase its social content.

There is no better allocation of capital and of work in a country than the decentralized allocation achieved by the thousands of consumer and productive units, which possess the best information with regard to profit

and preferences. Taxes should not unduly alter the productive structure, as this would mean a decline in production on a national level as compared to what could be obtained with a neutral tax system.

The reason for being of taxes is Public Spending. This spending requires financing, which should not signify inflationary pressures. For this reason public revenues, especially from taxes, are required to meet the greatest possible percentage of public expenditure.

In order to appreciate the efficiency of a tax system, we must examine the public budget in its totality, and analyze the role of expenditure. Moreover, in order to study the incidence of distribution, we must at the same time study taxes and expenditure. The taxpayer is not only a being subject to a particular tax burden; the taxpayer also participates in a series of public benefits as a member of society, even though he does not visualize them directly.

In the first place, there are what economic literature calls "public goods", a group of services which because of their nature, the State must provide. We refer to all of those items in the budget which pertain to benefits, which exceed the sphere of the individual, and which present numerous effects that imply collective enjoyment of such goods. We are dealing with such basic items in the running of a nation as the administration of Justice, Defense and National Security, Public Health, Public Education, etc. It is obvious that these expenditures must be met and provided for by the State, for all the inhabitants of the country without distinction.

It is also obvious that such goods and services are basic for the development of any private activity, and furthermore, they complement private activity, and substantially raise its productivity. Since these services cannot remain exclusively dependent on the Market, they require adequate financing, that is, taxes.

A second area in Public Spending, which is also very important for the normal development of individual activities, deals with social transfers. Here we include a series of services such as those related to social security, all of which constitute elements which guarantee equity and social peace. For example, it is natural that society assume responsibility for the unemployed, persons whom neither the Public Sector nor the Private Sector were able to absorb in productive work, and therefore, an entire program of unemployment subsidies must be administered by the State. None can deny that there is a similar responsibility with regard to the

dispossessed, and that the State should be concerned with the establishment of programs required to help, the assistance which is indispensable in any form of justice. All of these transfers require financing through taxes received from those who have the capacity to contribute to society.

Finally, we must recall that the price and amount solution reached by a particular market not always corresponds to the social optimum. There is waste when there are monopolies or oligopolies; there are imperfections as a result of flaws in the information mechanisms. At times equal opportunities are not available to the various economic agents, and finally, on some occasions society prefers to correct certain particular preferences which it considers erroneous. For this reason we see that all the States in this world have special discouraging taxes on certain types of consumer items such as tobacco, alcohol, certain forms of entertainment, etc., and they prefer to collect and to redistribute to a broader sector a determined volume of monopolistic profits. On the other hand, sometimes subsidies are granted to motivate some activities which society wants to encourage, and this also requires financing.

The essential is that collecting public revenues, both those destined to finance public expenditure in general and those for corrective purposes, should be carried out with a minimum of interference in the markets. When we speak of neutrality in general, we want to reflect precisely this fact: that the tax system should not produce unnecessary deviations. We know that such deviations would be costly in terms of social well-being.

A very basic aspect in the achievement of an adequate allocation of resources is the degree of coordination among the various instruments of the economic policy. The more coherent and consistent the application of public policies, the more effective will be each one of its instruments and the better the general results.

Internal taxes, tariff duties, the exchange rate, fiscal incentives, are all interdependent variables. The manipulation of one of these instruments usually produces effects on others. It is very important for public authorities to be aware of the existing interrelation between these instruments, and that they make decisions accordingly.

For example, if there is a tax on the production of a certain type of national goods, if the object of such a tax is only to contribute funds to the budget or to restrict the consumption of an item, but without the intention of reducing the protective margins for national domestic production, it is

logical to impose a tax on an imported good at the amount or rate as the tax on its national equivalent. In this case the tax is on consumption in general, and the absence of a tax on the imported article would really be an implicit reduction in the protection of domestic activity. The conclusion is that in that case, in order to study effective protection, it is not sufficient to study the level of the duty, but also the tax situation of the articles.

On the other hand, the interrelation between tax and export-developing policies should also be considered.

For example, the resolutions of the General Agreement on Tariffs and Trade base the indirect tax system in the taxation of the goods in the destination country and for the purpose of not altering in an artificial way the comparative advantage in the production of the various products; it is wise to have a subsidy policy for exports which only means the refund of the total of the indirect taxes on the final export article. This points up the need for indirect taxation such as the value added tax, which permits rational calculation for a sound draw-back policy.

In general a tax structure should be developed which, when united to the tariff, exchange rate and social security structures, would reduce to a minimum the discriminations among the various sectors of international production. The idea here is to produce a system of net effective protection with very few and mild intersectorial discriminations, so that by means of free foreign trade, the country manages to find its own comparative advantages. This is a new application of the concept of neutral taxation commented on above.

Finally, it should be noted that the use of multiple instruments with a similar role is not justified, except if there are difficulties in using a single selective instrument with all the intensity and agility required. There is no better quality of a tax system than the capacity to give clear, defined and stable signals.

Tax Policy as a Growth Factor

In general it is well known that domestic saving plays an important role as an economic growth factor. A basic component of saving is the surplus in the current account of the fiscal budget. This surplus or public saving when properly channeled to profitable investment in infrastructure, causes an important and sustained rate of growth of the National Product. On this level, not only the effect by means of demand on this sector is taken

into account, but also the indirect increase in productivity generated in its activities because of better quality and increased quantity of complementary resources with which to work. As the importance which the availability of basic capital infrastructure such as communications, transportation, basic services, access to certain natural resources and energy, etc. is very well known, we will not go further into this topic. It is sufficient to point out the role played by taxes as revenue in the budget system destined to finance this type of capital expenditure in the public sector. However, it is necessary to point out that the surplus in the current account can also be created by means of reducing the government current expenses, which makes a greater portion of public revenues available for investment.

Another area of public action that requires financial resources acquired through general taxation, is the investment in strategic sectors. All are lines in which because of the volume of capital required, the high degree of risk implied, and the magnitude and the extension of the benefits expected, it is indispensable to have public intervention, given that the private sector cannot, not does it wish to, nor should it develop these activities on its own.

This field, especially, is related to the exploitation of certain natural resources on a technologically viable scale.

There is another set of tax measures which can motivate and dynamize the private sector contribution to national development, namely the laws of regional and sectorial development. Tax exemptions not only can provide general and overall incentives for greater private investment, for example, by means of a tax credit system in the income tax schedule for enterprises which make new investments in plant and equipment, but also permit the establishment of selective incentives, differentiated by sector or region. This last tool which the tax policy offers should be used with the greatest care so as to avoid undue proliferation and to limit the discriminatory aspect, since it could lead to inefficiency if the principle of neutrality established above is disregarded.

On a regional plane, it is important for the development system to be as decentralized as possible, but it should tend to an efficient and balanced combination of public and private goods produced throughout the country, which when distributed will not be concentrated excessively in a few regions, and, that all the regional economic agents make decisions according to variables which correctly reflect the national benefits and costs of their actions. Thus, the analysis leads to the conclusion that an integral

and efficient regional exemption system should contain an overall subsidy package to finance a higher level in certain services such as health, education, housing, etc., for the acceleration of growth of certain depressed provinces and allocations to supplement expenditure financed by the regions for certain projects such as a corrective mechanism for the effects that such projects generate (for example, a dam, a road). Besides, consideration should also be given to a set of exemptions or subsidies, unrestricted in their application, free allocations which compensate on a regional level for the differences between tax efforts or burdens borne by the inhabitants and the benefits of public expenditure which they acquire, according to the regional distribution of taxes and spending. All this, keeping centralized tax collection in mind, that is, that the taxes, rates, taxpayers, and taxable base should always be established and applied by central authorities on a national level, and that they are not the faculties of regional authorities.

Then, on another plane, a possible strategy proposed is the granting of factorial rather than sectorial exemptions. That is, The State would try to achieve the maximum exploitation of existing resources, by means of general incentives, to increase saving and investment, to increase the use of existing capital, and to encourage the maximum use of employment, of available manpower. All these factors exercise powerful influence, on the economic growth of a country, and therefore are of great interest with respect to the formation and maximum use of resources. The exemptions would consist in systems such as the 'tax credit' or deduction of taxes for new investments, and direct subsidies to enterprises of every kind which employ and train additional manpower. One form of this could be that the State pays part of the social security taxes, since they are a distortion with a negative effect on the progress of development which maximizes employment.

To summarize then, the strategy proposed avoids the proliferation of special preferences for different productive lines or sectors. The idea is rather to encourage reproductive investment in general, and greater employment and better training for workers. On this level exemptions can definitely become basic levers for development.

Finally, we can add that in a certain way the tax system also motivates the economic growth of a country, by sanctioning the inefficient with taxes, and by obliging the groups which show excessive passivity to contribute with their productive efforts to the national well-being.

The Stabilizing Role of Taxation

In the context of an inflationary economy, the taxes can also play another role, one which is very important for the achievement of economic stability. The role of collecting in this respect, is that of reducing the values of the various components of the aggregate demand, especially, in the amount for private consumption. Since consumption is a direct function of available income, diminishing the income which remains available for private spending, for tax purposes, and especially by means of direct taxes on the profits of enterprises and personal income, a consequence of the tax system is that lower private consumer prices reach the market than those which would otherwise have reached it.

Every anti-inflationary program should consider the use of the tax tool as a coadyutant factor, and at least this stabilizing program cannot allow itself to mortgage the effectiveness of this instrument.

Taxation often acts as a break on the pressures on the balance of payments, limiting the value of the imports, especially in the consumer goods area, and thereby relieves any situation which may affect a country's trade balance. It also has certain characteristics which are favorable in the elaboration of policies on the foreign sector of the economy.

Obviously, taxation can fulfill this role of "automatic stabilizer" in both ways, cooperating in the reactivation of the economy by means of an automatic decline in income taxes, when depressions problems arise.

Basically, so that this stabilizing function can fulfill its role rapidly and effectively, the system of taxation, declaration and payment should be such that it does not allow for a decline in taxation effectiveness in real terms just because there is a period of inflation in the economy. Our country has gone through a decline in fiscal yield many times, with the resulting difficulties in financing the public budget, and the nearly inevitable corollary of money creation and inflation.

We can show the importance of this phenomenon and its urgency with respect to the fiscal financial structure in the following section of this paper in which we will elaborate on recent historical development and a diagnosis of Chilean public finances.

Thus far, we have presented a summary of the principles which should form the basis of every tax system, and of course, any reform scheme.

Aspects of the Historical Evolution of National Public Finances

There has been a noteworthy increase in the fiscal budget, well above the historical rise, beginning in the year 1970. Public Expenditure represents 27.0% of the total expenditure of the gross domestic product in 1970, 42.7% in 1973, and is estimated at 31.7% for 1974. Obviously such percentages are totally out of proportion with the scheme of a mixed economy as presented in the preceding analysis, since they imply that the State weighs excessively on the economy, strangling the decentralization required for a more competitive system. To begin with, then, there must be a reduction in fiscal spending so as to increase private participation. Since the end of 1973, and during this year, we have been working to achieve this; both the budget for next year as well as the content of the tax reform have been conceived from this point of view.

Another very striking fact is the nearly constant quota of Public Capital Expenditure in the 1970-1973 period, since the main part of the increase in spending took the form of Current Expense and other extrabudgetary entries to finance losses in the decentralized area. This has been and still is another one of the basic preoccupations of this Government in matters of public finance: to give priority to public investment and capital spending, so that the budget will once more contribute in a positive way to social growth.

With regard to revenues, the asymmetrical behavior of tax revenues and overall deficit should be noted, the first showing a percentage of decline and the second a severe rise from 1970 to 1973.

In any case, the percentage of the Gross Domestic Product acquired by the Fiscal Sector as Tax Revenues is a figure which has been around 20%, a high amount if compared with international patterns for other mixed Latin American economies. (The percentage of the Gross Domestic Product represented by Revenues from Taxes of the Central Government is 21% for Argentina - 1969, 13% for Colombia - 1969, 9.3% for Guatemala - 1969, and 11.3% for Mexico - 1969).*

This could be reflecting the fact that the tax burden is nearly reaching the maximum permissible levels, but without granting a higher degree of

*Source: CEPAL, based on official statistic published in "Documents and Conclusions of the III Interamerican Conference on Taxation." Secretariate General of the O.A.S., Washington, D.C. 1973.

liberty to state finances. In any case, it is important to realize that if little more than one fifth of the product generated annually by the Nation is received through the tax system, the structure and the character of the tax system will acquire decisive importance in the economic activity of the country. Thus the urgent need for tax reform.

To return to the comments on the tendencies in the structure of financing, we had that in the last three years a serious change in the composition has been detected, since from the historic tendency during the entire decade of the 60's in which taxation contributed more than sixty percent of the financing of public spending and reached figures even higher than seventy percent at the end of the decade a period develops in which the contribution of tax revenues does not represent much more than half of the expenditure. Meanwhile, the Deficit, which has already been reduced to figures below ten percent of the expenditure towards 1967-1969, experienced a disproportionate rise in the seventies, reaching over forty percent during 1972. Any one can realize the seriousness for the country of the fact that the deficit in the Public Sector reaches 13% of the total expenditure of the GDP. Even when the magnitudes provoked an enormous crisis during those years, it should be noted that the tendency to trust in indebtedness as a fiscal financial resource, is a secular characteristic in the history of Chilean public financing. It should be clear that a determined fiscal deficit is translated into: a) foreign debt and/or b) internal debt, whether with the Banking System (Central Bank, Commercial Banks) or with the Private Sector, and/or c) Cash variation. Scheme b) internal debt, has been particularly important; this is inevitably reflected in greater direct money creation and an increase in the monetary base, which finally causes inflation.

Some authors have made an estimate of the implicit tax collection on the part of government by means of the so-called "inflation-tax" generated by the deficit; they put this inflationary financing at around 40% of fiscal capital income and at around 19% of the total of direct taxes, for some years.*

However, this form of inflationary financing has meant a loss in the average well-being, of approximately 1.76% of the GDP, implying significant social cost for the entire community, measured exclusively by the concept of holding monetary balances. If we add the negative effect

*Source: Juan Carlos Méndez, "La Carga Tributaria de la Inflación en Chile," Cuadernos de Economía No. 20.

which inflation generated has had as a factor of erosion of direct tax revenues, product of the problems of the lack of readjustability of the tax base, and the considerable lag in the declaration and payment of taxes, other authors conclude it could well be that in net terms, ("tax-inflation" minus erosion of fiscal revenues), the result implies that for large periods of time the government experienced an effective loss of resources, a loss which could represent the equivalent of 0.35% of the GDP.*

To summarize, the preceding analysis indicates that by considering the problem only from the fiscal collection aspect, the existence of the deficit and its "tax - inflation" as an element in the budget revenue is unsuitable. Faced with significant and growing inflation rates even the net collected actually from this point of view can become negative. Besides this, the full weight of general social and economic evils which the inflationary phenomenon brings with it is added to this, together with the regressive burden. The government wants to attack all aspects of this problem and has not only taken action to reduce fiscal deficit, but also it no longer wishes to continue to receive resources in an unequal way, as a product of the consequences of inflation.

For this reason one of the basic points of the Tax Reform is the introduction of monetary correction in order to avoid taxation of enterprises on inflationary earnings, and the implementation of the Tax Unit, which together with protecting fiscal revenues, permits an automatic adjustment of the income brackets in the progressive tax system, in order to avoid this unjust and random discrimination especially against workers, a product of the inflation which we are experiencing at this time.

Without disregarding what has been stated here, what should remain quite clear from all this, and specially from the deficit problems, is the fact that the Government cannot run the risk of a significant real reduction in its tax revenues. We have already analyzed what this means. While it is true emphasis will have to be on the reordering of the budget from the point of view of reducing and restructuring Public Spending, it is no less true that the more normal the system of tax collection, the lower will be the short term cost to society with respect to unemployment and inflation. These elements also have influenced the elaboration of the Tax Reform which we are analysing today, so that particular care has been taken in this matter.

* K. Ruffing, "The Effects of Inflation on the Yield and the Structure of the Fiscal System of Chile," 1972, Columbia University, Ph. D. Dissertation.

We shall now comment briefly on some of the most serious structural problems in the present tax system in order to understand the specific motivation for each of the propositions contained in the Reform.

The Reform: Problems and Solutions

It is well to make a synthesis of certain problems which have been detected in the national tax regime, some of which have existed for years and some more recent ones.

The diagnosis is divided between the principal existing distortions on the level of direct taxes on the one hand, and the indirect taxes on the other.

The direct taxes represent 35.5% of total tax revenues, contributing 19.6% of the financing of the total Public Expenditure.

They cover the following items: income taxes for enterprises and private individuals with 28.6% of the total of Tax Revenues; property taxes, 2.7% of Revenues; the tax on copper which yields 1.9% of total taxes collected; and other direct taxes which amount to 0.4%.

a) Even when the traditional scheme for income taxes, which consisted in proportionate taxes of the category type according to whether the assessment was on capital income or on labor income has been modified, we still maintain a scheme which divides the tax regime in categories, but over and above that taxation an overall progressive tax is applied. This results in the persistence of certain problems of equity in the direct income tax, aspects which become very serious when considering that the overall progressiveness of the system, for example, is uncertain, which is in contrast with the normative requirement established in the sense that it should be at the level of direct taxes, especially on incomes, where the fair redistribution we are seeking is found. In fact, a system which allows division of the tax base between income from capital and income from labor, for example, necessarily implies that two persons with equal total incomes and subject to similar progressive scales but with a different functional composition of the income, will pay different total amounts in taxes.

b) On another plane, direct taxation in Chile has traditionally had a quite high degree of progressivity, which has resulted more nominal than real.

The high marginal taxes contemplated in the income tax normally are not translated in effective collections, a product of the legal and illegal erosion

observed in the taxable incomes and declared incomes, for the reasons already cited.

In this sense it is necessary to specialize the tax tool in a more realistic way, working on the scheme to broaden coverage and control of the taxable base rather than to continue to add elevated marginal rates of a fictitious nature. The history of Chilean public finance shows very well that the comparative advantages consist in basic broadening the basic scheme rather than in trying to impose more taxes on the different income brackets.

c) With respect to the previous point, there is the problem that occurs on the level of existing brackets and rates in the second category tax (a tax on income from labor). On the one hand, the maximum marginal tax at present exceeds that of the Global tax on income, which is obviously unfair. On the other hand, principally because of the inflationary process, the structure of brackets and rates in force provokes an excessive tax burden on the labor sector, an excess which is not intentional from the point of view of economic policies. It is evident then, that an adjustment is needed in the structuring and the progression of this tax.

d) On the Global and the Single tax level, there are also some defects of organization in the scheme for tax credits or personal exemptions. Even though it is a relatively insignificant aspect and easy to correct, it influences the equity of the system.

e) Some of the previous defects are overcome if the various existing formulas in the Law are considered to define the taxable base, thereby losing the required homogeneity in this respect.

The problems of defining the taxable base in each case lead to some situations in which there is double or triple taxation. Besides this, the subdivision by type of base (income, property, type of income, type of property, etc.) implies explicit discrimination among determined forms of income or the maintenance of private wealth, producing innumerable occasions for distortion in the allocation of resources, which cause a composition of wealth and of the flows of saving and investment that is different from the optimum.

Likewise, the negative effect produced with the treatment of real incomes on the one hand and presumed incomes on the other, should be studied.

f) Another very serious aspect of the present system is the coverage of

certain substitute regimes. For the same type of tax there are special tax scales and bases for certain types of activities such as, for example, small industries and artisans, part of agriculture, small and medium mining, because of the excessive legislation on exemptions, which even constitutes a separate chapter on inefficiencies. This is the reason why we stated without exaggeration that the general tax regime is the exception and that the exceptions to the regimes constitute the general rule. There is an urgent need to revise all of the substitute regimes so that the Income Tax Law becomes truly a general norm.

g) The subdivision, classification and differentiation of the tax bases and scales seriously affects the collecting power, and therefore, the interests of the National Treasury. This deterioration occurs for two reasons. The channels and ways open by means of these schemes facilitates legal and illegal evasion by means of the reclassification of income and bases which each taxpayer carries out, using legal figures for the sole purpose of paying less taxes. On the other hand, even though there were absolutely no tax evasion, the potential to be collected by the Government is reduced by a determined rate scheme when the number of tax bases is increased, since the progression obtained from a total is always greater than the sum of the progressions obtained from the fractions of that total.

h) Another important problem from the point of view of justice and allocation of resources is one which has to do with the differential treatment for the different schemes of organization of enterprises. Before we discussed the aspects of equity and collection in general and the problems produced in this respect by differentiated tax schemes, depending on whether we were dealing with corporations on the one hand, or with private individuals on the other, and on another plane, to contrast the traditional type of enterprise with a cooperative. Now we wish to talk about an additional specific point, the effect of profits retained by corporations.

The retention of profits has been a mechanism used by corporations for reinvestment in the enterprises, thus avoiding the Global Complementary rate which taxes shareholders when dividends are given out. Besides being unfair when compared with other types of enterprises, this mechanism which the present law is motivating, is inefficient from the point of view of allocation of resources. On the one hand, it permits the coexistence of similar enterprises but with different rates of return, first by coverage of a certain margin of comparative inefficiency. On the other hand, it restrains the required development of the capital market.

The urgency of improving and broadening the capital market is well known, and it is not compatible with the existence of certain institutional impediments to the free circulation of available funds for loans. The social rate of return and the growth of a country are not maximized when there is re-investment in the traditional enterprises simply for the purpose of avoiding taxes, an operation which in certain cases can be less profitable than possible alternative investments. The Government wishes to increase the flow of funds which moves the saving and investment market, so that people will freely assign capital to those sectors of the economy which are the most profitable. Besides this, if there are proportionately more dividends paid, small shareholders will have access to the market, given their concern for liquidity.

From the point of view of equity, we should also mention that some correction of the problem of retention and evasion of the Global tax could be obtained by means of the Capital Gains Tax, but given the inefficiency, complexity and the tremendous amount of evasion in its collection, it is preferable to eliminate that tax, and to integrate capital gains into the base of the taxable income.

i) Finally, we arrive at a very basic problem in the Income Law, namely, the effects of the application of article 35. This article, by establishing the possibility to readjust the capital of an enterprise, and to apply this readjustment to the exclusive revaluation of the fixed assets, leaves the rest of the real investments of the enterprises open to the effects of inflation by taxing them on the higher nominal value of the real assets caused by inflation, such as, inventories, investments in other enterprises, stocks and shares of other companies, etc., which means that a great part of the capital remains defenseless.

The most obvious problems which can be pointed out in this respect are:

First: For the enterprises it is unfavorable to "invest" in working capital, since this can only be partially revalued; second, the charges in the profit and loss statement for depreciation, and the value of some accounts of the balance, have no meaning from the real financial and economic point of view; third, indebtedness with third parties at interest rates which are inferior to the inflation rate, for the purpose of investing in readjustable assets, is rewarded in the tax system since the enterprises at the present time are not taxed on real profits.

These problems, besides the discriminations which they imply, lead to an

allocation of resources which is not optimum, and which is reflected in reduced demand of liquid assets, a high volume in raw material inventory, a low rotation of finished products, chronic problems in liquidity, and pressure from credit, etc.

Moreover, the negative aspects of information of the financial statements limit the schemes of participation in the enterprises.

All of the above demonstrate the urgency of drastic corrective measures in all of these aspects.

Indirect Taxes

Indirect taxes contribute a high percentage of the total of Tax Revenues 66.4% in 1973 and they include:

The tax on the sale of goods and services, the core of the indirect tax system and the largest individual tax, with a contribution of 36%; the taxes on production at 13.3%; the law of Taxes on Services gives 6.7%; taxes on legal actions 3.9% of the total; taxes on imports 6.5% of tax revenues, and other less important indirect taxes.

a) The law on Taxes on the Sale of Goods and Services, law 12.220, inspite of having been modified, simplified and reorganized several times still has significant structural defects. As a matter of fact, the principal characteristic of the present tax is that basically it concentrates taxation on the production stage; however, it contains other rates which are applied in a different area, whether within the productive sector at a lower rate but with an accumulative effect, or with respect to certain products qualified as luxury items. One disadvantage inherent in the system is the difficulty and the arbitrariness in the definition of the subject of the tax, since the general norm is the application of a tax to the price applied to the product once production has been finished, there are numerous cases in which it is impossible to distinguish exactly the termination of the industrial process whether or not particular product constitutes a component of another article subject to taxation. We have the cumulative effect of the "pyramid" or "cascade" type on prices; even though improved, it still subsists and weighs on the present system.

b) Likewise, the free price policy, the basis of sound competition for production, should not allow undue and unknown alterations in the relative price structure, since this would mean grouping productive activities to-

gether for the sole purpose of avoiding certain transactions in order to diminish the total tax margin. This is the phenomenon known as "excessive vertical integration."

c) On the other hand, there are a great many exemptions for products or institutions, or individuals, regions and sectors which prevent the rational management of the system and which cause distortions which impede sound competition.

d) In the field of foreign trade, this tax on sales influences in a special way.

It is known that the resolutions of the General Agreement on Tariffs and Trade (GATT) base the indirect tax system in the destination country, and in order not to change in an artificial way the comparative advantages on the production of the various goods, the countries are permitted and advised to maintain subsidies on exports which only represent the total refund of indirect taxes on the final product for export. However the present indirect tax system does not allow for rational calculation and a sound drawback policy.

With regard to the import policy, we have already pointed out in the section on principles the fact that the tariff structure should not be indirectly altered by the internal tax system. Hence, in accordance with what has been established in the present law 12.120, the imports as well as the substitutes will continue to be subject to the same indirect tax rate. However, it is important to point out the effects of an indirect tax system in which the burden or final tax on goods is in some way, a function of the number of transactions they undergo. There is no guarantee that an imported article is subject to the same number of transactions as its national equivalent. In so far as there is a difference in the number of transactions undergone by both articles, there will be a different tax burden which will be translated indirectly in a modification of the tariff structure itself.

There is, therefore, a need to construct a new system which avoids each and every one of the flaws mentioned.

e) Even within the area of indirect taxes, certain effects of Law No. 16.272 should be mentioned.

The Stamp Tax Law, in matters referring to the tax on judicial acts or contracts which arise from a credit operation, is one of the factors which has most strongly influenced the scarce development of our capital market,

since it discourages transfers and activity of financial intermediaries, by raising substantially the cost of funds to be lent and by tax discrimination among the different credit instruments, including those of similar characteristics.

f) The same can be said with regard to Taxes on Services, a tax which introduces a substantial difference between what the purchaser of credit pays and what the lender receives from these funds first, by making the credit extremely expensive for the borrower and second, diminishing the profits for the lender.

Surely the reason for these taxes on interest has been the supposition that the total of savings is not a function of the interest rate but rather of income and wealth, so that a rise in the bank interest rate for example, would only have implied higher income for the owners of the funds and redistribution of funds. It was thought, therefore, that this tax could also be redistributive in its incidence. The argument became a sort of vicious circle, since by not allowing the net interest rates certain significance for the savers, they would never have been able to consider the interest rates as a reward for their efforts, with the consequent limitation on the potential development of the capital market. Besides this, as we have said before, the tax policy should specialize its redistributive functions at the level of the progressive global tax on total income and wealth, rather than dilute them in a series of partial rates whose final result is uncertain.

g) Finally, we must point out that the present tax structure is extremely complex, not only in matters of financial instruments, but also in institutions, which makes it such that only a few experts in the matter can operate efficiently, which besides being unfair increases, in ultimate terms, the operating cost of the system.

Solutions

To enter upon a description of the solutions which have been adopted to face the problems detected in matters of indirect and direct taxes, we should point out in the first place, the norms already dictated by the Government, and which are already in force. Then, we shall refer to the propositions of the Reform.

Norms already Dictated with Respect to Taxation

The main objective of the intensive work in this field has been to reorganize the Tax Administration and the Tax System in General.



As for reordering taxation this work has been directed principally to the reorganization and regularization of the chaotic situation in which the present Government found the State finances and the abnormal tax situation of the majority of taxpayers. The dictation of these norms permitted timely fulfillment and the correction of various tax obligations, granting special conditions and terms of payments.

Once the provisions mentioned which permit the normalization of the tax situation of the taxpayers went into effect, the more profound business of modifying the Tax system as such was undertaken.

The modifications were the fruit of various studies later promulgated as Decree Laws, for the purpose of correcting the defects of existing legislation and to prepare the System for future reform.

The changes carried out in the tax system in matters of Direct Taxes, Provisional Payments, Indirect Taxes and modifications to the Tax Code are explained below.

a) Income Taxes:

D.L. No. 254 (Official Gazette 6-28-74) authorized taxpayers who run the balance on June 30 to close the period for this year on 12-31-74 in order to solve problems presented in these enterprises derived from problems of revaluation, implicit in the article 35 of the present Income Law. Those taxpayers who do not choose to change the closing date for the tax Balance may increase the charge to loss from 20% to 30% of net taxable income.

b) Real Estate Taxes:

D.L. No. 296 (D.G. 1-30-74) established a special readjustment of appraisals to bring amounts up to date in order to reflect a value close to the real one, the appraisals or commercial value of these goods. The readjustment was 10 times for non agricultural property and 30 times for agricultural property.

c) Wealth Tax or Patrimony Tax:

D.L. No. 298 (O. G. 1-30-74) eliminates the capital tax on the patrimony because it was considered an impediment to national capitalization and to the development of productive activities. However, and because of the

serious financial situation of the State, one last sacrifice will be required, and only for this year 1974, consisting of the payment of tax on the patrimony.

d) Tax on Licence Plates for Vehicles:

D.L. No. 243 (O.G. 1-30-74) consisted in the design of a new scale of progressive, cumulative assessments, thereby solving the problem of the former progressive structure in which two vehicles of very similar values paid very different taxes.

For these reasons, as in the case of real estate, the value of vehicles was brought in line with their commercial value.

e) Substitute Regimes:

D.L. No. 164 (O.G. 12-6-73). Classifies the tax regime applicable to small industry and artisans and includes them in the provisional payment system.

D.L. No. 297 (O.G. 1-31-74). Incorporates truck owners to the general regime of the Income Law. This sector has also been included in the provisional payment system applicable to all taxpayers, according to the Income Law.

f) Provisional Payments.

These modifications have been introduced for the purpose of broadening and strengthening the provisional payment system in order to maintain the collection of income taxes in real terms.

g) Sales Tax on Goods and Services.

The purpose of the modifications of Law 12.120 was to eliminate discriminations, to modernize and to reorganize the system. Concretely, the elimination of discrimination puts an end to the system of taxing the same article at different rates according to whether or not it is imported. Likewise, a series of discriminations in the tax rates which affected the various legal entities. On the other hand, the modification and reorganization of the system is basically summarized in the drastic reduction of the broad range of tax rates that made up the indirect tax system. The purpose of all the regulations dictated was to adapt taxation to the new free market

system and the opening to foreign trade. Decree Laws promulgated to this effect are: D.L. No. 95 (O.G. 10-24-73), D.L. No. 292 (O.G. 1-30-74).

h) Taxes on Stamps and Stamped Paper.

D.L. No. 291 (O.G. 1-30-74) introduced modifications to this tax which consisted in eliminating taxes which affected legal actions with the exception of sponsorship tax and recusation. In this way the government has eliminated the charges applied to litigants for stamp fees in legal transactions.

i) Modifications to the Tax Code.

The Decree Laws passed in this field deal with the readjustment of unpaid taxes, the simplification of complaints on property tax, and increases in the sanctions for tax evasion.

The Decree Laws passed on this subject are:

D.L. No. 95 (O.G. 10-24-73)

D.L. No. 294 (O.G. 1-30-74)

D.L. No. 482 (O.G. 5-29-74)

These have been the principal modifications of the Tax System, modifications of the Tax System, modifications which are the fruit of thorough studies designed to construct the fundamental bases for the tax reform to be implemented in 1975.

The following is an explanation of the basic content of the Tax Reform.

Reform Proposals

At this point it would be well to review the essential outlines of the Reform project to see the specific solutions proposed for the existing problems. Because of the complexity and the extent of the project and the limited time available we will not cover the entire project, nor any one of its clauses. More detailed knowledge may be obtained by reading each one of the documents especially prepared by the Ministry for the purposes of diffusion and through discussion of the subject. Further analysis of each topic will be presented by the experts participating in this forum. My main purpose here is to point out the most significant aspects of the project, in the order in which they appear in the previous section.

With regard to Direct Taxes, the proposal consists in:

a) The reinforcement of collection and effectiveness of the general Income Law, by grouping of real as well as presumed incomes in a single base to which the single wage, Global Complementary or Additional Tax will be applied according to the respective case. The reinforcement of the general tax base is the point around which we have worked; we are using the specialization of the personal income tax instrument in order to improve the progression and the equity of the system. In this respect we have tried to promote the maximum leveling in the conformation of the tax base by eliminating various discriminatory situations.

b) The creation of uniform progressive taxation so that the rates for the Single Wage Tax and the Global Complementary which apply to the taxpayer, coincide, since both are the basis of progressive taxation at the taxpayer level. This includes the elimination of some of the higher margins in the high Wage Tax, so that the maximum marginal tax rate will not exceed 60%.

c) The adjustment of the tax scale and the introduction of the concept of the Tax Unit in both the Single Wage Tax and the Global Complementary tax. The first contemplates a recomposition of the bracket structure of present taxable income in order to achieve wider distribution of the tax burden. The second is intended to correct the excessive burden generated as a result of the play of the inflationary process on the amount of taxable income. This is solved by means of the use of the "tax unit" to establish brackets, tax credits, exemption margins, minimum and maximum limits, etc. for the single or Global Complementary Tax. This measuring unit will be adjusted monthly on a permanent basis, according to the variations in the Consumer Price Index.

The "Tax Unit" will be another general leveling factor in the annual income tax declaration and of those which are periodically retained.

d) The simplification and the establishment of a uniform amount for credit against progressive taxes, with a fixed single deduction for each dependent. This credit system will be based on the "Tax Unit" and will be the same for the single as well as the Global tax.

The establishment of a limit level for exemption is proposed to provide equality in the area of taxes in the progressive categories.

e) To assure equal treatment of income from the practice of a profession, whether as an individual or as a member of a partnership. This refers to the establishment of a common Second Category Tax of 7% for profes-

sionals, and the establishment of norms for deduction options, reducing the presumed expense established for professionals in this category to motivate them to declare their real expenses.

The 7% rate will apply in general to second category taxes since this tax will also apply to the remunerations of corporation board members or advisors.

f) The elimination of a series of exemptions, as well as the exemption regimes in special legislation with respect to certain sectors of taxpayers such as small Mining, small Industry, Artisans and activities related to passenger transportation. In this way these sectors of taxpayers will be subject to the same general rules which now apply to all taxpayers.

For this reason we have also revised taxation in the agricultural sector respecting the special norms which should govern this sector, because of its characteristics, but trying to motivate efficient use of the land. Of course, as for any mechanism for the implementation of the Reform, adequate measures for the period of transition have been taken into consideration.

Modest business activity will receive very simplified treatment that does not cause further complication or problems. Substitute treatment which is less offensive has also been established for the small Mining Companies that operate with the real capital of less than 6 annual tax units and no more than five workers. We consider that those modest taxpayers require in all fairness, a more simple system with relatively lower incidence.

g) The treatment of corporations should be equal to that of partnerships and individual taxpayers. There are several aspects of this point.

i) To apply a single 12% First Category tax to all taxpayers regardless of their legal structure. This implies a substantial drop in existing first category rates.

ii) To eliminate the "Owner Salary" concept applied in individual enterprises and partnerships for tax purposes.

iii) Establish a system whereby the Global Complementary or the Additional tax is applied to corporation incomes which is not subject to the former condition that dividends had to be distributed. This tax will be provisional and will substitute for the Global Complementary or Additional

which is paid when dividends are passed on to shareholders. The stockholders will continue to pay the Global or Additional tax on income or benefits received, but beginning in the second year of the application of this additional tax on corporations, the stockholders will have the right to a special credit against the Global Complementary or Additional Tax, equal to 30% of the amount of benefits paid by the respective corporation and which should be declared for tax purposes.

Once again the Government is aware that the change must be carried out gradually in order not to cause problems during the period of transition. The additional rate for corporations will be only 30% for 1975, 35% for 1976 and in 1977 the 40% rate will become permanent. (Likewise the credit for the shareholders will be 20% and 25% for the years 1975 and 1976).

h) The elimination of the capital gains tax in order to tax the corresponding profits in the first category, or to declare them as not constituting income.

The norms on "frequency of transaction" will have to be studied so that they influence more those operations which generate profits which are not basically considered as income, as occurs with the greater value obtained in the case of the sale of real estate and other goods.

The elimination of other parallel taxes on income which are less significant is also being considered.

i) The modification of Article 35 of the Income Law so that enterprises pay taxes on the basis of real profits.

The proposal consists, basically in permitting the complete revaluation of real assets and liabilities, that is, those that are protected from inflation. In this way, the final capital of the enterprises will appear at its real value on the closing date; this will be compared with its initial value also expressed at its price on the closing date of the fiscal year, in order to determine the real profit accruing to the taxpayer, that is, the difference between the initial capital and the final capital, both being expressed in terms of money of equal purchasing power after having made the adjustments for operational changes in capital.

The 20% maximum on taxable profits which can be charged as a loss for excessive revaluation of capital is eliminated, since revaluation of all assets and liabilities subject to revaluation is permitted and the restrictive

concept of equity capital and of assets which could be revalued and which in some way affected negatively the optimum composition of the asset portfolio of the enterprise has been eliminated.

In other words, the adjustment proposed for the revaluation of equity capital consists in the revaluation of all of the real assets of the enterprise effective on the closing date, and to charge to the same account the revaluation of initial capital and the real liabilities at the closing date, which brings the norms contemplated in D.L. 455 in harmony with sound and just taxation.

Finally, with this method of calculating taxable income, enterprises will not pay for nominal increases in capital equivalent to currency devaluation during the fiscal year the charges against depreciation will be significant, and the balances and profit and loss statements will express figures which have real meaning, basic elements for information with respect to the equity schemes which are being developed on the basis of the Social Statutes for Enterprises as well as in decision making within economic units with allocation of resources structured on the market.

The following are the proposals for Indirect Taxes:

a) To replace the Sales Tax on Goods and Services with a Value Added Tax. This tax will be determined according to the subtraction method, that is, defining "value added" as the difference between sales and purchases carried out by each productive unit within a given period.

The value added tax will be applied according to the following norms:

- i) It will affect importers, producers, wholesalers and retailers.
- ii) Importers will have to pay the tax at the moment of entering the goods. The tax will be calculated on the customs value and will be credited to the sales tax.
- iii) Producers once the taxes on the sales for the month have been calculated, may deduct the tax paid at the acquisition or importation of raw materials or other goods or elements to be used, incorporated or consumed directly in the production process, including machinery and accessories, tools or spare parts, as long as these expenditures are for the manufacture or production of items subject to the value added tax.

iv) The wholesaler and the retailer will pay a tax only on the value added, represented in general by its sales margin, by means of the same system of credit against the sales tax.

v) With respect to certain luxury items and other products such as non-alcoholic beverages, an additional rate is established which will affect importers and producers, but there will be no credit for this tax.

vi) The single tax applied to production as established by the Law on Alcohol, will be applied in the usual way but, in the subsequent stages, in the production of wine, beer and liquors in general, they will be subject to the value added tax.

vii) Likewise, taxes on gasoline and other products derived from petroleum will be similar to the present system, but will be applied on the production level.

viii) Sale of articles in the primary sector will not be subject to the value added tax except in the case of farming if the products have been processed, such as the sale of wine (not wine making itself), canned foods, etc.

With respect to retailers, the project contemplates authorizing the Internal Revenue Service to establish a fixed monthly quota against which it will have the right to deduct taxes paid for purchases. In this way full advantage can be taken of the opposition of interest between buyers and sellers.

b) Tax on services rendered will be applied as follows:

i) In general terms, the structure of the present tax on services will be maintained.

ii) The tax rate should be the same as that of the value added tax, except for certain services which pay a lower rate.

iii) Restaurants, soda fountains, hotels, etc. are included in this tax, with special rates, but with the right to credit for the purchase of products subject to the value added tax.

c) As a general norm, all personal exemptions are eliminated.

d) The proposal includes the simplification and organization of the cum-

bersome system for payment of taxes under the Stamp Tax Law No. 16.272. The rate differentials for commercial credit instruments which range from 1% to 2% per annum will be eliminated; on the total of the credit granted for all such transactions the rate will be 1% per annum.

This tax shall be applied in proportion, according to the terms of the loan or the renewal of the terms, and will not be paid for periods which exceed ten months.

Finally, we must mention the basic principles proposed for Development Laws and Tax Exemptions.

a) Regional development laws shall be applied without discrimination to all activities undertaken in the region.

b) Sectorial exemptions shall be applied without discrimination within the sector to be benefited, and shall therefore be independent of the region in which the economic activity in question takes place.

c) The central Government will direct the programs of the various sectors and the regions will not be authorized to use taxation as a means to promote sectorial programs other than those established according to the norms set down by the Government.

d) The structure and level of exemptions will not be given for unlimited periods of time, as the true economic situation of a country and its objectives are continuously evolving and the exemption system should be intimately bound to the dynamics of the economy.

e) With respect to development laws, only the principles of taxation already mentioned will apply. This implies that no exemption will be granted which implies a reduction in the corresponding Global Complementary, Single Wage Tax or Additional taxes; moreover, those in existence will be eliminated.

f) All arbitrary or discretionary administration of these laws will be eliminated. In this way, the market forces and Government action to orient taxation will be the only factors which determine how the allocation of the country's resources will take place, thus avoiding any artificial restriction resulting from discretionary management which could compromise national development.

The very promulgation of the resolutions taken so far with regard to Direct and Indirect Taxation in the Tax Reform will be sufficient to clean up and reorganize many of the existing exemptions.

Besides this, we are working on the basis of modifying the nature of many exemptions which at present favor certain products, zones or enterprises, in order to solve the present imbalance with regard to the use of productive factors. Interference in the allocation of resources of a country should not exist in order to promote the production of certain goods; rather the production of the various goods and services should be in accordance with established social priorities. For this reason, mechanisms to correct the present scheme of preferences implied by the use of the capital factor have been proposed, to motivate the use of manpower-intensive techniques which will foster the population and well-being of many regions which have been neglected until now, and will also be quite positive in terms of employment on a national level.

It may be said that, unlike the anarchy which reigns in this field, the new norms, being coherent and clear, will tend to have a significant impact on the pattern of growth in the economy.

Final Comments

This, is, in synthesis, the spirit, the motivation and the essence of the Tax Reform proposed to the country by the Government.

As we said at the beginning, the reform corresponds to the desire to form a society which is more just, more efficient and which provides better conditions for its citizens.

Above all, the Reform is intended to delineate clearly the various fields of action so that each sector in the country will know what its responsibilities are, and will assume them as part of the task of reconstruction.

Part II

The Year Nineteen Seventy-Five

The Government Economic Recovery Program

Jorge Cauas Lama
Minister of Finance

Text of the address to the nation made by
Minister of Finance, Jorge Cauas on the
evening of April 24, 1975.

April 24, 1975

The President of the Republic and the Honorable Government Junta have asked me to design and carry out an economic program with the fundamental purpose of erradicating the inflation that has affected our country for more than seventy years and which recently has become extreme as a result of the demagogical economic policy carried out by the former Government.

With the assistance of a large group of specialists we have proposed an economic recovery program to the authorities. This program has been approved and is already in practice.

The main objective of this program is, as we have already stated, to put a brake on inflation by the end of this year. For this reason, certain basic measures have been approved. Although these measures imply continued sacrifice on the part of the community in the coming months, the compensations will be economic stability which will permit adequate economic development. This will mean that in the not too distant future poverty will be stamped out and all Chileans will be able to benefit from the advantages of the modern world.

Some of the goals set for this phase of the economic program have already been at least partially reached. Inflation has been reduced by half under circumstances in which hyperinflation was imminent and in which the scarcity of goods had converted our country into a community of speculators and in which direct productive activity was at a minimum.

The price system, the motor of the economy, has been radically corrected. Today we have a price structure that forces the private sector to assign resources only to those activities which have clear social advantages. Substantial progress has been made in the implementation of a modern foreign trade system and in the design of a capital market which is gradually coming to resemble capital markets in highly sophisticated economies. The public deficit has been reduced, although we realize that in this area conditions are still quite far from those considered desirable in a stable economy. It should be remembered, however, that we began with a situation in which more than half of the public expenditure was financed simply by printing money.

From the point of view of production, we have moved from a situation of absolute disorder to another one in which the productivity of labor has risen substantially and in which the activity of the population has a clearly productive effect. This effort will be translated, within a reasonable period of time, into improved welfare.

The agricultural situation has not only been stabilized but has shown notable increases. The production of wheat has increased 26%, potatoes 62%, eggs 24% and the area cultivated has increased by 265 thousand acres.

The same applies to mining, construction and exports. Copper production has increased 23%, iron 9%, new housing starts in the private sector 34%, completion of houses financed by the public sector 23% and exports, not counting copper, over 100%.

Production in the industrial area has normalized, but at varying rates of growth. The production of goods for export and investment has increased, whereas that of consumer goods has decreased with the exception of food products.

There have been substantial achievements so far, but this is not easily evident to the general public because the main effort has been concentrated on raising the level of savings and investment which had been at a very depressed level as a result of the irresponsible policy in practice until September 11, 1973.

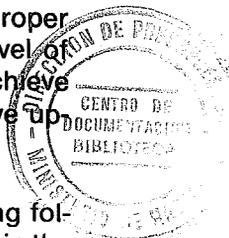
The substantial increase in investment has obviously meant a drop in the levels of consumption in spite of the notable increase in production.

The external situation, on the other hand, represents considerable losses for the country as a result of the low price of copper and the increase in price of some of the basic items imported, such as petroleum. As compared to a normal long term price of US\$1.06 per pound for copper, the average price thus far this year is 58 cents. The capital loss to the country is estimated to be some 800 million dollars.

Naturally we do not control the external conditions and a sound economic policy should be based on managing the variables which are under our control.

Our efforts in the future should be, therefore, to concentrate on the size of the public sector and primarily on the level of public expenditure. The correct handling of expenditure should result in a drastic reduction of money creation and of inflation in a reasonable period of time, as well as in an increase in the resources available to the private economic sector which should then necessarily produce a more adequate standard of living for the population.

The nation's productive structure and the key variables for its proper functioning are in good condition. We have only to adjust the level of public spending and that of the public enterprises in order to achieve greater stability, and with that, favorable conditions for a definitive upswing.



The economic measures presented today reinforce the policy being followed, correcting the principal defects derived from the violent drop in the price of copper and the exaggerated size of the public sector.

They should lead to the stabilization of the economy by year's end, creating thereby, optimum conditions for accelerated economic growth.

The purpose of the recovery program which we are discussing in general terms today is to bring about the definitive normalization of the economy by means of a drastic reduction in inflation.

The rises in prices should decrease substantially in the second half of this year as a result of the reduction in money creation which in turn is the product of the significant drop in public spending which is being carried out.

The budgets and programs in force for the purchase of goods and services in public institutions and state enterprises will be reduced between 15 and 25 per cent. These reductions will be implemented at any cost, including the dismissal of any functionaries who are unable to understand that the reduction of inflation receives top priority in the economic policy.

Public employees and the public enterprises at all levels must be aware that their particular interests as institutions or as individuals, although very respectable, are totally without importance in comparison with the principal preoccupation of all Chileans, namely inflation.

Together with the reduction in public spending, there shall be an increase in taxes in order to balance the fiscal budget once and for all. The graduated income tax will be increased 10% this year; a 10% additional tax shall be applied to luxury items; exemptions to the value added tax shall be eliminated, except those on regular bread, liquid milk, produce and fresh fruits and vegetables; the process of reappraisal of non-agricultural real estate shall be accelerated.

All citizens are warned that there will be no exceptions in the case of income tax or social security tax evasions.

There should be no doubt in the minds of the public that enforcement of tax payments will be increased and that evasion will be subject to heavy fines and sanctions including imprisonment according to the law.

The Government hopes that by means of these measures the fiscal deficit shall be of minor importance by the second half of this year, thereby laying the basis for the achievement of a lower rate of inflation within a short period.

It should be clear that for the next two months, price increases will continue as a result of the natural lags which affect economic policy.

The public should understand that the implementation of a drastic policy, such as the one we are explaining today, takes time. However, it is possible to guarantee a drop in inflation in the second semester.

Wages will have to be handled with caution. Just as we are demanding a sacrifice from taxpayers, so we must ask for the collaboration of those who live on a wage or salary.

The Government with a substantial effort will continue the policy of automatic wage readjustment. Besides the raise due in June according to the CPI there will be a E.°20,000 bonus at the end of April and an advance of E.°20,000 at the end of May, payable in two installments. In the second semester, the automatic wage readjustment will still apply, but it shall be adapted to the lower rate of inflation which will be in effect by that time.

In any case, the purchasing power of the workers shall be maintained, and measures will be taken to avoid unemployment.

The Government has decided to carry out a reform of the welfare system along the lines and based on the philosophy which have already been expressed by the authorities.

With respect to unemployment, the municipal programs which guarantee a minimum income to those workers who may find themselves without work as a result of the policy to restrain inflation shall be continued and expanded. The hiring of workers shall be subsidized and encouragement shall be given to production through improved promotion of exports and

by means of the implementation of a system of accelerated exchange rate depreciation.

The foreign trade policy followed thus far has proven very efficient and shall therefore continue.

The exchange rate shall continue to be readjusted in relation to domestic prices and the tariff structure will undergo some small corrections for the purpose of providing reasonable protection for local production. The goals of tariff modification set forth by the Government on previous occasions shall be maintained, that is, the maximum duty in effect by 1977 will be 60%.

The Government policy on tariffs shall be within the framework of the agreements signed with the Andean Group and the Latin American Free Trade Association, reserving the right to negotiate tariffs such as those we are now proposing when the time comes.

The capital market shall continue to develop with special emphasis on long term savings.

Some technical reforms shall be made to equalize taxation, legal reserve requirements and conditions for the operations of the various financial intermediaries and to liberalize operations of institutions currently restricted by poorly conceived State regulation.

We wish to advise the executives of the different companies which operate in the financial market that the authorities are alert to the possibility of illegal practices and that those executives or employees who spread unfounded damaging rumors with respect to financial institutions which have the full backing of the State and the Central Bank shall be severely sanctioned.

All financial intermediaries must comply fully with the present regulations and with those that are in the process of being formulated.

We wish to reiterate that all of the financial operations of the banking system as well as of the Savings and Loan Associations are guaranteed by the Central Bank, which has been financing the Savings and Loan Association deficits and shall continue to do so whenever this should be required.

My collaborators and I have no doubt that with the economic policy

outlined here, Chile will have inflation under control during the second semester of this year. We are also convinced that with the collaboration of the entire population, the effects of this policy will be minimized and of short duration.

I wish to remind my fellow Ministers, Government executives and executives of public enterprises that this must be a joint effort in which they play a fundamental role in the achievement of an effective reduction of public spending. Their responsibility is enormous, as they will have to carry out their tasks while submitting to drastic reductions in the budget.

I wish to point out to all of our citizens that these economic improvements will not come about tomorrow. There will be a tight squeeze for months, similar to our present situation. I also wish to inform you that experience throughout the world indicates that an improvement in the standard of living and the level of employment is only possible if the economy saves and invests and definitely grows.

Experience in our country, as in so many others, indicates that as long as there is inflation, there will never be guaranteed employment and an adequate standard of living. We are going to stop inflation and as a result, the country will grow, employment will increase and the standard of living will improve.

I wish to point out to all businessmen, regardless of their situation, that they must cooperate with the Government policy, unless they wish to find themselves facing untenable financial situations which could bring about the bankruptcy of their companies.

Demand should be limited since we are in an abnormal situation. As a result, any persistence in raising prices will cause accumulation of stock which later on will have to be liquidated at a serious loss. During the coming months it will be profitable for businessmen to believe in a restricted demand. The traditional incredulity, which so many times in the past gave good dividends, could mean the end of their activities in the next few months. The Government will not listen to the belated laments of those who did not trust in the present policy.

Finally, a few words to the housewives in this country who are the ones who suffer most from the economic measures.

I wish to point out to them that the purpose of what we are beginning to do

today is to solve once and for all the anxiety which the continuous rise in prices causes in our homes. For a few months the situation is going to be difficult. It will then begin to improve, slowly but surely. As this happens, the future will become more and more clear, and you will be able to observe that the unified development of the family unit and its components shall be increasingly guaranteed.

So-called economic miracles are not miracles at all but rather the result of work and saving within the framework of a coherent economic policy. They have usually come about after periods of tremendous sacrifice on the part of the population.

A program of economic recovery such as this one requires sacrifice from the entire community. The public should be alert in the face of demagogic interpretations that certainly will come from interested sectors.

We are greatly encouraged by the conviction that serious economic ills are only remedied by work and by savings.

The economic phase which we are initiating today will lead necessarily to the end of the struggle against inflation and then to a period of development heretofore unknown in this country. The way to recovery, although it is short and well known, is fraught with sacrifices and denials. We must enter into it in a spirit of optimism and with the certain hope that once we have gone through it, we shall find ourselves in a free and vigorous community that shall return to the position of leadership which it once occupied on this continent and in the world.

**Report on the State of
Public Finance**

Jorge Cauas Lama
Minister of Finance

October, 1975

Introduction

As Minister of Finance it is my duty to give an account of the present state of public finance and of the financial and economic situation of the country. I must also refer to the prospects for the economy in the short, near and long term, and to the programs which government intends to carry out in order to overcome permanently the problems which in the past have delayed the country's development.

By the end of 1973, we began to put in practice an organized and coherent economic policy. The goal of this policy is to reach a permanent rate of economic growth notably superior to that obtained in this country during the past decades.

The concept of this policy is very different from those which had been developing in this country during the last thirty years. This has meant the introduction of substantial changes in the Chilean economic system. At the beginning of the program it was pointed out, and we reiterate here, that a policy of this type does not produce spectacular short term results. Rather, it requires sacrifice during the period of correction, which only bears fruit in the medium and long term. If all this is valid for an economy operating under normal conditions, it is all the more serious in the case of a world crisis situation which has repercussions on the economy of a magnitude which can only be compared to the depression of 1930.

Analyzing the ground covered so far, the Government is convinced that there have been significant accomplishments in each one of the phases of the program.

Progress in 1974

During the year 1974, the application of the new policy had very positive effects in all areas.

Confidence in the government and in government authorities was re-established, permitting a return to normal production and a considerable increase in the productivity of labor. Growth in the agricultural, mining and non-traditional export sectors has augmented considerably.

The free price policy generated a rapid return to normal in the market and permitted the reestablishment of an organized price structure, which had and is still having very positive effects on the allocation of resources.

There were periodic readjustments according to the fluctuations in internal and external costs in the prices still controlled by the State, such as the exchange rate, the prices charged by public enterprises, the prices of goods produced under monopolistic conditions and of the most necessary articles, to avoid imbalance in the market. There was, at the same time, periodic readjustment of wages.

An adequate exchange rate and foreign financing policy, together with the freedom of imports and the abolishment of unnecessary, discretionary controls, permitted the normal development of foreign trade. This in turn provided adequate financing for the balance of payments. Local productive activities gradually began to face foreign competition, motivating increased efficiency and the development of sectors in which the country enjoys comparative advantage.

Hyperinflation, which was imminent by the end of 1973, was avoided by means of the control of monetary expansion. This also permitted a gradual reduction in the rate of inflation, in spite of the heavy cost pressure derived from the inevitable adjustments in prices of the exchange rate, wages, public enterprise rates, wheat, fuel and others.

The credit policy was brought in line with the new economic situation in which the market must play the basic role in allocation of resources.

The development of the capital market was begun, permitting an increase in the rate of internal savings and obtaining more productive use of resources.

The improved fiscal discipline reduced the deficit significantly, thereby diminishing monetary emission. A tax reform was studied and then applied in March of 1975. As a result, the resources necessary for the financing of normal government activity have been generated, the burden was distributed fairly and there was no interference with the normal allocation of resources.

The State initiated the process of transferring those enterprises whose administration does not correspond to the State in its role as a subsidiary agent.

Significant progress has been made in the study and the implementation of various social development policies for the purpose of providing definitive solutions for the problems of nutrition, health, welfare, educa-

tion, organization and training programs, among others. All of these aspects are of fundamental importance in the distribution of income and the elimination of extreme poverty, problems which had never been dealt with in the past.

Economic Conditions at the Beginning of 1975

In spite of the progress made in 1974, some problems related to the deficit situation in the public sector still persist and require more drastic action. On the other hand, the strong international recession which began at the end of 1974 produced a violent fall in the price of copper, which produced a situation of imminent crisis in the balance of payments in a relatively short period of time.

The country lost approximately US\$1 billion as a result of this drop in the price of copper and the increase in the foreign debt, because of the additional pressure generated during the period as a result of the successive renegotiations carried out in the past.

The need to continue with the stabilization policy and the depth of the world crisis obliged the government to adapt the policy to the new conditions.

If the world crisis, with which we are all familiar, had not occurred, the Chilean economy would have returned to normal in a relatively short period of time. Simply improving the price structure and reducing the deficit in the public sector would have been sufficient to achieve rapid recovery and a more stable economy.

However, the imminent crisis in the balance of payments required a more drastic economic policy. The estimates of the deficit at the beginning of the year were in the order of US\$800 million, a figure which was naturally impossible to finance in a country whose foreign debt exceeded US\$4 billion.

Thus we had to reduce the deficit, and at the same time decrease inflation, and maintain the basis for a policy which would permit rapid growth in the future.

We must also add the fact that the entire previous framework already comprised a situation in which the economic activity was declining, and the levels of unemployment, at least in Greater Santiago, were reaching rates of 14% in the month of April.

The economic correction and normalization policy carried out during 1974 has exposed deteriorated production and employment figures which formerly had remained concealed because of demagogic policies, which represented artificially high levels of consumption, maintained by means of heavy foreign indebtedness.

When the economic recovery program was undertaken, the situation was rather complex and in particular, the deficit in the balance of payments was impossible to finance in the traditional way. It has often been the custom to provide by artificial well-being obtained at the cost of mortgaging national sovereignty by means of irresponsible foreign debt commitments.

The imminent crisis in the balance of payments had made the operation of the productive systems practically impossible. This required a contraction of internal demand which, in the short term, implied a pullback in activity, while in the medium term, it allowed us to overcome a very unfavorable situation, which if we had not faced would have concluded in the greatest chaos, not only economic, but also social and political.

It should be remembered that a crisis in the balance of payments means that foreign currency will not be available for the import of foodstuffs, fuel and raw materials. This would cause generalized lack of supplies and would paralyze production with the resultant rationing, controls, lines and black markets.

The Economic Recovery Program

By instruction from the Government, the Minister of Finance has been charged with designing and carrying out a program to deal with this situation.

The policy proposed is well known. It consists in reducing government spending and an increase in public revenues, so as to create a restrictive situation which would diminish the pressure of demand for national as well as imported goods.

Because of the extent of the deficit in the State enterprises, the strict management of their finances and the acceleration of the process of transferring State-owned companies to private hands were required.

To contribute to rapid equilibrium of the balance of payments, the

adjustments in the exchange rate were accelerated. It was also decided to continue the tariff policy to orient the private sector with respect to the activities which would have preferred development, in order not to interfere with the long range development strategy.

The existing level of unemployment and the drop in the real income of practically all Chileans moved the authorities to carry out some extraordinary measures to ease the burden on the lowest income sectors.

The minimum employment program provided a solution for the most poverty-stricken group of the unemployed sector.

The social section of the fiscal budget was not affected by the public spending reduction policy, in spite of the unfavorable conditions the country was experiencing.

The government maintained the quarterly readjustments according to the reduction in inflation. The purpose of this was to maintain the purchasing power of wages, which does not depend solely on the amount of nominal readjustments, but also on the behavior of prices. As a result of the policy followed, real wages in September of 1975 reached a level superior to the average for 1974. This improvement would not have been achieved if the readjustment system had been maintained with the rates of inflation observed during the first semester.

It is important to point out the Government's financial effort in order to continue with the quarterly readjustments, defying the opposition of some well-known experts who said that this fact alone would cause irremediable problems.

The purchasing power of the minimum wage was preserved and the hiring of labor was motivated by means of direct subsidies.

The State, aware of the situation of the most needy, has made significant financial efforts to protect them. This action, which is without parallel in the known history of stabilization programs throughout the world, has not been appraised as it should be, especially by those whose mission seems to be to predict crises for which they are incapable of offering viable alternative solutions.

The recovery program also contemplates significant legal reforms, for the purpose of creating effective economic decision making organs within the

cumbersome bureaucratic system which we have inherited from the past and which many times has immobilized any social action on the part of the Government. The creation of the Monetary Council, the extension of the faculties of the Superintendency of Banks to control all financial institutions, modifications of the Banking Law, the transfer of the Savings and Loan Associations to the Ministry of Finance, and the Ministry of Economy control of the management of State enterprises are some examples of the progress made.

Progress in the Recovery Program

Beginning in May, 1975, the government began to finance its expenses in currency without having to resort to loans from the Central Bank, thus eliminating the most important cause of money creation.

Credits extended to the State enterprises, which in the past constituted another substantial source of emission, have been notably reduced.

These accomplishments, which it is easy to list, have basic economic and social meaning, as they indicate an irreversible advance towards economic stability. They have meant important mitigation in the balance of payments and the growing elimination of the principal source of inflation in Chile.

Deficits in State enterprises form part of the economic history of our country, and the resulting social and political unrest is not usually understood by traditional political bureaucrats.

These companies, sometimes described as pillars of development, have contributed notably to the impoverishment of our country.

The useless outlays which were common in a large part of fiscal activity and State enterprises have their practical application in less availability of goods for our citizens which today some persons very casually try to attribute to the present government.

The reduction of the deficit in the public sector creates the possibility of an important increase in the standard of living in Chile, both because of the improved use of resources and the elimination of inflationary pressures.

The recovery program has led to equilibrium in the balance of payments, an incredible situation when we think that the price of copper is the lowest in real terms in the past decades.

The initial deficit, which was estimated at US\$800 million in 1975, has been reduced to figures in the order of US\$270 million; in the second semester of this year the balance of payments will be practically in equilibrium.

This has been accomplished simply by using what common sense in the science of economics indicates in these cases. The normalization of the balance of payments was costly and meant a lowering of the standard of living in Chile. These costs, however, are not a product of the recovery program, but correspond to the recognition of the losses which the country had already sustained as a result of the international recession. We have pointed out that these losses, without considering their indirect effects, reached US\$1 billion, which measured in terms of the national product, equals 12%.

If we had undertaken a reactivation program instead of an economic recovery program, the cost would have been much greater, because no economic program can cause the price of copper to rise, nor diminish the burden of the foreign debt, but it can aggravate the crisis.

An alternative policy in this matter would have meant a total loss of confidence in our country in international financial circles. This in turn would have led to a balance-of-payments crisis which would definitely have caused a loss in well-being far superior to the one we actually had.

It is not a mystery to anyone that a crisis in the balance of payments means shortage of raw materials, drastic declines in production, rationing, lines, violent rises in prices and complete social and political chaos.

The critics of the present economic experience know that any other economic policy would have meant the submission of the national authorities to foreign governments and to an internal disintegration which no government would survive.

The focal points of inflation have either disappeared or are definitely declining. The balance of payments is back to normal. There are very few occasions in our history when the economic authorities could make statements such as the ones we are making today.

It is true that unemployment is high. It is also true that the Chilean standard of living has fallen. This is, however, by no means the result of the economic recovery program.

This restriction is a consequence of the depletion of fiscal resources, of the artificial creation of jobs, of the drop in the price of copper, of the rise in the price of petroleum, the very high foreign debt generated in the last 20 years, and the low level of investment.

The economic recovery program has obliged Chileans to face their own situation. In the past, the country has been deceived, and led toward policies which did not correspond to the actual conditions. The courage of a government with no demagogical interests was required to undertake a realistic program with the idea of permanently stabilizing our economy.

The truth is that today Chile has been converted into a respectable country which can participate in any international financial milieu.

The success of this effort has been recognized outside the country. We can once more conduct our commercial relations with dignity. The clearest demonstration of this statement is in the increased flow of foreign investment and the renegotiation of the foreign debt on terms which are favorable for the country.

Distribution of Costs and Benefits of the Program

Since the end of 1973 many criticisms of the economic policy have been heard. Each time that the facts disproved a criticism, a new one appeared to replace it. It is interesting to present a chronology of the most significant ones.

At the beginning some said that freedom of prices would mean that the prices would multiply several times from one day to the next. At the same time, they said that free prices would not eliminate the black market, the lines and the shortages.

Then it was said that inflation could not be reduced without price controls; after that, the critics announced that the balance of payments was unmanageable and that this government could not overcome the problem without submitting to foreign powers or without returning to the former political practices.

It was also said that the sacrifice required was unacceptable and that the present government would deteriorate within a brief period of time.

All of these predictions turned out to be erroneous, and events have shown that what did occur is exactly the opposite of what was predicted.

Likewise, the latest criticism that the economy will not be reactivated, shall also be forgotten when the Chilean economy demonstrates its dynamism, once the present international and internal conditions have been overcome.

There is one proposition which merits special consideration, as it constitutes an intelligent effort of the spokesmen of the affected economic and political interests to return to past practices.

They have attempted to damage the prestige of the economic authorities by accusing them of a lack of social sensitivity and of carrying out a policy which favors the capable sectors at the expense of the country's poor.

They exhibit figures which show the decline in real wages and they speculate on the fantastic profits obtained by the high income sectors of the country.

The argument is attractive and has been thoroughly exploited, especially by the traditional political bureaucracy and by the economic sectors which have been affected by the present policy.

In our country it has been a tradition that small economic or political groups invoke the name of the poor in order to criticize economic measures which affect their particular interests.

Calm reflection on this point will show that the criticism of the economic policy does not come from the large national majority, but rather from the representatives of small interest groups who have been affected by the general stability which is being generated and by the loss of wealth which some economic groups have suffered. It is well to enumerate some of the economic policies, with their effects, in order to understand better what we have just said.

Tax evasion, which favored the wealthier sectors, has been substantially reduced. The Value Added Tax has eliminated this important source of illicit income for some sectors, carried out with funds belonging to the community. The income tax system with its surcharges means that in the medium and high income levels, nearly 60% of marginal income goes to the State. The rationalization of exemptions has ended irritating unfairness, drawing into the tax base sectors which in spite of their high incomes had not been paying taxes.

The progressive redistribution of income generated by the present tax policy is unparalleled in the past history of our country, and it is natural that the affected groups should complain.

The public expenditure policy signifies reinforcement of social spending in favor of the poorest sectors of the community. Statistics show that nutritional levels have improved and infant mortality has been reduced, especially in the low income sectors. The social significance of these indicators greatly exceeds the happy tales which are sometimes heard with respect to income redistribution.

If we think that reforms of health, welfare, and elementary and secondary education are about to be undertaken, it is understandable that these criticisms are, to say the least, at best unfounded.

The social reforms which are already in progress and the structure of public spending lead to a massive transfer of capital to the really poorest sectors of the country. This situation, which is also unheard of, cannot be ignored in an analysis of what is happening with the distribution of income and wealth of this country.

The impersonal quality of State intervention and better control of expenditure in public enterprises, so criticized by the state bureaucracy, have been doing away with the most important source of sudden wealth characteristic of the situation in the past.

The elimination of innumerable subsidies to the wealthy sector should also be considered as a correct evaluation of this point. Realistic prices of fuel, among other items, have signified a real loss of income to the high income sector.

The interest rate policy, greater competition in the capital market and the active direction of the authorities in the market have improved the functioning of this important productive sector. The elimination of subsidized interest rates has contributed to better income distribution.

The economic policy in force, by creating the conditions for greater internal and external competition, is eliminating the monopolies generated in the past decades, which have produced clearly regressive effects in income distribution.

The improved relative development of agriculture, derived from changes

in the price and foreign trade structure, has meant the transfer of resources toward a sector of the economic activity in which the majority of our poorest fellow citizens are living.

The program of guaranteed minimum employment has permitted those most seriously affected by unemployment to obtain a minimal income with dignity.

The restrictive monetary policy has determined substantial losses of wealth for the highest income sectors. An example is the reform of the readjustable mortgage bonds.

Is it possible to ignore the effects of these facts when speaking of the redistribution of the cost of the recovery program?

Could it not be that the criticism is the result of resentment over the significant loss of capital and power of certain sectors which suddenly remembered the country's poor?

It is true that real income has declined in the last few years. How could it be otherwise when the real product per capita has been drastically reduced because of the international economic crisis and the enormous decapitalization of the country produced by the Popular Unity?

It is a mistake to infer an eventual regressive distribution of income solely from the drop in real wages. The availability of goods per person has declined more than the real income. However, the minimum remunerations, considering the equalization of family allotments and other benefits, have not deteriorated in spite of the decline which has really taken place in the product per person. On the other hand, the behavior of salaries is not a good indicator of what has occurred with income distribution since as the study of extreme poverty has shown, this is not concentrated in the salaried sector.

The government would like nothing better than to raise the level of real wages. This is the final goal of the economic program. However, we must not return to the errors of the past, in which sometimes in order to ingratiate themselves with the workers, they had to face additional problems of unemployment, the artificial creation of public jobs, and financing the readjustment through increasing rates of inflation.

The economic policy of this government will produce a substained and

permanent improvement in the distribution of wealth and income, assuring real equality of opportunity for all Chileans. This fundamental goal cannot be sacrificed only to show a short term improvement in certain indicators which some people use without any basis in order to attribute regressive effects to the economic policy.

As the new economic structure continues to take shape, in Chile the only way to make money will be by working and saving. The times when a fortune could be made just by having a friend in a public position or in a financial institution will be nothing but a memory.

The vast majority of Chileans understand that the country must make sacrifices in order to face an unfavorable economic situation. They are suffering from the unemployment and the inflation which still persist with the great understanding that countries only progress when they make sacrifices.

The vast majority of Chileans back the Government, as the opinion polls have shown.

The public appreciates frankness and values the fact that it is not being deceived. The great intuition of the Chilean people leads them to confide in policies which, although difficult, provide a definite solution to the problems which affect them.

Greater stability and economic development are the only guarantee that in our country employment and the standard of living of the most poor will be raised.

Problems to be Solved

An analysis of the present economic conditions shows the problems which must be faced during the remaining months of this year and part of next year.

In the first place, the narrow conditions derived from the world economic situation have not been changed. The price of copper is still extremely low and the impact of the service on the foreign debt for next year will be even stronger than that of 1975. While this situation continues, the country will not be able to recover the loss of resources sustained in 1975, which meant a reduction in the level of consumption and investment. However, today the country is prepared to function under the conditions given as the

result of policies followed. The country's present financial solvency permits us to expect a greater flow of foreign resources, which will make it possible to finance a higher volume of imports than in 1975. In this way we can improve the level of activity and gradually recover the level of well-being.

The second problem is that of the degree of liquidity in the economy. In a normal situation there is a stable relation between the volume of liquid resources and the level of production, which is determined by the habits of payments, expenditure and by the existing legal framework. In Chile, this relation measured by the Money/Production coefficient has been approximately in the order of 10%.

However, when the inflationary process is accelerated, as occurred in Chile in 1972, the people change their habits, and spend their money more rapidly in order to anticipate the rises in prices. In other words, the same volume of money permits the financing of a greater volume of transactions, because of the increase in the speed of circulation. This phenomenon meant the relation fell progressively to 3.5% by the middle of that year. With a drastic reduction in the rate of inflation, a process which began in July and which will be intensified during the next few months, the people will tend toward the normal habits, producing excessive liquidity, since the existing volume of money is insufficient to finance the flow of transactions. If the rhythm at which the speed of circulation will decline could be foreseen, liquid resources could gradually return to the systems, thus avoiding a contraction in the levels of real activity for lack of liquidity. Since this cannot be anticipated with precision, it is necessary to adopt a cautious attitude, and to increase liquidity gradually once the restrictive effects of the decline in velocity have been proven.

The economy must necessarily return to operating with a normal level of liquidity under stable conditions. This means that during some period money should increase more rapidly than the prices and when this occurs, it is not correct to speak of excess of liquidity. The reestablishment of a volume of money that represents a higher percentage of the product has the enormous advantage of guaranteeing a greater stability in the functioning of the economy. This occurs because the inevitable fluctuations in fiscal spending, in internal credit or in foreign trade operations under these conditions represent a percentage which is much less than the monetary mass, thus moderating its impact on the economy.

Objectives of the Economic Policy for 1976

The economic policy during 1976 has four basic objectives. In the first

place, an accentuation of the reduction of the rate of inflation, which has been in progress since the second semester of 1975 and which will continue during the coming months. Likewise, steps have been taken to assure external equilibrium, assuming that there are no substantial changes in the present conditions of the world economy. The policy also contemplates a gradual recovery of production and employment levels. These goals shall be accomplished within a framework of consolidation of the process of legal reforms basic for the efficient functioning of a decentralized, mixed and modern economy.

Any serious economic program, which has any possibility to accomplish the goals set down for it, must guarantee coherence among the goals. It would be very easy to propose to the country a program which contemplates the simultaneous achievement of spectacular goals such as, for example, a 10% increase in the Product within the year, the elimination of unemployment, income redistribution, obtained under conditions of price stability and equilibrium in the balance of payments. This sort of program has been proposed in the past and even though we all know the results, there are still those who for demagogy or through ignorance, continue to favor them. This government neither accepts nor needs to make promises which later become impossible to fulfill. On the contrary, the government considers that it is the basic duty of those who are governing, to present the public quite honestly with the problems we are facing and the manner in which they will be dealt with, no matter how difficult the solution. This style is often attacked as insensitive, as giving attention exclusively to economic matters and ignoring other social, political or other types of problems. It is forgotten, however, that precisely because we are well aware of the disastrous political and social consequences of programs which attempt to create artificial short-term well-being without a solid, permanent basis, this Government is not willing to sacrifice the medium and long term goals for the sole purpose of achieving easy popularity in the present and which would also be of short duration.

The principle disequilibria in the economy are practically solved or are on the way to being solved soon. However, the problems of extreme poverty caused by past "populist" policies, proposed by very socially sensitive people, will take years to be solved.

The program for 1976 contemplates economic reactivation. However, this will depend necessarily on the achievement of internal and external equilibrium. It means that economic recovery will be neither spectacular nor in the short term. We have already said that the external conditions do not ap-

pear to be significantly different from those of this year. If there is an important increase in the price of copper, the country will not be able to assign all of the additional resources to financing a higher level of activity, since for normal operation of the economy it is indispensable to reconstruct a reasonable level of international reserves. Internally, we must consolidate the achievements in matters of financing the fiscal sector, public enterprises and the savings and loan associations. In the measure in which we advance in this area, we will be able to free resources which, when transferred to the private sector, could generate an improved level of real activity.

What danger is there in forcing rapid reactivation?

In the foreign sector, it would generate a deficit in the balance of payments, since the country does not possess sufficient resources to finance the greater volume of imports. This would require the measures necessary to reestablish the equilibrium, forcing a drop in the level of activity, so that the initial reactivation would be a passing phenomenon.

In the internal sector a rapid reactivation could be generated by transferring resources to the private sector before they are freed by the process of financial correction of the public sector, or simply by increasing the level of activity in the latter. In both cases there would be a renewed increase in inflation which would definitely void the initial effects of reactivation. The second alternative has the further disadvantage of pouring additional resources into the least productive sector.

In short, the reactivation which is proposed, should be produced without generating either internal or external disequilibria. This sort of reactivation is gradual, but has the enormous advantage of being permanent and of growing over a period of time.

The Economic Program for 1976

Fiscal spending shall be maintained at a level which is compatible with the revenues generated by the tax system and with the subsidiary role of the State.

There will be significant reassignment of fiscal spending according to the priority of the functions assigned to the State. In the 1976 budget priority sectors are housing, health, nutrition, and pre-basic, elementary and secondary education, activities in which the state must play a permanent and significant role.

Together with the re-assignment of spending, a new accounting system shall be implemented to guarantee an effective control of expenditures and commitments of the various State institutions.

Given the many advantages of the existing tax system, it shall remain unchanged. However, the surcharge on income shall be reduced from 10% to 5%.

The present wage policy based on quarterly readjustments shall be maintained. As we have pointed out, a special raise for teachers is contemplated in the 1976 budget.

The self-financing policy for the enterprises which remain under State control shall continue, and the remainder shall be transferred to the private sector.

With regard to the savings and loan systems, the policy of adjusting these functions to the purposes for which they were created shall be continued, without generating financial disequilibria.

With respect to foreign trade, the exchange and tariff policies in force as well as the encouragement of exports shall be maintained.

In the measure in which the price of copper recovers, a policy to rebuild international reserves and to improve the structure of the foreign debt shall be implemented.

The monetary and credit policies must be compatible with economic stability and the need to monetize the economy in the terms already proposed.

The free price policy shall be maintained in order to allow for organized allocation of resources and normal market development.

The State shall maintain the control of some key prices, which shall be adjusted in accordance with objective internal and external conditions.

Future Structure of the Chilean Economic System

The economic policy in force has progressed substantially. There can be little doubt of the greater stability of prices observed today.

With respect to savings, a substantial increase has been achieved. The

growing development of the capital market is providing for a significant improvement in the levels of saving and the allocation of funds to more productive investments.



The fiscal situation has improved to the point that there is equilibrium in local currency operations. The deficit in foreign currency, however, continues as a consequence of the heavy foreign debt and the low price of copper.

The situation of public enterprises continues to improve and in a reasonable period of time we will have eliminated a source of inflation which, together with the fiscal deficit, explains our long history of inflation.

Public spending has been increasingly reoriented to social activities, which are translated into a substantial change in the structure which preserves a true redistribution of income on a permanent basis.

The balance of payments has been corrected to the extent that there will be practically no deficit of importance in the future, in spite of the heavy burden of foreign debt and the low price of copper.

The country has worked out a clear policy in matters of exports by means of which exports, not including copper, have been duplicated in one year.

The exchange rate and tariff policies as well as the internal monetary policy, are permitting the country to rebuild the international reserves and have changed the situation in relation to external financial organizations of the public as well as private sectors.

The anxious moments of extreme dependence in which almost no financial institution was willing to extend credit because of the high risk of insolvency which the country showed, are now behind us.

The changes in the price structure and the tariff reforms are showing clear indications to the private sector with respect to the areas which the country should develop and, therefore, the lines in which they should invest.

A gradual transformation of the productive sector is producing a shift of resources toward the dynamic sectors such as, agriculture, mining, and exports in general.

Continuation of the corrections in the relative prices will obtain the max-

imum advantage of capital and work resources, permitting a rate of economic growth hitherto unknown.

A significant flow of foreign capital has developed which should continue to grow as the national economy tends to normalize.

In the coming months there should be an accentuation of these positive characteristics and the country shall continue to achieve greater stability and definite conditions for greater development, with the resulting effects on the levels of income and employment.

The economic progress cited together with a set of exemptions and local incentives have laid the groundwork for sustained economic growth.

This process will necessarily be slow but constant until the rates of economic and social development are achieved. In fact, the effects can already be clearly observed in the agricultural and foreign trade sectors.

These effects should extend to construction and to the new industrial activity which will be generated when the new price, tariff and exchange rate structures are in force.

A sustained improvement of the income of the poorest sector shall be observed in the future. The same will be true of the development levels in the measure in which productive activity continues to develop.

The country is headed towards an economy characterized by sustained and stable economic growth.

All this is not the result of improvisation but rather the application of a set of coherent and dynamic policies. They constitute in themselves a development plan which is effectively guiding the conduct of economic agents toward optimum use of resources, the only means to guarantee maximum well-being for the population. This concept of a development plan departs from the former idea that planification consists in the enumeration of a detailed set of rigid goals which, when there is ignorance of the behavior of economic agents, go no further than the expression of the good intentions of their authors.

A mixed economic system is being designed in which the role of private activity will be much more active than it has ever been in recent decades.

The State will foster efficient and non monopolistic operations in the private sector, by the generation of competitive markets on the national as well as on the international levels.

The State, in its subsidiary role, will engage in productive activities only when concrete facts show that its social efficiency is greater than that of the private sector.

The effort of the State shall be concentrated in the development of social activity. To a great extent, the social, political, economic and moral crisis which the country has been suffering, is derived from an incredible misunderstanding of the role which the State should fulfill.

The antiquated statist orientation of this country must be changed drastically. We have arrived at this conclusion not only through observation of the extreme inefficiency which state action has demonstrated in the past, but rather because we believe that the private sector is much more effective in the development of productive activities.

The State must develop social programs which truly benefit the poor, in order to give real meaning to equality of opportunity, so often guaranteed by the letter of the law, but never carried out because of the incredible lack of concern on the part of the State in the past.

Modern economies are mixed economies and the degree of State intervention is determined by the relative efficiency in the development of the various activities which the country must carry out.

We are in favor of using the market as a technical instrument for the allocation of resources. We think it is the best way to obtain the best from our limited resources, without generating the hateful discriminations which usually are translated into illegitimate earnings.

Through the market, we want to generate a set of impersonal norms that regulate economic operations without the need for bureaucratic decisions which, besides having been inefficient in the past, created unacceptable social conditions.

The most significant changes of fortune in this country have been derived from the discretionary handling by the State of instruments of economic policy.

It should be recognized that in the past the state did fulfill a social function. The use of inefficient mechanisms of intervention, however, caused a vast waste of resources that explain to a great extent the low standard of living of Chileans today. Unfortunately, they also explain a large part of the unequal distribution of income and wealth.

We are not in favor of discriminatory rates of interest or exchange. We shall oppose every form of subsidy which is not of a social nature. The reiteration of these practices in the past has meant the enrichment of a few at the expense of the vast majority of Chileans.

We are designing an economic structure based on the past experience of our country. We want to arrive at a stable and impersonal economic system in which the authorities cannot be accused of favoring any sector but the poorest.

The economic policy in force has elements in common with other policies which have been implemented in other countries. Social and economic sciences do not exist in vain. If there were nothing in common in economic behavior, there would be no economic science.

Our experience, however, is clearly different from the others which some desperate critics are trying to impose on us as a model. The traditional lack of originality of some makes them think that everything has to be copied from foreign experience.

The present economic policy is neither dogmatic, nor is it based on any foreign model. On the contrary, it is only based on our own situation and on the application of the pertinent elements of modern social science.

The present economic policy means sacrifice, as do all the successful policies in the world. It is not a policy for the temerous or the easily frightened. Those who address the public assuring them that the problems can be solved without sacrifice and in a short time, are not helping the country. They know that their demagogy, if it succeeded, would only obtain a definite return to chaos.

Chileans understand that those who offer short term improvements are only deceiving them. They recognize them because they have been saying the same thing for years. For this reason, the Government is counting on the support of the population, in spite of the difficult economic situation we are experiencing.

The country will advance slowly but steadily. Once again the facts will contradict the pessimistic predictions of affected interest groups just as they have all along during the past months.

The Chilean people know who is telling the truth and who is deceiving them; for this reason they trust. Based on this trust, the government will eradicate the economic ills which led our country to the complete crisis which we are now overcoming with great effort.

Part III

Effort, Perseverance, Achievement

**We Are Truly Independent
Thanks to the Effort of
All Chileans**

**General
Augusto Pinochet Ugarte
President of the Republic**

June 29, 1976

Last evening on a nationwide radio and television broadcast the President of the Republic, General Augusto Pinochet analyzed the achievements of this government particularly in the economic and social orders.

In this address the President announced new measures to be taken in the management of the nation's economy. This subject was then discussed by Minister of Finance, Jorge Cauas.

The following is the complete text of the President's speech:

Ladies and Gentlemen, Fellow Chileans:

Ever since the Armed Forces assumed the administration of this Nation, our principal preoccupation has been—with the support of the respective technical organizations—to evaluate the social, economic and moral recovery of the country.

Few recall with the depth required, the conditions under which we were living from 1970 to 1973. Few recall that by 1973, when we made the decision to rescue the country from the clutches of Marxist-Leninism, Chile was a State in which the legal basis for the national institutions was being completely disregarded, civic morality non-existent, the social structure undermined, the domestic economy at a stand-still and with an excessively high foreign debt.

The Military Government found Chile to be without foreign reserves and to have lost prestige for failure to meet obligations abroad. An increasing fiscal deficit, deficit in the balance of payments and rampant inflation, together with disorder in political, institutional and social aspects threatened the nation's very existence.

From September, 1973 and throughout 1974, it was necessary to reorganize on all fronts, and measures were taken to this effect.

However, at the beginning of 1975, a review of the country's situation showed the need to apply new corrective measures to palliate the effects of conditions in two areas beyond our control: the increase in the price of petroleum and a sharp decline in the price of copper.

At the same time an intensive political campaign was launched by the Marxist-Leninists and by mistaken or ambitious individuals who joined together in a fruitless effort to recover power in order to reimplant doctrines which would induce us to open the way for their return.

Thus, at the beginning of 1975, a further analysis of the socio-economic situation was required. We ordered the formulation of a plan to implement the country's economic and social recovery. At the same time the Ministry of the Interior undertook the preparation of a social program to complement the economic measures.

Since every action in the economic order always affects some sectors of the population more than others, some persons criticized these measures in a constructive way, but others indulged in false declarations, setting off an intensive campaign against the program adopted by the Government. This program had been designed to create solid and stable bases for sustained recovery, and at the same time to cure the endemic ills of the Chilean economy.

One year after the economic recovery program was undertaken, I have seen that we have been able to move forward with the efforts of all Chileans who faced the challenge. Furthermore, I can state today, that we are truly independent and that we have recovered our international credibility. There is a surplus in the balance of payments, and we have sufficient reserves and foreign credit to meet any emergency; the enormous fiscal deficit and that of public enterprises have been reduced, and at the same time, the financial system is returning to normal, thereby reducing inflationary pressures.

In support of the economic measures, the social program, including minimum employment, school breakfast and lunches, low-price community built food stores, housing, etc., has achieved the goals set in every area. In this way we have been able to relieve the effects of the international economic crisis which had more serious repercussions among Chileans in low income sectors. We are well aware that in those sectors, those no longer in power have tried once more to sow the seeds of doubt, of mistrust and of bitterness. But I am sure that those who receive this negative pressure, as intelligent beings, will recognize the difference between disinterested patriotism and the desire to serve, and the use of demagogic practices in an attempt to recover what has most seriously affected them, namely the loss of power.

In this brief analysis of our present situation, it gives me great satisfaction to announce today that the goal we had set for the first, and perhaps the most difficult, stage has been reached, and that there will be a definite decline in inflation as a result of the measures to be adopted in the next phase.

In order to provide more technical information, I have requested the Minister of Finance to explain to the Nation the manner in which the economic measures shall be implemented in order to accomplish the projects which I will outline further on. The present conditions which make it possible for us to accelerate the process of economic recovery and to initiate a new phase of expansion and improvement in the standard of living, I repeat, have been made possible through the sacrifices which all Chileans have made.

The excellent balance of payments situation permits us to establish new goals to be met during the second stage. They will require modifications in the areas of credit, taxation, foreign trade and investment.

Broadened lines of credit shall be available to the productive sector, which together with foreign investment and corrective measures in the banking system, will induce moderation in interest rates.

Special emphasis will be placed on construction of low-cost housing and on the construction of new houses through Savings and Loan Associations.

During this stage of tax reform, steps shall be taken in order to distribute the burden more fairly and efficiently.

These measures will have to be studied together with the budget system in the public sector, and in any case, will go into effect next year.

In the budget analysis for 1977 special emphasis will be given to activity generating measures and to the implementation, in the public sector, of the second phase of the public sector Wage Scale modification program which will deal with both level and structure.

We shall continue to encourage nontraditional exports which have been an important factor in reaching equilibrium in the balance of payments during the second semester of last year, and the surplus of US\$250 million in the first five months of this year. All this has been accomplished while the price of copper is at sixty-one cents, and while we are meeting all of our financial commitments abroad.

The Minister of Finance will announce the manner in which the exchange rate shall be established in order to guarantee a viable and permanent value for foreign currency in the long term and which shall be adjusted according to internal prices. This measure shall be effective immediately.

These conditions will bring about a definite decline in inflation beginning in July.

Steps shall be taken to continue to encourage foreign investment. The process shall be simplified and measures shall be taken to demonstrate the safety of such investments to those who wish to create or to promote industries.

In the social welfare area, Chileans with very low incomes shall continue to receive aid until the country reaches a situation which could be considered normal given its stage of development.

With the reforms set forth here, the country is entering a new phase, one of more intense activity, higher employment and a better standard of living for all Chileans.

Timing is always basic in the implementation of economic changes. Today it is possible to do certain things which would not have been advisable only a few months ago.

Haste as well as delay in decision making have high costs to the community in terms of the standard of living and the stability of the system.

The steps taken today correspond to the objective conditions derived from recent developments in our economy that allow and justify this new phase which will represent a definite and sustained improvement in the standard of living for all Chileans.

To conclude, I wish to point out that nothing is achieved without effort, work and sacrifice.

A long road still lies ahead to reach in due time the goals set by this government in order to make of our beloved country a great, free and powerful nation, for the happiness of all Chileans united in true brotherhood.

**Failure of Protectionist Policy
in Chile
(Round Table Discussion
on Andean Pact)**

Sergio de Castro Spikula
Minister of Economy

August, 1976

The Minister of Economy, Sergio de Castro, explained the Chilean position with regard to the Andean Pact at a round-table discussion on integration organized by the Business Enterprise Development Study Center, at the Sheraton Hotel.



The following is the text of his speech:

In order to understand the Chilean position on the Andean Pact, it is necessary to have some economic background information. One of the most salient features of the Chilean economy is the traditionally low rate of economic growth. If you go back thirty or forty years and review the figures on economic growth, you will see that in that period the average rate of growth was relatively low, discouragingly low. It is also significant that since the 1930's we have not had prolonged periods of growth at relatively high rates. The periods of growth are relatively short and are followed by prolonged periods of discouragingly low rates. Let us make a projection starting with the gross national product for 1930 and project growth at the rate of 7%. A yearly rate of 7% is certainly higher than the country has usually had, but it is a rate which many countries have achieved by means of efficient and coherent economic policies over extended periods (rates even higher than these are known). Even so, 7% is a reasonable rate. If we project the GNP for 1930 at a rate of 7% per year until 1970, we reach the conclusion that the GNP for 1970 would have been two and one-half times what it actually was. As a result, if in 1970 we had a GNP equal to 100, we would have had an index of 250 (if we had been able to grow at 7%). This shows that really the political and social problems which Chile experienced in the year 1970 are explained to a great extent by the low level of growth which had created a relatively frustrating situation for the population.

The GNP increased at an arithmetical rate of 3.3% between 1965 and 1974 and the growth in production per capita for the same period was 1.3%. This means that in order to double the GNP Chile would have to wait 25 years, and that to double per capita production would take 40 years. It seems to me that, under the present circumstances, everyone would agree that no country could afford to wait such a long time for substantial increases in its standard of living. Without accelerated economic growth there is absolutely no way to achieve redistribution of income in favor of the most needy sectors of the population. It must not be forgotten that although many previous Chilean governments have announced redistribution of income as part of their policy, the 1970 census showed that 23% of the Chilean population was living in conditions of extreme poverty.

Economic Growth: Requisite for Redistribution of Income

In Chile there is an extensive middle sector. Since there is not a large high income sector from which the government could obtain significant resources in order to bring about a redistribution toward the more needy sectors, it is obvious that any attempt at redistribution —unless there is accelerated economic growth— would have to be made with the sacrifices of the middle sectors. And as the middle sector creates opinion in this country and, in fact, governs it, it is obvious that a process of redistribution which means the sacrifice of its own standard of living could not be too big. As a result, the improvement of the most needy sectors of the population would necessarily be limited. This means that within the middle sector which is being sacrificed, frustration would occur, because the people would not see that their own level of income would also be rising as a natural and logical consequence of this process. On the other hand, the poorest sectors, even though they “benefit” from the redistribution policy, also feel frustrated because the redistribution process cannot be very intensive. There would be, therefore, an almost generalized sense of frustration throughout the entire population. That is the reason why accelerated and sustained economic growth in this country is a must for this Government and for any other government. The groups which oppose the Government see this very clearly and so they try to frustrate the economic development in any way they can, even to the extent of defending positions that are definitely contrary to the national interest and which propitiate the financial strangling of our country.

Faced with the problem of breaking the pattern which has produced discouraging economic development in Chile, the present government had to develop a series of efficient and coherent policies. It was necessary, therefore, to diagnose the causes of the frustrating development during the last forty years.

Obviously the diagnosis which I am going to give is really only a sketch. In the little time that we have it is impossible to paint an exact picture, but I am sure that you will recognize the main features.

The Import-Substitution Plan

During this forty-year period, with few exceptions, Chile has followed the economic development plan known as import substitution. The basic idea was for Chile to produce locally those goods that were being imported.

The idea was that the country could develop in that way and that, by producing what had been imported, the limited amount of foreign currency usually available would be saved. The theory of the scarcity of foreign currency prospered, as a product of the crisis in 1930 which hit Chile very hard. Exports dropped to a rate far below normal, which produced a crisis in the balance of payments. At that time it was thought that this situation would be relatively permanent, thus lending validity to the import substitution theory.

The relatively forced industrialization of the country was obtained through various mechanisms. One of these was the foreign exchange rate policy. From 1939 on, the exchange rate was maintained artificially low. In terms of the present situation, the exchange rate is at \$13.80, let us say \$14. An artificially low exchange rate would be, for example, to maintain the exchange rate at \$7 per dollar. This is only a comparison, and is not meant to reproduce a situation of the past. It is useful so that you understand the relation between the exchange rate which they should have had and that which actually existed.

What was the effect of having the exchange rates at \$7 when a realistic rate would have been \$14? Obviously that policy allowed for the import of capital goods and raw materials at relatively low prices which were needed for the industrialization which was being encouraged. As a result, this policy was truly tending in the desired direction, but obviously the exchange rate not only motivated the import of capital goods and of raw materials required for industrialization, but it also motivated the importation of all sorts of goods. If the policy had been maintained, it would obviously have created a large deficit in the balance of payments. In order to avoid this, a tariff policy was applied which consisted in prohibiting or in applying extremely high duties to those products which it was thought could be produced domestically. Thus, foreign currency could be spent to import capital goods and raw materials but not to import goods and services which could be produced within the country by means of the import substitution policy. It seemed as though a panacea for development had been discovered because the balance of payments problem was solved, local production was motivated and protected against foreign competition. But all this refers to the import-substitute sector. What happened in other sectors, for example, in agriculture and in exports in general? The exporting sector lost all possibility to export because with the exchange rate at \$7 per dollar instead of \$14, they could not manage to cover their local production costs and were subject to a tax which in this case was 100%. The agricultural sector could not export either, and had to

sell locally the totality of its production. Why were the same protective measures which were applied to the industrial sector not applied to the agricultural sector? (This measure would have consisted in prohibiting the importation of agricultural products or in applying excessively high taxes to them.) The answer is that the governments in general did not want the cost of living to go up and they wanted to keep food prices relatively low for consumers and, in this way, an infrastructure could be created for industrial production at a slightly lower cost than would have existed if the prices of foodstuffs had also been excessively high. The idea then, that all Governments of the period pursued was that all of the most necessary products were to have relatively low prices. These low prices were achieved by means of subsidized imports, and by the artificially low exchange rate at which the importation of necessary articles was carried out. But the products which were not among the most necessary, that is luxury items, or things which could be done without were not viewed by the Government in the same way. Prices were permitted for these articles, no matter what they were, so as to encourage domestic production. It was thought that those products, after all, were purchased by the people who were better able to pay for them.

To the mechanisms already mentioned such as a low exchange rate, excessively high tariffs on luxury items, and non-existent tariffs on the necessary items, was added government price controls.

Effects of the Import-Substitution Plan

With these mechanisms, what happened to the distribution of Chilean productive resources? Businessmen got the message that it was unreasonable to produce necessary items, as these had low prices because of price controls, the subsidized competition of foreign products and, therefore, were not profitable to produce. It was more advantageous to produce luxury goods, since these either could not be imported or were subject to excessively high duties. As a result, their domestic prices were high and they were profitable to produce.

In this way the productive structure of the country was developed with quite negative results since the only activities which were really encouraged were import substitutions, and these were condemned to serve the home market, which was relatively small. The exchange rate policy prevented these sectors from expanding their production by seeking the international market because at \$7 per dollar they were unable to cover their local production costs. As a result the export sector—the agricultural

sector in general— saw its productive potential reduced. The only sector which was encouraged —the import substituting sector— had motivation to produce for home consumption, but was unable to turn toward the international market. Since the domestic markets were relatively small, the volume of production which they could absorb was also relatively small. Therefore, they could not apply the modern large-scale production methods whereby they would have obtained reductions in production costs.

The limited size of the domestic market was exacerbated by the fact that because these products had high tariffs, the local prices were also relatively high. Depending on whether they were non-strategic or luxury items, these articles were purchased by the medium high and high income sectors, which in our country form a relatively small percentage of the total population. As a result, the market for these industries was necessarily small. The only sector which survived this type of policy was, of course, copper, which had very high productivity. Some export sectors maintained some activity and are included in what became known as the traditional sector. From time to time, when the circumstances made it obvious and in fact practically imposed it, the rate of exchange was devalued. This would mean a momentary gain for the export sectors, but those devaluations did not generate new lines of exports, nor even expand the existing ones because the people operating in those sectors realized that the devaluation was short-lived, and that little by little, inflation would go on “eating up” the devaluation, and the previous conditions would return. In this way, then, the Chilean economic development was discouraged, paving the way for the coming of the Marxist nongovernment. The periods of bonanza for the economy coincided with increases in copper prices which occurred for reasons completely unrelated to the country’s domestic policy. Agriculture and the export sectors were in poor condition and the highly protected manufacturing industry was limited to the small internal market. Thus, Chile’s economic development could hardly have been more discouraging than it actually has been.

The Present Development Strategy

Having diagnosed the causes of the slow economic development in Chile over the years, the next step was to establish the new policy which would manage to break out of the forced import substitution system which had failed, and replace it with another plan which would achieve an effective import-substitution system and the development of exports in general, the non-traditional as well as the traditional.

The current plan, as you know, consists of a realistic exchange rate policy, a gradual reduction of tariffs in order to eliminate the excessive protection that has existed and still does exist in some industrial sectors, and the suppression of the price controls which were imposed for political purposes, maintaining price controls only in sectors where monopoly is prevalent. In areas of reasonable competition there is absolute freedom of prices. The local productive sector has seen the right signs in this policy and has begun the reallocation required for the accelerated and sustained economic development that we need in the future.

It should be emphasized that the exchange policy and the tariff policy are indissolubly bound together in an inverse relation. To explain: if a country, for example, wishes to maintain a tariff level equal to 100 percent, then there must be an exchange rate level, let us say, of 100. But if for some reason the country decides that the tariff level should be at 50 (half of the previous rates), it is also necessarily saying that the exchange rate should be for example, 200, which is very much higher than the previous rate. There is no relation of half to double (in this case it is only an example). There is, however, a relation in that a lower tariff schedule necessarily implies a higher exchange rate, whereas a higher tariff schedule necessarily means a lower rate of exchange. In this way the lack of protection which may affect a particular sector when the tariffs are lowered is compensated for in part by the additional protection afforded by what should be an automatic rise in the rate of exchange in real terms. But for the export sectors this movement of reduction in customs duties and increase in the exchange rate has positive effects in both cases. The reduction of the tariff lowers the cost of imported raw materials and the rise in the exchange rate increases the over-all return on the product exported. For this reason, numerous activities which it was thought would not be able to subsist because of lower tariffs, have not only subsisted but are exporting as well. The reallocation of productive resources is oriented toward activities which require a lesser amount of productive resources per unit of final product manufactured. This is the only means by which we can improve the standard of living and the level of consumption for all inhabitants of the country, and achieve the accelerated and sustained economic development which we require as well.

Unfortunately, this has been delayed by the world recession which, as you know, has caused a relatively strong decline in the price of copper, which is our principal source of income.

With a knowledge of the principles that I have pointed out, Chile's position on the Andean Pact is perfectly understandable.

The Origin and Purpose of the Andean Pact

According to the traditional policies whereby each country produced for a very limited home market formed by the high income sectors, with erroneous exchange policies, with hideous tariffs, and political price controls, all factors which to a greater or lesser extent exist in our countries, and with a growing tendency towards statism, the Andean Pact was a logical solution. It was expected to provide joint markets and a breath of fresh air for the process of import substitution. What was not foreseen was that the high level of protection to which the subregion aspired with respect to other countries would substitute a flow of cheaper imports (from other countries which were also generating revenues by means of tariffs) for other flows of more expensive imports (those of the members of the Subregion), which would "compete" only because intraregional tariffs would be non-existent.

The higher the common import duties, the higher the cost of this interchange in terms of well-being. Taken from this point of view, the intraregional interchange figures lend themselves to tragic errors in interpretation, since the higher growth supported by high customs barriers would generate a decline rather than an increase in the well-being of the member countries. Obviously, ideological factors have contributed to the development of this integrationist scheme which will be inefficient to the extent that the exaggerated protectionism sponsored by some of our members is put into effect.

A country like Chile, which has a very clear idea of what has caused such frustrating and weak economic development, cannot accept the commitment on a regional scale to a program which it has rejected as a failure at home.

Chile neither wishes nor intends to impose her own program on other nations; nor are we willing to accept that another country impose its program on us.

Chile has repeatedly declared its interest in integration. We are willing to make certain sacrifices, but the nature of these sacrifices must not be such as to conspire against our legitimate right to obtain the economic development required for the population.

Chile must grow at a minimum rate of 7% per year. I explained how things would have been if we had had such a growth rate between 1930 and 1970.



This would have been possible with an efficient and coherent economic policy such as the present one. The difference between the potential development that could have been attained in that period and the actual achievement has an extremely high cost in social terms, but we never hear any comments about that.

Investment: The Basis for Economic Development

The economic development of a country depends not only on efficient and consistent economic policies such as the current one, but also on another ingredient, namely investment. In order to generate the investment required for Chile to grow at a minimum of 7% per year by means of savings, the population would have to sacrifice consumption to a very high degree. (I calculate that to be about 15% of present consumption.) It would be impossible and absurd even to mention it. It is, therefore, indispensable to bring in foreign investment to add to the domestic efforts to save and at the same time permit us to reach the level of investment we require.

It is interesting to note that foreign investment not only contributes capital and capital goods, but also technology, talent, business experience, knowledge of the markets and an entry into those markets.

We are absolutely sure that in order to attract the investment we require, it is necessary to modify Decision 24 and to make it suitably flexible.

The Chilean Position

I think it is interesting to explain briefly the main issue in Chile's position. This is very important, because lately efforts have been made to convince the public that Chile's partners in the Andean Pact have deferred on many issues of the Chilean position. This has been done by attributing to Chile a number of petitions which in fact she has not proposed, but has simply backed because other countries have suggested them. Then, by saying that this is our position, they try to claim that they have yielded on many issues.

The main issues regarding Decision 24 are as follows:

The origin of capital does not define an activity as national or foreign because the capital is only one of the many factors in the production of any given product.

Chile is in favor of using the national value added when determining whether or not a product should have access to the subregional market. It should not be decided solely on the basis of the origin of the capital. We have used the example of INFORSA (Industria Nacional Forestal S.A.) at the meetings of the Commissions. They produce with Chilean lumber, Chilean labor, Chilean water and Chilean energy. What difference would it make if the machinery and the capital were foreign? (which in fact, they are not). If that were the case, there would still be no difference because the product would still be just as Chilean as it was before. Therefore, it seems to us that the origin of the capital should not determine whether a product is national or foreign. We think that the concept of the national value added should be taken into account in the present criteria. It would be absurd to assign the internal savings, which in our case are limited and difficult to generate, to the purchase of activities which are already developed in order to label them "Chilean" instead of to the creation of new sources of employment and production of goods and services.

We also feel that internal activities, which are the product of foreign investment and which are not intended for the subregional market, should be exempt from the norms of Decision 24. Some claim that more flexibility in the terms of Decision 24 would unleash fierce competition among the countries which would begin to promise higher profits for foreign investments in order to attract them to their own countries instead of to other countries. We think that this is valid argument. We have suggested that the way to avoid this is not to prevent the entry of foreign capital into the subregion, but rather to require each country that offers any special conditions or tax exemptions to foreign investors to automatically offer the same facilities to the national investors. This simple clause would put a stop to any exaggeration in the benefits which apply to foreign capital. Any country which reduces the taxation on foreign capital would likewise be obliged to do so in the case of national investment. This is the sovereign choice of each country.

We also think that the best, if not the only, way to incorporate technology in our countries is by means of foreign investment. If we force the nationalization of this investment, what will happen is that we will be purchasing obsolete technology. The foreign investor will figure that taking into account the vertiginous advances in technology, if he has 15 years to nationalize, it would be better for him to introduce technology which would be completely obsolete by the 15th year. In this way we would be using internal savings to buy obsolete technology. To think that the foreign investor will act in any other way is naïve, to say the least.

It also seems naïve to assume that the foreign investor will come to our countries, take all the risks involved, and if the investment does not perform as expected, get "Bad luck. Those are the risks you take," as an answer, but if all goes well for him, on the other hand, he is told, "Congratulations. Now you have to nationalize," or rather, sell what has been a proven success to local investors.

In November of 1974, we discussed the need to modify Decision 24. So far we have received expressions of good will which have never gone any further. Only the firm attitude of the Chilean Government has finally achieved the initiation of serious discussions on the modification of Decision 24.

Tariff Duty Levels

Another controversial aspect of the Andean Pact is the subject of tariffs. Some countries favor excessively high customs duties, which shows that forced import substitution persists even though it has obviously failed. Chile considers that there should be reasonable but not excessive protection for regional production, because excessive protection penalizes other productive sectors, and especially the standard of living of the consumers of the region. As I explained before, Chile is proposing levels of protection through tariffs which range from a minimum of 10 percent on raw materials to a maximum of 35 percent on manufactured goods, taking into consideration the problem of defining these concepts. We think that, for want of information in most cases, some people criticize these rates as excessively low. For this reason, I think it is necessary to clarify the concept of tariffs or effective protection, which is the degree of protection that the tariffs grant to the national value added, which is what really counts when we talk about protection.

Let us suppose that a given product, without tariffs, were composed of 50% of imported raw materials and of 50% of national value added. If the product in question were worth US\$1.000, for example, we would have a cost of US\$500 in raw material and US\$500 in national value added. Let us suppose that to the final price we now add a 70% tax. The value would increase from US\$1.000 to US\$1.700 for the tax. Suppose that we put a 30% duty on the raw materials. Then the cost of raw material would go from US\$500 to US\$650. The national value added would rise from US\$500 to US\$1.050 (the difference between US\$1.700 which is the final price, and the cost of raw materials rising to US\$650). This means that the protection

rises to 110 percent, which appears to be excessively high, in spite of the "reasonable" tax figures on the final product and on the raw materials.

Using the same example, but putting 70% duties on both the final product and the raw materials, we get effective protection of 70% and not 0 percent as some think. Actually the final price rises from US\$1.000 to US\$1.700; the imported raw material goes up from US\$500 to US\$850. As a result, the national value added also goes up from US\$500 to US\$850 (US\$1.700 which is the final price, minus US\$850, which is the cost of the raw materials) and consequently the effective protection goes up to 70 percent.

Let us take the example of an assembly plant in which the national value added will be low. As an example, let us look at an article with 90 percent imported raw material and 10 percent national value added. If the tax on the article were 10 percent, the final price would rise from US\$1.000 to US\$1.100; if the tariff on the raw material were 5 percent, the cost of the raw materials would rise from US\$900 to US\$945, and as a result, the national value added would go up from US\$100 to US\$155 (US\$1.100, which is the final price minus US\$945, or the cost of the imported raw materials). The effective protection is, then, 55 percent (the % increase of the national value added that goes up from US\$100 to US\$155).

These examples allow one to see that a tariff schedule ranging from 10 to 35 percent is perfectly adequate for the Chilean economy since it provides reasonable levels of protection for the nation's industrial activity.

It is absurd to accept high tariffs because they penalize the efficient non-industrial sectors and the regional consumer who has to pay high protectionist prices when cheap imports are substituted for by expensive imports from the subregion.

On the other hand, this is a threat to Chile's sovereign right to establish its own exchange policy, since tariffs and exchange rates—as I showed you before—are indissolubly bound together, and if the member countries impose an elevated tariff as they plan, they will in fact likewise impose a lower exchange rate. This would destroy the Chilean development strategy since it would prevent the export of non-traditional items and would quash the incentive which has been created to achieve greater efficiency in the remaining areas of activity.

As a matter of fact it is on record in the Commission that other members recognize that the economic policies of all of the countries differ in a great variety of aspects. As a result, it is absurd to demand that only one of the policies be identical in all countries, namely the tariff policy. If we differ on all the other policies, it is reasonable to accept that we differ on tariff policies as well. It seems to me that the insistence on high tariffs for other countries would lead to the disintegration of the Andean Pact rather than to integration. It is true that with higher tariff levels, the possibilities for each member country to have all kinds of similar industries are better because they will be protected by this high external tax. Consequently, the tendency will be that with high tariffs each country will want to have the same type of industry as the others. The best example of this is the case of the automotive industry in which in the preliminary discussions there are about forty installations requested for a group of countries which possibly may not be able to sustain more than two or three plants, speaking optimistically. Consequently, it seems to us that high tariffs will disintegrate the group rather than integrate it. If the tariffs are low, many of these countries are going to have to give up the idea of having "prestige" industries and will have to seek alliances with other countries in order to produce this type of product. Then there would be an efficient process of integration.

The other serious problem which this policy implies is that integration of the group with other countries such as the other members of the Latin American Free Trade Association (LAFTA) will be impossible. Those countries are not going to accept our absurd and inefficient conditions for foreign investment and the inefficient productivity caused by high tariffs. This group is going to become isolated from the broader groups within LAFTA. It is strange that some of the same groups and individuals which criticize the present policy to open the economy which the Chilean consumer is now experiencing, also criticize the Government's wish to insist on low tariffs for the subregion, since these low tariffs are the only effective means of protection which would defend the nation's consumers. Chile understands and respects the fact that other countries have different plans for development. For this reason we do not insist that our program be imposed on others. **Rather, we have advocated a broad tariff spectrum which would allow each country to follow the tariff and exchange rate policies which most suit their national interests.**



**Cartagena Agreement
XX Period of Ordinary Sessions**

Sergio de Castro Spikula

**Declaration of Minister of Economy
at the Signing of Protocol**

**Lima,
August 4, 1976**

Gentlemen:

It has become clear not only to the member Governments of the Andean Pact, but also to the general public of the subregion that for several months Chile has had serious reservations about the application of certain mechanisms of the Cartagena Agreement.

These reservations stem from the fact that some of the applications imply sacrifices which are unacceptable for Chilean economic development and, in our opinion, for that of the other member countries as well.

It is a fact that Decision 24 is so rigid and anachronistic that it prevents a reasonable flow of foreign capital to our countries. For Chile, and we think that for the other contracting members as well, the effect of this would be to condemn our respective populations to a low rate of development or to an exaggerated sacrifice in living standards in order to generate, by means of domestic savings, the amount of investment required to achieve and maintain the high levels of development necessary in order to guarantee full employment and well-being for our workers.

On the other hand, it is also true that the high protective tariffs for products of the subregion, as compared to those coming from non-member countries, and which some members are trying to impose, would oblige our consumers to pay high prices, thus permitting unacceptable inefficiency in production. Such a policy would eliminate the possibility of extending the process of integration to other countries, such as the other members of the Latin American Free Trade Association (LAFTA). These countries can hardly be expected to accept such a sacrifice for their consumers. Finally, it would motivate the creation of an exaggerated number of similar or identical industrial installations in each country of the subregion even though the subregion would not be able to sustain them all if a reasonable level of productive efficiency were required. The acceptance of this situation would mean disintegration rather than integration for our economies, and would squander our already scarce resources.

For these reasons, Chile has pointed out the necessity to make Decision 24 more flexible so that the area may attract foreign capital when the member countries so desire. Then the technology, managerial capacity and access to the world market which accompany investment will justify large scale production. This in turn facilitates low-cost production, a definite advantage for the subregional consumer. Such foreign contributions, and a reasonable local effort to save —so as not to require an exaggerated

sacrifice of the welfare of our citizens— will permit us to achieve the goals of economic development which are indispensable in order to solve the problems of extreme poverty, malnutrition, unemployment, inadequate or non-existent housing, and the generally precarious standard of living in which varying percentages of our respective populations are struggling.

For these reasons our country has requested that the other members of the Agreement formulate more realistic tariff policies and create more flexible import duties within a broader range, allowing each country to follow its own development policies and the allocation of its productive resources.

Until today—and based on the many official and extra-official declarations of the associated countries— we have maintained in good faith the hope that the agreements required to make the norms to which we have referred more flexible would have been adopted, and that integration would not be imposed at a cost impossible to pay. As proof of our integrationist spirit, we had planned to attend the XXth Ordinary Period of Sessions of the Commission, to be held on the second of August, which unfortunately and for reasons against Chile's will, did not take place as originally scheduled. We have been defrauded since this situation reveals the absence of the willingness and determination to deal with and resolve these matters to the satisfaction of all parties. This is also in violation of the obligation which the Commission has imposed upon itself to deal with this matter as recorded in the Proceedings of the XVI Period of Extraordinary Sessions.

There is nothing to gain by simply postponing meetings without concrete definitions that lead to a solution of the basic problems which affect the integration process. It is our opinion that, the only way to obtain the full political backing required for the smooth functioning of the Agreement is to solve these problems. The recommendation contained in Decision 100 was approved in this spirit. It was approved subject to the express condition that the basic problems already mentioned were to be solved before its being signed by the Plenipotentiaries.

There is proof that this condition had not been met before the initiation of the XXth Ordinary Period of Sessions. Chile is, therefore, obliged to go on record with a negative vote. Furthermore, we state for the record that the signing of the Protocol which has been submitted for the consideration of the Plenipotentiaries of the Member Countries is illegal and invalid. The text of this document is not the same as that of the original Decision 100 and should, therefore, have been presented to the Commission as a new

Decision, and should have gone through the entire solemn process of approval established by the Cartagena Agreement for such cases.

This declaration shall be presented to all of the proper Authorities.

**Report on the State of
Public Finance**

Jorge Cauas Lama
Minister of Finance

November, 1976

Introduction

As Minister of Finance, it is my duty to inform the public on the state of the Public Treasury and on the country's economic situation.

It is important to begin by affirming that the economic situation which we observe today is the result of an economic policy that has been applied systematically since the end of 1973.

The main objective of this economic policy is the use of the resources available to this country in the most efficient way possible, and the assurance of future growth.

Traditionally, in the Chilean economy, resources were used basically by the least productive sector and were allocated according to central decisions. According to the present economic policy, it is preferable that the private sector channel resources and that the market be the basic determining factor in allocation, reserving to the State the correction or elimination of distortions which may occur in the functioning of the market, without, however, trying to replace it.

Also by tradition, the Chilean economy has been sustained by programs featuring a high degree of protectionism. The present economic policy contemplates greater openness to the exterior with the resultant increase in activity and well-being normally associated with a more open economy.

In this context of long-term goals, the Chilean economy has been faced with very difficult conditions since 1975, as a result of the crisis in the world economy.

In order to face these conditions at the beginning of that year, a short term economic policy was adopted, which would allow an adjustment of the level of economic activity to the restrictions in resources that the country was undergoing at every moment. This is an unavoidable task of the economic authorities, regardless of the long-term policy which is in force.

Toward the end of 1975, notable progress had been made in both aspects. The Economic Recovery Program had achieved its aims. The levels of economic activity had been adjusted to the external conditions the country was facing, creating at the same time stable bases for future economic development.

This permitted the formulation of a set of objectives for the year 1976, the achievement of which would mean an improvement of the economic situation for the country. It is important to emphasize that this concept was not based on a favorable change in world economic conditions, but rather on the realistic conditions under which the economy was already operating.

In the Report on the State of Public Finance for 1975 four basic objectives were proposed: reduction in the rate of inflation, the assurance of equilibrium in the balance of payments, the gradual recovery of the levels of production and employment, and the necessity to maintain and to consolidate the process of basic legal reforms required for the development of the long-term economic policy.

This set of goals is characterized by its coherence and realism. It constitutes the maximum the country could achieve, given the restrictions the country was facing. It is very satisfying for the Government to be able to state that the goals proposed to the country one year ago have been fully accomplished, allowing us to look to the future with greater optimism.

II. The Evolution of the Economic Situation during 1976

With this analysis of the evolution of the various sectors of the Chilean economy in the year 1976, we intend to show the consistency of the measures adopted and their results, in relation to the role assigned to each sector in the long-term development program.

The Fiscal Situation and The Public Sector

In Chile, the State has by custom been assigned a practically monopolistic role in the allocation of resources.

The mistrust in the performance of the economy based on free operations in the market led the State to intervene progressively both directly and indirectly in the allocation of resources. This was translated into considerable waste of the scarce resources available to the country, in permanent financial imbalance, and neglect on the part of the State of the activities which are proper to it.

In the present development programs, the State has been assigned a subsidiary role in matters of production and an active role in the activities which pertain to the State, especially in social programs which deal clearly in redistribution and which tend to eliminate extreme poverty.

This meant a significant reallocation of public spending for the sectors which have priority in action on the part of the State, together with a significant reduction in the size of the public sector.

In 1976, the level and structure of public spending were adjusted in conformity to amounts compatible with the requirements of the long-term policy. Public spending reached 27% of the GNP; of this amount, 5.3% corresponds to payment of the foreign debt. The deficit is 2.7% of the GNP. With copper at a price similar to that for the last ten years, there will be a surplus in fiscal operations.

The process of reducing the size of the public sector has been continued since 1973 when Government spending was 43% of the GNP with a deficit in the order of 24% of the product.

It is important to point out that the transformation of the public sector had to be carried out quickly as an indispensable means to achieve a high and sustained rate of growth in the near term under stable conditions in the internal and external sectors. The effect of the fluctuations in the world economy on the economic situation in Chile were not a cause of the adjustment in the fiscal sector; they only conditioned the rhythm of this adjustment.

The favorable external conditions which the country faced at the beginning of 1974, together with the natural difficulties associated with the initiation of a reduction and reallocation process, explain the slowness at the beginning of the adjustment process.

The changes in economic conditions produced in 1975 obliged us to accelerate the reduction process. The necessity to achieve adjustment to the new conditions in a very short period of time obliged us to emphasize steady reduction rather than reallocation of public spending.

The equilibrium achieved in 1975 permitted us to continue in 1976 the process of gradual reallocation of spending in favor of the priority sectors. The higher resources received by the Government as a result of the up-trend in the levels of activity were not used, nor will they be used in the future, to increase the real level of fiscal spending, but they will permit a reduction in taxation.

Balance of Payments and Foreign Commercial Relations

Traditionally the country has placed its relations with other countries on a protectionist basis which permitted the country to industrialize and to achieve self-sufficiency in the productive area.

This caused the development of an inefficient monopolistic industrial sector with high consumption of imported intermediate materials. Agriculture and non-traditional exports remained unprotected.

The policy with regard to foreign capital prevented the entry of a significant amount of foreign resources to complement efforts to capitalize in the development of productive activities.

The country became more and more dependent on other countries, and had to resort increasingly to foreign indebtedness in order to maintain its levels of consumption and investment.

The present development program assigns a substantially different role to the foreign sector. It is basic in order to achieve the efficient use of the resources, that the internal productive activities begin gradually to face foreign competition. This presupposes a relatively low level of protection, similar for all productive activities.

A policy open to foreign capital has been proposed to permit foreign resources which can develop productive activities under conditions similar to those of internal capital. This is valid except for those sectors which because of their special characteristics, have been reserved for internal capital.

When the policy began in 1973, the country was faced with a crisis in foreign trade. Even though the price of copper that year reached US\$1.11 per pound, in 1976 dollars, the commercial balance showed a deficit of approximately US\$340 million. The foreign debt had been renegotiated, with payments deferred to future years, and the country did not possess the minimum reserves required in order to import the most urgent necessities.

In 1976 there will be a surplus of US\$339 million in the commercial balance, with copper at US\$0.65 per pound and service on the foreign debt over US\$860 million. At the same time, and for the first time in many years, the level of the foreign debt has begun to decline.

It is important to point out the magnitude and the transcendence of the adjustment which has been achieved.

The country has reorganized the balance of payments and recovered adequate reserve levels to meet extremely unfavorable external conditions.

This process has been carried out together with a policy to gradually lower the tariff duties, while allocating a substantial amount of funds to payment in full of the foreign debt commitments.

The financial solvency which has been achieved has allowed us to conduct our foreign relations on a strictly commercial basis. The country's sovereignty is not at stake because of the fact that foreign capital is brought here to produce, but there is no doubt that a country does compromise its sovereignty when it must resort indiscriminately to foreign indebtedness because it does not possess the resources required to finance its own imports.

The opening of the economy to the outside and the adjustment of the balance of payments were proposed from the beginning of the economic program as the basic requirements in order to reach the goals that this program had set. The policies proposed have been carried out gradually and consistently. As a result of the unfavorable situation of the world economy, it was necessary to make certain adjustments such as the devaluation of the rate of exchange in 1975, and the revaluation of the peso in the middle of 1976.

These measures, which were misinterpreted as an abandonment of the foreign trade policy, had just the opposite effect. That is to say, they were to guarantee the achievement of external balance and the opening of the economy to the exterior.

Activity and Employment

Until 1973 the Chilean economy was stagnating and unable to generate an adequate level of new jobs.

This was caused basically by the unproductive use of resources in the fiscal sector and the allocation of a significant portion of resources to the import-substitution industrial sector which, because of high cost, was unable to compete outside.

The lack of a capital market and fixed interest rates prevented significant growth in the level of savings. All this, together with a negative foreign investment policy, did not permit adequate growth in the stock of resources.

The present development program is designed to alter substantially these conditions, so as to guarantee a high growth potential for the Chilean economy on sound and realistic bases.

However, the first stage of this process of reallocation of the country's resources from the public sector to the private sector and from the inefficient industrial sector to the agricultural and exporting sectors, causes temporary disuse of resources, with negative effects on the levels of activity and employment.

It was also necessary to allow the economic units to adjust their artificially high employment rates so as to return to normal levels of production.

The decline observed in the levels of activity and employment at the beginning of 1975, was the result of the adjustment measures required by the long term policy.

The tight restriction of resources that the country began to feel at that time required an adjustment of the level of economic activity to the new conditions. This caused additional declines in production and employment.

The success of the economic recovery program permitted a slight but sustained recovery in the levels of activity in 1976.

The equilibrium achieved in the fiscal sector and in the balance of payments provided more resources for the economy, according to the basic lines of the development program.

The symptoms of recovery demonstrated in the level of employment are concurrent with the rhythm of recovery seen in economic activity.

According to figures available for the Greater Santiago Area, employment has increased steadily, having reached its lowest point in 1975. The case of industrial production is very similar.

In spite of this, the unemployment rate according to figures available for Greater Santiago, continued to increase during the first semester of 1976,

reaching a rate of approximately 19%. This is explained by the increased rhythm of growth in the labor force—especially among women—over and above the growth in employment.

In the third quarter of 1976 this situation is reversed, with a rate of about 17% in Greater Santiago.

We must point out that on a nationwide level, the unemployment rate is substantially below that of Santiago, since unemployment in rural areas, which depends on agricultural and mining activities, is relatively inferior to unemployment in urban areas.

Money and Prices

Since the decade of the 1940's, the Chilean economy has experienced permanent financial imbalance which causes inflationary pressures.

Massive price-fixing worsened the negative effects of inflation, producing serious distortion in relative prices, which originated irrational allocation of productive resources.

The achievement of economic stability was cited at the outset of this program as a basic condition for the long range development expected for the economy.

The correction of internal financial imbalance began at the end of 1973, when the economy was on the verge of hyperinflation. The basic cause of this was the deficit in the fiscal sector and the public enterprises, on which we commented earlier.

In 1974, inflation was reduced to 375.9%, in 1975 the rate dropped to 340.7%, and this year it shall be reduced to approximately half of that of the previous year.

As in other areas of the economy, the goals set for control of inflation have been accomplished. In some sectors people are not clearly aware of the importance of these achievements.

In a country with more than thirty years of inflation, a series of mechanisms and habits had been created and established as a means of protecting the various sectors from the effects of inflation which, however, only reinforced and fomented the inflationary process. The reduction of infla-

tion as high and as persistent as that known in Chile, is a much more arduous task than the reduction of moderate inflation.

This process was even more problematic because of the demonitization of the Chilean economy, as a result of the maintenance of excessively high rates of inflation over such a prolonged period. This causes the monetary effects of slight internal or external imbalance to bring about substantial changes in the amount of money, with the resulting effects on the stability of the system.

These achievements permit us to state that the year 1976 is a significant milestone in matters of inflation control.

Objectives of the Economic Policy for 1977

The economic policy undertaken at the end of 1973 has permitted us to rectify the abnormal economic situation which existed when the present Government assumed control, to overcome successfully the effects of a world crisis which affected the country very seriously, and to create the basic conditions for the social and economic development of the country.

The year 1977 and those which follow shall be characterized by an accentuation of the conditions for economic recovery and internal as well as external stability that were observed in 1976.

An organized and coherent economic policy, such as the one we have been applying, and which is already beginning to bear fruit, cannot be irresponsibly altered for the purpose of obtaining spectacular short term results, which are short-lived and very costly in terms of a loss of permanent well-being for the entire population.

The objectives of the economic policy for 1977 do not differ in quality from those of 1976.

The control of inflation will be stressed even more, and higher levels of activity and employment shall be achieved, while continuing to maintain normalcy in the external sector.

The Fiscal Situation and the Public Sector

The equilibrium achieved in the fiscal sector shall not be altered.



The additional resources acquired by the Government as a result of the improved levels of activity will permit us to achieve more normal levels of expenditure in 1977 in some sectors.

The budget contemplates an improvement in the level of wages in the public sector and significant real increments in spending on housing and the infrastructure.

Fiscal spending in directly productive activities should continue to decline.

The process of internal reallocation of expenditure in sectors such as education and health should increase so as to assure that the greater proportion of resources is channeled toward the sectors most in need of them.

It is important to point out that the level of fiscal spending reached as a percentage of the GNP is adequate, and should not be altered, regardless of whether the external conditions of the country improve significantly.

Balance of Payments and Foreign Relations

The country's foreign trade situation for 1977 does not differ significantly from the present one. It does not seem reasonable to assume that the price of copper will rise significantly above the present level, and the country must face the foreign debt due in the amount of US\$ 900 million. The effect of the policies in force with regard to foreign trade will allow us to be better prepared to face unfavorable international economic conditions should it be required.

In 1977 we will be able to finance a higher level of imports than in 1976.

We will be able to meet foreign debt commitments without the need to resort indiscriminately to further foreign indebtedness. On the contrary, the foreign debt policy shall continue to be conducted on the basis of the long-run profitability of these resources.

The international reserve policy to be followed will permit the country to face future fluctuations in external economic conditions without sharp alterations in the level of internal activity.

The exchange rate and tariff policies tending toward the opening of the economy to the exterior shall continue.

Activity and Employment

The levels of activity shall continue to increase gradually, but systematically.

Unless external economic conditions change substantially, a very rapid reactivation process is incompatible with the maintenance of external equilibrium, and so the reactivation could not be permanent.

The level of employment shall continue to rise as the economic activity recovers, which will allow us to reduce gradually the temporary programs designed to absorb unemployment.

It is important to point out, however, that in the medium run there will still be relatively high rates of unemployment in the economy.

The traditional inefficiency of various productive sectors, the low rates of investment and low investment productivity created an economic structure which was incapable of generating productive employment for the labor force.

Only in the medium and long run, and insofar as the process of reallocation of productive resources is consolidated and high rates of investment in highly productive sectors are achieved, will the traditional problem of unemployment in the economy be permanently solved.

Money and Prices

As we have pointed out before, the year 1976 is a landmark in matters of inflation control.

The Government shall continue inalterably its policy to control elements which cause inflation.

Equilibrium in the fiscal sector and the systematic reduction of deficit in the companies in the public sector and in the Savings and Loan Associations will guarantee the end of the long history of inflation in Chile.

As we have pointed out, the characteristics of the Chilean economy make the control of the inflationary process particularly difficult and slow. However, the maintenance of a policy which acts on the causes of the process, and not on its symptoms, assures the achievement of the final goal.

The Government has been consistent in the application of an economic policy which we believe is the only one that will permit us to achieve a high level of well-being for all Chileans. The Government has also been consistent in pointing out to the country the cost of this policy and the benefits that can be expected from its application in the short, medium and long term.

It is very easy to promise spectacular and immediate results. But experience teaches us irrefutably that the cost of adventures in economic policy inevitably has to be paid and that cost is infinitely superior to that produced in the transition toward a more realistic and less discretionary policy. This sort of policy, achieved by effort, is the only one that guarantees a stable, fairer and more prosperous social system.

**Latin American Association
of Financial Development
Institutions**

Sergio de Castro Spikula
Minister of Finance

March 29, 1977

The Seventh Meeting of the Latin American Association of Financial Development Institutions opened on March 29, 1977. On that occasion the Chilean Minister of Finance made the opening address. He spoke on the basic principles of the economic policy of the present government, especially in terms of allocation of resources, income distribution and stability and growth. The text of the address is as follows:

Introduction

It is an honor for me to open the Sessions of the Seventh Ordinary Meeting of the General Assembly of the Latin American Association of Financial Development Institutions. I would like to take this opportunity to explain the basic principles of the economic policy of the present Chilean Government.

Given the objectives pursued in matters of allocation of resources, income distribution, and stability and growth, many have mentioned the existence of an economic trichotomy. However, I am sure that if we exaggerated the neglect of only one of these objectives, we would run the risk of a serious conflict in the achievement of the other two. There is no doubt that in the economic history of our country, the tragic errors in economic policy committed over the last decades represented a serious lack of attention to the allocation of resources, thus transforming the objective of redistribution of income into pure rhetoric, while stability and growth were impossible to attain. The exacerbation of these erroneous policies during the Popular Unity regime led to economic, political and social chaos from which we had to be rescued by the Armed Forces.

A. Subsidiary State and Allocation of Resources

An indispensable requisite for the achievement and maintenance of an adequate standard of living for the population is a productive structure capable of sustaining and backing up the work of the economic agents with a system which permits the type of management that will provide a stable economy. In this respect, we are certain that Government must establish norms and take direct action in order to assure fair distribution of income. The most effective way to achieve this is through tax mechanisms and the allocation of public spending, rather than by undue interference in the market, which is the best system for the allocation of resources.

Perhaps it would be worthwhile to pause for a moment to analyze what we understand by the subsidiary role of the State. It is clear that at a particular

point in time, a situation may exist in which the area covered by what is understood as the subsidiary role of the State is much broader than what it is thought it should be. The job of the economic authorities is to create conditions so that either directly or indirectly (as is most obviously the case of the sale of public enterprises) incentives are built into the system, so that the private sector feels motivated to participate in an ever broadening variety of activities. There is little reason to doubt that the process towards statism began in our country nearly forty years ago with the creation of public enterprises with their own exclusive tax system; by the granting of preferential treatment to foreign investment as compared to national investment which was out of all reasonable proportion, and which led to special mechanisms for participation in these businesses such as mixed enterprises and in extreme cases, expropriation; the creation of semi-public financial institutions with a monopoly in the use of certain clauses, for example, the Savings and Loan Associations with respect to the indexation system; and finally, many other actions which kept our private businessmen and certain smaller foreign investors from participating in basic activities in the productive structure. For this reason, we understand that we are creating, not only in fact, by means of passing enterprises directly into private hands, but also by right, a subsidiary State, which we see reflected in profound changes such as the reforms in the areas of taxation, tariffs and banking, as well as in the Law of Financial Administration of the State, and the Foreign Investment Statutes, to name the fundamental instruments that govern economic activity in our country.

For this reason Chile, in view of its role as a subsidiary State, cannot and should not withdraw from the management of the internal economy. Chile is giving ample proof of being an integrationist and "Americanist" country. Foreign trade continues to grow; economic interchange with our Spanish-speaking brothers has increased and we hope it will continue to do so based on solid principles capable of maintaining this growth. The norms for foreign investment guarantee fair, equitable and non-discriminatory treatment with respect to local businessmen. Geographical integration through the creation of a large infrastructure is also convincing proof of the openness which characterizes this Government.

B. Income Distribution

Much has been said about the distribution of income. However, not one of the critics of the current system which, it is claimed, will lead to eventual regressive distribution, has paused to consider two of the system's fundamental aspects. We have already mentioned that carelessness in the pur-

suit of an objective can lead to destruction of the end itself. There is no doubt that in order to distribute, there must be something to give out. It is not strange that the very complexity of many situations makes the one who is analyzing lose perspective and distract his efforts, giving attention to other problems, implying that the essential is under control. However, it is no less strange that as a result of these efforts which had neither direction nor purpose, the analyst has never even questioned the essential and the obvious of the situation. In 1973 Chile was an exhausted country, socially and economically destroyed. This situation was nothing less than the result of an absolute lack of perspective and projection.

Innumerable measures mistakenly called means of redistribution were undermining the basis of society, that is, its social harmony. Together with this, the ever-widening breach between the demand for necessities and their availability was increased by these measures that only seemed to redistribute poverty and hatred. This point is one which the critics of the present system have always omitted from the framework of analysis.

The second aspect which has been ignored in the opinions published on income distribution, is related to the superficial level of the focus of the analysis. The distribution of income is the result of different variables, some of which are the direct concern of Government. It is really surprising that those who express serious concern for this matter have said and analyzed so little about the serious efforts in matters of allocation of public spending that has been used to improve the activities such as the milk program, child nutrition, the National Scholarship and Student Aid Society, and the creation of other projects with similar or even larger scope, such as the Training and Employment Fund, the creation and revitalizing of Kindergartens, the Minimum Employment Program, the equalizing of the family allowances for dependants of workers and employees, the housing programs and others for the express purpose of improving the standard of living of the most dispossessed. A convenient lapse of memory permits some to overlook the fact that according to the 1970 Census, 23% of the Chilean population lived in utter misery in spite of the fact that from 1965-70 Chile enjoyed the highest copper prices in history and unprecedented foreign political and financial support. What was not done during long periods of relative prosperity is expected to be accomplished now in a short period, and at a time when the country has had to face the worst world economic crisis since 1930, and when we have just emerged from the destruction provoked by the former Government in its attempt to Sovietize our country.

It is also strange that no one mentions the nearly total annulment of the vast and confused system of tax and tariff exemptions whose direct beneficiaries were not exactly those who comprise the poorest sectors of our country. It is surprising too, that no one refers to the fact that, as a result of the impartial framework created by the market, today we have a clear and precise subsidy system basically directed to the hiring of labor and to efforts to develop specific geographic areas of the country. Formerly, because of the subjective nature of the various economic relations, there was an accumulation of hidden subsidies which were highly regressive in nature.

Only when these two aspects have been taken into account is it possible to speak of income distribution in an objective way.

C. Stability and Growth

The seed of sustained growth takes hold amidst harmony between efficiency goals and income distribution, but the consolidation of progress in these matters requires, among other things, a stable financial framework which avoids exaggerated fluctuations in economic activity as a whole.

Every financial policy must produce coherence among the three main sectors—the foreign sector, the monetary sector and the real sector. However, coherence in these sectors alone is not a guarantee of stability; there must also be sufficient flexibility so as to prevent imbalance in some sectors from causing serious disequilibria on being passed on to the others.

In matters of macro-finance, the effort has been concentrated on creating the conditions for providing Chile with a stable financial structure.

In the foreign sector, the purpose of the exchange and tariff policies has been to vitalize the entire productive area and to guarantee consumers access to goods and services at reasonable prices, while correcting the serious distortions in the structure of relative prices. In this way, the growth of non traditional export activity has gradually been freeing the balance of payments from the influence of sudden variations in the price of copper. A more flexible foreign sector, really subject to economic policy guidelines, has developed. There are still some rigidities and we cannot fail to mention the magnitude of the service on the foreign debt which is in the order of US\$900 million per annum for the 1976-81 period; that is to say, for 1977, about 8% of the G.D.P.

From this point, through adequate management of international reserves, of the income from copper, and from the continuity of a policy which favors an opening to foreign trade, a sector can be created in which the economic authorities can meaningfully create policy guidelines.

Substantial changes, from the elimination of controls on the interest rate and credit, to the creation of an institutional framework for the banking system which permits financial intermediaries to function as they should, have been introduced into the monetary sector where the spectrum of activity is perhaps the broadest. With regard to interest rates and credit, we must not fail to mention that permitting real market factors to determine their own levels and distribution has been one of the greatest achievements in matters of allocation of resources. Systems which exercise direct control of these variables become irremediable growth-retarding factors and cause regression in the distribution of income. It is sufficient to recall that interest rates arbitrarily established by the authorities at levels which did not even compensate for inflation permitted those same authorities to distribute among their friends the scant savings generated by the public. Under this system many quick fortunes were amassed by certain individuals and groups who recall those times with nostalgia. Those who needed credit, but who had no political strings to pull, could only resort to the black market for credit at usurers' rates, many times converted into abuse by those who enjoyed access to cheap official rates. There is no usury worse than that generated by systems which distribute the resources of the community by means of pressure and personal involvement, without reflecting the true value of these resources. It is usury for those who invest their savings at the disposition of the system and for those who need the credit and are willing to pay its true price, but cannot obtain it.

The extension of credit on the basis of real prices has permitted the management of money which, although still lacking the flexibility and the effectiveness really required, is based on impersonal mechanisms of which the public is fully informed. Today, by means of instruments issued by the Central Bank and the Treasury Department, financial management tools are available that had been virtually non-existent during these last periods.

There is no doubt whatsoever that the creation of a legal framework for the financial system has brought about the revitalization of one of the most important activities in a modern economy. Financial intermediaries must exist in every economic program which has as one of its objectives the best use of national resources. It is within this system that good ideas and the

availability of funds to transform these ideas into deeds are found. The risk should be measured and weighed in all dimensions by savers as well as by investors. They, and only they, should be the ones who profit by or lose out on the final results. This is the basis of an economy designed to achieve high and sustained rates of growth. There can be no other way, because if the Government guarantees irrational risks, the moment will not be long in coming, as occurred in Chile during the previous administration, in which the resources for transforming good ideas into concrete facts have already been squandered in an effort to maintain alive an accumulation of activities and situations which have proven to be erroneous.

There is still a great deal to be done in this sector. The economy must recover as soon as possible the normal levels of real cash balances. This can be achieved as the rate of inflation diminishes in such a way that the cost of maintaining this asset will be lowered. The tendency of each one of these variables points toward a quick recovery in the monetary sector. But at the same time, we must take additional steps to create a legal framework for the system itself and the monetary policy as such. It is important to open the banking systems so that those who are specialists in this complex field are those who in fact occupy executive positions. The legal reserve requirements and reserves are still high. When the time is right, therefore, adequate measures shall be taken.

The thorough going corrections in the foreign trade and financial sectors have included, both directly and indirectly, positive modifications in the real sector. It is by means of a realistic exchange rate, limited customs duties, and a policy of real prices and interest rates that an economic infrastructure can be established which is capable of maximizing domestic saving and of directing resources to the investment sectors that are comparatively advantageous for the country. At the same time, there are management variables proper to the Government in the real sector which make it indispensable to refer to the basic aspects which have inspired policies on public revenue and spending.

In the case of the public sector, it is necessary that the increased flexibility in the finances of the sector be consistent with the objectives of allocation of resources, income distribution and reduction in the size of the public sector. Obviously, the flexibility sought means changes in both the structure and the level of revenues and expenditure in the public sector.

With respect to the structure and level of income in the public sector, the measures which have been adopted should be classified according to the principal sources of income.

With regard to tax revenues, the principal measures taken are those dealing with implicit and explicit distortions from these sources of income. Thus, for example, and in relation to implicit distortions, the tax reform has, in fact, brought about allocation of resources fundamentally based on the market mechanisms, by means of the elimination of innumerable exemptions, thus preventing obligatory prior investment, whether in the public sector itself or in the private sector.

As for the elimination of explicit distortions, it should be recalled that as a result of the economic legislation of previous governments, many regulations earmarked the resources from certain taxes or from part of general taxes to certain activities and/or regions. However, Decree Law 155 of 1973, ordered the first general repeal of this type of obligation, which had only prevented flexibility in the management of the national public treasury and therefore, in financial policy.

From the point of view of public income (and of public spending as well), the Financial Administration Law (D.L. N.º 1,263) signifies the total repeal of this type of regulation and puts emphasis on the principle of non-earmarking of public income.

The positive effects of tax reform on the entire business sector (basically the private and public enterprise sector) should be mentioned. Significant modifications such as indexation meant the solution of serious problems and financial distortions in the national business sector, so that payment of taxes on artificial profits have been avoided, and the debt-equity ratio based solely and exclusively on the tax system has been corrected. Serious vertical integration problems have been solved with the application of the value added tax; a rational drawback mechanism has been designed; the reform of the Stamp Tax Law and Decree Law N.º 455 have eliminated serious distortions which were generated in the financial system among the various instruments, thus eliminating artificial preference of certain types of instruments and maturity structures.

With regard to the policy on income of institutions in the public sector, regulations or situations have been created which directly increase or motivate investment.

In all those sectors which finance or which exercise financial functions, a series of norms have been issued ranging from regulations (regulation of titles, for example, in housing and agriculture) to an improvement in the

systems of recovery and maintenance of capital, basing part of the growth in these activities on their own income-generating capacity.

The achievement of greater flexibility in the structure and level of public spending has brought about countless profound changes.

Parallel to the correction of the distortions on the revenue side, identical measures have been taken with regard to public spending.

The legal basis for this is to be found in the State Financial Administration Law, D.L. 1,263.

There it is established that there are no predetermined expenses as a percentage of revenues or as a percentage of the total expenditure in the budget, which concedes a significant degree of freedom in matters of fiscal policy.

Perhaps the greatest margin of flexibility in matters of public spending stems from the effort to define which activities a subsidiary State should perform. The concept of the role to be played by the State has meant significant reallocation of resources and a decline in the total expenditure level.

As an indicator of the process of reallocation in public spending, it is worth noting that fiscal spending in the social area as a percentage of total fiscal expenditure reached its highest level ever in 1977.

Additionally, as was indicated in the section on income, the policy applied here is to control the use of foreign debt in the direct financing of public spending, so that in most cases the payment of the credit must be made with resources generated from the investments themselves.

It is important to mention that there are huge sectors in which the State, without changing its role, can in the near and long term, add a high degree of flexibility to fiscal policy and likewise to the economic systems in general. In order to do this, functions must be defined independently so as to generate systems which present a higher degree of financial self-sufficiency. Within this program we must point out the sector of Health, Education, Housing and Welfare. The point is not to spend less than what is allocated to those sectors at present, but rather to defer its cost in time for the agents and beneficiaries, thus generating a financial system capable of improving the use of these resources, of maintaining the present level of

spending and eventually, of becoming one of the principal sources of growth in the benefits granted by this large subsector within the Public Sector.

The advances achieved in matters of reallocation and reduction in public spending are considerable. However, it is necessary to point out that the task is not complete and that there is still much to be done.

To sum up, a set of measures has been applied to organize the public sector, consistent with the objectives of income distribution and reallocation of resources so as to obtain a flexible public sector, and moreover, with automatic stabilizers which help to avoid large fluctuations in the rest of the economy (especially in the real and foreign trade sectors).

Some of these built-in stabilizers consist in certain public spending programs such as the minimum employment program, the direct tax system and certain development laws.

D. Economic Development

By economic development we mean the harmonious balance of objectives.

Notable progress has been achieved in the objectives set forth in the programs. The conditions for internal and external stability, measured by the decline in the rate of inflation and the improvement in the balance of payments situation (with a surplus of US\$459 million in 1976), as well as the favorable tendencies which are observed in the various sectors of the economy, clearly demonstrate this to be so. During the year 1976 and, especially, in the second semester, there is a significant increase in the wage and salary index, a notable decline in the rate of unemployment (13.6% in December of 1976, after having reached as high as 19%), and reactivation in the productive sector of the economy (especially in agriculture and industry).

These are the characteristics of the economy which have allowed us to continue to adopt additional measures, such as the revaluation of the peso, the lowering of the legal reserve requirement, in taxation, and in the social security taxes paid by employers, and which tend toward continued adjustment, by means of the economic policy of the rate of activity and employment and the over-all conditions of the economy, and by means of which we will reach the goals established for economic development.

Higher levels of production are achieved through the improvement of the allocation of our productive resources; high rates of growth are sustained with the improvement of human resources and physical capital and by growing rates of domestic savings. The fruits of this are a better standard of living for the population and the achievement of an equitable distribution of income, so that all of our citizens may participate in the progress which the country is to achieve, and is achieving.

Responsibility in asking and responsibility in giving are the essence of the seriousness which should inspire what we all long for so ardently —to make Chile a great nation.

**Report on the State
of Public Finance**

Sergio de Castro Spikula
Minister of Finance

January, 1978

I. Protectionism and Statism, Causes of Economic Stagnation

The administrative management of the country under the Popular Unity Government led to a profound social and economic crisis. In the purely economic aspect a thorough analysis of those three years of government leads to the conclusion that there were no changes in the orientation of the political economy of the country with respect to previous years, but rather, the degree in which these policies were applied was increased. Thus, the crisis which had been in the making for half a century flourished in its full magnitude.

In the decade of the 1930's, the idea of inducing forced industrialization of the country by raising import duties was introduced. This was the origin and the basis of a development program that was inappropriate for a small country such as ours. An analysis of the repercussions of the rise in tariffs on imports leads us to the conclusion that this was the fundamental cause of the stagnation in this country in recent decades. The exchange rate fell as a result of this measure, thereby decreasing exports. The high protective tariffs granted to import-substitution industries caused an immediate reallocation of national productive resources. This meant less production of necessary goods, as was the case of agricultural products, in favor of greater production of luxury items which formerly had been imported. Naturally, a small economy which closes itself to international trade faces the problem of the limited size of its own market. Many products were no longer attractive for such a small market. The State began to substitute for private enterprise in the most varied areas of the economy. The very inefficiency of the companies created led to the necessity for credit creation to finance the deficit. An attempt was made to conceal the resulting inflation by fixing the prices of a large number of goods and services. Price fixing led businessmen to look for guaranteed prices which would cover the cost of undertaking new activities. As a result, we could not make use of our comparative advantages in relation to other economies in the world, and state action gradually replaced private initiative. Controlled prices led to poor allocation of resources. To add to this, inflation, which has already become chronic because of the necessity to finance enterprises and because of political price fixing, finally minimized the role of the market in the orientation of economic activity.

Throughout this period until 1973, fiscal expenditure, state participation in production and the coverage of price controls, etc. continued to grow. Since no importance was given to the market in resource allocation, what did it matter to disturb its functioning even more by inflation? Thus the

different pressures which led to state intervention in price fixing, in the use of productive resources and in the absorption of the unemployed which the economic inefficiency had produced, in the final balance were financed by means of inflationary money creation.

Who can fail to recognize these same tendencies which had prevailed for over fifty years, and which were only more exaggerated in the economic handling of the three years of Popular Unity Government? Thus, in terms of results, what already existed became worse. Between the years 1950 and 1970, per capita income only increased by an average of 1.3% per annum, and the average rate of inflation reached 32.3% during the same period. In the years 1972 and 1973, the Expenditure of the Gross National Product per capita dropped by 1.9% and 5.3% respectively. Inflation reached a rate of 163.4% in 1972 and around 1,000% in 1973. The extent of state control was reflected not only in an increase in Fiscal Spending from 27% of GNP in 1970, to 43% of the GNP in 1973, but also, and it is necessary to emphasize this, price fixing became generalized, and so did the controls on marketing channels, and the quotas on production, imports and exports. The State acquired control of an immense percentage of the land and of 464 companies, not to mention the large affiliates of the Development Corporation (CORFO).

II. A New Economic Order

With this analysis in mind, the Government designed an Economic Development Program. Our problem at the end of 1973 was not to return to historic rates of inflation, or to historic levels of State participation, and to the traditional inefficiency and awkwardness of the economy.

The explanation of the social crisis does not lie in the last three years of poor government. These were rather, a result of various decades of unfortunate management of this country, of our permanent status as a developing country, with 22% of the population in extreme poverty. The basic solution to our social problems lay in liberating Chile from being the test tube for totalitarian and socializing ideologies which resulted from the lack of prospects for the future, or in overcoming poverty or in guaranteeing individual freedom and economic well-being, which would have resulted from policies which would have allowed the country to grow and to incorporate the entire population into a way of life in keeping with the standard of living which modern technology and our country's resources permit.

The structural reforms which have been implemented are in response to this objective. Today, in this respect practically all of the basic measures have been taken. From a tariff structure among the highest and most distorted in the world, we now have a maximum of 25% and a minimum of 10%. In line with tariff policy outlined since the beginning of this Government, and in accordance with the announcements which have already been made, a single tariff of 10% has been established and will be in force as of July of 1979. In this way the most basic obstacle for growth in this country has been eliminated, laying the groundwork for the future strategy. At the same time, government spending has been reduced from 43% of the GNP in 1973 to 28% in 1979. Of the 464 companies which were not strategic but were under state control in 1973, 394 have been sold or normalized. The market determines the price of goods and services in general in the economy, including the allocation of savings, thanks to the profound modifications in the national capital market. Public investment projects are decided upon according to an evaluation of their ability to provide social returns.

The conditions for optimum allocation of the country's resources exist and the bureaucratic "red tape" which prevented Chileans from making better use of business initiative has been minimized. The State has stopped using the tools of economic policy which it controls to subsidize the growth of some productive sectors at the expense of general economic growth. Within the new development framework we are not trying to impose preconceived ideas about the structure of the economy. Rather, we try to create the conditions so that the structure is adapted to the country's resources and in that way it is the economy as a whole which grows consistently at the highest possible rates. For this we affirm that having abandoned the dogmatism which oriented the economic policy in the past, we have created the groundwork for development according to the characteristics of our country.

Having put the economy on the road which leads to a definitive solution for these problems, we may now look forward with confidence, which gives greater value and more meaning to the efforts to stabilize the economy and to refine short term management in order to overcome soon the crisis we have experienced.

III. Progress in the Government Development Program

As Minister of Finance, it is my duty to inform the public of the progress which has been made during the past year in matters of stabilization, eco-

conomic activity, social policy, and the conduct of our external economic relations. In this respect, we can state that the priorities established by the President of the Republic in the Presidential Message of September, 1976, have been satisfactorily accomplished.

Balance of Payment

On that occasion the President emphasized the necessity to guarantee an uncompromised situation in the Balance of Payments. I can now inform the country that we ended the year 1977 with equilibrium in the Balance of Payments. There is a surplus of US\$18 million and the Gross International Reserves of the Monetary System exceed US\$840 million. This situation has been accomplished in spite of a very low price of copper and in spite of the heavy commitments in foreign debt payments. The lower price of copper has been compensated for to a certain extent by a new and substantial increase in non traditional exports. On the other hand, the image of economic solvency and responsibility which the country has shown, has attracted foreign capital and credit which permit us to meet all foreign debt obligations promptly, and to avoid additional heavy restrictions on the Chilean standard of living.

The correct management of the foreign trade program has permitted us to continue with all of the phases of the tariff reduction program. This was indispensable in order to accomplish the transformation in the productive area so that the country could achieve higher and more stable rates of growth than those to which we had become accustomed.

Decline of the Inflationary Spiral

The second of the priority tasks entrusted to us was the reduction of the inflationary spiral. The public has been able to recognize the achievements in this area. While the rate of inflation measured by the variation in the Consumer Price Index reached 174.3% in 1976, this index only rose 63.5% in 1977. The moderation in the rhythm of inflation was reflected not only in consumer prices, but also in wholesale prices. Thus, variations in the Wholesale Price Index for the years 1976 and 1977 were 151.5% and 65.0% respectively. These advances in matters of stabilization have come about to a great extent because of adequate management of fiscal funds and of public enterprises. In 1973 the deficit in the Fiscal Sector reached 55.1% of expenditure; this year closed with a deficit of 9.4% of the outlay. The fiscal deficit is explained in part by the reduced income as a result of the low price of copper. We should also mention the fact that the price of

copper this year (US\$0.595 per pound) was 15 cents less than the price which would have balanced the fiscal budget, which is likewise 15 cents below the real average price for the last 10 years.

An orderly organization of expenditure also permitted the Government to raise the salaries of public workers while simultaneously reducing the tax rates for the first time in many years. We should also point out the reduction in income taxes, the drastic reduction of the transfer tax on house sales and the reduction of the rates of first category taxes. First category taxes are proportional taxes applied to enterprise profits. This tax has been reduced from 20% to 10%. The Social Security tax has also been reduced by 10 additional points.

On the other hand, the Government has decided that as of February, 1978, the system of declaration and payment of annual taxes due between the 1st and the 15th of each month from taxpayers subject to the Value Added Tax and the special tax as stipulated in Decree Law 825 shall be eliminated, except in the case of taxes on fuel. Therefore, in the future, the declaration and payment of these taxes shall take place once a month.

With regard to public enterprises, which four years ago were also important recipients of bank credit because of high deficits, it should be noted that better administration has practically eliminated losses. There are still slight deficits in some of them because of social considerations in matters of employment.

Economic Activity and Employment

The third task was to make an effort to improve production, wages and economic activity in general. In this regard, the year 1979 has also been an enormous success. The GNP grew at a very good 8.6%, with production in the agricultural areas increasing more than 15% and recovery in the industrial sector in the order of 12%. Purchasing power of wages and salaries has improved substantially this year as compared to the previous year, with figures near 25% in real terms. Employment has increased consistently—growth on the national level of 180,000 persons, or 6.3% as compared to 1976.

A Summary of Results. Some Inferences From these Facts

In the light of these figures we see notable advances. However, we are

far from thinking that the crisis is over. There is still a long way to go to fulfill all of the Government objectives. Inflation must drop from today's annual rate of 63.5%; the rate of unemployment in the labor force must continue to decline; workers' incomes must continue to improve.

However, we do feel justified in mentioning the progress made thus far as a confirmation that the strategy followed in order to overcome the crisis was the correct one. In the first moments of application of the Economic Program, and in the light of the means used to correct inflation, the fiscal deficit and the difficult balance-of-payments situation, many people doubted its efficacy, qualifying the program as monetarist and biased towards the financial sectors. The Government was always aware that the financial readjustment would be costly in terms of production in the short term, but was willing to bear this, convinced that stability was a necessary condition for rapid and sustained growth in production. The purpose of the Program has always been to improve the standard of living for Chileans by means of improved availability of goods, which is the product of better growth. The critics saw the financial adjustment as an alternative goal to growth, whereas the Government saw it only as the means to guarantee the long-run objective of increasing production.

Today we can show that the sacrifices in production were truly momentary and without abandoning strict financial discipline, production and wages increased while unemployment decreased, even though in 1977 the real price of copper is below that of 1975, and we have higher debt payments than in 1975.

The various economic indicators clearly demonstrate the progress toward a situation of stability and the improvement in foreign trade with an increase in consumption and well-being for the population. This improvement in the standard of living under such adverse conditions is the fruit neither of time nor of chance. And for us it is evidence that there is no permanent contradiction between stability and growth. We have already passed the most difficult period of the stabilization program and now the real variables of the economy are improving within the context of a sound financial situation, which permits us to be optimistic about the durability of these real improvements.

IV. Perspectives for 1978

Until the middle of 1976, the stabilization policy consisted in the use of all

the mechanisms for the control of the amount of money oriented towards diminishing the rate of money growth. The greater control which we have today has permitted us to enter upon the second phase of the stabilization policy as of July, 1976, with periodic decreases in bank legal reserve requirements. With inflation clearly under control, since we started from hyperinflation in 1973 and by 1977 had a rate of 63.5%, the greater control of money growth which has made it possible to increase credit to the private sector, has caused favorable changes in the levels of activity.

We look upon the monetary situation for this year with confidence. The principal sources of inflation have practically disappeared. This will give us a substantially lower rate of inflation than we had last year. Equilibrium is expected in the Balance of Payments. All this will allow for even greater reductions in bank legal reserve requirements than we had announced, within the limits which the level of and fluctuation in production permit, in order to increase internal credit. Our excellent image in the world capital markets allows us access to foreign credit, which means that the Government is in a position to continue to lower the cost of capital in the country without the risk of new outbursts of inflation. All of this will have significant effects on the increase in production, employment and wages in 1978.

We wish to point out one more time that a very important role in reactivation is being played by those activities which have developed as a result of the opening to international trade, which not long ago was nonexistent in this country. Between 1973 and 1977, nontraditional exports have increased more than six times. Although there are still problems, the economy has begun to renew itself and a productive structure which is better adapted to our resources and in accordance with our comparative advantages is developing.

V. Initiatives in the Social Field

Finally, it is important to refer to the line of action followed by the Government in the social field. The Government has defined as the responsibility of the State assistance to the most needy groups in the population. One objective established is the reorientation of Government spending in the social field so as to provide more resources for those sectors which are beset by extreme poverty.

This has taken the form of various measures destined to palliate the effects of the economic stabilization policy. The hiring of additional labor

is subsidized for 50% of the minimum wage per worker. The subsidy for the use of capital in the provincial zones of the country has been substituted by a 35% subsidy for the hiring of labor. Forestation, which has a cost structure in which 75% of the costs are for labor, has been subsidized. The minimum Employment Program was created and benefits approximately 180,000 workers.

Together with this, an unemployment subsidy was created for workers of the Social Security Service, and the family allowance was equalized for blue collar and white collar workers. As a complement to this, a nationwide training program was instituted and is in operation. This program is organized to perform on a large scale and the activities are concentrated in low income sectors.

In order to counter the high rates of inflation, an automatic wage and salary readjustment system has been implemented. Within the general plan for the eradication of extreme poverty, a system for the detection of and assistance to the families of undernourished children has been instituted. The pre-school and school food programs have been reorganized to make them more effective in the most needy sectors. Important steps have been taken to reorient expenditure in Education toward Primary Education so that it will reach especially those children in the poorest strata where 40% of the children failed to attend school, whereas in the rest of the country that rate is 20%. In Health, spending has been increased in the area of outpatient clinics and in preventive medicine, which has a direct effect on the low income sector of the population. In Housing, subsidies have gone to low-cost housing, and for the rest more realistic readjustments for the loans granted have been established.

The importance given to financing of public spending stems from the high social security tax rates in 1970 which were substituted by the inflation tax in 1973, and which has been replaced in this Government by indirect taxes, specifically the Value Added Tax. Thus, from the point of view of both the financing of expenditure and the actual use of the resources, the taxation and public spending systems have become progressive and a higher percentage of the benefits reach the poorest groups.

The reorientation of public spending toward the sectors in which the lack of resources is more acute, is in response to the Government conviction that the social and political problem in Chile will only be permanently solved if the country is able to grant access to a dignified standard of living and possibilities for progress to all of its inhabitants.

A Government which had this purpose in mind could not perpetuate the conditions of misery in which the development of the country left 22% of the population, according to the 1970 Census.

Nor could we postpone the structural reforms which provide the conditions for economic growth, and are part of the definitive solution.

The advances presented here are the result of the systematic application of a policy which minimizes the social cost of stabilization without compromising any of the long term objectives on which rests the possibility of accelerated and sustained economic development which will permit the eradication of extreme poverty from Chile forever.



**Report on the State of
Public Finance**

Sergio de Castro Spikula
Minister of Finance

January, 1979

Report on the State of Public Finance

Progress in 1978

It is well to remind the citizenry about the priorities established by His Excellency, the President of the Republic in his 1976 Presidential Message, so as to proceed with the analysis of the economic and political evolution of the country in 1978. In the light of these concepts, it is easier to make a comparison with previous years, and a clearer appreciation of these accomplishments is obtained.

Balance of Payments

In 1976, the President of the Republic established as a priority the necessity to guarantee a sound Balance of Payments situation, so as to lessen the risk of paralyzing our international trade, which would have had most serious consequences for the country. In 1977 we achieved equilibrium in the Balance of Payments, and in 1978 we had a surplus of over US\$600 million. Gross International Reserves, therefore, exceeded US\$1.500 million last December.

It is important to point out that these achievements have been possible in spite of the fact that the price of copper in 1977 and 1978 has been lower, in real terms, than the already depressed levels reached in 1975. The key to overcoming the Balance of Payments crisis has been the notable increase in exports other than copper, which increased by 20% in the last year. Exports in these lines have increased from US\$255 million in 1973, to US\$1.257 million in 1978. It must be realized that this increase in exports other than copper constitutes a significant increase in internal production and therefore in jobs for the labor force. It is also the basic element which inspires confidence in our country as a debtor in the international financial markets. And finally, these increases in exports have permitted us to meet our debt commitments contracted in previous years without additional restrictions on internal consumption at a time when the country has been impoverished by external factors or by events that occurred prior to this Government. The reduction of tariffs, an important corrective measure in the structure of our economy, together with an adequate management of the exchange rate policy and of monetary policy, have made these results possible.

Just as important as the figures on increases in exports, is the degree of diversification in exports both in the number of products exported and in

the number of markets these products are reaching. Thanks to this diversification, today the country is less vulnerable to fluctuations in prices or to attempts to restrict our international commerce.

The Control of Inflation

The second item in priority as established by the President in 1976, was the reduction of the inflationary spiral, a requisite for increasing investment and production, and for generating employment in the national economy.

In 1977, inflation had reached the rate of 63.5%, a significant improvement over 1976; when the rate of inflation was 174.3%. In 1978 there was a rise of only 30% in this index. Obviously, this does not constitute the definite achievement of the goals we had set for stabilizing the economy, but it is a significant approximation. No country can even consider having a sound process of investment and the generation of employment with the rate of inflation at this level. It is impossible not to recognize that the fact of having once more reduced the rate of inflation by half within a year, as we had in 1977, constitutes definite success of the program against inflation, and confirms once more the wisdom of this policy.

It is well to insist on the importance of safeguarding the basic principles of the anti-inflationary policy, that is, adequate handling of public finances and well organized administration of public enterprises in order to avoid excessive money creation. The year 1978 closes with a Fiscal Deficit of 4.1% over total expenditures. This deficit will continue as a result of the fact that copper prices and, therefore, Government income from this source will be at every low levels.

It is estimated that the public enterprises as a group will show a slight surplus in 1978, one which would be much higher except for the deficits in Railroads, The Chilean Nitrate Association (Soquimich), National Coal Enterprise (ENACAR) and the Chilean National Airline LAN-CHILE. From this statement we have also excluded the performance of the Greater Copper Mining Companies. If we recall that in 1974, the enterprises controlled by the State represented a burden to the State of over US\$500 million, a figure which is considerably inferior to that of 1973, we can appreciate the enormous progress made. These advances inspire the confidence that we shall continue to progress until the public enterprises are no longer an economic burden for the rest of the country, but rather each one of them is making a positive contribution in proportion to the billions of dollars worth of capital invested in them.

This organization of the Public Sector, in the Public Enterprises as well as in the Fiscal Sector, permitted us to carry out certain very important measures in 1978 such as the completion of academic training for school teachers at an annual cost of approximately 100 million dollars, the re-valuation of pensions, the 20% increase in the minimum wage according to the lowest grade in the Uniform Wage Scale of the Fiscal Sector as of January 1, 1978, an increase in the exemptions from the Real Estate Tax, the application of the value added tax to fuel and energy which means less revenues and a reduction in social security tax which favorably affects employment.

Increase in Economic Activity

The third task established by the President was to increase employment, wages and production. In 1978, employment increased 4.6%, which means 140,000 new jobs, while at the same time the purchasing power of wages and salaries increased by 14% in real terms.

Current estimates indicate that the Gross National Product increased 7.1% in 1978. Although this rate is not equal to the 8.6% attained in 1977, which is only natural if we consider that in previous years the economy was recovering from serious depression, it is far superior to the rates of economic development in the country in the past. This growth has been especially accelerated in the industrial sector, with rates of 12.2%, 9.2% and 10% in 1976, 1977 and 1978, respectively.

The results in matters of Balance of Payments, inflation and economic activity confirm the appraisal of both national and foreign observers, that we are advancing steadily toward complete stabilization, on the basis of a sound economy much less vulnerable than it has been in the past, and with a great potential for growth.

The mention of these advances should not be interpreted as satisfaction with the achievements in inflation, employment or economic activity. The Government is fully aware that the economic situation of many Chilean families is very difficult, and that there is still much to be accomplished in every field. We mention these achievements only in order to point out the rapid progress from a crisis situation to one of prosperity and the possibilities of development for all Chileans. The figures are eloquent proof of the direction and the speed of this adjustment, and that the correct methods were chosen and applied. There are no grounds to think that the crisis has been overcome and that there will be a relaxation in the policies;

it would only be a mockery to those who suffer restrictions and it would interrupt a sure route to progress on which the country has embarked with great success.

The Value of These Achievements

What is the importance of pointing out the success in the economic program and in the consolidation of a definite trend toward the stabilization of an economy prepared to grow?

The Government has established three fundamental objectives, none of which can be achieved without significant economic success.

Independence and National Security

One great objective is the guarantee of Independence and National Security.

A quick look at the world situation is sufficient to show that the poor countries maintain a submissive attitude toward more powerful nations in order to obtain necessary resources, and that they even run the risk of not being able to maintain territorial integrity. Today no one doubts the importance of a country's wealth when it comes to total political independence.

Freedom for all Chileans

Another basic objective is related to the perfecting of a political, economic and social system which will permit the full development of human potential. The Declaration of the Principles of the Government clearly defines the vision of man and of the characteristics of the society in which he can live without endangering his rights. This society is characterized by the freedom granted to the individual in every field, limiting the action of the State to what is strictly required in order to preserve the common good.

A State which controls the economic activity in a country necessarily inhibits initiative, imagination and the enterprising spirit of its inhabitants, limiting in this way the development of abilities and concerns which enrich peoples' lives. And what is more serious, the control of economic activity gives the State with no counterbalance political power which, experience has shown, can be used to control the life of the individual impeding his freedom to decide not only in economic matters, but also in cultural, family or religious matters.

The thorough reform of the Chilean economic system which has been carried out in the last five years by this Government has always been consistent with the necessity to perfect a society which by its very structure will guarantee true liberty for the Chilean people.

On the other hand, the efficient production of the goods and services required by the population is an essential requisite for the stability and the permanence of an economic system. The importance of the economic achievements mentioned before resides in this concept.

Now, the economic system which has taken shape in this country, besides being essential for the preservation of liberty, has shown itself before the eyes of the world to be very efficient from the point of view of maximizing production and thereby obtaining the maximum potential well-being for the citizenry. This system also provides for true respect for the individual and for the conditions in which he can develop the tendencies proper to human nature, such as the search for well-being and material and spiritual security, orienting his action toward the achievement of national goals.

Equal Opportunities and Social Justice

A third important objective established by the Government consists in the attainment of true social justice which is understood as a guarantee to all the inhabitants of the country of equal access to those goods and services which establish the possibilities to live in dignity and with the possibility to progress. The concrete actions undertaken in this sense constitute what is known as the Government Social Policy and efforts to achieve equal opportunities for all Chileans have taken the form of policies to eradicate extreme poverty.

A diagnosis prior to the formulation of the social policy carried out in 1973, on the basis of the last Population and Housing Census showed that in 1970, 22% of the Chilean population was living in extreme poverty. One lesson from this study was that the high percentage of the population living in extreme poverty corresponded to families of people who are self-employed, because of lack of opportunities in better paid positions in the regular labor market, resorting to various forms of employment which are relatively unproductive.

This fact, together with some others, indicated that the definitive solution to this problem depends essentially on the capacity of the economy to create stable and well-paid positions for all Chileans, which is an indis-

pensable means of increasing the productivity of the population through investment in the fields of nutrition, health and education.

In this way, the totality of the reforms of the economic system was considered as the basic ingredient in the Government's social policy. These reforms permit accelerated and sustained growth in production and employment, in accordance with the country's potential.

The intensity of the effort to create the conditions required for greater economic growth in the country is illustrated by the various measures taken, some of which include the transfer of State enterprises to the private sector, assignment of property titles to individual agricultural workers, tax reforms, tariff reform, free prices, development of the capital market and the free interest rates, fiscal reforms, inflation control, the regionalization of the country and the simplification of economic activity, the reorganization of public enterprises, and the socio-economic evaluation of investment projects.

Nearly all of these measures have already been carried out, and their fruits can be noted in the rates of growth which are far superior to those of recent years.

Having created the conditions for more rapid economic growth, which increases the availability of employment for the Chilean people, distortions which directly restricted the demand for work have also been eliminated. It is not sufficient for production to increase rapidly in order to maximize the demand for labor if at the same time conditions for hiring labor are unfavorable. Emphasis has been put, therefore, on measures to encourage the use of more labor in the production process.

The reduction of tariffs on imports has permitted the development of activities which, while unlike the sectors which were being protected by high tariffs, require a high degree of labor. The establishment of real negative interest rates which had the effect of inducing substitution of labor for capital in production has been removed and substituted by free interest rates. The rates of social security taxes paid by employers, which in the final analysis operate as a tax on the hiring of labor, have been reduced in order to put an end to the discrimination against hiring which these taxes encouraged.

All of this means that the economy will give more work and will permit better wages at every stage in the production process. Production will then

continue to grow more rapidly than in the past because of these reforms. The increases in employment and wages will automatically reduce the sector living in extreme poverty. In this way, a very significant part of the medium and longterm struggle against poverty has been completed.

These long term measures to reduce poverty over a period of time are not the only ones. During the last five years, this Government has steadily increased Social Expenditure, channeling more funds to social projects, in both relative and absolute terms of the Gross National Product than any of the previous Governments. This increase in the resources and the re-orientation of the social programs so that they will benefit more fully the most needy sectors, shows the consistency permitted by our economic system between an emphasis on short range social objectives and the necessity to obtain economic growth in order to solve the long run problem.

Resources Assigned to the Social Sector

Social Assistance and Employment

The crisis inherited from the former Government and the serious deterioration in terms of trade experienced in this country in 1975 led to very serious employment problems. The rate of unemployment in the labor force in Greater Santiago increased during 1975 to a maximum of 19.8% in March of 1976. For this reason, besides the permanent measures taken in the field of labor, such as the reduction in social security taxes, the creation of unemployment subsidies for laborers, and other general measures mentioned previously, the Government took certain temporary measures to alleviate the sacrifices caused by the economic crisis.

Thus, in May of 1975, a subsidy for the hiring of labor was created which consisted of a bonus in the amount of 50% of the minimum income per person hired over and above the number of permanent workers in the company as of March 31 of that year. Since unemployment remains high, this measure remains in force. In June of 1978, while extending this measure for one more year, the rate was dropped from 50% to 30% of the minimum income in force, as a means of adjusting the initial rate to take into consideration the reduction in social security taxes which had occurred during the same period. The number of workers who benefit from this system has increased over this period, reaching an annual total of over 600,000 monthly subsidies paid in 1978.

In 1975, the Minimum Employment Program was created as another solu-

tion to the problem of unemployment. This program offers work to anyone who wishes, for a certain period of time at a rate that is below the minimum wage. The number of beneficiaries of this program, which reached its maximum at the end of 1976, has been gradually reduced as the economy recovers, to about 120,000 by the end of 1978.

On the other hand, the Government has been continuously encouraging training as the best means of improving the possibilities for work and wages obtained by those who make up the labor force. For these purposes, significant resources have been assigned to a scholarship program administered by the National Training and Employment Service oriented especially to those who are looking for work for the first time and to the unemployed. In 1978, training scholarships were granted to 50 thousand people, who have by this means increased their productivity and degree of specialization. The funds assigned to scholarships are added to those which the various companies that participate in programs under the Training and Employment Statutes (D.L. No. 1,446 of 1976). The plan benefitted more than 50,000 people in 1978.

Carrying out these programs has had a very high cost which the Government deemed necessary to assume in view of the difficult employment situation. On an average, between the years 1969 and 1970, the last two normal years, for effective comparison purposes, US\$36.46 million, at 1976 prices, were spent on Social Assistance and Employment. In 1976, US\$ 149.63, at the same prices, were spent for the same purpose.¹ That is, in a period of eight years, the resources assigned to programs related to employment have quadrupled. This corresponds to an average rate of increase of 19% in the funds assigned each year to these projects. This figure is higher than the general increase in revenues. This average rate of growth of 19% per year in the Expenditure on Social Assistance and Labor reflects the high priority granted to solving the problem of unemployment.

Since the middle of 1976, the situation in matters of employment has evolved favorably. In September, 1978, the rate of unemployment in Greater Santiago reached 13.7%. Although this figure has diminished considerably in the last few years, it still reflects a persistent problem. The Government is particularly concerned with this situation, so that a maximum of resources, in accordance with the possibilities of the economy, will be assigned to the solution of this problem. This will be facilitated by

¹ In the comparisons, values of equal purchasing power have been used, that is, the dollar at 1976 prices.

the high rhythm of growth in employment which has been reached as a result of the strengthening of the productive system.

Health, Housing, Welfare, Education and Regional Development

The emphasis on redistribution of income in favor of the lowest income sectors is also reflected in the increase in Expenditure on Health, Housing, Welfare, Education, and Regional Development.

Between 1969 and 1970, an average of US\$750.8 million were spent in these sectors. In 1978, 1,047.7 million dollars (at the same price) were spent. This corresponds to an increase in real terms of 43.1% during that eight-year period, which amounts to a 22% increase in spending per capita, given an increase of almost 17% in the population for that period. Once again, it is easy to see that this 22% is far superior to the increase in the Gross Domestic Product per capita or in fiscal income for the same period. In order to be able to allocate more resources to the social sector, while adjusting fiscal spending, the percentage of Fiscal Expenditure assigned for social purposes has been increased from 40.5% (the average for the 1969-1970 period) to 53.9% in 1978.

On an average, between 1969 and 1970, 9.03% of the Expenditure of the Gross Domestic Product were Government contributions to the social sectors. This percentage reached 12.26% in 1978, which clearly reflects the effort on the part of the Government in social matters and the possibilities which our economic system provides for social action without disturbing the functioning of the productive system.

Reorientation of Social Expenditure

The Government has not only increased Social Spending, but has also carried out numerous programs for the reassignment of the resources for social projects, so as to reach more precisely the extremely poor sectors and to improve the goods and services which they receive.

Housing

In the Housing Sector, one of the most significant measures is the implementation of a new subsidy mechanism by which the beneficiaries receive a direct donation, the amount of which depends in inverse proportion on the assessment of the dwelling, whose value may not exceed a predeter-

mined, fixed amount. This guarantees that the subsidy granted by the State favors only people of very limited means and in greater proportion those who have the greatest necessities.

Health and Nutrition

In the last five years, the Health Sector reflects assignment of resources to programs which have a direct effect on the health conditions of Chileans of very limited income. This new orientation gives great importance to the furnishing of clinics in the marginal areas of cities and rural areas, which are centers for intensive programs of prevention and recovery from the illnesses which most affect the level of health of the population.

Besides the activities in the area of health as such, a great emphasis has been placed on nutrition. To incorporate the extremely poor into the community and extend social and economic benefits to them, there must be an increase in the productivity of this sector of the population, but educational or health programs which permit such an increase in productivity are fully effective only when the beneficiaries are in optimal physical and intellectual condition. In 1978, 27,000 tons of milk and enriched food for children were distributed and US\$26 million were granted to the National Scholarship and Student Aid Society to finance breakfasts and meals for low income sector students. In a parallel program, food has been distributed through the kindergartens, and centers for the treatment of seriously undernourished children are functioning throughout the country.

Numerous indicators show that this emphasis on massive health programs and on the nutrition of the members of the population at the most vulnerable age have produced a favorable and rapid evolution in the state of health of Chileans. The infant mortality rate has diminished from 79.3 per thousand born alive in 1970 and 65.2 in 1973 to 47 of every thousand born alive in 1977. The mortality rate in children between one and four years has dropped from 3.8 per thousand inhabitants in 1970 and 2.52 in 1973 to 1.88 per thousand inhabitants in 1977. The rate of maternal mortality has been reduced from 1.68 per thousand children born alive in 1970 and 1.32 in 1973 to 1.01 in 1977.

Education

As a consequence of the Government Social Policy, there has also been a notable reassignment of resources in Education. Means have been sought

to eliminate absence from education, by incorporating the student population in inaccessible and sparsely populated areas into rural school programs and border schools, where knowledge more appropriate for the type of work in which the students will engage on leaving school is imparted.

The emphasis on the extension and transformation of elementary education has required a volume of resources superior to that which the State could provide without denying attention to other equally urgent necessities. For this reason, students of higher education must make a greater effort to finance their studies. During the Popular Unity Government a disproportionate expansion in the enrollments in Chilean Universities led to the assignment of 40% of the education budget to higher education. In 1978 this figure was 31.0%, reflecting the Government policy consistent with concentrating State assistance in the sectors with more limited means.

The National Fund for Regional Development

The National Fund for Regional Development has been a very useful tool for the eradication of extreme poverty during the last few years. It was created in 1974 with the implementation of the regionalization process. This Fund has spent over US\$60 million in 1978, thus permitting regional authorities to solve urgent problems which, because of their particular characteristics, would hardly have been detected by the central Ministries.

The Elimination of Regressive Taxes

It is important to point out that the Government's Social Policy, oriented to the eradication of extreme poverty, has not only meant the increases of resources assigned to social projects and their reorientation so as to benefit the most unprotected sectors. During the last five years, the Government has also eliminated the most regressive forms of taxation. Inflation, through the deterioration in purchasing power which it causes, is the most negative element which affects the distribution of income. Any effort on the part of Government to help low income sectors is easily reversed when there are permanent increases in the prices of the goods and services which these sectors require.

For this reason, the control of inflation has had great importance during this period. The Government has conscientiously rejected the inflationary credit creation as a means of financing its expenses, because the rise in

prices upsets the productive system and causes misery to those who depend on a wage or a salary for their subsistence. It is also worth pointing out here the policy of periodic and automatic wage readjustment applied since 1974 and whose purpose is to guarantee the recovery of the purchasing power of the workers with respect to the effects of inflation.

The same emphasis has been placed on the reduction of the social security taxes, since it is a tax which limits employment and the net wage of workers. This fact converts it into a tax mechanism which is completely unfair and contradictory to the basic premises of the Social Policy being applied. The average social security rate of the main Social Security Institutions, which in the years 1970–1973 represented 54% of taxable remunerations and which in 1974 fluctuated around 60%, has been gradually reduced to a rate close to 40% of the present taxable income.

Chile has been affected by serious economic problems in recent years. Although we do not possess great wealth, having faced the problem of extreme poverty in a reasonable and systematic way, as this information illustrates, has permitted significant advances.

Perspectives

Legals Aspects of National Institutions

As we have stated, the economic program is part of a coherent and integral whole which stems from the very principles established by the Government.

The economic system plays a basic role in the progress toward a new legal framework for the national institutions. The year 1979 will see the implementation of profound changes in this process.

The Social Order

In matters of labor, the policy defined requires as never before, a more explicit enunciation of the duties and rights both of workers and of businessmen. Workers as well as entrepreneurs must measure their aspirations wisely so as not to work against the enterprise itself, as it constitutes their source of livelihood. Neither side can expect of the Government any more than its role as director of the norms of labor relations, which as such will establish norms within a framework of justice and efficiency for both laborers and businessmen. Therefore, the Government

will not be throwing life preservers to help ratify unrealistic aspirations.

The grave crisis which began years ago in the welfare system does not permit delay in the corrections which must be introduced in the Social Security System. The center of these modifications is the solution of the problem in the retirement age and the calculation of pensions. It also contemplates obligatory periodic readjustments of all pensions. In this matter, the basic steps have already been taken. However, the essential part remains to be applied. This means a sound capitalization system which truly motivates the eventual beneficiary of the welfare system, so that he will save an amount which will permit him to obtain a suitable pension at the end of his productive life.

In the field of health, a plan must be developed for the decentralization of the administration of state health organizations, and which separates the financial conduct and execution in this enormous sector. There is no doubt that the existence of a health system which does not require the presence of the State, should acquire more importance.

Government efforts in education have been obvious; the improvement in salaries for teachers, and the substantial increase in subsidies to free private schools indicate this. The Government looks with satisfaction on the increased capacity and number of private educational establishments, as a partial materialization of the concept of freedom in education. During this year, the basic characteristic which will orient the process of restructuring this sector, will be the administrative decentralization and deconcentration and as in previous years, an effort to assign the significant resources of this sector toward the most dispossessed and the priority sector of education which are pre-elementary and basic education.

The Economic Order

An analysis of the history of our country and the experience and results obtained during this Government, have strengthened the conviction that a subsidiary normative State which permits ample freedom of action and that does not act contrary to the common good, is the central axis of all policy. In the economic order, the long studies of the functions and attributes of State organs have permitted the conclusion and the application of an impersonal, non-discretionary economic system based on the market, the success of which is by now unquestionable.

The State, in its role as entrepreneur, must be sure that a legal framework

guarantees the functioning of its enterprises, corporations and banks so that they operate with the efficiency characteristic of a competitive economy. This will guarantee the consolidation of the legal management of administration which has been carried out during this Government in these institutions, and which has given very positive results.

This year, we must proceed with the final discussions on legislation which has already been formulated and which determines the functions, faculties and structure of the Ministry of Economy and the organs which depend on it.

The Economic Situation in General

For the year 1979, as in 1978, special care will be taken to adjust the management of monetary, fiscal and foreign trade variables, so as to continue the process of stabilization, by means of an indispensable reduction in the levels of inflation in order to obtain increasingly improved levels of activity. This means, among other things, that there still must be a real increase in internal credit in the private sector, guaranteed fundamentally by maintaining balance in the fiscal sector and the reduction of the deficit in public enterprises.

As can be deduced from the preceding information, the wise and strict management of public finance will permit the transfer of resources to the private sector which will steadily acquire growing importance in the country's economy. The Fiscal Budget today is nearly 30% of the Expenditure of the Gross National Product. This figure must not increase, and a very great effort must be made to decrease it. Any additional revenues in the treasury must be used to finance changes in the social security system which will provide for a reduction in the cost of hiring, and also to continue the process of reducing the present tax burden.

The sound position of the Balance of Payments has permitted, among other things, the establishment of much broader stability in the exchange rate policy. Thus, for the second consecutive year we have been able to establish the price of the dollar for the entire year.

In order to predict the inflation figure for 1979, it would be unreasonable to add to the rate of devaluation, and the expected external inflation, since similar inflationary pressures in goods not traded internationally should not be generated, if the possibility exists to increase production by incorporating existing productive resources. For the same reason, a devalua-

tion rate of 14.76% should be considered as a significant stimulant to the export sector, and as a means of adjustment in the recent growth trends in the export sector.

Exports will continue to increase, especially non-traditional exports. The import of capital goods will also continue to increase, and foreign credit will be a reliable source of resources because of the economic solvency demonstrated by the country.

The foreign sector will follow the policy of opening to the exterior in all fields. New financial markets will be explored and gradually and prudently an external credit policy will be formulated to allow greater freedom in the establishment of periods of debt. This, together with the growth of internal credit to the private sector, will continue to create the conditions for proceeding on the only sound and continuous way to diminishing the real interest rate.

The year 1979, will be a new year of growing stability and strong expansion in the economy. It will be possible to sustain these achievements by the consolidation of a sound management of public finances and growing economic freedom which will contribute to the perfecting of the new legal framework which has been announced.

Inflation and Financial Discipline in Chile

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Document presented at the XVIth Plenary
Assembly of the CICYP and in a Seminar
on Private Enterprise and Inflation.

April 5, 1979

Inflation and Financial Discipline in Chile

I. Brief Outline

Chile, like many of the numerous countries on this continent, has suffered from a long tradition of inflation.

In the last three decades the rates of inflation have been significant by any standard of comparison.

The decade of 1940 to 1950 was characterized by an average annual rate of inflation of 17.7% with annual (nominal) increases in money and quasi-money of 19.8% and 14.2% respectively. Meanwhile, the rhythm of growth of the public sector began to accelerate in relation to growth in the private sector. In the foreign sector, as a legacy of the problems generated by the world crisis in the 1930's, a closed economic policy was carried out by the creation of ever increasing barriers to foreign trade, resulting in the artificial development of a protected import-substituting industrial sector.

The decade from 1950 to 1960 followed the same pattern as the previous decade but with an accentuation of all of its manifestations. The average rate of inflation was 36.6% while in 1954 and 1955 these rates reached 70% and 80% respectively. The yearly average for rates of growth for money and quasi-money for this period were of 37.6% and 38.9%, which, given the exchange rate policy, produced sharp deficits in the balance of payments; instead of dealing with the cause of the balance of payments deficits, increased reliance on foreign debt was used as a means of overcoming the symptoms.

The decade from 1960 to 1970 must be divided in two. In the first years of the decade a crisis occurred in the balance of payments as a result of the increase in credit to the public and private sectors at a rate which was incompatible with the policy of fixed exchange and interest rates. The public sector continued to expand until the fiscal deficit bordered on 5.0% of the Gross Domestic Product. The last six years of the decade show a profound change in government intervention in the economy. This period saw the initiation of the process which later culminated in massive expropriations in the agricultural, mining and banking sectors. It was the prelude to the exacerbated manifestation of these actions during the thousand days of the Popular Unity Government.

The average rate of inflation was 26.0% per year, aggravated by an increase in the public debt which would have a negative effect on the economy. The domestic and foreign public debt reached unprecedented heights, in spite of the extraordinarily high price of copper which in those six years rose to the equivalent of US\$1.293 per pound (in 1978 dollars), double the rate of any other six year period in the history of Chile. In other words, in spite of the most favorable conditions, the future of the country was mortgaged on behalf of six years of government.

The increase in credit to the private sector and the fiscal deficit in local currency were incompatible with the inflation goals the government of the period had itself set in its economic program. As a result, once again instead of dealing with basic causes, the manifestations of inflation were repressed by emphasis on price controls.

In the 1970-1973 period, during the Popular Unity Government, the economic authorities implemented several intervention mechanisms whose possibilities had not been fully exploited by the previous governments.

Price controls became generalized. The multiple exchange rate system was revived. The fiscal deficit reached unmanageable magnitudes: from 2.8% of G.D.P. in 1970 it rose to 10.8% in 1971, and 12.9% in 1972, to reach 23.6% in 1973. The rates of growth in the nominal supply of money were 113%, 152% and 363% respectively in the years, 1971, 1972 and 1973.

The country's net international reserves fell by more than 600 million dollars even though the foreign debt increased in those years by nearly one billion dollars. This caused a dramatic balance of payments crisis which resulted in a moratorium on foreign debt payments. In the year 1973, production indices registered significant reductions and the real income of workers fell sharply. Actually, by the end of the Popular Unity Government, real wages and salaries were reduced to figures in the order of 50% (some studies put that figure around 40%) of real income for 1969. The measured inflation, underestimated because the great majority of items on the Consumer Price Index were subject to price controls, reached 508% in 1973. However, the actual rate, according to studies made by academic institutions, was close to 1,000%. The Wholesale Price Index, on the other hand, increased 1,147%.

II. The Causes of the Disorder

In the first place, on the macroeconomic plane, it can be deduced from the

previous information that in the majority of cases, the economic policy measures implemented were incompatible with the intended goals.

In spite of limited availability of foreign financing, vigorous fiscal programs were carried out which led to significant increases in domestic credit, which together with a fixed exchange rate policy, led to balance of payments deficits and crises. The result was a series of sharp exchange rate devaluations which produced discontinuous increases in the price level of important magnitudes.

Although the goal was stable prices, a relatively flexible exchange rate policy was designed, but accompanied by significant increases in domestic credit to the public sector in order to augment its participation in the economy, while simultaneously expanding credit to the private sector. As if to unbalance the situation even further, a restraint was placed on the only remaining macroeconomic adjustment variable, price levels, since price controls became increasingly strict. In other words, while stable prices were supposedly the goal, policy was set as if the true objective were a balance-of-payments target. Conclusion: incompatibility, inconsistency, and as a result, failure to achieve the objectives established.

There is a common denominator for each and every one of the previous mistakes: a chronic imbalance of public revenues and public spending, brought about by substantial growth in spending. The consequences of this chronic imbalance have profoundly affected the social, political and economic life of the country.

III. Effects of Inflation

Without exception the economic programs of the various governments have stated stable prices as their goal, and justifiably so, given inflation's harmful social, political and economic effects.

As its social implications, inflation produces serious friction and conflict, since those who suffer from it, without fully understanding its causes, erroneously identify as the cause of this evil the sector directly and immediately involved in the rise of prices. Thus, the consumer blames the merchants, merchants the wholesale dealers, and these in turn blame the manufacturers and farmers, borrowers blame lenders, and so on, and finally, and this time correctly, the government is blamed. This atmosphere favors the development of social conflict and political instability in a country.

At the same time, inflation affects income distribution, since the continuous rises in prices between one wage increase and another produces significant but unstable changes in workers' purchasing power. This produces new friction and conflicts between management and labor which make good relations within firms very difficult. Government intervention in these conflicts only makes the situation worse. The recent increase in world inflation has coincided with serious business-labor conflicts in countries which for years had enjoyed efficient channels of understanding, guaranteed by a stability in prices which minimized friction between the two parties.

In a strictly economic sense the results are no less harmful. Controls on interest rates, prices and foreign trade are an indirect result of inflation, and the direct result of the tendency to seek the easy solution to the problem by suppressing its manifestations instead of attacking the problem at its roots. With these controls and a fixed exchange rate, inflation soon creates a crisis in the balance of payments, a decline in saving and domestic investment, the flight of capital overseas, and in general, a decline in wealth, in economic activity and in employment. Without making an absolute affirmation, the Chilean experience allows us to affirm that a sustained reduction in inflation at a rate which the inhabitants of the country interpret as successful, and the achievement of price stability, are indispensable prerequisites for a stable balance of payments situation and the elimination of the aforementioned problems.

From a microeconomic point of view, chronic inflation, aggravated by price controls, causes distortions throughout the economy. The price system loses value as a source of information because the relative prices are continuously affected in different ways by the monetary imbalance. Distortions are created in the tax system which usually does not have adequate adjustment mechanisms for contracting the inflationary phenomenon, with consequent negative effects on the equity and the efficiency which the system should have.

The shrinkage and eventual long term disappearance of the capital market is another notable effect of inflation, with unfortunate implications for a country's development possibilities. In general, the autarchy in commerce as well as in investment caused by inflation which is different from that of the rest of the world, has predictable, negative results for the development possibilities of a small country.

To summarize, price stability must be one of the most important goals of any government for social and political reasons as well as economic ones.

IV. The Causes of Inflation

Inflation has its origin in stock imbalances between the amount of money desired and the amount, actually in existence in the economy. The persistence or maintenance of a determined rate of inflation depends on the rate of monetary expansion. When there is an excess in the supply of money, a generalized excess in demand of goods and services as well as financial assets, tradable as well as non-tradable on the international market, appears as its counterpart. The solution for this excess demand will be carried out by means of price increases for domestically produced goods and services and national financial assets, and by increases in imports of goods and foreign financial assets as well as in domestic production.

The exchange rate system adopted is decisive in determining the final result of monetary disequilibrium. Monetary expansion at a rate greater than international inflation is incompatible with a nominal fixed exchange rate system. Therefore, internal inflation which is continuously superior to international inflation is only compatible with a system in which the exchange rate varies.

Let us distinguish between an excess in monetary supply which occurs once and for all and a rate of monetary expansion which is consistently superior to international inflation.

With an exchange rate that varies freely, a once and for all excess supply of money will result in a once and for all increase in the price level, and an equivalent increase in the rate of exchange. However, a rate of monetary expansion which is continuously superior to the international rate, will result in a rate of inflation superior to the international rate and a deterioration in the value of local currency with respect to foreign currency at an equivalent rate.

With the exchange rate fixed, in nominal terms, a once and for all increase in the money supply will result in a once and for all loss of international reserves, without effecting the price level system. A rate of monetary expansion continuously superior to international inflation, however, will result in the eventual exhaustion of international reserves, which will cause a crisis in the reserves. Thus a fixed nominal exchange rate is incompatible with a rate of monetary expansion which is continuously higher than the international rate, if foreign financing is not available.

With a freely fluctuating exchange rate, the source of monetary expansion is an increase in domestic credit, in both the public and the private sectors. Exchange operations should also be added as a source when there is a fixed nominal exchange rate.

Variations in the factors which condition monetary equilibrium will be resolved most rapidly when interest rates are freely determined. As a matter of fact, when people expect the rate of inflation to decrease, the private sector will want to increase its money holdings, which in turn may be satisfied by an increase in domestic credit to that sector.¹ If interest rates were controlled, however, there would be imbalance and some form of credit rationing, and consequently the desired increase in credit would be prevented.²

It is particularly relevant to analyze monetary expansion caused by public sector operations. Unlike the private sector, in which it is possible to identify economic behaviour on the part of business as well as of individuals, the public sector is not easy to analyze. The variables which determine the amount of money which the private sector is willing to demand, such as the cost of holding money, either in terms of interest rates or the productivity of foreign currency or assets, are not significant for decision making in the public sector. It is all the more difficult, therefore, to relate an increase in credit to the public sector to a corresponding increase in the demand for money in that sector.

Of the sources of monetary expansion, the most uncertain, with the least amount of information and, therefore, the most dangerous, is public sector credit, since the probability of producing economic imbalance is very great, regardless of the exchange rate policy. Moreover, if an excess supply of money is created through the validation of a fiscal or public deficit, the process of correction is difficult and lengthy because of the greater inflexibility in the public sector, due to the direct results of a

¹ Or in lieu of domestic credit, by foreign credit through the capital account of the balance of payments.

² In this case the increase brought about in the amount of money has a destabilizing effect. This situation is analogous to an increase in the amount of money through exchange operations coming from the influx of capital, explained by differences between the domestic and foreign interest rates. The former, in the context of a fixed rate of exchange, produces a deficit in the commercial balance, which will persist as long as there is control over domestic interest rates. If interest rates are free, they will exceed foreign rates and the creation of money will continue.

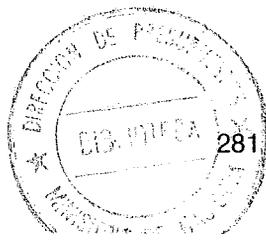
reduction of the public sector on real activity, prices, and the foreign sector.

This is an additional argument in favor of the conclusion that a sound means of safeguarding economic stability is to preserve financial discipline by means of a balanced budget.

In order to establish a definitive exchange rate policy, an indispensable and basic prerequisite is the certainty that the fiscal sector will not be a source of imbalance.

Other conditions are also required. A market-determined interest rate policy is another factor necessary so that the changes in the interest rate serve as clear indicators in the formation of economic policy and give a precise idea of movements in the real interest rate. Another important element is an open foreign sector which fluidly can solve the monetary imbalances which occur in the monetary and real sectors. An economy which breaks a historic tradition of decades of protectionism will produce a definitive and sound reallocation of resources, which in both the near and long terms will mean producing more with the same resources. This gain in efficiency is coupled with the establishment of a ceiling on domestic price levels due to the change in relative prices which are implicit in the adoption of a liberalized tariff and foreign trade system. Finally, it is indispensable to evaluate the country's foreign financing capacity in light of alternative situations in the Commercial Balance and the Current Account of the balance of payments. From this point of view, the basic economic instrument for producing the incentive necessary for the entrance of foreign capital is the elimination of the fiscal deficit. With this the circle is complete.

If the fiscal situation is in equilibrium, and there are no foreign financing problems, but the rate of inflation is still high, then it would seem advisable to move toward a fixed exchange rate policy. The result of this is two-fold. First, this exchange rate policy constitutes a stabilizing factor in prices and in the economic activity. Second, a decrease in the rate of inflation produces a higher demand for real monetary balances, which gives a further impulse to stability, and also allows for a margin of freedom in money creation by means of credit to the private sector. It should be remembered that the establishment of the exchange rate level should be at a level compatible with the stock of international reserves. In other words, the fixing of the exchange rate should not threaten one of the requirements for the establishment of the rate itself, which was that the balance of payments situation did not constitute a restriction.



Now, if the rate of inflation is close to zero, the fiscal situation is in equilibrium and there are no problems in foreign financing; theoretically, the exchange system chosen is a matter of indifference. However, the continued preservation of financial discipline is much more feasible when local currency may be converted into foreign currency at a fixed rate.

Throughout this exposition of the subject, we have deliberately avoided the analysis of periods of adjustment or transition. Our economy is neither as closed nor as open as the classical economic theory or the monetary view of the balance of payments suggest. In a fixed exchange rate situation, an increase in the amount of credit to the private sector would not produce an immediate one hundred percent adjustment by means of the balance of payments. There will be pressures from internal and external sources, and the adjustments in the economic system will be mixed: in quantity (commercial balance and perhaps internal activity) and prices; the required equilibrium will only come through the balance of payments in the long run. The monetary and exchange rate policies must be designed within the relatively ambiguous framework of information actually available with an idea regarding the correct transition path to equilibrium. In addition, there may be a restriction which should be taken into consideration. The economic policy and its goals, which in our countries is basically the reduction of the rate of inflation, may not be endangered by measures which, although they may be consistent in the long run, may in the short run lead to erroneous interpretations, and many times to the generation of expectations of an increase in inflation. While it is true that in the context of a fixed rate of exchange, the economic policy instrument is credit, it is no less true that alteration in the money stock implicit in the increase in credit will have an impact on prices during the period of adjustment. If this impact is such that it inverts the expectations which are held with respect to the course of the inflationary process, or more, if even without changing the sign of the expectations with respect to the tendency of the process, produces a sensation of stagnation or scanty achievement in the battle against inflation, then it is advisable to be cautious with regard to credit expansion goals.

V. Objectives and Results of the Economic Policy Applied Since 1974

The foregoing analysis is the base for the economic policy applied since 1974.

The magnitude of the errors generated by previous economic policies constituted very strong support for the rapid adoption of corrective measures.

Once the basic objectives were defined, what occurred from then until now constitutes movement toward the final goals, although sometimes rendered difficult by exogenous circumstances.

The first basic consideration of the new economic policy was that the size of the public sector in general was incompatible with an economic structure in which private initiative played a fundamental role. The growing volume of real resources invested in the public sector implied a gradual strangling of economic activity in the private sector.

Along with this, the market mechanism was recognized as a vehicle for a more efficient allocation of resources, provided that the prices and signals which flow from the market truly represent the relative scarcity of goods and factors.

A basic element of policy definition, then, was the elimination of every kind of control on prices, among them the interest rate. Another simultaneous factor was the elimination of non-tariff trade barriers and the reduction of customs duties as a mechanism for achieving efficient allocation of resources, eliminating these instruments as a means to stabilize the balance of payments.

Together with reducing the size of the public sector, the necessity for financial equilibrium in this sector was emphasized as the only means to eliminate inflation permanently.

Within this framework of clearly specified objectives, the economic policy has also been gradually dealing with the distortions.

The following magnitudes are an indication of the economic chaos we lived: one thousand percent inflation per year; customs duties up to 550%, with a great many goods prohibited by means of prior deposits of 10,000%; fiscal spending at 43% of the GDP; fiscal deficit of 23.6% of the GDP; real interest rates of 70% per year; and no more than 26 million dollars cash in foreign currency as gross international measures.

The first corrective measure that had to be applied in October 1973, was to devalue 506%. The process of reducing the size of the public sector began gradually, principally by means of dissolving the mis-named Social Area. The creation of the Social Area of the economy had meant that nearly the entire national industrial complex had come under the control of the State.

The first stage of the tariff reduction program reduced customs duties from 550% to 250% and eliminated innumerable prior deposits of 10,000%.

The financial legislation was modernized, and interest rates were decontrolled.

The purpose of the exchange rate policy was to maintain the real value of the exchange rate by means of periodic unannounced devaluations.

In short, the market recovered its role in the allocation of resources, the private sector once again undertook its true productive work, conditions were created to open our economy to the exterior, and the initial impulse was given to the creation of a true capital market. However, there was one measure which was not taken with the necessary vigor, as subsequent events later showed. Even though the decline in the deficit in the Public and Government Sectors was significant, it was not sufficient to guarantee a significant and sustained decline in inflation and to guarantee a balance of payments situation which would not cause difficulties later on.

Therefore, as a fruit of money creation provoked by the increase in credit to the public and private sectors, an increase of over 200% in the price of petroleum, and a decline in the price of copper, (a situation that was to continue over a period of four consecutive years) at the beginning of the third quarter of 1974 a serious balance of payments deficit was foreseen for the end of the year, estimated at the time to be over US\$1,000 million. The rate of inflation was still 375.9%.

Thus, 1975 began with considerable rates of inflation and a potential deficit in the balance of payments which constituted a real restriction in economic management.

The only solution for such a situation was to adjust the country to the true resources available in order to avoid payments defaults.

This over-all economic situation required substantial correction of the public sector. The objective was to reduce the deficit drastically and in order to accomplish this, measures were adopted affecting revenue as well as expenditures. With regard to tax receipts, the tax reform that had been undertaken in 1974 was accelerated. Tax revenue was raised without introducing distortions into the productive system and taking care to protect the equity of the system. That is, the long term goals of the reform program were safeguarded. Nearly the entire extensive range of tax ex-

emptions was eliminated, a value added tax was implemented and a generalized monetary correction system (indexing) was put in practice. Another important source of public income, the prices of goods and services produced by state enterprises, was brought into line with real values, either by submitting these companies to external competition or in the case of public utilities or other state monopolies, by establishing prices based on real values.

Efforts were also made to control the level of public spending. Fiscal spending in national and foreign currency was reduced 15% and 25% respectively, all this while maintaining social programs at their 1974 levels in order to distribute more equitably the social cost imposed by nearly three years of destruction and chaos. At the same time, a severe reduction in spending was applied in the public enterprises and the Development Corporation (CORFO), which in some cases reached a rate of 40% in real terms.

These measures were accompanied by an acceleration in the rhythm of devaluation as a direct stimulus to the correction of the deficit in the balance of payments, and financial policy was defined based on legal reserve requirements that permitted greater growth in more efficient institutions, replacing the discretionary system of credit expansion that had existed until then.

The 1975 experience really laid the groundwork for the control of inflation, besides providing a clear indicator of the need to define an expenditure policy for the public sector based on a long run price for copper, and the problem which can be caused by assuming debt without a secure means to meet these obligations in the future.

The contraction of fiscal spending, having eliminated a cause of money creation, and given the current rate of inflation which was on the order of 340% per annum, was the equivalent of a monetary reform which would make part of the money stock disappear from the economy in a few months. Since the means to replace the nominal stock of money which had been depreciated by inflation were not generated, the real stock of money quickly declined, reducing the general demand for goods and services. Therefore the deficit in the Balance of Payments was reduced to a manageable level, and pressures on internal prices were relieved.

There is no other way to explain that beginning in 1976, the rate of inflation demonstrated a consistent tendency to decline, a fact that was possible

only because of the elimination of the fiscal deficit in domestic currency. As a result, the 1974 rate of inflation of 174% has been reduced to 63.5% and 30.3% in the following years.

Although a balanced budget seems to be an indispensable condition for achieving stable prices, with the positive effects that this produces on economic activity, it is important not to forget two other very significant elements in the Chilean case.

The first is the market-determined interest rate. The interest rate has been the vehicle by means of which financial savings have increased at rates unprecedented in our history. The high elasticity of the supply of savings with respect to the interest rate has constituted an important stabilizing element.

The second element is the important role of exchange rate and tariff policies in the orientation of expectations. The tariff policy, which in February of 1973 set as a goal a uniform tariff rate of 10% by June of 1979, has put a brake on expectations with respect to rises in prices. Even if in theory tariff policy only affects the allocation of resources, in the context of cuts in customs duties, it has this secondary effect.

The effect of the exchange rate policy appears to have had much more importance once the Balance-of-Payments crisis was overcome. In June of 1976, principally because of a reduction in demand to levels compatible with available resources, conditions were adequate for revaluing the peso. As a result of this, inflation which had stabilized at around 11.0% per month, was reduced to 6% per month because of changes in expectations. In March of 1977, the phenomenon was repeated, with inflation stabilized at 6% which then dropped to 3% or 4% per month.

In February of 1978, a daily exchange rate schedule was established through December 31, 1978. In December, 1978, a similar schedule was set for 1979.

What these programmed revaluations and devaluations had in common was that they gave a signal to the country since certain objective facts (the substantial drop in the fiscal deficit and the surplus in the balance of payments) had not been assimilated rapidly enough by the public.

If we assume that a balanced public sector budget implies the elimination of the basic cause of inflation in Chile, then part of the inflation we observe

can be attributed to expectations. Therefore exchange rate policy has provided a reasonable orientation of inflationary expectations on the part of the public, because it was solidly supported by the absence of the need for money creation for the public sector.

Finally, it should be noted the objective of this sketch has been to analyze the consistency and the results of the economic policy, one of the effects of which has been price stability, without intending to present it as an ideal model.

Thus far we have had success by emphasizing the variables we pointed out, but it is quite clear that one of the fundamental causes which could upset the stabilization process would be imprudence and lack of financial discipline in the public sector.

Part IV

Statistical Addenda

**Chilean Economic Policy:
Dogmatism or Realism**

The Measures Adopted

The transformation of the economy from a state-controlled system to a competitive free market system which constitutes the basis for the economic policy applied in Chile from the end of the year 1973, is reflected in a series of reforms introduced and which flow from the following fundamental conceptions:

- A. The restriction of the field of action of the State to the macroeconomic function;
- B. The creation of conditions favorable to the development of competitive markets;
- C. The allocation of resources and conditions of equity;
- D. The reaffirmation of the concept of private property.

A. Restriction of the Field of Action of the State to the Macroeconomic function.

The Declaration of Principles of the Government of Chile (March, 1974) establishes, among other things, the subsidiary role of the State in productive activities, and the extent of its functions.

Decree Law No. 966 (promulgated in April of 1975), as set forth in its text, confers on the Ministry of Finance the extraordinary faculties which permit it to carry out the economic and financial policy of the Government in a unified manner, recognizing the existence of frictions ("micro" versus "macro") in the system and, what it is more important, a solution is provided for the problem of the responsibility of the direction of the economy.

Decree Law No. 1.078 (June, 1975) defines the activity of the Central Bank of Chile; article 2 of the decree establishes the creation of the Monetary Council. Articles 29 and 30 prohibit the participation of persons connected with the private or public sector as members of the Executive Committee of the Central Bank. The Executive Committee is composed only by the President, the Vice President and the General Manager of the Central Bank of Chile.

Article 20 restricts the Central Bank's faculty to grant credit to the fiscal sector to the maximum established by the Monetary Council for each year. In this way the possibility of indiscriminate lending to public or private institutions is eliminated.

This Decree Law has eliminated the frictions which existed in the former structure and the conflicts of interest.

B. The Creation of Conditions Favorable to the Development of Competitive Markets.

Finance Ministry Decree No. 522 (October, 1973) establishes that the majority of formerly fixed prices will now be free, with a few exceptions.

Beginning in December of 1973, a series of progressive tariff reductions go into effect, in accordance with the respective Finance Ministry Decrees No. 2.138 of December, 1973, No. 225 of March, 1974; No. 24 of January, 1975 and various subsequent modifications to the Tariff Schedule in general). Finance Ministry Decree No. 1.192 of December, 1977 and subsequent decrees dispose general reduction in tariffs to reach 10% by July of 1979.

Exchange rate policy: Among the first corrective measures of the present Government was the drastic devaluation of the peso and the elimination of the complex multiple exchange rate system (Central Bank circular No. 1.972, September 30, 1973). As of August, 1975, a single exchange rate goes into effect and from February, 1978, the Central Bank publishes the daily exchange rate in force for the entire year.

Foreign Investment: Decree Law 1.748 of March, 1977 (and formerly Decree Law No. 600 of 1974) establishes objective norms for any foreign investor, eliminating arbitrary treatment and discrimination between foreign and national investors.

C. Allocation of Resources and Conditions of Equity.

Tax reform: Decree Law No. 824 and 825 of December, 1974, and subsequent modifications, establish the Value Added Tax system and a new conception of and structure for the Income Tax system. A monetary correction system has been applied and innumerable exemptions and discriminations have been eliminated.

Wage policy: As of the promulgation of Decree Law No. 670 in 1974, a general periodic and automatic readjustment system is established in order to minimize the losses in purchasing power caused by inflation. In the years

1975 and 1976, four general readjustments were granted and since 1977, there have been three yearly readjustments. This is the only Government that has given more than one general yearly readjustment.

Pension policy: A series of special additional readjustments have been authorized for the minimum pension in order to increase their real value (D.L. Nos. 255 and 550 of 1974, D.L. No. 958 of 1975, D.L. No. 1.401 of 1976; and in January of 1977 and 1978).

In order to correct the loss of purchasing power of the other pensions, a revaluation of pensions has been authorized (D.L. No. 2.444 of December, 1978), to bring the initial value of the pensions in line with inflation.

D.L. No. 2.448 of February, 1979, establishes for the first time in Chile, an automatic overall system guaranteed by law to reajust pensions according to the rate of inflation. Besides this, the decree law establishes a uniform retirement age, according to the number of years of participation in the various social security institutions.

D.L. Nos. 446 and 786 of 1974, D.L. Nos. 1.753 and 2.062 of 1977 and D.L. No. 2.154 of 1978 establish significant reductions in the social security tax.

D. Reaffirmation of the Concept of Private Property.

Agrarian Reform: The need to correct the numerous anomalies and injustices in which the expropriation of rural properties incurred through the application of the Agrarian Reform Law (Law No. 16.640 of 1967), and for the efficient assignment of property, in order to avoid the proliferation of the "minifundia," led to the promulgation of various Decree Laws (1.125 in 1975, 1.875 in 1977, 1.848 in 1977, 2.221 in 1978, 2.247 in 1978), whereby norms have been established to regulate the process, principally in what refers to the establishment and reassignment of the reformed sector, granting the respective titles, returning or duly indemnizing the landowners whose property had been taken over and to guarantee properly documented readjustable payments (indemnizations).

The Area of Social Property: In September of 1973, the State controlled nearly 500 enterprises, of every kind, and nearly all of the banks.

Decree Law No. 333 of February, 1974 established the conditions whereby companies which had been requisitioned, taken over, or in any way administered by the former Government and which had contracted signif-

icant debts of every kind, could normalize their credit situations, thus being able to return to the private sector.

The debt situation of the public institutions, generated during that period, was returned to normal by means of D.L. No. 233 of January, 1974, and Resolutions Nos. 961 and 962 of the Ministry of Finance.

Statistics

The following is the functional distribution series for the Fiscal Expenditure during the 1970 - 1978 period in order to analyze the relative importance of the various functions performed by the State over a period of time.

Structure of Percentage of Fiscal Outlay (Excludes Debt Service)

	1970	1971	1972	1973	1974	1975	1976*	1977*	1978*
Overall Administrative Function	27,2	23,1	24,2	17,9	27,8	31,1	30,8	32,6	32,5
Social Function	40,5	48,6	47,1	27,4	39,8	47,2	48,2	50,0	53,9
Economic Function	32,3	28,3	28,7	54,7	32,4	21,7	21,0	17,4	13,6

* Provisional Figures.

Note:

Although it is true that this series does not correspond exactly to the close indication of function of the State as set forth in this paper, it is possible to make the following parallel.

The General Administrative function is related to the regulatory function of the State and to the production of certain goods and public services (Foreign Relations, Defence, Justice, etc.);

The Social Function refers to the distribution function of the State, directed to the lower income sectors; and

The Economic Function, which diminished progressively in recent years, is basically oriented to some productive activities and to subsidies to the private sector.

The macroeconomic management function of the State is directed to achieving the objectives of Stability, Growth and Development.

The achievement of stability in prices is reflected in the progressive reduction of the rate of inflation through a careful monetary policy and the reduction of fiscal debt and the correction of the public finances.

(Percentage of variation from December to December of each year)

YEAR	Inflation Objective	Money (M ₁)	Money Creation
1970	34,9	66,2	70,3
1971	22,1	113,4	132,7
1972	163,4	151,8	173,7
1973	508,1	362,9	461,6
1974	375,9	231,2	222,5
1975	340,7	257,2	312,7
1976	174,3	189,4	266,3
1977	63,5	113,5	94,4
1978	30,3	65,0	56,2

Revenue, Expenditure and Consolidated Fiscal Deficit as percentages of EGDP

(Figures in percentage)

YEARS	Expenditure	Revenues	Deficit	Deficit/ Expenditure
1970	26,97	24,19	2,78	10,3
1971	30,97	20,21	10,76	34,7
1972	30,74	17,86	12,88	41,9
1973	42,72	19,17	23,55	55,1
1974	31,65	21,33	10,32	32,6
1975	26,22	23,17	3,05	11,6
1976	27,22	24,50	2,72	10,0
1977	28,04	25,76	2,28	8,1
1978	30,11	28,87	1,24	4,1

External stability is reflected in the increase in Net International Reserves (Surplus or deficit in the Balance of Payments), a consequence of the opening of the economy to foreign trade as a result of the application of a realistic exchange rate and tariff reforms which eliminate many of the existing tariff barriers.

When making the analysis, the low price of copper and the high amount of Debt Service during the last few years should be kept in mind.

Balance of Payments
(Figures in millions of Dollars)

ITEM	1970	1971	1972	1973	1974	1975	1976	1977	1978 ¹
EXPORTS	1.255	1.133	978	1.429	2.294	1.782	2.392	2.635	3.071
—Copper	840	701	618	1.056	1.624	868	1.233	1.139	1.216
—Other Goods	272	296	229	255	527	722	883	1.046	1.257
—Services	143	136	131	118	143	192	276	450	598
IMPORTS	1.160	1.225	1.331	1.626	2.331	1.999	1.946	2.723	3.386
TRADE ACCOUNT BALANCE ²	156	- 18	- 255	- 137	135	- 118	460	- 58	- 417
CURRENT ACCOUNT BALANCE	- 81	- 189	- 387	- 288	- 211	- 491	148	- 399	- 721
AUTONOMOUS CAPITAL BALANCE	268	- 27	327	242	228	299	235	346	1.351
BALANCE OF PAYMENTS	114	- 300	- 229	- 112	- 45	- 275	455	- 7	630

¹Provisional Figures.

²Defined as balance between exports and imports of goods.

YEAR	Ratio	<u>Current exchange rate¹</u> Implicit exchange rate	Real Price of Copper ² (US\$ cents Dec. 1978/pound)
1970		0,64	126,18
1971		0,57	94,03
1972		0,51	88,63
1973		0,62	130,29
1974		0,74	126,73
1975		1,01	69,49
1976		0,90	75,48
1977		0,82	66,45
1978		0,93	64,27

¹The implicit exchange rate reflects the internal inflation as well as world inflation. (See Report on the State of Public Finance, January 1979).

²Deflated by the Wholesale Price Index for the United States. In the 1964-1969 period copper prices were as follows: (cents US\$ December, 1978).

1964	1965	1966	1967	1968	1969
100,87	132,07	151,35	111,15	119,11	135,80

Development of Tariff Structure¹

PERIOD	Nominal average tariff rates %	Nominal maximum of tariff rates %
1973 2nd Semester	94	600
1974 1st Semester	80	160
1974 2nd Semester	67	140
1975 1st Semester	52	120
1975 2nd Semester	44	90
1976 1st Semester	38	70
1976 2nd Semester	33	60
1977 1st Semester	24	50
1977 2nd Semester	20	35
1978 1st Semester	15	25
1978 2nd Semester	13	20
1979 1st Semester	11	14
1979 Month of July	10	10

¹The automobile industry is an exception. This situation has been changed recently with the establishment of a 10% tariff on all vehicles as of 1986.

With respect to prior deposits, in September, 1973, 2,872 tariff items were subject to prior deposits of 10,000%. In September of 1977 there were only 32 categories which remained subject to these prior deposits and at the present time this regulation only applies to certain types of used vehicles.

The Growth objective is visualized by means of higher levels of expenditure of the gross domestic product, (EGDP), employment and savings.

Rates of Growth
(Percentages)

YEAR	E.G.D.P.	EMPLOYMENT (Greater Santiago, Dec. each year)
1970	3,6	- 1,0
1971	7,7	7,4
1972	- 0,1	2,1
1973	- 3,6	5,4
1974	4,0	1,1
1975	-12,9	- 6,1
1976	4,0	9,3
1977	8,6	4,9
1978	7,3	5,0

The process of internal saving has been strengthened by the development of national capital markets. This had been possible because of free interest rates (which previously were fixed), the implementation of a tax system which does not discriminate among financial instruments and the elimination of the principal state monopolies in investment. All this has resulted in the creation of a number of instruments and financial institutions.

YEAR	Real annual interest rate (In % deflated by CPI) ¹ (Interest charged)	Real Quasi money Private Sector (Average real balance each year in millions of 1976 dollars) ²
1970	- 11,05	290
1971	- 5,82	408
1972	- 54,45	367
1973	- 70,5	221
1974	- 36,9	118
1975	16,0	213
1976	64,2	345
1977	56,7	639
1978	41,2	991

¹Taking into consideration that the official CPI may be overvalued between 1971 and 1973, the real rates of interest for this period would be even more negative.

²SOURCE: Report on the State of Public Finance, January 1979.

The achievement of the objective of greater Development is closely related to the target of increased and sustained growth under stable conditions and a State policy on distribution that guarantees that improved well-being reaches all sectors of the country, especially those presently living in poverty.

With respect to the functional distribution of income, the following analysis should be made: Between 1970 and 1978, employment has increased 15.1% and the product has increased 12.6%. By deflating the nominal wage and salary index by various consumer price indices (considering different types of corrections in the prices for the 1971-73 period because of the existence of black markets for a great many products), an increase in real salaries between 1970 and 1978 is obtained that fluctuates between 1% and 55%.

Given that the real wages at least are similar in 1970 and 1978 it can be stated that, in the worst case, the participation of labor in the product has increased by 2.2 points between 1970 and 1978.

A similar comparison for the years 1970 and 1973 will reveal that between both years, using similar deflators as in the former case, the real Wage and Salary Index, shows a variation that fluctuates between -29.6% and +3.0%. It can be deduced that in the worst case, the percentage of labor participation (or share) in the product has improved with respect to 1970 and it becomes clear that there has been a significant improvement since 1973.

In the field of Development, the problems which the Government has to face require two types of measures:

- a) Palliative measures to solve adjustment problems and,
- b) Long term measures, basically intended as investments in human capital, and on the other hand, to raise the standard of living in the passive sector.

Within the palliative measures related to unemployment, the Government has implemented several subsidies, for example:

The Minimum Employment Program (MEP).

The unemployment subsidy for blue collar workers, which formerly only existed for white collar workers through the social security systems.

Bonuses for hiring additional manpower.

Fiscal Expenditure for Unemployment



Fiscal Expenditure in: millions of 1976 US\$

YEAR	Rate of Unemployment (Nationwide)	M.E.P.	Bonus for Additional Hiring
1970	6,1	—	—
1971	3,8	—	—
1972	3,1	—	—
1973	4,8	—	—
1974	9,2	—	—
1975	14,5	34,10	—
1976	13,7	82,67	4,30
1977	12,7	74,03	10,96
1978*	10,9	45,27	13,75

*Provisional figures.

Within the long term measures, the following are the most noteworthy:

- Progressive reductions in social security payments deductions.
- Programs directed to minors.
- Reorganization of expenditures in education.
- Improving the standard of living in the passive sector.

Rates of social security deductions payments for white and blue collar workers (% over taxable wages)

YEAR	WHITE COLLAR	BLUE COLLAR
1970	59,3	48,9
1971	59,0	49,7
1972	59,0	49,9
1973	59,0	49,9
1974	64,8	56,9
1975	59,3	51,4
1976	59,1	51,2
1977	56,1	48,2
1978	46,2	38,7
1979	44,0	36,2

—Programs directed to minors.

These are a set of programs for the purpose of aiding children from lower income sectors. These programs are the following:

—Free milk to children under six years and pregnant mothers.

—National Day Care Commission.

—National Council for Minors that coordinates attention to homes for children in irregular situations.

YEAR	Milk Program (thous. of kilos)	National Day Care Commission		National Council for Minors
		No. Centers	No. Children	No. of Children
1970	12.695	n.d.	n.d.	n.d.
1971	18.961	n.d.	n.d.	n.d.
1972	19.286	n.d.	n.d.	n.d.
1973	20.291	123	10.085	9.308
1974	20.806	179	16.199	15.515
1975	23.584	381	31.743	20.316
1976	24.490	364	33.041	25.340
1977	28.657	414	39.753	28.244
1978	32.391	407	39.948	29.682

Some of the effects of these programs are observed in the following charts:

Population under six years, receiving nutritional assistance

YEAR	Population in control	% Normal	% undernourished (light to serious)
1975	920.161	82,0	18,0
1976	1.047.796	84,1	15,9
1977	1.070.767	85,1	14,9
1978	1.149.000	87,6	12,4

Infant mortality
(Rate per 1,000 born alive)

1970	1971	1972	1973	1974	1975	1976	1977	1978
79,3	70,5	71,1	65,2	63,3	55,4	54,7	47,5	38,7

The Education policy has been directed toward the production of an improvement in the quality of education.

The subsidies to private schools have been improved and there has been a reallocation of fiscal expenditure in Education, especially from higher education toward elementary education.

Percentage of Fiscal Expenditure in Education

YEAR	Higher Education	Elementary & Other
1970	30,5	69,5
1971	31,8	68,2
1972	36,1	63,9
1973	39,8	60,2
1974	40,9	59,1
1975	33,3	66,7
1976	31,8	68,2
1977	34,1	65,9
1978	33,9	66,1
1979	30,8	69,2

Subsidies to Private Schools

YEAR	Total Subsidies (Thousands US\$ 1976)	No. Students Subsidized	Subsidy per Student (US\$ 1976)
1969	12.773	327.434	39,0
1970	13.866	330.671	41,9
1971	16.190	314.836	51,4
1972	15.783	320.434	49,3
1973	8.567	315.717	27,1
1974	8.304	326.021	25,5
1975	8.625	321.793	26,8
1976	13.286	321.959	41,3
1977	17.148	334.245	51,3
1978	19.529	365.998	53,4
1979	37.493	401.000	93,5

With respect to the Social Security System, the minimum pensions and family allowances for blue collar and white collar workers, which formerly had been different, are now exactly the same.

Several special improvements in the minimum pensions have also been authorized.

In real terms, and using various deflators (according to whether or not the distortions produced in the 1971-1973 period by the black markets are taken into account), the following evolution in the minimum pensions can be observed:

Minimum Pensions for Blue Collar Workers

	In \$ Dec. 78 (1)	% variation for the period (1)	In \$ Dec. 78 (2)	% variation for the period (2)
1970	812	—	1.246	—
1973	1.095	34,9	1.153	- 7,5
1978	1.800	64,4	1.800	56,1

NOTE: (1) Figures deflated by the CPI, National Bureau of Statistics.

(2) Figures deflated by the CPI corrected on the basis of estimates from the Department of Economics of the University of Chile.

Minimum Pensions for White Collar Workers

	In \$ Dec. 78 (1)	% variation for the period (1)	In \$ Dec. 78 (2)	% variation for the period (2)
1970	1.360	—	2.091	—
1973	1.115	- 18,0	1.172	- 44,0
1978	1.800	61,4	1.800	53,6

NOTE: (1) Figures deflated by the CPI, National Bureau of Statistics.

(2) Figures deflated by the CPI corrected on the basis of estimates from the Department of Economics of the University of Chile.

The family allowances for blue and white collar workers have been the same since 1974.

Family allowance of blue collar worker as % of family allowance of white collar worker

YEAR	Family allowance of blue collar worker as % of family allowance of white collar worker
1970	38,44
1971	53,39
1972	50,85
1973	46,25
1974	100,00
1975	100,00
1976	100,00
1977	100,00
1978	100,00

The family allowances of a blue collar worker has grown in real terms since 1970 to 1978 between 70% and 14%, according to the various deflators.

D.L. No. 869 of 1974 establishes a pension assistance system for the elderly and the invalids without means of support. The number of beneficiaries has been as follows:

YEAR	No. of Beneficiaries
1975	5,627
1976	37,359
1977	75,309
1978	101,440

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Fiscal Income, Expenditures and Deficit *
1960-1978

Local Currency
(Thousands of pesos for each year)

	1960	1961	1962	1963	1964	1965	1966	1967
TOTAL EXPENDITURE	810,9	898,0	1.143,5	1.646,8	2.377,8	3.912,0	5.474,9	6.611,8
— Debt Service	17,7	12,9	10,5	15,2	20,7	38,7	58,6	65,5
— Total Expenditure, excluding debt service ..	793,2	885,1	1.133,0	1.631,6	2.357,1	3.873,3	5.416,3	6.546,3
TOTAL REVENUES	592,1	707,0	841,0	1.253,1	1.836,7	3.046,9	4.388,6	5.708,7
— Direct Taxes	142,1	186,3	211,3	285,3	507,4	898,6	1.247,9	1.663,5
— Indirect Taxes	413,3	485,8	569,5	807,4	1.140,4	1.749,7	2.487,8	3.324,5
— Non Tax Income	36,7	34,9	55,0	77,7	109,1	241,4	272,1	261,1
— Copper	—	—	—	—	—	—	—	—
— Customs Duties and Extrabudgetary Adjustments	—	—	5,2	82,7	79,8	157,2	380,8	459,6
DEFICIT	218,8	191,0	302,5	393,7	541,1	865,1	1.086,3	903,1

Foreing Currency
(Millions of dollars for each year)

	1960	1961	1962	1963	1964	1965	1966	1967
TOTAL EXPENDITURES	91,51	112,10	117,60	113,10	113,50	120,70	144,50	142,60
— Debt Service	52,49	74,20	69,00	85,00	79,40	78,80	84,76	99,13
— Total Expenditure, excluding Debt Service	39,02	37,90	48,60	28,10	34,10	41,90	59,74	43,47
TOTAL REVENUES	110,13	96,29	103,60	99,40	121,10	142,30	217,10	203,60
— Direct Taxes	7,28	8,38	4,90	10,40	11,20	17,30	14,90	22,10
— Indirect Taxes	12,85	3,52	3,60	2,10	2,50	2,60	4,60	2,80
— Non Tax Income	2,28	11,86	2,50	0,60	2,60	0,90	0,30	—
Copper	87,72	72,53	92,60	86,30	104,80	121,50	197,30	178,70
— Customs Duties and Extrabudgetary Adjustments	—	—	—	—	—	—	—	—
DEFICIT	— 18,62	15,81	14,00	13,70	— 7,60	— 21,60	— 72,60	— 61,00

SOURCE: Budget Office, Ministry of Finance.

*The budget in Chile is calculated both in local as well as in foreign currency.

1968	1969	1970	1971	1972	1973	1974	1975	1976	1977	1978
8.956,7	13.771,0	21.223,1	34.377,8	68.931,9	486.898	2.298.072	7.448.718	24.101.700	57.024.800	94.534.400
152,7	235,6	310,6	234,2	659,9	2.424	35.439	87.712	289.200	1.054.700	1.237.400
8.804,0	13.535,4	20.912,5	34.143,6	68.272,0	484.474	2.262.633	7.361.006	23.812.500	55.970.100	93.297.000
7.838,8	12.758,6	18.175,8	24.754,4	41.351,8	226.970	1.775.068	7.901.704	25.204.700	57.601.100	100.565.500
2.136,8	2.869,4	4.349,6	7.222,0	9.893,9	59.598	512.326	2.425.447	6.538.100	14.745.900	24.742.500
4.915,1	7.398,0	10.407,1	14.704,1	26.006,0	123.287	1.034.075	5.114.402	17.947.300	41.069.600	70.817.000
408,3	713,4	1.024,0	1.753,0	2.861,0	16.500	228.667	361.855	719.300	1.785.600	5.006.000
—	0,8	1,1	0,3	—	—	—	—	—	—	—
378,6	1.777,0	2.394,0	1.075,0	2.590,9	27.585	—	—	—	—	—
1.117,9	1.012,4	3.047,3	9.623,4	27.580,1	259.928	523.004	452.986	-1.103.000	-576.300	-6.031.100

1968	1969	1970	1971	1972	1973	1974	1975	1976	1977	1978
153,27	193,40	272,20	257,35	118,37	169,41	618,69	555,74	694,74	623,82	664,43
101,26	137,09	176,98	185,57	50,96	78,88	337,92	387,69	543,64	444,78	492,48
52,01	56,31	95,22	71,78	67,41	90,53	280,77	168,05	151,10	179,04	171,95
195,20	248,10	291,90	60,92	34,88	28,60	216,39	218,69	382,92	374,30	342,87
20,00	20,30	18,50	12,63	1,32	2,39	10,63	20,87	14,00	10,30	13,51
2,50	2,50	2,80	7,11	5,07	5,57	10,92	13,78	9,70	9,33	11,08
0,20	1,40	2,70	2,10	2,77	1,43	4,24	7,50	7,28	1,48	1,92
172,50	223,90	267,90	39,08	25,72	19,21	190,60	176,54	351,94	353,19	316,36
—	—	—	—	—	—	—	—	—	—	—
— 41,93	— 54,70	— 19,70	196,43	83,49	140,81	402,30	337,05	311,82	249,52	321,56

Money, Quasimoney and Credit
(Balance as of December of each year in thousands of Pesos)

Date	Money Private Sector	Money Public Sector	Total Money	Quasi-Money (1)	Investments Banking System Local Currency
1960	383	94	477	161	426
1961	431	109	540	199	601
1962	557	199	756	296	767
1963	746	227	973	359	1.038
1964	1.129	347	1.476	506	1.406
1965	1.864	387	2.251	621	1.918
1966	2.590	472	3.062	982	2.384
1967	3.240	497	3.737	1.314	3.311
1968	4.480	943	5.423	1.793	4.423
1969	6.057	1.686	7.743	2.539	5.807
1970	10.068	2.046	12.114	4.329	8.206
1971	21.488	4.350	25.838	8.176	13.403
1972	54.111	16.373	70.484	17.551	29.995
1973	250.477	111.309	361.783	85.205	94.341
1974	829.578	426.129	1.255.707	404.092	358.559
1975	2.963.294	1.772.297	4.735.591	1.886.727	1.642.223
1976	8.574.645	5.659.737	14.234.382	3.887.913	7.676.757
1977	18.305.043	13.553.278	31.858.321	24.334.688	29.889.660
1978 (Oct.) (2)	25.544.674	21.319.466	46.864.140	48.505.229	57.997.170

SOURCE: Central Bank of Chile.

(1) Includes Readjustable Saving Certificates (CAR), series A and D.

(2) Provisional figures.

Balance of Payments 1960 - 1978 *
(Figures in Millions of US\$.)

ITEMS	1960	1961	1962	1963	1964	1965	1966	1967
EXPORTS OF GOODS AND SERVICES	551,7	530,6	567,6	583,1	674,9	774,8	976,6	983,5
— Copper	321,5	305,6	330,9	339,8	363,4	428,5	598,6	651,3
— Other Goods(4)	148,2	159,8	169,8	164,2	228,7	255,5	267,9	221,9
— Services	82,0	65,2	66,9	79,1	82,8	90,8	110,1	110,3
IMPORTS OF GOODS AND SERVICES	661,6	726,9	680,7	646,3	712,8	715,2	887,0	907,9
— Food	109,3	116,0	118,0	141,5	144,5	137,3	158,6	167,8
— Capital	156,7	203,4	190,7	149,3	179,0	159,6	222,4	227,3
— Intermediates (not food-stuffs)	209,9	236,4	220,5	218,3	247,0	274,1	342,5	316,2
— Consumption (not food-stuffs)	79,5	63,8	59,3	55,9	41,4	44,5	51,9	57,7
— Services	106,2	107,3	92,2	81,3	100,9	99,7	111,6	138,9
TRADE BALANCE (2)	— 85,7	— 154,2	— 87,8	— 61,0	— 19,8	68,5	91,1	104,2
BALANCE CURRENT ACCOUNT	— 148,1	— 263,8	— 202,1	— 198,8	— 128,5	— 56,6	— 82,2	— 127,4
BALANCE AUTONOMOUS CAPITAL	76,3	187,1	136,0	105,2	148,0	46,7	173,0	104,9
BALANCE OF PAYMENTS (3)	— 28,4	— 108,6	— 49,0	— 28,4	23,6	46,7	119,6	— 23,4

* Figures revised according to new method for calculating International Reserves as stipulated by the IMF.

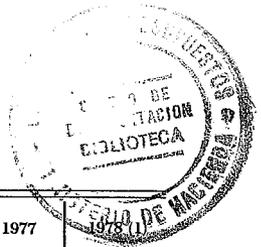
(1) Estimate.

(2) Defined as balance between Exports and Imports of Goods.

(3) Calculated on the basis of the new definition of international reserves.

(4) Does not include non monetary gold.

SOURCE: Central Bank of Chile.



1968	1969	1970	1971	1972	1973	1974	1975	1976	1977	
1.030,9	1.306,6	1.254,7	1.132,8	978,2	1.429,3	2.293,7	1.781,7	2.391,6	2.635,5	3.071,0
684,3	925,5	839,8	701,2	618,2	1.055,7	1.623,3	868,2	1.233,2	1.139,3	1.216,0
226,6	246,4	271,9	295,6	229,2	254,8	527,2	721,3	882,4	1.046,2	1.257,0
120,0	134,7	143,0	136,0	130,8	118,8	143,2	192,2	276,0	450,0	598,0
958,0	1.088,4	1.160,2	1.225,1	1.330,9	1.625,6	2.330,8	1.998,8	1.946,0	2.722,6	3.386,0
164,6	165,2	135,5	192,2	338,4	511,6	445,5	361,0	342,0	331,4	458,0
237,3	244,2	276,2	248,0	165,1	243,3	281,2	325,4	366,5	465,5	688,0
320,7	434,5	445,0	485,2	460,2	553,4	1.172,5	903,7	845,5	1.105,6	1.331,0
79,0	82,9	99,3	89,5	138,9	139,1	116,3	117,7	101,0	341,1	413,0
156,4	161,6	204,2	210,2	228,3	178,2	315,3	291,0	291,0	479,0	496,0
109,3	245,1	155,7	18,1	255,2	136,9	135,0	118,3	460,6	58,1	417,0
135,2	5,6	81,1	188,8	386,6	287,6	210,8	491,3	148,0	399,0	721,0
282,8	219,9	267,5	26,5	327,4	242,3	228,0	298,7	235,0	346,0	1.351,0
117,9	174,5	113,5	299,8	229,0	111,9	45,1	274,6	455,0	7,0	630,0

Projection of Balance of Payments
1977 - 1978 *
(In millions of dollars)

Items	1977	1978
Export	2.636	3.071
Goods (1)	2.186	2.473
Services	450	598
Imports	2.723	3.386
Goods	2.244	2.890
Services	479	496
Commercial Balance	— 87	— 315
Remittances from abroad	50	57
Donations	(50)	(57)
Central Bank Interest	—	—
Remittances Overseas	362	463
Profit	23	36
Interest	339	427
— Medium and Long Term Debt	(291)	(401)
— Short Term Debt and IMF	(48)	(26)
Balance Current Account	— 399	— 721
Balance Autonomous Capital	346	1.351
Utilization	1.221	2.280
Amortization	871	924
— Long and Medium Term Debt	(866)	(919)
— Capital Investment Overseas	(5)	(5)
Adjustment, Errors and Omissions	46	—
Balance of Payments	— 7	630

SOURCE: Central Bank of Chile.

(1) Includes non monetary gold.

* Because of the use of round numbers, the totals may not correspond exactly to the sub-totals.

Exports of Goods *
(In millions of dollars)

Items	1977	1978
I. Minerals	1.336	1.420
Copper	1.139	1.216
— Large Mining	(947)	(1.012)
— Small and Medium Mining	(192)	(204)
Iron	82	96
Nitrate, Iodine	44	50
Others (1)	71	57
II. Agricultural and Seafood	160	220
Agricultural	127	170
Cattle	23	34
Forestry	1	2
Fishing	9	14
III. Industrial	690	833
Foodstuffs	170	197
Beverages	8	9
Lumber	70	100
Paper, cellulose, cardboard	136	150
Chemical products	78	105
Basic metal industries	166	186
Metal prods., small elect. appliances	37	55
Other	28	31
IV. Total	2.186	2.473

(1) Includes non monetary gold.

*Because of the use of round numbers, the totals may not correspond exactly to the sub-totals.

Copper Exports

ITEMS	1977	1978
I. Large Mining		
Exports of raw materials (thousands M.T.)	830,7	849,8
(Mills. lbs.)	1.826,0	1.868,0
CIF Price LME (c/lb)	59,29	61,00
Discounts (c/lb)	8,43	6,80
FOB Price (c/lb)	50,86	54,20
FOB Value (mills. US\$)	947,0	1.012,0
II. Small and Medium Mining		
Production (thousands M.T.)	160,6	165,6
Sales (thousands M.T.)	160,6	165,6
(Mills. lbs.)	353,0	364,0
CIF Price LME (c/lb.)	59,29	61,00
Expenses abroad (c/lb.)	4,85	5,00
Price FOB Chile (c/lb.)	54,44	56,00
Value FOB Chile (Mills. US\$)	192,0	204,0
III. Total Copper Exports		
(Mills. US\$)	1.139,0	1.216,0

Exports of Selected Important Products in 1978
(Excludes copper)

Products	Volume Thous. Tons.	FOB US\$/Ton.	Value Mill. US\$
A. Minerals			
Iron*	6,685.2	14.37	96.0
Nitrate	458.9	83.1	38.1
Iodine	2.3	4,769.2	10.8
B. Industrials			
Fish meal	250.0	360.0	90.0
Paper	80.0	384.6	30.8
Cellulose	401.6	257.6	103.5
Cardboard	12.5	830.0	10.4

*Includes mineral iron and pellets.

Merchandise Imports
(In millions of dollars)

ITEMS	1977	1978
I. Consumer Goods	672	871
Non-foods	341	413
Food	331	458
II. Intermediate Goods	1.106	1.331
Raw Materials	303	339
Spare parts and Intermediate products	324	469
Petroleum	378	378
Lubricants and other fuels	40	80
For Large Copper Mines	61	65
III. Current Goods (I + II)	1.778	2.202
IV. Capital Goods	466	688
— Copper	35	42
— Remaining	431	646
TOTAL (III + IV)	2.244	2.890

Food Imports

	1977 Value (Mills. US\$)	1978 Value (Mills. US\$)
Wheat	70,5	145,6
Corn	14,6	23,0
Rice	5,0	6,0
Oil	37,4	39,0
Sugar	37,4	50,4
Meat	8,2	20,2
Milk	8,6	15,0
Butter	9,6	9,0
Tea	19,0	14,0
Coffee	13,8	14,0
Bananas	8,0	17,0
Others	72,5	70,2
Donations	26,0	35,0
TOTAL	330,6	458,4

International Reserves
(Millions of Dollars)

	1960	1961	1962	1963	1964	1965	1966	1967
I. CENTRAL BANK OF CHILE (A-B)	38,4	— 55,8	— 55,5	— 84,8	— 65,2	— 34,2	45,1	20,1
A. Assets	131,7	98,9	103,8	101,8	113,6	162,5	197,3	153,1
1. Gold	45,1	47,8	42,8	43,1	43,1	43,9	45,4	45,1
2. SDR's	—	—	—	—	—	—	—	—
3. Reserve Tranche	18,7	25,0	25,0	25,0	25,0	25,0	25,0	25,0
4. Foreign Corresponding Banks	65,5	26,1	36,0	33,9	45,5	93,6	125,9	80,4
a) Freely disposable	(65,5)	(26,1)	(36,0)	(33,9)	(45,5)	(93,6)	(125,9)	(80,4)
b) Blocked	(—)	(—)	(—)	(—)	(—)	(—)	(—)	(—)
c) Frozen	(—)	(—)	(—)	(—)	(—)	(—)	(—)	(—)
5. IBD, IBRD, CAF*	—	—	—	—	—	—	1,0	1,0
6. Santo Domingo Agreement and Others	—	—	—	—	—	—	—	—
7. Reciprocal Trade	—	—	—	—	—	—	—	—
8. Notes, Bonds and CD's	2,4	—	—	—	—	—	—	1,6
B. Liabilities	93,3	154,7	159,3	186,6	178,8	196,7	152,2	133,0
1. I.M.F.	29,4	88,7	76,0	116,0	126,0	125,0	110,2	95,0
2. Short Term Credit	34,4	50,6	70,3	60,3	48,7	69,4	32,3	34,2
3. Reciprocal Trade Agreements	29,5	15,4	12,4	10,3	4,1	2,3	9,7	3,0
II. COMMERCIAL BANKS AND BANCO DEL ESTADO (A-B)	— 15,4	— 29,8	— 79,1	— 78,2	— 74,2	— 58,5	— 18,2	— 16,6
A. Assets	16,9	20,6	14,8	22,3	21,9	21,7	46,3	50,7
1. Gold	2,1	4,2	5,7	5,2	5,5	5,5	4,7	5,0
2. Foreign Corresponding Banks	14,8	16,4	9,1	17,1	16,4	16,2	41,6	45,7
B. Liabilities	32,3	50,4	93,9	100,5	96,1	80,2	64,5	67,3
1. Debts with foreign Banks	31,0	49,1	87,9	98,0	94,1	77,5	62,7	65,7
2. Deposits of foreign banks	1,3	1,3	6,0	2,5	2,0	2,7	1,8	1,6
III. TOTAL NET INTERNATIONAL RESERVES (I+II)	23,0	— 85,6	— 134,6	— 163,0	— 139,4	— 92,7	26,9	3,5
IV. MEDIUM AND LONG TERM LIABILITIES	56,8	77,9	99,9	100,2	99,3	90,1	93,0	94,8
1. Central Bank of Chile	56,8	77,9	99,9	100,2	99,3	90,1	93,0	94,8
a) Renegotiation of foreign debt	—	—	—	—	—	—	11,0	12,6
b) Other Credits to Central Bank	56,8	77,9	99,9	100,2	99,3	90,1	82,0	82,2
2. Other Banks	—	—	—	—	—	—	—	—
a) Banco del Estado de Chile	—	—	—	—	—	—	—	—
b) Others	—	—	—	—	—	—	—	—

SOURCE: Central Bank of Chile. *Andean Development Corporation.

1968	1969	1970	1971	1972	1973	1974	1975	1976	1977	1978 (1)
125,4	285,2	393,8	154,1	33,5	12,9	— 42,3	—375,7	43,5	164,2	814,8
242,3	381,1	435,0	253,5	194,7	306,0	312,1	241,3	658,5	722,0	1.296,2
46,4	47,5	46,7	47,1	51,5	58,1	60,7	54,8	56,4	57,6	56,8
—	—	21,8	38,3	2,2	0,4	16,8	24,5	55,9	66,2	26,3
31,3	31,3	39,5	39,6	42,9	47,6	48,2	46,3	45,7	47,8	50,3
160,4	290,5	310,3	120,9	96,7	134,9	37,7	31,4	343,1	316,1	744,2
(160,4)	(290,5)	(310,3)	(120,9)	(94,6)	(132,7)	(35,7)	(19,0)	(325,7)	(290,7)	(726,1)
(—)	(—)	(—)	(—)	(2,1)	(2,2)	(2,0)	(0,7)	(4,8)	(10,2)	(0,2)
(—)	(—)	(—)	(—)	(—)	(—)	(—)	(11,7)	(12,6)	(15,2)	(17,9)
1,5	5,5	9,9	7,5	—	—	—	2,0	8,0	14,0	13,5
—	—	—	—	—	—	—	0,8	—	3,7	3,8
2,7	6,3	6,8	0,1	1,4	65,0	148,7	81,5	149,4	186,6	183,7
—	—	—	—	—	—	—	—	—	30,0	217,6
116,9	95,9	41,2	99,4	161,2	293,1	354,4	617,0	615,0	557,8	481,4
110,3	88,3	41,0	79,0	128,7	143,0	243,3	433,7	511,5	411,8	339,1
—	—	—	—	14,3	78,7	—	132,3	—	4,8	9,5
6,6	7,6	0,2	20,4	18,2	71,4	111,1	50,4	103,5	141,2	132,8
— 4,0	10,7	15,5	— 44,6	—153,0	—244,3	—234,2	—175,4	—139,4	—266,7	—358,5
52,2	59,3	66,7	44,2	56,2	71,5	107,1	96,2	124,2	104,7	115,6
4,9	5,1	4,2	4,1	4,3	4,3	5,7	5,7	5,9	5,6	5,7
47,3	54,2	62,5	40,1	52,0	67,2	101,4	90,5	118,3	99,1	109,3
56,2	48,6	51,2	88,8	209,2	315,8	341,3	271,6	263,6	371,4	483,5
53,6	46,3	47,6	82,9	204,9	302,3	338,5	267,7	255,8	363,9	481,1
2,6	2,3	3,6	5,9	4,3	13,5	2,8	3,9	7,8	7,5	2,4
121,4	295,9	409,3	109,5	—119,5	—231,4	—276,5	—551,1	—95,9	—102,5	446,3
83,6	75,8	66,1	75,2	323,1	493,5	589,9	528,3	601,4	577,0	1.123,7
83,6	73,7	61,1	65,1	295,4	454,4	522,3	476,2	568,5	537,6	831,2
11,5	6,4	—	—	152,4	186,8	188,6	158,2	98,5	72,3	54,9
72,1	67,3	61,1	65,1	143,0	267,6	333,7	318,0	470,0	465,3	776,3
—	2,1	5,0	10,1	27,7	39,1	67,6	52,1	32,9	39,4	232,5
—	2,1	5,0	10,1	27,7	39,1	67,6	52,1	32,9	22,8	107,8
—	—	—	—	—	—	—	—	—	16,6	184,9

(1) Provisional figures. November, 1978.

Explanatory Notes

The new presentation of International Reserves includes the following changes:

The Reserve Tranche in the I.M.F. which had been eliminated as of January, 1974, from both the Assets and the Liabilities of the Central Bank, has been included in order to reflect more accurately the situation with the I.M.F. and to make it compatible with the figures of the Monetary Accounts and the Central Bank Balance.

In the Liabilities of the Central Bank as well as of the Banco del Estado and Commercial Banks, only debts which expire in less than one year have been included. The only exception is in the case of longer term I.M.F. credits, which do, however, constitute part of the compensating capital in the Balance of Payments.

Those Liabilities which expire after one year are listed in Point IV by way of information.

Gross figures are given for Assets and Liabilities of Commercial Banks and Banco del Estado. In the previous presentation, net values were included, that is, the credits granted to foreign banks were subtracted from the Liabilities and were not included in the Assets.

In order to obtain the International Reserves according to the previous definition, the medium and long term Liabilities (IV) must be subtracted from the total of Net International Reserves (III).

For the confection of the present series the information has been thoroughly checked; this has caused adjustments in some of the figures.

SOURCE: Years 1960-69: Banking Statistics of the Superintendency of Banks.

Overall Chilean Foreign Debt at December 31 of each year (1)
Nominal Series 1960 - August, 1978
(Millions of dollars of each year)

	1960	1961	1962	1963	1964	1965	1966	1967
I. Traditional Foreign Debt	456	530	653	816	931	1,079	1,198	1,237
II. Other Foreign Liabilities	290	480	602	653	704	702	654	671
1. I.M.F.	29	89	76	116	126	125	110	95
2. Credit from Suppliers to the Private Sector (Deferred Payments)	121	161	199	219	270	233	218	207
3. Financial Credit to Private Sector Decree 1,272 (Art. 14, 15 and 16)	75	130	168	160	165	197	231	269
4. Short term lines of credit to commercial banks, Banco del Estado and Central Bank	65	100	159	158	143	147	95	100
TOTAL (I + II)	746	1,010	1,255	1,469	1,635	1,781	1,852	1,908

SOURCE: Central Bank of Chile.

NOTES:

- (1) Excludes balances to be used. With the exception of point II 4., the rest refer to credits of one year or more.
- (2) Includes balances of credits contracted by private enterprises which are incorporated in the public sector (Pacific Steel Company (CAP) mining companies and others). In the following years, these companies are classified as belonging to the public sector.
- (3) Excludes balances of credits contracted by enterprises incorporated in the public sector.

1968	1969	1970	1971	1972	1973	1974	1975	1976	1977	August 1978
1.422	1.873	2.533(2)	2.640	2.880	3.159	3.779	3.787	3.654	3.673	4.134
779	816	590	556	722	889	995	1.476	1.541	1.761	2.109
110	88	41	79	129	143	243	434	513	412	371
299	292	88(3)	74	64	59	91	141	172	180	177
316	390	413	320	310	306	322	500	600	800	1.134
54	46	48	83	219	381	339	401	256	369	427
2.201	2.689	3.123	3.196	3.602	4.048	4.774	5.263	5.195	5.434	6.243



Product, Consumption, Investment, Exports and Imports (1)

(Figures in thousands of pesos for each year)

Years	Consumption Outlay-of indi- viduals and non-profit institutions	Consumption Outlay Government in General	Gross Invest- ment in Fixed Capital	Increase in Stocks	Exports of Goods and Services	Minus: Imports of Goods and Services	Outlay of GDP at market prices
1960	3.114	447	641	81	574	697	4.160
1961	3.576	510	793	65	568	773	4.739
1962	4.317	613	873	17	665	746	5.739
1963	6.480	842	1.441	106	1.091	1.306	8.654
1964	9.858	1.266	2.111	111	1.644	1.763	13.227
1965	13.359	1.993	2.859	395	2.515	2.369	18.752
1966	18.438	2.953	3.793	672	3.894	3.594	26.156
1967	25.004	3.824	4.761	311	4.931	4.464	34.367
1968	33.574	5.251	6.711	423	6.649	6.261	46.347
1969	47.437	7.631	9.655	1.102	11.430	9.818	67.437
1970	68.610	12.613	13.306	1.790	14.539	13.887	96.971
1971	92.723	19.370	16.772	1.475	13.927	15.226	129.041
1972	179.067	37.700	28.241	648	22.482	29.153	238.985
1973	906.755	149.971	162.652	19.458	137.781	166.065	1.210.552
1974	7.038.242	1.252.122	1.335.154	(3) —	1.523.709	1.685.206	9.464.020
1975 (2)	30.598.385	4.605.233	4.670.989	(3) —	6.018.209	7.211.365	38.681.452

SOURCE: National Accounts of Chile, Planning Office.

(1) Includes modifications for change in the Housing Ownership Sector since 1960, in Agricultural and Foreign Trade Sectors since 1970.

(2) Provisional figures subject to revision.

(3) Waiting for new statistical data; no estimates of this variable have been made.

Product, Consumption, Investment, Exports and Imports (1)

(Figures in thousand of 1965 pesos)

Years	Consumption Outlay of indi- viduals and non-profit institutions	Consumption Outlay Government in General	Gross Invest- ment in Fixed Capital	Increase in Stocks	Exports of Goods and Services	Minus: Imports of Goods and Services	Outlay of GDP at market prices
1960	10.746	1.656	2.142	259	1.938	2.068	14.673
1961	11.465	1.685	2.546	207	1.992	2.328	15.567
1962	11.857	1.792	2.626	53	2.106	2.147	16.287
1963	12.376	1.752	2.834	193	2.155	2.195	17.115
1964	13.063	1.824	2.735	149	2.366	2.287	17.850
1965	13.359	1.993	2.859	395	2.515	2.369	18.752
1966	14.780	2.187	2.900	542	2.662	3.005	20.066
1967	15.298	2.186	2.941	191	2.851	2.912	20.555
1968	15.790	2.296	3.166	204	2.875	3.159	21.172
1969	16.222	2.431	3.313	417	3.055	3.533	21.905
1970	16.868	2.591	3.407	467	3.043	3.678	22.695
1971	18.563	2.831	3.446	300	2.982	3.682	24.440
1972	19.555	2.931	2.837	167	2.536	3.607	24.419
1973	19.019	3.116	3.000	579	2.387	4.566	23.535
1974	18.381	3.568	3.363	(3) —	3.379	4.193	24.498
1975 (2)	15.783	3.017	2.431	(3) —	3.264	3.157	21.333

SOURCE: National Accounts of Chile, Planning Office.

(1) Includes modification for change in the Housing Ownership Sector since 1960, in Agricultural and Foreign Trade Sectors since 1970.

(2) Provisional figures subject to revision.

(3) Waiting for new statistical data; no estimates of this variable have been made.

**Rates of Growth in Outlay of GDP
at Market Prices**

	Outlay of GDP (in thousands of 1965 \$)	% Annual Variation	% Per Capita Variation
1960	14.673	—	—
1961	15.567	6,1	3,6
1962	16.287	4,6	2,1
1963	17.115	5,1	2,7
1964	17.850	4,3	2,0
1965	18.752	5,1	2,8
1966	20.066	7,0	4,9
1967	20.555	2,4	0,5
1968	21.172	3,0	1,0
1969	21.905	3,5	1,5
1970	22.695	3,6	1,6
1971	24.440	7,7	5,8
1972	24.419	— 0,1	— 1,9
1973	23.535	— 3,6	— 5,3
1974	24.498	4,0	2,2
1975 (*)	21.338	— 12,9	— 14,5
1976 (*)	22.192	4,0	2,1
1977 (*)	24.101	8,6	6,6
1978 (*)	25.860	7,3	5,3

SOURCE: Chilean National Accounts, Planning Office.

* Provisional estimate.

Employment and Population on National Level
(Thousand of Persons)

	Total Population	% Var.	Active Population	% Var.	Employed Population	% Var.	Unemployed Population	Rate of Unemployment
1960	7.585,3	—	2.427,3	—	2.255,0	—	172,3	7,1
1961	7.773,3	2,5	2.474,6	1,9	2.276,6	1,0	198,0	8,0
1962	7.961,3	2,4	2.522,8	1,9	2.323,5	2,1	199,3	7,9
1963	8.147,3	2,3	2.572,0	2,0	2.379,1	2,4	192,9	7,5
1964	8.330,4	2,2	2.622,1	1,9	2.438,6	2,5	183,5	7,0
1965	8.509,9	2,2	2.673,2	1,9	2.502,1	2,6	171,1	6,4
1966	8.685,9	2,1	2.725,3	1,9	2.559,1	2,3	166,2	6,1
1967	8.858,9	2,0	2.778,4	1,9	2.647,8	3,5	130,6	4,7
1968	9.029,6	1,9	2.832,6	2,0	2.693,8	1,7	138,8	4,9
1969	9.199,1	1,9	2.887,8	1,9	2.714,5	0,8	173,3	6,0
1970	9.368,6	1,8	2.950,1	2,2	2.770,1	2,0	180,0	6,1
1971	9.539,1	1,8	3.020,9	2,4	2.906,1	4,9	114,8	3,8
1972	9.711,9	1,8	3.093,9	2,4	2.998,0	3,2	95,9	3,1
1973	9.887,9	1,8	3.167,6	2,4	3.015,6	0,6	152,0	4,8
1974	10.068,1	1,8	3.243,6	2,4	2.945,2	—2,3	298,4	9,2
1975	10.253,0	1,8	3.321,3	2,4	2.839,7	—3,6	481,6	14,5
1976	10.443,2	1,9	3.404,7	2,5	2.938,8	3,5	465,9	13,7
1977	10.639,0	1,9	3.490,2	2,5	3.046,9	3,7	443,3	12,7
1978 *	10.840,5	1,9	3.577,8	2,5	3.187,4	4,6	390,4	10,9

SOURCE: Total Population Planning Office/Latin American Demographic Center. Projection of Chilean population by sex and by 5-year age groups 1950—2,000, Santiago, May, 1975.

Active Population-1970-1974 Latin American Demographic Center, Chile. Projection of the economically active population 1970 - 2,000 Bulletin No. 15.

Employment and Unemployment Population, Planning Office.

*Provisional Estimate.

Population and Employment in Greater Santiago

		Total Population	Labor Force	Employed	Unemployed	Rate of Unemployment
February - April	1973	3.334,6	1.094,5	1.034,4	60,1	5,5
May - July	1973	3.358,3	1.028,0	984,8	43,2	4,2
August - September	1973	3.378,0	1.028,3	986,2	42,1	4,1
October - December	1973	3.397,7	997,5	943,2	54,3	5,5
January - March	1974	3.421,6	1.031,7	963,3	68,4	6,6
April - June	1974	3.449,6	1.086,3	997,0	39,3	8,2
July - September	1974	3.469,7	1.083,8	992,6	91,1	8,4
October - December	1974	3.490,0	1.123,7	1.014,2	109,5	9,7
January - March	1975	3.401,5	1.078,6	944,3	134,3	12,4
April - June	1975	3.426,5	1.133,7	966,1	167,6	14,8
July - September	1975	3.451,8	1.080,7	903,9	176,8	16,4
October - December	1975	3.481,9	1.103,7	921,2	182,5	16,5
January - March	1976	3.508,8	1.147,8	945,7	202,1	17,6
April - June	1976	3.535,7	1.235,4	998,7	236,7	19,1
July - September (1)	1976	3.509,0	1.219,9	1.002,6	217,3	17,8
October - December	1976	3.533,1	1.177,0	1.016,5	160,5	13,6
January - March	1977	3.557,4	1.183,6	997,1	186,5	15,8
April - June	1977	3.582,1	1.234,6	1.050,6	184,0	14,9
July - September	1977	3.606,6	1.203,3	1.044,3	159,0	13,2
October - December	1977	3.630,9	1.186,8	1.050,2	136,6	11,5
January - March	1978	3.655,1	1.245,7	1.073,0	167,7	13,5
April - June	1978	3.679,4	1.304,5	1.132,7	171,8	13,2
July - September	1978	3.703,7	1.349,1	1.151,8	197,3	14,6

(1) Calculations made with a new projection of the population as of July - September 1976.

SOURCE: National Statistics Bureau.

Population and Employment in Greater Santiago
(Thousands of persons)

Year	Month	Total Population	Labor Force	Employed	Unemployed	Rate of Unemployment (%)
1960	December	1.996,1	736,7	684,9	51,8	7,0
1961	March	2.014,5	741,0	684,5	56,5	7,6
	June	2.033,1	724,0	672,8	51,2	7,1
	September	2.051,8	729,6	679,5	50,1	6,9
	December	2.070,7	741,9	705,0	36,9	5,0
1962	March	2.089,8	761,6	714,7	47,0	6,2
	June	2.109,1	754,5	711,5	43,0	5,7
	September	2.128,5	773,7	740,8	33,0	4,3
	December	2.148,1	774,1	737,1	37,1	4,8
1963	March	2.167,9	778,3	735,5	42,8	5,5
	June	2.187,9	775,3	735,2	40,2	5,2
	September	2.208,1	788,3	747,3	41,0	5,2
	December	2.258,5	779,2	745,7	33,5	4,3
1964	March	2.279,3	790,9	750,6	40,3	5,1
	June	2.300,3	793,6	754,5	39,2	4,9
	September	2.321,5	814,5	764,4	50,1	6,2
	December	2.342,9	794,2	756,1	38,1	4,8
1965	March	2.364,5	825,2	774,9	50,3	6,1
	June	2.386,3	828,0	786,6	41,4	5,0
	September	2.408,3	840,5	790,9	49,6	5,9
	December	2.430,5	845,8	806,1	39,8	4,7
1966	March	2.452,9	841,3	801,8	39,5	4,7
	June	2.475,5	854,6	803,6	51,1	6,0
	September	2.498,3	874,4	828,1	46,3	5,3
	December	2.521,3	895,1	846,7	48,3	5,4
1967	March	2.544,5	877,9	822,5	55,3	6,3
	June	2.568,0	898,8	845,8	53,0	5,9
	September	2.591,7	914,9	861,8	53,1	5,8
	December	2.615,6	920,7	861,8	58,9	6,4
1968	March	2.639,7	902,7	852,4	50,3	5,6
	June	2.664,0	929,1	869,7	59,4	6,4
	September	2.688,6	943,2	879,5	63,6	6,7
	December	2.713,4	965,1	912,9	52,2	5,4
1969	March	2.738,4	953,0	888,2	64,8	6,8
	June	2.763,6	968,1	899,0	69,1	7,1
	September	2.789,1	992,9	940,3	52,6	5,3
	December	2.814,8	1.012,6	958,0	54,7	5,4
1970	March	2.840,7	987,4	920,0	67,5	6,8
	June	2.866,9	1.023,4	951,9	71,5	7,0
	September	2.893,3	1.021,0	955,3	65,6	6,4
	December	2.920,0	1.034,1	948,8	85,4	8,3
1971	March	2.946,9	1.031,4	946,4	85,0	8,2
	June	2.974,1	1.073,8	1.018,0	55,8	5,2
	September	3.001,5	1.061,8	1.011,1	50,7	4,8
	December	3.029,2	1.059,4	1.019,3	40,1	3,8

Continued on following page.

Population and Employment in Greater Santiago
(Thousands of persons)

(Continuation)

Year	Month	Total Population	Labor Force	Employed	Unemployed	Rate of Unemployment (%)
1972	March	3,057,1	1,060,6	1,010,2	50,4	4,8
	June	3,085,3	1,105,3	1,064,7	40,7	3,7
	September	3,113,7	1,065,9	1,034,0	31,9	3,0
	December	3,142,4	1,079,4	1,040,9	38,5	3,6
1973	March	3,171,4	1,104,1	1,062,5	41,6	3,8
	June	3,200,6	1,135,0	1,099,8	35,2	3,1
	September	—	—	—	—	—
	December	3,382,0	1,180,3	1,097,6	82,8	7,0
1974	March	3,413,2	1,179,2	1,070,3	109,0	9,2
	June	3,444,7	1,182,9	1,060,6	122,3	10,3
	September	3,476,5	1,198,7	1,086,1	112,6	9,4
	December	3,508,5	1,228,6	1,109,3	119,2	9,7
1975	March	3,540,8	1,230,9	1,067,2	163,7	13,3
	June	3,573,4	1,226,7	1,029,5	197,2	16,1
	September	3,606,3	1,223,3	1,019,9	203,5	16,6
	December	3,639,5	1,280,2	1,041,2	239,0	18,7
1976	March	3,673,0	1,298,7	1,041,1	257,6	19,8
	June	3,706,9	1,333,5	1,093,0	240,5	18,0
	July	3,718,4	1,284,4	1,074,6	209,8	16,3
	August	3,729,8	1,291,4	1,071,9	219,5	17,0
	September	3,741,1	1,291,5	1,069,2	202,3	15,7
	December	3,775,6	1,317,5	1,138,3	179,2	13,6
1977	March	3,810,3	1,336,6	1,151,4	185,2	13,9
	June	3,845,5	1,368,8	1,190,4	178,4	13,0
	September	3,880,9	1,371,3	1,195,6	175,8	12,8
	December	3,916,7	1,374,9	1,193,9	180,9	13,2
1978	March	3,952,8	1,417,2	1,208,9	208,4	14,7
	June	3,989,2	1,426,9	1,244,8	182,1	12,8
	September	4,026,6	1,466,7	1,265,1	201,6	13,7

SOURCE: University of Chile, Economics Department.

NOTE: These figures take into account the new demographic projection approved by Latin American Demographic Center, Planning Office and the National Bureau of Statistics.

Consumer Price Index
(Laspeyres, base December 1969 = 100)

Dates	General Index	% VARIATION			Food	Housing	Clothing	Miscellaneous
		Yearly Average	Dec. to Dec.	Variation in 12 months				
Average 1960	11,74	11,6	5,4	—	10,96	15,75	12,60	
" 61	12,65	7,7	9,7	—	12,05	16,88	12,92	10,83
" 62	14,40	13,9	27,7	—	14,11	18,65	14,45	9,77
" 63	20,78	44,3	45,4	—	21,14	24,46	20,48	15,90
" 64	30,33	46,0	38,4	—	31,77	33,09	30,86	21,73
" 65	39,08	28,8	25,9	—	41,16	41,87	38,67	29,17
" 66	48,01	22,9	17,0	—	50,41	50,51	46,54	38,49
" 67	56,72	18,1	21,9	—	57,70	60,48	56,81	49,10
" 68	71,83	26,6	27,9	—	72,41	75,30	71,34	66,50
" 69	93,84	30,7	29,3	—	94,65	94,94	91,17	92,69
" 1970	124,35	32,5	34,9	—	128,12	119,41	116,45	127,63
" 71	149,29	20,1	22,1	—	158,63	138,99	146,73	143,53
" 72	265,46	77,8	163,4	—	341,45	177,33	233,24	230,79
" 73	1.202,05	352,8	508,1	—	1.627,03	562,22	1.251,03	1.001,86
" 74	7.268,80	504,7	375,9	—	9.985,08	3.568,97	4.572,51	7.761,41
" 75 (3)	34,51	374,7	340,7	—	45,89	18,82	17,43	42,07
" 76	107,64	211,9	174,3	—	143,55	59,06	55,22	126,85
" 77	206,63	92,0	63,5	—	267,36	115,46	109,74	253,06
" 78	289,46	40,1	30,3	—	359,90	175,54	154,73	362,80
December 77	248,28	(1) 3,1	63,5	63,5	313,65	145,00	130,13	313,65
January 78	252,79	1,8	(2) 1,8	57,2	317,66	148,08	132,34	322,81
February	258,88	2,4	4,3	52,4	325,73	151,55	134,75	331,06
March	266,46	2,9	7,3	47,5	333,13	158,71	138,34	341,53
April	273,42	2,6	10,1	44,6	342,49	161,35	144,08	348,08
May	279,20	2,1	12,5	42,2	349,10	164,94	150,50	351,07
June	284,84	2,0	14,7	40,4	352,30	173,68	153,96	356,95
July	292,01	2,5	17,6	38,5	362,26	176,37	159,24	364,05
August	300,20	2,8	20,9	37,7	374,73	181,34	160,83	373,43
September	308,81	2,9	24,4	36,6	385,23	191,39	163,48	379,36
October	314,53	1,9	26,7	33,5	391,01	196,08	168,14	384,87
November	318,74	1,3	28,4	32,4	391,50	199,00	174,31	394,38
December	323,56	1,5	30,3	30,3	393,59	204,04	176,81	405,98

SOURCE: National Bureau of Statistics.

(1) % Variation with respect to previous month.

(2) % Variation with respect to December.

(3) Beginning in 1975, the Index has been simplified by 1,000 to facilitate the reading of the figures. This does not alter the base.

Wholesale Price Index
(Laspeyres, base 1968 = 100)

Dates	General Index	% Variation			National Products				Import Products
		Yearly Average	Dec. to Dec.	In 12 months	Agriculture	Minerals	Industry	Total	
Average 1960	16,66	5,3	1,6	—	16,2	17,9	15,0	15,7	19,1
" 1961	16,78	0,8	1,6	—	16,3	17,6	15,2	15,8	19,3
" 1962	18,17	8,3	26,8	—	18,4	18,4	16,6	17,4	20,1
" 1963	27,92	53,7	45,4	—	26,5	27,7	24,7	25,6	33,8
" 1964	42,03	50,6	43,7	—	40,2	38,9	37,9	38,8	50,3
" 1965	52,25	24,3	24,5	—	55,2	57,1	48,5	51,7	53,8
" 1966	64,21	22,9	19,6	—	69,4	71,0	62,2	65,5	60,8
" 1967	76,62	19,3	19,7	—	80,4	82,2	76,4	78,4	72,2
" 1968	100,0	30,5	33,1	—	100,0	100,0	100,0	100,0	100,0
" 1969	136,5	36,5	39,4	—	141,0	129,2	135,6	136,2	137,4
" 1970	185,8	36,1	33,7	—	191,7	166,7	186,1	186,1	184,6
" 1971	219,1	17,9	21,4	—	240,5	221,3	212,0	217,2	225,5
" 1972	372,5	70,0	143,3	—	502,1	380,3	352,4	378,6	352,3
" 1973	2.277,6	511,4	1.147,1	—	2.752,5	2.279,2	2.132,1	2.242,1	2.396,9
" 1974	25.711,1	1.029,0	570,6	—	20.372,3	36.547,6	22.796,5	23.024,3	34.749,2
" 1975	(3) 149,82	482,0	410,9	—	135,92	211,54	118,78	134,93	189,68
" 1976	480,51	221,1	151,5	—	470,21	617,15	374,80	440,05	572,00
" 1977	893,99	86,0	65,0	—	842,96	1.069,17	702,03	804,43	1.142,99
" 1978	1.278,05	42,9	38,9	—	1.135,36	1.615,73	1.072,04	909,80	1.541,65
December 1977	1.040,51	(1) 1,4	65,0	65,0	883,12	1.282,18	877,12	934,00	1.342,31
January 1978	1.061,16	2,0	(2) 2,0	57,7	896,69	1.389,38	896,27	956,35	1.347,86
February	1.104,78	4,1	6,2	50,4	934,03	1.420,18	933,56	994,71	1.408,56
March	1.153,36	4,4	10,8	45,5	993,16	1.481,74	960,89	1.037,64	1.474,29
April	1.196,16	3,7	15,0	43,1	1.027,82	1.505,71	1.006,84	1.079,60	1.510,63
May	1.231,38	2,9	18,3	41,6	1.055,08	1.561,66	1.040,96	1.113,41	1.543,89
June	1.266,21	2,8	21,7	41,3	1.107,37	1.575,66	1.065,96	1.149,70	1.561,11
July	1.294,35	2,2	24,4	40,1	1.153,76	1.625,43	1.082,96	1.180,88	1.564,74
August	1.341,44	3,6	28,9	40,0	1.204,18	1.681,81	1.117,78	1.224,41	1.618,51
September	1.385,54	3,3	33,2	42,0	1.268,81	1.772,73	1.149,25	1.273,54	1.622,75
October	1.416,46	2,2	36,1	41,5	1.330,00	1.792,92	1.176,52	1.315,05	1.586,68
November	1.440,85	1,7	38,5	40,4	1.338,52	1.778,58	1.209,05	1.336,65	1.619,80
December	1.445,00	0,3	38,9	38,9	1.314,92	1.802,95	1.224,43	1.337,45	1.640,96

SOURCE: National Bureau of Statistics.

NOTES: (1) % Variation during the month.

(2) % Variation with respect to December.

(3) Beginning in 1975, the Index has been simplified by 1,000 to facilitate the reading of the figures. This does not alter the base.

Wage and Salary Index
(Base: April 1959 = 100)

Years and Months	General Index		Partial Indices		Index by Sector				
	Wage and Salary Index	% Variation	Wage Index	Salary Index	Public Utility	Mining	Manu- facturing	Fiscal Institutions	Semi-Fiscal Institutions
1959 April	100,0	—	100,0	100,0	100,0	100,0	100,0	100,0	100,0
1960 April	115,1	15,1	—	—	—	—	—	—	—
1961 April	132,5	15,1	—	—	—	—	—	—	—
1962 April	150,9	13,9	—	—	—	—	—	—	—
1963 April	205,7	36,3	200,5	210,5	240,1	230,0	208,9	211,0	186,5
1964 April	274,4	33,4	282,6	266,5	344,9	317,4	310,7	241,3	225,9
1965 April	422,6	54,0	432,5	413,0	477,1	483,7	445,8	386,4	390,9
1966 April	574,5	35,9	592,9	577,3	753,7	630,2	640,9	513,5	486,2
1967 April	817,2	42,2	816,5	817,8	1.098,9	1.025,9	821,8	848,5	684,5
1968 April	984,8	20,5	1.076,7	898,9	1.321,6	1.376,2	1.082,4	879,3	775,3
1969 April	1.478,4	50,1	1.510,0	1.448,8	2.159,4	1.939,2	1.503,7	1.480,8	1.194,4
1970 April	2.126,2	43,8	2.094,8	2.155,6	2.641,4	2.677,4	2.110,8	2.337,1	1.774,1
1971 April	3.253,5	53,0	3.184,3	3.318,2	4.342,7	4.440,1	3.117,1	3.473,6	2.754,1
1972 April	4.563,3	40,3	4.793,0	4.348,4	6.878,6	5.405,5	4.927,8	3.887,3	3.869,7
1973 April	12.601,8	176,2	13.878,1	11.408,0	16.985,7	15.448,9	14.853,3	11.266,0	9.086,7
1974 April (2)	8,1	546,2	8,4	7,9	9,3	8,7	9,6	9,1	5,5
1975 April	41,6	411,3	41,3	42,0	41,7	53,6	43,8	54,3	28,2
1976 April	158,6	280,9	158,7	158,5	176,1	200,0	174,6	191,2	104,8
1977 April	453,2	185,7	455,0	451,5	439,8	609,9	500,7	555,0	290,5
1978 April	754,3	66,5	755,9	752,8	705,4	930,4	861,6	(1) 641,7	
1974 January	6,2	177,9	6,5	5,8	7,9	5,6	7,6	7,4	3,6
April	8,1	32,1	8,4	7,9	9,3	8,7	9,6	9,1	5,5
July	14,2	74,9	14,6	13,9	15,8	18,2	15,5	17,6	9,9
October	19,5	36,7	19,3	19,6	20,9	21,7	21,1	24,8	13,4
1975 January	27,5	41,4	26,6	28,4	31,0	31,9	29,5	35,1	18,8
April	41,6	51,3	41,3	42,0	41,7	53,6	43,8	54,3	28,2
July	67,8	62,8	65,2	70,2	75,5	85,1	68,7	91,8	46,2
October	86,7	27,9	85,8	87,5	95,9	111,1	92,0	109,3	58,1
1976 January	113,9	31,4	113,1	114,6	130,1	141,6	124,5	138,5	75,4
April	158,6	39,3	158,7	158,5	176,1	200,0	174,6	191,2	104,8
July	224,8	41,7	227,7	222,0	242,0	286,3	251,2	273,4	142,8
October	293,8	30,7	300,3	287,8	307,1	393,9	328,4	354,2	183,9
1977 January	373,1	27,0	375,8	370,6	371,7	507,9	413,5	(1) 315,5	
April	453,2	21,4	455,0	451,5	439,8	609,9	500,7	386,9	
July	553,4	22,1	548,2	558,2	526,8	701,4	607,5	484,8	
October	572,5	3,5	573,4	571,7	539,4	737,4	646,2	486,2	
1978 January	678,0	18,4	674,0	681,7	650,2	807,1	772,7	582,2	
April	754,3	11,3	755,9	752,8	705,4	930,4	861,6	641,7	
July	850,8	12,8	860,0	842,2	902,3	991,3	988,0	710,6	
October	881,8	3,6	902,5	862,5	940,0	1.077,9	1.033,9	718,9	

NOTES:

(1) The sectors originally identified as Fiscal and Semi-Fiscal have been incorporated into the Public Sector, as they have lost meaning as individual entities because of the modifications in the administrative structure of the State.

(2) This Index has been simplified by 10,000 in order to facilitate the reading of the figures. The base has not been altered. Variations have been calculated on the original figures, which differ if they are calculated with respect to the simplified Index in some cases.

SOURCE: National Bureau of Statistics.

Exchange Rate
(\$ per dollar, Buyer, Banking Market)

Annual Average

Year	Value	Year	Value
1960	0,001051	1970	0,011552
1961	0,001051	1971	0,012409
1962	0,001142	1972	0,019485
1963	0,001875	1973	0,110798
1964	0,002372	1974	0,8320
1965	0,003128	1975	4,9100
1966	0,003955	1976	13,0542
1967	0,005031	1977	21,54
1968	0,006787	1978	31,67
1969	0,008974		

Monthly Averages

Periods	1970	1971	1972	1973	1974	1975	1976	1977	1978
January	0,01012	0,01221	0,01580	0,02500	0,371	1,906	9,19	17,96	28,35
February	0,01039	0,01221	0,01580	0,02500	0,416	2,247	10,10	19,04	29,12
March	0,01077	0,01221	0,01580	0,02500	0,483	2,786	10,76	18,30	29,86
April	0,01112	0,01221	0,01580	0,02500	0,545	3,537	11,51	18,69	30,61
May	0,01143	0,01221	0,01580	0,02758	0,611	4,045	12,56	19,39	31,30
June	0,01173	0,01221	0,01580	0,06500	0,725	4,580	13,54	20,23	31,83
July	0,01201	0,01221	0,01580	0,06500	0,790	5,339	12,82	20,96	32,29
August	0,01221	0,01221	0,02322	0,07400	0,889	5,806	13,51	21,96	32,73
September	0,01221	0,01221	0,02500	0,08500	1,021	6,190	14,33	23,86	33,05
October	0,01221	0,01221	0,02500	0,28900	1,173	6,800	15,17	24,71	33,32
November	0,01221	0,01221	0,02500	0,29300	1,340	7,440	16,13	25,66	33,57
December	0,01221	0,01460	0,02500	0,34300	1,619	8,250	17,03	27,59	33,84

SOURCE: Central Bank of Chile.

Price of Copper 1960 - 1978
 (London Metals Exchange)
 (US\$ cents per pound)



	Nominal Price (US\$ c year)	Real Price (US\$ 1976)
1960	30,77	59,30
1961	28,71	55,57
1962	29,26	56,45
1963	29,30	56,71
1964	43,98	84,94
1965	58,64	111,03
1966	69,47	127,32
1967	51,13	93,52
1968	56,10	100,10
1969	66,54	114,28
1970	64,10	106,19
1971	49,27	79,12
1972	48,57	74,59
1973	80,78	109,68
1974	93,27	106,55
1975	55,94	58,51
1976	63,55	63,55
1977	59,34	55,98
1978	61,89	54,11*
January 1978	57,18	
February	55,19	
March	56,91	
April	58,29	
May	59,06	
June	60,43	
July	60,62	
August	64,72	
September	65,40	
October	68,29	
November	66,67	
December	69,51	

(*) Value estimated assuming 7.8% increase in WPI-USA in the year 1978.

SOURCE: Central Bank of Chile.

Real Price: Deflated by WPI-USA.

Methodology for Interseasonal Comparisons (Implicit Exchange Rate)

The development of this methodology fulfills the purpose of building historical series of economic data which permit an adequate comparison of the variables among themselves and over time. This especially permits the consolidation of values in domestic and foreign currency, in order to obtain, for example, their relative dimension when compared to additional factors such as the gross domestic product or to compare their real levels at determined periods in time.

The methodology used consists in converting the nominal figures in domestic currency into dollars for each year, using the implicit exchange rate which is obtained from the relation between the gross domestic product in pesos for each year in the "National Chilean Account" of the Planning Office, and the GDP expressed in dollars for each year.

The series of the gross domestic product in dollars for each year was constructed on the basis of the Planning Office real series of the gross domestic product in 1965 pesos. The Expenditure of the GDP for 1974 which is obtained from the value of the GNP as estimated by the World Bank for that year was established as a pivot value in dollars. This permits an adequate comparison of the levels of economic activity between Chile and other countries in the world.

In order that the figures may be compared over time, they have been expressed in constant terms (1976 dollars), deflating the figures in dollars for each year by world inflation, as measured by the Wholesale Price Index of the United States.

It is interesting to observe that the implicit exchange rate will differ from the actual exchange rate observed in the economy to the extent that the latter is under or overvalued as a result of Balance of Payment problems, or of import-export subsidy policies.

When each of the nominal variables is expressed through the use of the same methodology, it is necessary to point out that the relations which exist in each period or year among the different nominal variables remains unchanged, and consistency is maintained among them.

The following table provides the nominal and real figures for the GDP for the 1960-1978 period and the values of the resulting exchange rate, as well as a comparison with the exchange rate for each year.

In the subsequent tables the methodology described here is applied to the most significant variables in the fiscal, monetary and the balance of payment situations.

NOTE: Let $IERT$ = implicit exchange rate for the year t

$EGDPT_{ip}$ = expenditure of gross domestic product in the period t , expressed in pesos for that year (at internal prices).

$EGDPT_{ep}$ = expenditure of gross domestic product in the period t , expressed in dollars for that year (at external prices).

$$\text{Then } IERT = \frac{EGDPT_{ip}}{EGDPT_{ep}}$$

Then let

ier = rate of variation in the implicit exchange rate

g = real rate of variation in the EGDPT

pi = rate of variation in internal prices

pe = rate of variation in external prices.

$$\text{Then } ier = \frac{(1+g)(1+pi)}{(1+g)(1+pe)} - 1 = \frac{(1+pi)}{(1+pe)} - 1$$

That is, between one period and another, the implicit exchange rate will only vary in function of internal inflation and world inflation.

Expenditure of Gross Domestic Product
Implicit Exchange Rate
1960 - 1978 Period

	(1) Real EGDP (Thous. 1965 \$)	(2) Real EGDP (Mill. US\$ 1974)	(3) Real EGDP (Mill. US\$ 1976)	(4) Nominal EGDP (Mill. US\$ each year)
1960	14.673	5.022	5.737	2.977
1961	15.567	5.328	6.087	3.145
1962	16.287	5.575	6.368	3.301
1963	17.115	5.858	6.692	3.458
1964	17.850	6.110	6.980	3.614
1965	18.752	6.418	7.332	3.872
1966	20.066	6.868	7.846	4.281
1967	20.555	7.035	8.037	4.394
1968	21.172	7.247	8.278	4.639
1969	21.905	7.497	8.565	4.987
1970	22.695	7.768	8.874	5.356
1971	24.440	8.365	9.556	5.951
1972	24.419	8.358	9.548	6.217
1973	23.535	8.055	9.202	6.777
1974	24.498	8.385	9.579	8.385
1975	21.338	7.303	8.343	7.976
1976	22.192	7.596	8.877	8.677
1977	24.101	8.249	9.423	9.998
1978	25.860	8.851	10.111	11.565

- NOTES: (1) : Source: Planning Office, "Chilean National Accounts."
Years 1974 - 1975: provisional figures subject to revision.
Years 1976 - 1978: provisional estimate.
- (2) : Estimate based on level of US\$ 8,490 million of GNP for 1974.
(Source: World Bank Atlas 1975). This figure was corrected to pass to EGDP for 1974 of US\$ 8,385 million),
which is used as a pivot, considering the real implicit rates of growth in the series (1).
- (3) : Base changed in series (2) using the Wholesale Price Index the United States. (Assumed 7.8% for 1978).
- (4) : Series (3) deflated by the Wholesale Price Index of the United States.
- (5) : Source: Planning Office, "Chilean National Accounts."
Years 1974-75: provisional figures, subject to revision.
Years 1976-78: provisional estimate.
- (6) : Obtained from (5) : (4).
- (7) : Source: Central Bank of Chile.
- (8) : Obtained from (7) : (6).

(5) Nominal EGDP (Thous. of \$ each year)	(6) Implicit Exchange Rate (\$/1,000 US\$)	(7) Actual Exchange Rate (\$/1,000 US\$)	(8) Actual Exchange Rate and Implicit Rate Ratio
4.160	1,397	1,051	0,75
4.739	1,507	1,051	0,70
5.739	1,739	1,142	0,66
8.654	2,503	1,875	0,75
13.227	3,660	2,372	0,65
18.752	4,843	3,128	0,65
26.156	6,110	3,955	0,65
34.367	7,821	5,031	0,64
46.347	9,991	6,787	0,68
67.437	13,523	8,974	0,66
96.971	18,105	11,552	0,64
129.041	21,684	12,409	0,57
238.985	38,441	19,485	0,51
1.210.552	178,627	110,798	0,62
9.464.020	1.129,000	832,000	0,74
38.681.452	4.850,000	4.910,000	1,01
125.473.347	14.460,000	13.054,000	0,90
261.626.985	26.168,000	21.540,000	0,82
393.296.780	34.007,000	31.670,000	0,93

Expenditure, Revenues and Fiscal Deficit 1960 - 1978

Local Currency (2)

(In millions of dollars for each year)

	1960	1961	1962	1963	1964	1965	1966	1967
TOTAL EXPENDITURE	580,46	595,88	657,56	657,93	649,67	807,76	896,06	845,39
— Debt Service	12,67	8,56	6,04	6,07	5,66	7,99	9,59	8,37
— Total Expenditure excluding Debt Service	567,79	587,32	651,52	651,86	644,01	799,77	886,47	837,02
TOTAL REVENUES	423,84	469,14	483,61	500,64	501,83	629,13	718,29	729,92
— Direct Taxes	101,72	123,62	121,50	113,99	138,63	185,55	204,24	212,70
— Indirect Taxes	295,85	322,36	327,49	322,57	311,59	361,28	407,17	425,07
— Non Tax Income	26,27	23,16	31,63	31,04	29,81	49,84	44,53	33,38
— Copper	—	—	—	—	—	—	—	—
— Customs Duties and Extra budgetary Adjustments	—	—	2,99	33,04	21,80	32,46	62,33	58,77
DEFICIT	156,62	126,74	173,95	157,29	147,84	178,63	177,79	115,47

Foreign Currency

(Millions of dollars for each year)

	1960	1961	1962	1963	1964	1965	1966	1967
TOTAL EXPENDITURE	91,51	112,10	117,60	113,10	113,59	120,70	144,50	142,60
— Debt Services	52,49	74,20	69,00	85,00	79,40	78,80	84,76	99,13
— Total Expenditure excluding Debt Service	39,02	37,90	48,60	28,10	34,10	41,90	59,74	43,47
TOTAL REVENUES	110,13	96,29	103,60	99,40	121,10	142,30	217,10	203,60
— Direct Taxes	7,28	8,38	4,90	10,40	11,20	17,30	14,90	22,10
— Indirect Taxes	12,85	3,52	3,60	2,10	2,50	2,60	4,60	2,80
— Non Tax Income	2,28	11,86	2,50	0,60	2,60	0,90	0,30	—
— Copper	87,72	72,53	92,60	86,30	104,80	121,50	197,30	178,70
— Customs Duties and Extra budgetary Adjustment	—	—	—	—	—	—	—	—
DEFICIT	— 18,62	15,81	14,00	13,70	— 7,60	— 21,60	— 72,60	— 61,00

SOURCE: Ministry of Finance, Office of the Budget.

NOTE: In order to compare the series of fiscal expenditure and revenue in the period under consideration, fiscal customs duties and extrabudgetary adjustments have been included in both the revenues and the expenditures. In the years 1972 and 1973, contributions via the monetary system to finance enterprises in the social area have also been included

(1): Provisional estimate.

(2): The figures in local currency were converted to dollars using the implicit exchange rate.

1968	1969	1970	1971	1972	1973	1974	1975	1976	1977	1978 (1)
896,48	1.018,34	1.172,22	1.585,40	1.793,19	2.725,78	2.035,49	1.535,82	1.666,78	2.179,18	2.779,9
15,28	17,42	17,16	10,80	17,17	13,57	31,39	18,09	20,00	40,30	36,4
881,20	1.000,92	1.155,06	1.574,60	1.776,02	2.712,21	2.004,10	1.517,73	1.646,78	2.138,88	2.743,5
784,59	943,47	1.003,91	1.141,60	1.075,72	1.270,64	1.572,25	1.629,22	1.743,06	2.201,20	2.957,2
213,87	212,19	240,24	333,06	257,38	333,65	453,79	500,09	452,15	563,51	727,6
491,95	547,07	574,82	678,11	676,51	690,19	915,92	1.054,52	1.241,17	1.569,46	2.082,4
40,87	52,75	56,56	80,84	74,43	92,37	202,54	74,61	49,74	68,23	147,2
—	0,06	0,06	0,01	—	—	—	—	—	—	—
37,90	131,40	132,23	49,58	67,40	154,43	—	—	—	—	—
111,89	74,87	168,31	443,80	717,47	1.455,14	463,24	— 93,40	— 76,28	— 22,02	— 177,3

1968	1969	1970	1971	1972	1973	1974	1975	1976	1977	1978
153,27	193,40	272,20	257,35	118,37	169,41	618,69	555,74	694,74	623,82	664,43
101,26	137,09	176,98	185,57	50,96	78,88	337,92	387,69	543,64	444,78	492,48
52,01	56,31	95,22	71,78	67,41	90,53	280,77	168,05	151,10	179,04	171,95
195,20	248,10	291,90	60,92	34,88	28,60	216,39	218,69	382,92	374,30	342,87
20,00	20,30	18,50	12,63	1,32	2,39	10,63	20,87	14,00	10,30	13,51
2,50	2,50	2,80	7,11	5,07	5,57	10,92	13,78	9,70	9,33	11,08
0,20	1,40	2,70	2,10	2,77	1,43	4,24	7,50	7,28	1,48	1,92
172,50	223,90	267,90	39,08	25,72	19,21	190,60	176,54	351,94	353,19	316,36
—	—	—	—	—	—	—	—	—	—	—
— 41,93	— 54,70	— 19,70	196,43	83,49	140,81	402,30	337,05	311,82	249,52	321,56

**Expenditure, Revenues, and Real Fiscal
Deficit 1960 - 1978**
Consolidated in Local and Foreign Currency
(In millions of 1976 dollars)

	1960	1961	1962	1963	1964	1965	1966	1967
TOTAL EXPENDITURE	1,295,09	1,370,22	1,495,51	1,492,25	1,473,99	1,757,95	1,907,03	1,807,03
— Debt Service	125,58	160,17	144,77	176,26	164,29	164,33	172,91	196,62
— Total Expenditure Excluding Debt Service ...	1,169,51	1,210,05	1,350,74	1,315,99	1,309,70	1,593,62	1,734,12	1,610,41
TOTAL REVENUES	1,029,12	1,094,33	1,132,90	1,161,32	1,203,13	1,460,63	1,714,25	1,707,41
— Direct Taxes	210,08	225,47	243,86	240,74	289,38	384,08	401,62	429,45
— Indirect Taxes	594,96	630,71	638,77	628,37	606,63	688,97	754,65	782,58
— Non-Tax Income	55,02	67,78	65,85	61,24	62,60	96,07	82,16	61,05
— Copper	169,06	140,37	178,65	167,03	202,41	230,05	361,59	326,84
— Customs Duties and Extra- budgetary Adjustments	—	—	5,77	63,94	42,11	61,46	114,23	107,49
DEFICIT	265,97	275,89	362,61	330,93	270,86	297,32	192,78	99,62
% Deficit/Total Expenditure ...	20,5	20,1	24,2	22,2	18,4	16,9	10,1	5,5

**Expenditure, Revenue and Fiscal Deficit as Percentage
of Expenditure of Gross Domestic Product.**
(Figures in percentage)

TOTAL EXPENDITURE	22,58	22,51	23,48	22,30	21,12	23,98	24,31	22,48
— Debt Service	2,19	2,63	2,27	2,63	2,35	2,24	2,21	2,44
— Total Expenditure Excluding Debt Service	20,39	19,88	21,21	19,67	18,77	21,74	22,10	20,04
TOTAL REVENUES	17,94	17,98	17,79	17,35	17,24	19,92	21,85	21,24
— Direct Taxes	3,66	4,20	3,83	3,60	4,15	5,24	5,12	5,34
— Indirect Taxes	10,37	10,36	10,03	9,39	8,69	9,39	9,62	9,74
— Non-Tax Income	0,96	1,11	1,03	0,91	0,90	1,31	1,05	0,76
— Copper	2,95	2,31	2,81	2,50	2,90	3,14	4,61	4,06
— Customs Duties and Extra- budgetary Adjustments	—	—	0,09	0,95	0,60	0,84	1,45	1,34
DEFICIT	4,64	4,53	5,69	4,95	3,88	4,06	2,46	1,24

SOURCE: Ministry of Finance, Office of the Budget (See previous tables).

(1) : Provisional estimate.

*Definitive figure is 4.1%.

1968	1969	1970	1971	1972	1973	1974	1975	1976	1977	1978 (1)
873,17	2.081,04	2.392,97	2.959,09	2.935,58	3.931,09	3.032,13	2.187,77	2.361,52	2.641,85	3.011,38
207,95	265,35	321,63	315,33	104,63	125,53	421,90	424,44	563,64	457,19	462,40
665,22	1.815,69	2.071,34	2.643,76	2.830,95	3.805,56	2.610,23	1.763,33	1.797,88	2.184,66	2.548,98
748,34	2.046,40	2.146,77	1.931,01	1.705,55	1.764,11	2.043,34	1.932,91	2.125,98	2.427,43	2.885,25
417,32	399,28	428,65	555,11	397,29	456,28	530,55	544,92	466,15	540,82	647,95
382,30	943,83	956,94	1.100,33	1.046,70	944,70	1.058,82	1.117,44	1.250,87	1.488,03	1.830,33
73,28	93,00	98,18	133,18	118,56	127,36	236,23	85,89	57,02	65,70	130,38
307,81	384,63	443,93	62,77	39,50	26,08	217,74	184,66	351,94	332,88	276,59
67,63	225,66	219,07	79,62	103,51	209,69	—	—	—	—	—
124,83	34,64	246,20	1.028,08	1.230,03	2.166,98	988,79	254,86	235,54	214,42	126,13
6,7	1,7	10,3	34,7	41,9	55,1	32,6	11,6	10,0	8,1	4,2*

22,63	24,30	26,97	30,97	30,74	42,72	31,65	26,22	27,22	28,04	30,15
2,51	3,10	3,63	3,30	1,09	1,36	4,40	5,09	6,50	4,85	4,63
20,12	21,20	23,34	27,67	29,65	41,36	27,25	21,13	20,72	23,19	25,52
21,12	23,89	24,19	20,21	17,86	19,17	21,33	23,17	24,50	25,76	28,89
5,04	4,66	4,83	5,81	4,16	4,96	5,54	6,53	5,37	5,74	6,49
10,66	11,02	10,78	11,52	10,96	10,27	11,05	13,39	14,41	15,79	18,32
0,88	1,09	1,11	1,39	1,24	1,38	2,47	1,03	0,66	0,70	1,31
3,72	4,49	5,00	0,66	0,41	0,28	2,27	2,22	4,06	3,53	2,77
0,82	2,63	2,47	0,83	1,09	2,28	—	—	—	—	—
1,51	0,41	2,78	10,76	12,88	23,55	10,32	3,05	2,72	2,28	1,26

Money in Private Sector = M
(Annual average of end of month balances)

	(1) M (In thous. \$ each year)	(2) M (Mill. US\$ each year)	(3) M (Mill US\$ 1976)	(4) $\frac{M}{EGDP}$ (%)
1960	326	233,4	449,8	7,8
1961	387	256,8	497,0	8,2
1962	473	272,0	524,8	8,2
1963	659	263,3	509,6	7,6
1964	931	254,4	491,3	7,0
1965	1.476	304,8	577,1	7,9
1966	2.188	358,1	656,3	8,4
1967	2.792	357,0	653,0	8,1
1968	3.648	365,1	651,5	7,9
1969	5.161	381,6	655,4	7,7
1970	7.872	434,8	720,3	8,1
1971	15.755	726,6	1.166,8	12,2
1972	31.261	813,2	1.248,8	13,1
1973	122.270	684,5	929,4	10,1
1974	484.973	429,6	490,8	5,1
1975	1.610.948	332,2	347,5	4,2
1976	4.959.017	342,9	342,9	4,0
1977	12.814.605	489,7	461,5	4,9
1978 (5)	23.467.000	690,0	603,3	6,0

SOURCE: (1) Central Bank of Chile.

(2) Column (1): implicit exchange rate

(3) Using Wholesale Price Index of the United States.

(4) EGDP. Source: Planning Office.

(5) Provisional estimate.

Quasi Money in Banks (*)
(Yearly average of end of month balances)

	(1) (in thous. \$ each year)	(2) (mill. US\$ each year)	(3) (mill. US\$ 1976)	(4) (as % of EGDP)
1960	148	106	204	3,6
1961	182	121	234	3,8
1962	258	148	286	4,5
1963	339	135	261	3,9
1964	454	124	239	3,4
1965	595	123	233	3,2
1966	820	134	246	3,1
1967	1.207	154	282	3,5
1968	1.267	127	227	2,7
1969	2.208	163	280	3,3
1970	3.160	175	290	3,3
1971	5.515	254	408	4,3
1972	9.197	239	367	3,8
1973	29.066	163	221	2,4
1974	115.938	103	118	1,2
1975	988.261	204	213	2,6
1976	4.994.607	345	345	4,0
1977	17.752.136	678	639	6,8
1978 (5)	38.550.955	1.134	991	9,9

(*) Quasimoney in Banks, excludes Readjustable Savings Bonds (CAR), includes public sector

SOURCE: (1) Central Bank of Chile.

(2) Column (1): Implicit exchange rate.

(3) Using Wholesale Price Index of the United States.

(4) EGDP. Source: Plannings Office.

(5) Provisional estimate.

Balance of Payments 1960 - 1978
 Real Figures
 (In millions of 1976 dollars)

	1960	1961	1962	1963	1964	1965	1966	1967
Exports	1.063,3	1.026,9	1.095,1	1.128,5	1.303,5	1.467,0	1.789,8	1.798,8
— Copper	619,6	591,5	638,4	657,6	701,9	811,3	1.097,0	1.191,2
— Other goods	285,6	309,3	327,6	317,8	441,7	483,8	491,0	405,9
— Services	158,1	126,1	129,1	153,1	159,9	171,9	201,8	201,7
Imports	1.275,0	1.406,8	1.313,3	1.250,8	1.376,7	1.354,1	1.625,6	1.660,5
— Food	210,6	224,5	227,7	273,8	279,1	328,0	290,7	306,9
— Capital	302,0	393,7	367,9	289,0	345,7	302,2	407,6	415,7
— Intermediate goods (not food)	404,5	457,5	425,4	422,5	447,1	519,0	627,7	578,3
— Consumer (not food)	153,2	123,5	114,4	103,2	80,0	84,2	95,1	105,5
— Services goods	204,7	207,6	177,9	157,3	194,8	188,7	204,5	254,0
Trade Balance (3)	-165,1	-298,4	-169,4	-118,1	- 38,2	129,7	166,9	190,6
Balance Current Account	-285,4	-510,6	-389,9	-384,8	-248,2	-107,2	-150,6	-233,0
Balance Autonomous Capital ..	147,1	362,1	262,4	203,6	285,8	88,4	317,0	191,9
Balance of Payments	- 54,7	-210,2	- 94,5	- 55,0	45,6	88,4	219,2	- 42,8

SOURCE: Balance of Payments 1960-1978 Central Bank of Chile.

Figures deflated by Wholesale Price Index of United States.

(1) Provisional figures.

(2) Estimate.

(3) Defined as balance between Exports and Imports of Goods.

1968	1969	1970	1971	1972	1973	1974	1975	1976	1977 (1)	1978 (2)
1.839,5	2.243,9	2.078,7	1.819,1	1.502,2	1.940,7	2.620,3	1.863,6	2.391,6	2.484,0	2.848,8
1.221,1	1.589,4	1.391,3	1.126,0	949,4	1.433,4	1.854,4	908,1	1.233,2	1.073,8	1.128,0
404,3	423,2	450,4	474,7	352,0	346,0	602,3	754,5	882,4	986,1	1.166,1
214,1	231,3	237,0	218,4	200,8	161,3	163,6	201,0	276,0	424,1	554,7
1.709,5	1.869,2	1.922,1	1.967,2	2.043,8	2.207,2	2.662,7	2.090,7	1.946,0	2.566,1	3.141,0
293,7	283,7	224,5	308,6	519,7	694,6	508,9	377,6	342,0	312,4	424,9
423,4	419,4	457,6	398,2	253,5	330,3	321,2	340,4	366,5	438,7	638,2
572,3	746,2	737,2	779,1	706,7	751,4	1.339,5	945,3	845,5	1.042,0	1.234,7
141,0	142,4	164,5	143,8	213,3	188,9	132,9	123,1	101,0	321,5	383,1
279,1	277,5	338,3	337,5	350,6	242,0	360,2	304,3	291,0	451,5	460,1
195,0	420,9	257,9	- 29,1	-391,9	-185,8	154,2	123,8	460,6	- 54,7	-386,8
-241,3	- 9,6	-134,3	-303,2	-593,7	-390,5	-240,8	-513,9	148,0	-376,7	-668,8
504,6	377,7	443,2	- 42,6	502,8	329,0	260,5	312,4	235,0	326,1	1.253,2
210,4	299,7	188,0	-481,4	-351,7	-151,9	51,5	-287,2	455,0	- 6,6	584,4

Overall Chilean Foreign Debt
Nominal and Effective Series 1960 - 1978 (1)
(Millions of dollars, percentages)

Year	I Overall Foreign Debt	II Gross Reserves	III Overall Foreign Debt minus Gross Reserves (I-II)
1960	746	119	627
1961	1.010	104	906
1962	1.255	106	1.149
1963	1.469	114	1.355
1964	1.635	131	1.504
1965	1.781	182	1.599
1966	1.852	234	1.618
1967	1.908	200	1.708
1968	2.201	288	1.913
1969	2.689	433	2.256
1970	3.123	505	2.618
1971	3.196	290	2.906
1972	3.602	271	3.331
1973	4.048	401	3.647
1974	4.774	535	4.239
1975	5.263	427	4.836
1976	5.195	816	4.379
1977	5.434	871	4.563
1978 (August)	6.243	1.405	4.838

(1) August, 1978.

SOURCE: Central Bank of Chile.

Column I: **Overall Foreign Debt:** Net balances pending payment abroad on December 31 of each year considering: —Traditional foreign debt that is, debt of public sector and private sector with public guarantee. —IMF debt. —Direct foreign debt of private sector (deferred payment). —Financial credit to private sector Decree 1,272 (arts. 14, 15 and 16) and short term lines of credit to monetary system (Central Bank, Commercial Banks, Banco del Estado).

Column II: **Gross Reserves in the Monetary System:** All assets of the monetary system (Central Bank and Commercial Banks) on December 31 of each year. In this series the value of gold put in the international reserves has been corrected by the average purchase price at the close of the London market in December of each year. The net value of reciprocal credit agreements was considered.

IV Effective Overall Foreign Debt (US\$ 1976)	V Effective Overall Foreign Debt Index 1960 = 100	VI Annual Variation Effective Overall Foreign Debt (%)
1.235	100,0	—
1.792	145,1	+ 45,1
2.265	183,4	+ 26,4
2.680	217,0	+ 18,3
2.968	240,3	+ 10,8
3.046	246,6	+ 2,6
3.030	245,3	— 0,5
3.170	256,7	+ 4,6
3.455	279,8	+ 9,0
3.886	314,6	+ 12,5
4.408	356,9	+ 13,4
4.707	381,1	+ 6,8
5.065	410,1	+ 7,6
4.807	389,2	— 5,1
4.620	374,1	— 3,9
5.058	409,6	+ 9,5
4.379	354,6	— 13,4
4.309	348,9	— 1,6
4.302	348,3	— 0,2

Column III: **Overall Foreign Debt minus Gross Reserves:** Refers to the country's net foreign debt position (Column I - Column II).

Column IV: **Effective Overall Foreign Debt:** Corresponds to Column III deflated by the WPI of the United States with a base of December, 1976. This series permits a yearly comparison of the foreign debt in real terms.

Column V: **Effective Overall Foreign Debt Index:** Refers to the variation with the base of 1960 = 100 of the series presented in Column IV.

Column VI: **Annual Variation of Effective Overall Foreign Debt:** Refers to the annual variation of indebtedness. It is deduced from Column IV or V.

Inflation and Financial Discipline in Chile

Table I

AVERAGE ANNUAL VARIATION BY DECADES

a) Monetary Variables (Balance in December of each year)

% Annual Variation								
	Nominal				Real *			
	M ₁	Q	E	M ₂	M ₁	Q	E	M ₂
Dec.39/Dec.49	19,8	14,2	20,6	18,1	1,8	-2,9	2,5	0,4
Dec.49/Dec.59	37,6	38,9	38,3	37,9	0,8	1,8	1,3	1,0
Dec.59/Dec.69	35,3	36,9	39,6	35,8	8,9	10,1	12,3	9,2
Dec.69/Dec.73	153,6	132,5	179,4	147,9	11,9	2,6	23,3	9,4
Dec.73/Dec.78	160,8	270,5	171,7	202,3	-0,3	41,6	3,8	15,6

SOURCE: Figures from the Central Bank of Chile.

*The nominal figures have been deflated according to the corresponding CPI.

b) Consumer Price Index

% Annual Variation	
Dec.39/Dec. 49	17,7
Dec.49/Dec.59	36,6
Dec.59/Dec.69	24,3
Dec.69/Dec.73	126,7
Dec.73/Dec.78	161,6

SOURCE: National Bureau of Statistics.

Table II.I
CONSUMER PRICE INDEX
 (Base: December 1978=100)

Years	Average Yearly Index	% Variation Dec. to Dec.	Years	Average Yearly Index	% Variation Dec. to Dec.
1940	3,261 (1)	9,1	1960	3,629 (3)	5,5
1941	3,755 (1)	23,1	1961	3,908 (3)	9,6
1942	4,723 (1)	25,5	1962	4,451 (3)	27,7
1943	5,489 (1)	7,8	1963	6,421 (3)	45,3
1944	6,127 (1)	15,0	1964	9,373 (3)	38,5
1945	6,669 (1)	7,7	1965	12,076 (3)	25,8
1946	7,734 (1)	30,1	1966	14,838 (3)	17,0
1947	10,333 (1)	23,1	1967	1,753 (4)	21,9
1948	12,187 (1)	16,8	1968	2,220 (4)	27,9
1949	14,466 (1)	20,6	1969	2,900 (4)	29,3
1950	16,663 (1)	16,5	1970	3,843 (4)	34,9
1951	20,372 (1)	23,4	1971	4,614 (4)	22,1
1952	24,887 (1)	12,0	1972	0,820 (5)	163,4
1953	31,192 (1)	56,2	1973	3,715 (5)	508,1
1954	5,373 (2)	71,1	1974	2,247	375,9
1955	9,413 (2)	83,8	1975	10,665	340,7
1956	14,681 (2)	37,7	1976	33,268	174,3
1957	19,552 (2)	17,2	1977	63,859	63,5
1958	23,460 (2)	32,5	1978	89,459	30,3
1959	3,253 (3)	33,2			

SOURCE: National Bureau of Statistics

NOTE: In order to facilitate the calculations, the figures for the yearly average index have been adjusted according to the following coefficients:

- (1) x 10⁻⁵
- (2) x 10⁻⁴
- (3) x 10⁻³
- (4) x 10⁻²
- (5) x 10⁻¹

For example, the value of the index for 1940 should be multiplied by 10⁻⁵. Its real value then is 3.261 x 10⁻⁵ = 0,00003261

— It should be noted that the average yearly index is used to deflate the yearly average figures.

— Variations from December to December of each year correspond to the traditional methods for measuring inflation.

Table II.2**INFLATION**

(% Variations in C.P.I.)

	1973	1974	1975	1976	1977	1978
January	10,3	14,1	13,9	10,5	5,9	1,8
February	4,1	24,5	16,5	10,1	5,8	2,4
March	6,2	14,2	21,2	13,5	6,1	2,9
April	10,2	15,3	20,8	11,9	4,7	2,6
May	19,4	8,7	16,0	9,8	3,8	2,1
June	15,6	20,8	19,8	12,3	3,3	2,0
July	15,3	11,5	9,3	8,9	3,9	2,5
August	17,1	10,9	8,9	5,5	3,4	2,8
September	16,9	12,8	9,2	7,6	3,7	2,9
October	87,6	18,9	8,4	6,7	4,2	1,9
November	5,7	9,7	8,2	3,8	2,2	1,3
December	4,7	6,5	7,1	5,1	3,1	1,5
Dec. to Dec.	508,1	375,9	340,7	174,3	63,5	30,3

SOURCE: National Bureau of Statistics.

Table III.1

MONETARY VARIABLES

(Nominal balances at December of each year)

	M_1^*	Q^*	E^{**}	M_2^*
1940 (Millions of old pesos)	2,401	1,253	1,311	3,654
1941	3,035	1,362	1,574	4,397
1942	3,744	1,472	1,962	5,216
1943	4,768	1,758	2,347	6,526
1944	5,491	2,212	2,525	7,703
1945	6,176	2,546	3,117	8,722
1946	7,635	3,118	4,035	10,753
1947	8,541	3,392	4,681	11,933
1948	9,978	3,656	5,754	13,634
1949	12,085	4,078	7,071	16,163
1950	14,764	4,284	8,052	19,048
1951	18,839	5,083	10,462	23,922
1952	26,161	6,378	14,863	32,539
1953	37,220	8,576	22,539	45,796
1954	53,406	10,045	31,767	63,451
1955	91,767	14,559	51,200	106,326
1956	128,777	23,377	73,209	152,154
1957	164,850	35,601	91,625	200,451
1958	221,567	50,511	124,167	272,078
1959	293,664	109,502	181,094	403,166
1960	383,422	160,038	263,508	543,460
1961	431,465	196,853	290,350	628,318
1962	556,691	294,975	498,052	851,666
1963	746,255	358,628	529,000	1,104,883

	M_1^*	Q*	E**	M_2^*
1964 (million E. ^o)	1,129	506	921	1,635
1965	1,864	621	1,271	2,485
1966	2,590	982	2,038	3,572
1967	3,240	1,314	2,467	4,554
1968	4,480	1,793	3,602	6,273
1969	6,057	2,539	5,108	8,596
1970	10,068	2,768	8,701	12,836
1971	21,488	7,215	20,244	28,703
1972	54,111	15,662	55,407	69,773
1973	250,477	74,156	311,189	324,633
1974	829,578	336,394	1,003,524	1,165,972
1975 (million \$)	2,963	1,639	4,141	4,602
1976	8,574	8,193	15,168	16,767
1977	18,305	22,975	29,486	41,280
1978	30,207	51,772	46,064	81,979

* M_1 = Money in Private Sector

Q = Quasi money in Private Sector in local currency

E = Emission

$M_2 = M_1 + Q$

** From 1940 to 1963, is considered Accountable Emission.

From 1964 to 1978 in amounts corresponding to the Adjusted Emission. The difference between them is not very significant, which implies that they are almost equivalent.

Monetary and disaggregate accounting data for making the respective adjustments was not available in the Central Bank.

The accountable emission equals the money in circulation plus reserves of the banking system.

Adjusted emission equals accountable emission plus minus the average of the emergency loans (Central Bank licitation), and the average of Central Bank refinancing which have not been paid during the month in question and have not been reflected in the accounting.

Table III.2**MONETARY VARIABLES**

(Percentages of annual variation in nominal balances)*

	M₁	Q	E	M₂
1941	26.4	8.7	20.1	20.3
1942	23.4	8.1	24.7	18.6
1943	27.4	19.4	19.6	25.1
1944	15.2	25.8	7.6	18.0
1945	12.5	15.1	23.4	13.9
1946	23.6	22.5	29.5	22.6
1947	11.9	8.8	16.0	11.0
1948	16.8	7.8	22.9	14.3
1949	21.1	11.6	22.9	18.5
1950	22.2	5.1	13.9	17.8
1951	27.6	18.7	29.9	25.6
1952	38.9	25.5	42.1	36.0
1953	42.3	34.5	51.6	40.7
1954	43.5	17.1	40.9	38.6
1955	71.8	44.9	61.2	67.6
1956	39.8	60.6	43.0	43.1
1957	28.5	52.3	25.2	31.7
1958	34.4	41.9	35.5	35.7
1959	32.5	116.8	45.8	48.2
1960	30.6	46.2	45.5	34.8
1961	12.5	23.0	10.2	15.6
1962	29.0	19.8	71.5	35.5
1963	34.1	21.6	6.2	29.7
1964	51.3	44.1	74.1	48.0
1965	65.1	22.7	38.0	52.0
1966	38.9	58.1	60.3	43.7
1967	25.1	33.8	21.1	27.5

	M₁	Q	E	M₂
1968	38.3	36.5	46.0	37.7
1969	35.2	41.6	41.8	37.0
1970	66.2	9.0	70.3	49.3
1971	113.4	160.7	132.7	123.6
1972	151.8	117.1	173.7	143.1
1973	362.9	373.5	461.6	365.3
1974	231.2	353.6	222.5	259.2
1975	257.2	387.2	312.7	294.7
1976	189.4	399.9	266.3	264.3
1977	113.5	180.4	94.4	146.2
1978	65.0	125.3	56.2	98.6

* Calculated considering nominal balances in December of each year from Table III.1.

Table III.3.**MONETARY VARIABLES**

(Real Balances in December of each year in millions of pesos of
December, 1978)*

	M₁	Q	E	M₂
1940	7,193	3,754	3,928	10,947
1941	7,383	3,313	3,829	10,696
1942	7,256	2,853	3,802	10,109
1943	8,571	3,160	4,219	11,731
1944	8,582	3,457	3,947	12,039
1945	8,962	3,695	4,523	12,657
1946	8,517	3,478	4,501	11,995
1947	7,287	3,074	4,242	10,361
1948	7,741	2,837	4,464	10,578
1949	7,774	2,624	4,549	10,398
1950	8,152	2,365	4,446	10,517
1951	8,430	2,275	4,682	10,705
1952	10,450	2,548	5,937	12,998
1953	9,520	2,194	5,765	11,714
1954	7,984	1,502	4,749	9,486
1955	7,464	1,184	4,164	8,648
1956	7,606	1,381	4,324	8,987
1957	8,305	1,793	4,616	10,098
1958	8,424	1,920	4,721	10,344
1959	8,381	3,125	5,168	11,506
1960	10,374	4,330	7,130	14,704
1961	10,648	4,858	7,166	15,506
1962	10,759	5,701	9,626	16,460
1963	9,925	4,770	7,036	14,695



	M ₁	Q	E	M ₂
1964	10,843	4,860	8,846	15,703
1965	14,228	4,740	9,702	18,968
1966	16,903	6,409	13,300	23,312
1967	17,345	7,034	13,207	24,379
1968	18,745	7,502	15,071	26,247
1969	19,596	8,214	16,525	27,810
1970	24,144	6,638	20,866	30,782
1971	42,191	14,167	39,749	56,358
1972	40,321	11,671	41,287	51,992
1973	30,703	9,090	38,145	39,793
1974	21,370	8,665	25,851	30,035
1975	17,318	9,580	24,204	26,898
1976	18,268	17,456	32,317	35,724
1977	23,855	29,941	38,426	53,796
1978	30,207	51,772	46,064	81,979

*Figures of Table III.1, deflated by the CPI by for December of each year.

NOTE: The strong increase in quasi money in the years 1971 and 1972 is explained basically by the expansion in money which occurred during those years. This excess was partially translated into an increase in quasi money (Savings Accounts in Banco del Estado and others).

Table III.4.**Real Indices of Monetary Variables***

(Base: December 1978 = 100)

	M₁	Q	E	M₂
1940	23.8	7.3	8.5	13.4
1941	24.4	6.4	8.3	13.0
1942	24.0	5.5	8.3	12.3
1943	28.3	6.1	9.2	14.3
1944	28.4	6.7	8.6	14.7
1945	29.7	7.1	9.8	15.4
1946	28.2	6.7	9.8	14.6
1947	24.1	5.9	9.2	12.6
1948	25.6	5.5	9.7	12.9
1949	25.7	5.1	9.9	12.7
1950	27.0	4.6	9.7	12.8
1951	27.9	4.4	10.2	13.1
1952	34.6	4.9	12.9	15.9
1953	31.5	4.2	12.5	14.3
1954	26.4	2.9	10.3	11.6
1955	24.7	2.3	9.0	10.5
1956	25.2	2.7	9.4	11.0
1957	27.5	3.5	10.0	12.3
1958	27.9	3.7	10.2	12.6
1959	27.7	6.0	11.2	14.0
1960	34.3	8.4	15.5	17.9
1961	35.3	9.4	15.6	18.9
1962	35.6	11.0	20.9	20.1
1963	32.9	9.2	15.3	17.9
1964	35.9	9.4	19.2	19.2
1965	47.1	9.2	21.1	23.1

	M_1	Q	E	M_2
1966	56.0	12.4	28.9	28.4
1967	57.4	13.6	28.7	29.7
1968	62.1	14.5	32.7	32.0
1969	64.9	15.9	35.9	33.9
1970	79.9	12.8	45.3	37.5
1971	139.7	27.4	86.3	68.7
1972	133.5	22.5	89.6	63.4
1973	101.6	17.6	82.8	48.5
1974	70.7	16.7	56.1	36.6
1975	57.3	18.5	52.5	32.8
1976	60.5	33.7	70.2	43.6
1977	79.0	57.8	83.4	65.6
1978	100,0	100,0	100,0	100,0

* Calculated according to real balances in December of each year presented in Table III.3.

Table III.5

EFFECTIVE RATE OF BANK RESERVES

	Reserves (R)*	Total (TD)* Deposits	$\frac{R}{TD}$
(Millions of old pesos)			
1940	318	3,017	0.11
1941	359	3,401	0.11
1942	410	3,886	0.11
1943	575	4,879	0.12
1944	639	5,954	0.11
1945	720	6,832	0.11
1946	934	8,703	0.11
1947	1,102	10,311	0.11
1948	1,424	12,645	0.11
1949	1,917	15,402	0.12
1950	2,088	16,176	0.13
1951	2,676	19,937	0.13
1952	3,677	25,063	0.15
1953	4,980	34,713	0.14
1954	7,416	50,887	0.15
1955	10,026	78,821	0.13
1956	13,934	113,137	0.12
1957	18,089	155,744	0.12
1958	24,848	206,120	0.12
1959	42,258	289,452	0.15
(Thousands of E. ^o)			
1960	88,752	400,279	0.22
1961	103,880	514,991	0.20
1962	183,627	662,245	0.28
1963 (Million E. ^o)	283	925	0.31
1964	331	1,258	0.26

	R	TD	$\frac{R}{TD}$
1965	466	1,833	0.25
1966	930	2,639	0.35
1967	1,090	3,361	0.32
1968	1,474	4,575	0.32
1969	1,998	6,454	0.31
1970	4,037	9,555	0.42
1971	7,340	17,803	0.41
1972	17,948	35,007	0.51
1973	82,224	131,840	0.62
1974	428,352	645,462	0.66
1975 (Thousands \$)	1,331	2,896	0.46
1976	6,133	11,861	0.52
1977	15,818	33,652	0.47
1978		67,502	

SOURCE: Central Bank of Chile

$$\text{*Effective Rate of Reserves} = \frac{\text{Reserves}}{\text{Total Deposits}}$$

R = Banking System Cash Reserves + Deposits of the Banking System in the Central Bank.

TD = Money on deposit of the Private Sector + Money on deposit of the Public Sector + Total Quasi-money in Private Sector in local currency.

NOTE: The sharp decline in the 1975 rate is explained by a change in the composition of total deposits (with quasi-money, which has a lower legal reserve rate than money on deposit, acquiring greater relative importance) rather than by a reduction in the legal reserve rates. The legal reserve rates vary according to the different kinds of deposits.

Table III.6

EVOLUTION OF ANNUAL RATE OF INTEREST ON LOAN OPERATIONS

	Regular Bank Interest (1)	Maximum Legal Interest (2)	Rate of Inflation Dec. Dec.	Maximum Legal Real Interest (3)	Current Real Bank Interest (3) (4)
1940	8.31	12.46	9.8	2.42	- 1.36
1941	8.33	12.49	22.7	- 8.33	-11.72
1942	8.64	12.96	25.6	-10.07	-13.51
1943	8.82	13.23	7.9	4.93	0.85
1944	9.02	13.53	15.2	- 1.45	- 5.37
1945	9.08	13.62	7.8	5.39	1.18
1946	9.16	13.74	29.9	-12.45	-15.97
1947	9.24	13.86	14.9	- 0.91	- 4.93
1948	9.84	14.76	16.9	- 1.84	- 6.04
1949	10.00	15.00	20.5	- 4.57	- 8.72
1950	10.38	15.57	16.8	- 1.06	- 5.50
1951	11.43	17.15	23.2	- 4.92	- 9.56
1952	12.16	18.24	12.1	5.47	0.05
1953	12.05	14.46	56.1	-26.68	-28.22
1954	12.91	15.49	71.2	-32.55	-34.05
1955	13.52	16.22	83.8	-36.77	-38.24
1956	13.82	16.58	37.7	-15.34	-17.35
1957	14.11	16.93	17.3	- 0.32	- 2.72
1958	15.47	18.56	32.5	-10.53	-12.86
1959	16.25	19.50	33.3	-10.36	-12.80
1960	16.55	19.86	5.4	13.71	10.57
1961	15.88	19.06	9.7	8.53	-15.63
1962	14.62	17.54	27.7	- 7.96	-10.25
1963	14.21	17.05	45.4	-19.50	-21.46
1964	14.63	17.56	38.4	-15.06	-17.18

	Regular Bank Interest (1)	Maximum Legal Interest (2)	Rate of Inflation Dec. Dec.	Maximum Legal Real Interest (3)	Current Real Bank Interest (3) (4)
1965	15.30	18.36	25.9	- 5.09	- 8.42
1966	15.84	19.01	17.0	1.71	- 1.00
1967	15.84	19.01	21.9	-23.80	- 4.98 (0.2)
1968	16.61	19.93	27.9	- 6.24	- 8.83 (- 1.33)
1969	19.59	23.51	29.3	- 4.48	- 7.51 (- 1.60)
1970	20.00	24.00	34.9	-11.37	-11.05 (- 5.1)
1971	15.00	18.00	22.1	- 3.36	- 5.82 (- 0.9)
1972	20.00	24.00	163.4	-52.93	-54.45 (-51.4)
1973	79.6*		508.1		-70.5
1974	200.4		375.9		-36.9
1975	411.3		340.7		16.0
1976	350.7		174.3		64.2
1977	156.3		63.5		56.7
1978	84.0		30.3		41.2

(1) The rate for the second semester of the respective year was used.

(2) Until September, 1953, the maximum interest allowed by Law N.º 4,694 (Nov. 1929) was 50% over and above the current bank interest for the previous semester. This rate was reduced to 20% by Law N.º 11,234, on September 9, 1953.

(3) Real interest was obtained with the following formula:

$$\text{Real Interest} = \frac{\text{Nominal Interest} - \text{rate of inflation}}{1 + \text{rate of inflation}}$$

(4) As of 1967 the real interest rate including tax on bank interest is shown in parenthesis.

* As of 1973, current bank interest is considered the cumulative rate for 12 months (Dec. to Dec. of each year), on the basis of the average monthly rates actually charged.

SOURCE: 1940-1972, Central Bank of Chile, "Estudios Monetarios III".
1973-1978, Central Bank of Chile, Financial Policy Department.

Table IV.1
BALANCE OF PAYMENTS

(Millions of dollars)

	Merchandise Exports	Merchandise Imports	Trade Account Balance	Current Account Balance	Overall Surplus or Deficit (-)
1944	198.5	152.1	46.4	13.4	
1945	212.3	167.7	44.6	19.6	
1946	237.7	201.4	36.3	4.6	
1947	281.9	268.2	13.7	- 48.2	
1948	344.4	275.2	69.2	21.2	
1949	276.5	305.9	- 29.4	- 62.8	
1950	308.3	255.7	52.6	- 3.2	
1951	383.8	361.3	22.5	- 36.4	- 3.4*
1952	469.3	388.9	80.4	17.3	15.0*
1953	468.9	357.7	111.2	31.4	- 7.3*
1954	383.4	348.7	34.7	- 17.8	- 23.1*
1955	489.4	394.7	94.7	11.5	47.7*
1956	497.9	379.9	118.0	5.7	- 11.8*
1957	396.8	459.3	- 62.5	-112.1	- 62.4*
1958	354.0	426.1	- 72.1	- 87.1	- 13.2*
1959	457.8	426.2	31.6	- 24.7	32.2*
1960	469.7	555.4	- 85.7	-148.1	- 28.4
1961	465.4	619.6	-154.2	-263.8	-108.6
1962	500.7	588.5	- 87.8	-202.1	- 49.0
1963	504.0	565.0	- 61.0	-198.8	- 28.4
1964	592.1	611.9	- 19.8	-128.5	23.6
1965	684.0	615.5	68.5	- 56.6	46.7
1966	866.5	775.4	91.1	- 82.2	119.6
1967	873.2	769.0	104.2	-127.4	- 23.4
1968	910.9	801.6	109.3	-135.2	117.9
1969	1,171.9	926.8	245.1	- 5.6	174.5

	Merchandise Exports	Merchandise Imports	Trade Account Balance	Current Account Balance	Overall Surplus or Deficit (-)
1970	1,111.7	956.0	155.7	- 81.1	113.5
1971	996.8	1,014.9	- 18.1	-188.8	-299.8
1972	847.4	1,102.6	-255.2	-386.6	-229.0
1973	1,310.5	1,447.4	-136.9	-287.6	-111.9
1974	2,150.5	2,015.5	135.0	-210.8	- 45.1
1975	1,589.5	1,707.8	-118.3	-491.3	-274.6
1976	2,115.6	1,655.0	460.6	148.0	455.0
1977	2,185.5	2,243.6	- 58.1	-399.0	- 7.0
1978	2,437.0	2,890.0	-417.0	-721.0	630.0

SOURCE: Figures from Central Bank of Chile.

*: Figures estimated according to variation in the Net International Reserves (NIR)

Table IV.2

REAL BALANCE OF PAYMENTS

(Millions of 1976 dollars)

	Merchandise Exports	Merchandise Imports	Trade Account Balance	Current Account Balance	Overall Surplus or Deficit (-)
1944	677.7	519.3	158.4	45.7	
1945	711.5	562.0	149.5	65.7	
1946	698.3	591.7	106.6	13.5	
1947	674.4	641.6	32.8	-115.3	
1948	761.1	608.2	152.9	46.9	
1949	642.9	711.2	- 68.3	-146.0	
1950	689.7	572.0	117.7	- 7.2	
1951	771.0	725.8	45.2	- 73.1	- 6.8*
1952	969.2	803.2	166.0	35.7	31.0*
1953	981.8	749.0	232.8	65.7	- 15.3*
1954	800.9	728.4	72.5	- 37.2	- 48.3*
1955	1,020.0	822.6	197.4	24.0	99.4*
1956	1,004.6	766.5	238.1	11.5	- 23.8*
1957	778.3	900.9	-122.6	-219.9	-122.4*
1958	684.9	824.3	139.4	-168.5	- 25.5*
1959	883.8	822.8	61.0	- 47.7	62.2*
1960	905.2	1,070.3	-165.1	-285.4	- 54.7
1961	901.8	1,199.2	-298.4	-510.6	-210.2
1962	966.0	1,135.4	-169.4	-389.9	- 94.5
1963	975.4	1,093.5	-118.1	-384.8	- 55.0
1964	1,143.6	1,181.8	- 38.2	-248.2	45.6
1965	1,295.1	1,165.4	129.7	-107.2	88.4
1966	1,588.0	1,421.1	166.9	-150.6	219.2
1967	1,597.1	1,406.5	190.6	-233.0	- 42.8
1968	1,625.4	1,430.4	195.0	-241.3	210.4

	Merchandise Exports	Merchandise Imports	Trade Account Balance	Current Account Balance	Overall Surplus or Deficit (-)
1969	2,012.6	1,591.7	420.9	- 9.6	299.7
1970	1,841.7	1,583.8	257.9	-134.3	188.0
1971	1,600.6	1,629.7	- 29.1	-303.2	-481.4
1972	1,301.4	1,693.3	-391.9	-593.7	-351.7
1973	1,779.4	1,965.2	-185.8	-390.5	-151.9
1974	2,456.7	2,302.5	154.2	-240.8	- 51.5
1975	1,662.6	1,786.4	-123.8	-513.9	-287.2
1976	2,115.6	1,655.0	460.6	148.0	455.0
1977	2,059.9	2,114.6	- 54.7	-376.7	- 6.6
1978	2,294.1	2,680.9	-386.8	-668.8	584.4

SOURCE: Central Bank of Chile, deflated according to WPI-USA

*Figures estimated according to variation of the NIR.

Table IV.3

CHILEAN GENERAL FOREIGN DEBT

1946-1978*

(Millions of dollars, percentages)

Year	I Total Foreign Debt*	II Gross Reserves	III Total Foreign Debt Minus Gross Reserves (I - II)	IV Real Total Foreign Debt	V Real Total Foreign Debt Index 1960 = 100	VI Yearly Variation Real Total Foreign Debt (%)
1946	354					
1947	374					
1948	370					
1949	384					
1950	392					
1951	389					
1952	395					
1953	411					
1954	397					
1955	407					
1956	403					
1957	443					
1958	499					
1959	551					
1960	746	119	627	1,235	100.0	
1961	1,010	104	906	1,792	145.1	+45.1
1962	1,255	106	1,149	2,265	183.4	+26.4
1963	1,469	114	1,355	2,680	217.0	+18.3
1964	1,635	131	1,504	2,968	240.3	+10.8
1965	1,781	182	1,599	3,046	246.6	+ 2.6
1966	1,852	234	1,618	3,030	245.3	- 0.5
1967	1,908	200	1,708	3,170	256.7	+ 4.6
1968	2,201	288	1,913	3,455	279.8	+ 9.0
1969	2,689	433	2,256	3,886	314.6	+12.5

Year	I Total Foreign Debt*	II Gross Reserves	III Total Foreign Debt Minus Gross Reserves (I - II)	IV Real Total Foreign Debt	V Real Total Foreign Debt Index 1960 = 100	VI Yearly Variation Real Total Foreign Debt (%)
1970	3.123	505	2.618	4,408	356.9	+13.4
1971	3.196	290	2.906	4,707	381.1	+ 6.8
1972	3.602	271	3.331	5,065	410.1	+ 7.6
1973	4.048	401	3.647	4,807	389.2	- 5.1
1974	4.774	535	4.239	4,620	374.1	- 3.9
1975	5.263	427	4.836	5,058	409.6	+ 9.5
1976	5.195	816	4.379	4,379	354.6	-13.4
1977	5.434	871	4.563	4,309	348.9	- 1.6
1978 (August)	6.243	1.405	4.838	4,302	348.3	- 0.2

SOURCE: Central Bank of Chile.

*For the 1946-1959 period only figures for the Nominal Foreign Debt were available.

- Column I General Foreign Debt: Net balance pending payment overseas as of December 31 of each year considering: The traditional foreign debt, that is, the debt of the public sector and of the private sector with government guarantee. Debt with the IMF. Direct foreign debt of the private sector for medium and long-term import financing. Lines of credit to private sector registered under Decree 1.272 (art.: 14, 15 and 16) and short term lines to the monetary system (Central Bank, Commercial Banks, Banco del Estado).
- Column II Gross Reserves in the Monetary System: All assets of the monetary system (Central Bank & Banks) as of December 31 of each year. In this series the value of gold in the international reserves has been corrected according to the average buying price at the close of the LME in December of each year. Reciprocal credit agreements are considered at net value.
- Column III General Foreign Debt Minus Gross Reserves: This is Chile's net foreign debt. (Column I - Column II).
- Column IV Real General Foreign Debt: Correspond to Column III deflated according to the WPI of the United States as of December, 1976. This series permits annual comparison of the foreign debt in real terms.
- Column V Real General Foreign Debt Index: Refers to the index of variation with a base of 1960 = 100 of the series presented in Column IV.
- Column VI Annual Variation of the Real General Foreign Debt: Refers to the annual variation in the debt, as deduced from Columns IV or V.

Table IV.4

INTERNATIONAL RESERVES

(Millions of dollars each year)

	Assets	Liabilities	Net	Variations		
				Assets	Liabilities	Net
1950	85.6	12.7	72.9	-	-	-
1951	84.2	14.7	69.5	- 1.4	2.0	- 3.4
1952	105.0	20.4	84.6	20.8	5.7	15.1
1953	106.6	29.4	77.2	1.6	9.0	- 7.4
1954	105.9	51.8	54.1	- 0.7	22.4	- 23.1
1955	164.9	63.1	101.8	59.0	11.3	47.7
1956	175.7	85.7	90.0	10.8	22.6	- 11.8
1957	76.4	48.8	27.6	- 99.3	-36.9	- 62.4
1958	91.0	76.6	14.4	14.6	27.8	- 13.2
1959	164.6	118.0	46.6	73.6	41.4	32.2
1960	148.6	125.6	23.0	- 16.0	7.6	- 23.6
1961	119.5	205.1	- 85.6	- 29.1	79.5	-108.6
1962	118.6	252.2	-133.6	- 0.9	47.1	- 48.0
1963	124.1	287.1	-163.0	5.5	34.9	- 29.4
1964	135.5	274.9	-139.4	11.4	- 12.2	23.6
1965	184.2	276.9	- 92.7	48.7	2.0	46.7
1966	243.6	216.7	26.9	59.4	- 60.2	119.6
1967	203.8	200.3	3.5	- 39.8	- 16.4	- 23.4
1968	294.5	173.1	121.4	90.7	- 27.2	117.9
1969	440.4	144.5	295.9	145.9	- 28.6	174.5
1970	501.7	92.4	409.3	61.3	- 52.1	113.4
1971	297.7	188.2	109.5	-204.0	95.8	-299.8
1972	250.9	370.4	-119.5	- 46.8	182.2	-299.0
1973	377.5	608.9	-231.4	126.6	238.5	-111.9
1974	419.2	695.7	-276.5	41.7	86.8	- 45.1

	Assets	Liabilities	Net	Variations		
				Assets	Liabilities	Net
1975	337.5	888.6	-551.1	- 81.7	192.9	-274.6
1976	782.7	878.6	- 95.9	-445.2	- 10.0	455.2
1977	826.7	929.2	-102.5	44.0	50.6	- 6.6
1978	1,520.8	1,006.0	514.8	694.1	76.8	617.3

SOURCE: Central Bank of Chile

Table IV.5

REAL EXCHANGE RATE 1940 - 1978

	WPI-USA Dec. 1978 = 100	CPI-Chile c Dec. 1978 = 100	Nominal Exchange Rate (NR) ^b	Real Exchange Rate (RR) ^a in \$ Dec. 78
1940	18.6	3.261 (1)	19,37	11.05
1941	20.7	3.755 (1)	19.37	10.68
1942	23.4	4.723 (1)	24.22	12.00
1943	24.5	5.489 (1)	31.00	13.84
1944	24.7	6.127 (1)	31.00	12.50
1945	25.1	6.669 (1)	31.00	11.67
1946	28.7	7.734 (1)	31.00	11.50
1947	35.2	10,333 (1)	31.00	10.56
1948	38.1	12,187 (1)	31.00	9,69
1949	36.2	14,466 (1)	31.00	7.76
1950	37,6	16,663 (1)	31.00	7.00
1951	41.9	20,372 (1)	31.00	6.38
1952	40.8	24,887 (1)	31.00	5.08
1953	40.2	31.192 (1)	50.75	6.54
1954	40.3	5,373 (2)	110.00	8.25
1955	40.4	9,413 (2)	110.00	4.72
1956	41.7	14.681 (2)	401.82	11.40
1957	42.9	19,552 (2)	619.77	13.60
1958	43.5	23,460 (2)	787.47	14.60
1959	43.6	3,253 (3)	1.13	15.15
1960	43.7	3,629 (3)	1.05	12.64
1961	43.5	3,908 (3)	1.05	11.69
1962	43.6	4,451 (3)	1.05	10.29
1963	43.5	6,421 (3)	1.88	12.74
1964	43.6	9,373 (3)	2.37	11.02
1965	44.4	12,076 (3)	3.13	11.51
1966	45.9	14,838 (3)	3.96	12.25

	WPI-USA Dec. 1978 = 100	CPI-Chile c Dec. 1978 = 100	Nominal Exchange Rate (NR) ^b	Real Exchange Rate (RR) ^a in \$ Dec. 78
1967	46.0	1,753 (4)	5.03	13.20
1968	47.1	2,220 (4)	6.79	14.41
1969	49.0	2,900 (4)	8.97	15.16
1970	50.8	3,843 (4)	11.55	15.27
1971	52.4	4,614 (4)	12.41	14.09
1972	54.8	0,820 (5)	19.48	13.02
1973	62.0	3,715 (5)	110.80	18.49*
1974	73.6	2,247	831.91	27.25
1975	80.5	10,665	4.91	37.06
1976	84.2	33,268	13.05	33.03
1977	89.3	63,859	21.53	30.11
1978	96.3	89,459	31.66	34.08

NOTES: $\frac{\text{WPI (USA)}}{\text{CPI (CHILE)}}$

a) $RR = NR \times \frac{\text{WPI (USA)}}{\text{CPI (CHILE)}}$

b) NR: 1940 – 1958 old \$/dollar
1959 – 1974 E.^o/dollar
1975 – 1978 \$/dollar

c) In order to simplify calculation, the CPI has been adjusted according to the following coefficients:

CPI: (1) $\times 10^{-5}$
(2) $\times 10^{-4}$
(3) $\times 10^{-3}$
(4) $\times 10^{-2}$
(5) $\times 10^{-1}$

* The real increase in 1973 is explained by the significant devaluation which took place in October of that year. The real figures for each quarter are:

I 9.10
II 10.62
III 13.25
IV 24.43

SOURCES: Nominal Rate: Central Bank of Chile
CPI CHILE: National Bureau of Statistics
WPI USA: International Financial Statistics

Table IV.6

PRICE OF COPPER 1940 _ 1978

(London Metals Exchange)
(US\$ - Cents / pound)

	Nominal Price	Real Price	
	(US\$ cents)	(US\$ cents, 1976)	(US\$ cents Dec. 78)
1940	10.60	47.90	56.99
1941	11.16	45.29	53.91
1942	11.17	40.17	47.74
1943	11.17	38.35	45.59
1944	11.17	38.14	45.22
1945	11.16	37.40	44.46
1946	13.89	40.80	48.40
1947	23.48	56.17	66.70
1948	24.11	53.28	63.28
1949	21.90	50.92	60.50
1950	22.35	50.00	59.44
1951	27.54	55.32	65.73
1952	32.35	66.81	79.29
1953	32.18	67.38	80.05
1954	31.27	65.32	77.59
1955	43.90	91.50	108.66
1956	41.07	82.87	98.49
1957	27.46	53.86	64.01
1958	24.73	47.84	56.85
1959	29.74	57.41	68.21
1960	30.77	59.30	70.41
1961	28.71	55.57	66.00
1962	29.26	56.45	67.11
1963	29.30	56.71	67.36
1964	43.98	84.94	100.87

	Nominal Price	Real Price	
	(US\$ cents)	(US\$ cents, 1976)	(US\$ cents Dec. 78)
1965	58.64	111.03	132.07
1966	69.47	127.32	151.35
1967	51.13	93.52	111.15
1968	56.10	100.10	119.11
1969	66.54	114.28	135.80
1970	64.10	106.19	126.18
1971	49.27	79.12	94.03
1972	48.57	74.59	88.63
1973	80.78	109.68	130.29
1974	93.27	106.55	126.73
1975	55.94	58.51	69.49
1976	63.55	63.55	75.48
1977	59.34	55.98	66.45
1978	61.89	54.11	64.27

SOURCE: Central Bank of Chile

Real price: deflated by WPI - USA

**FOREIGN CREDITS UTILIZED UNDER THE LEGISLATION OF
ARTICLE 14.***

(Figures in millions of dollars)

Year	Quarter	Public Sector	Private Sector	Total
1976	I	—	33.6	33.6
	II	—	56.6	56.6
	III	10.0	70.6	80.6
	IV	25.0	66.5	91.5
	Total	35.0	227.3	262.3
1977	I	—	55.9	55.9
	II	—	77.9	77.9
	III	31.0	78.1	109.1
	IV	12.6	74.1	86.7
	Total	43.6	286.0	329.6
1978	I	14.0	105.4	119.4
	II	3.8	169.9	173.7
	III	0.8	207.5	208.3
	IV	14.0	267.1	281.1
	Total	32.6	749.9	782.5

SOURCE: Central Bank of Chile.

*These are direct credits contracted by the public or private sectors in the foreign financial markets.

Table V

FISCAL SPENDING & DEFICIT, DEFICIT/SPENDING RATIO,
DEFICIT/EGDP RATIO*

(in millions of US\$ of 1976 and percentages)

Fiscal Spending Index (Base 1976 = 100)		Fiscal Spending		Fiscal Deficit (+) Surplus (-)		(5) EGDP	(3:1)	(4:2)	(3:5)	(4:5)	
Local Currency	Total	(1) Local Currency	(2) Total	(3) Local Currency	(4) Total						
1940	29.6		700.00		58.29	3,221	8.3			1.8	
1941	34.6		816.96		104.71	3,561	12.8			2.9	
1942	27.0		638.26		92.77	3,932	14.5			2.4	
1943	28.6		675.59		166.15	4,474	24.6			3.7	
1944	30.3		715.94		143.05	5,176	20.0			2.8	
1945	34.3		810.66		118.97	5,794	14.7			2.1	
1946	34.9		824.32		151.59	6,406	18.4			2.4	
1947	40.2		949.28		154.31	6,174	16.3			2.5	
1948	46.8		1,104.97		28.51	7,720	2.6			0.4	
1949	53.0		1,252.50		22.55	9,638	1.8			0.2	
1950	66.6		1,572.71		332.00	11,431	21.1			2.9	
1951	79.6		1,879.27		239.86	13,037	12.8			1.8	
1952	123.8		2,924.62		752.79	17,588	25.7			4.3	
1953	98.9		2,335.22		701.42	14,547	30.0			4.8	
1954	68.0		1,606.64		423.44	11,206	26.4			3.8	
1955	129.7		3,061.90		803.46	19,718	26.2			4.1	
1956	53.4		1,260.49		223.97	8,374	17.8			2.7	
1957	47.7		1,126.32		289.53	7,306	25.7			4.0	
1958	47.5		1,122.65		281.10	7,281	25.0			3.9	
1959	49.4		1,167.00		446.72	7,105	38.3			6.3	
1960	67.1	54.8	1,118.42	1,295.09	301.77	265.97	5,737	27.0	20.5	5.3	4.6
1961	69.3	58.0	1,154.81	1,370.22	245.62	275.89	6,087	21.3	20.1	4.0	4.5
1962	76.2	63.3	1,269.42	1,495.51	335.81	362.61	6,368	26.5	24.2	5.3	5.7
1963	76.5	63.2	1,275.06	1,492.25	304.83	330.93	6,692	23.9	22.2	4.6	5.0

(Continued on next page)

**FISCAL SPENDING & DEFICIT, DEFICIT/SPENDING RATIO,
DEFICIT/EGDP RATIO***

(in millions of US\$ of 1976 and percentages)

Fiscal Spending Index (Base 1976 = 100)		Fiscal Spending		Fiscal Deficit (+) Surplus (-)		(5) EGDP	(3:1)	(4:2)	(3:5)	(4:5)	
Local Currency	Total	(1) Local Currency	(2) Total	(3) Local Currency	(4) Total						
1970	116.6	101.3	1,943.98	2,392.97	279.12	246.20	8,874	14.4	10.3	3.2	2.8
1971	152.7	125.3	2,544.78	2,959.09	712.36	1,028.08	9,556	28.0	34.7	7.5	10.8
1972	165.3	124.3	2,754.52	2,935.58	1,102.10	1,230.03	9,548	40.0	41.9	11.5	12.9
1973	222.2	166.5	3,703.50	3,931.09	1,977.09	2,166.98	9,202	53.4	55.1	21.5	23.6
1974	139.7	128.4	2,328.94	3,032.13	530.02	988.79	9,579	22.8	32.6	5.5	10.3
1975	96.4	92.6	1,606.51	2,187.77	-97.70	254.86	8,343	-6.1	11.6	-1.2	3.1
1976	100.0	100.0	1,666.78	2,361.52	-76.28	235.54	8,677	-4.6	10.0	-0.9	2.7
1977	121.2	111.9	2,020.74	2,641.85	- 2.22	214.42	9,423	-0.1	8.1	0.0	2.3
1978	145.8	127.5	2,429.92	3,011.38	-151.37	126.13	9,989	-6.2	4.2	-1.5	1.3

SOURCE: Ministry of Finance, Budget Office.

*The nominal figures for the 1940-1959 period were converted to US\$ according to the exchange rate in effect at the time, since a homogeneous series for the EGDP, by which to calculate the implied exchange rate, are not available. The nominal figures for 1960-78 were converted according to the implied rate. (See Report on the State of Public Finance, 1979).

As the EGDP series for 1940-1959 is obtained by means of the respective exchange rates, it is affected by the real variations produced in the exchange rate. This explains the sharp annual fluctuations that were produced in that period. In this respect, only the percentage relations are valid.

Between 1940 and 1959 the Fiscal series are expressed only in local currency and they appear in the table in the total spending, total deficit or surplus columns.