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Industrial and Neoliberal Policies During the Pinochet Era: A Second Look

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Industrial and Neoliberal Policies During the Pinochet Era: A Second Look

by

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I. Introduction

The political economic history of Chile from the years of the Great Depression to the end of the Pinochet dictatorship in 1989 has been characterized by instability, policy reversals, and direct and/or indirect foreign interventions. The political economic models that were predominant during different phases in these years were the socialist, developmental state, and neoliberal models. The three administrations that will be highlighted the most are those of Eduardo Frei (1964-1970), Salvador Allende (1970-1973), and Augusto Pinochet (1973-1989). These administrations were the epitomes of the experimentation with the different political economic models highlighted above. The analysis of these models provides the reader with an insight into the drawbacks and advantages of each model when implemented by themselves, and of the different applications of their combinations in an effort to identify which model or combination of these were the ones that benefited Chile the most in its economic growth, production efficiency, and rising wealth and earnings. The analysis identifies that the model that benefited Chile the most in terms of these variables was a mixed model of industrial and neoliberal policies that was implemented in the latter years of the Pinochet dictatorship from 1981-1990. The study however does not attempt to explain which model was the most successful in distributing earnings in an equitable manner and in alleviating poverty, but it does explain why the model of mixed industrial and neoliberal policies was the most successful in increasing overall earnings and wealth, generating economic growth, and increasing the efficiency in domestic production.

There are a variety of questions that will be addressed throughout the analysis, the main ones being the following: Why did the switch from the free market policies to a developmental state model occur after the Great Depression? How did President Eduardo Frei solidify a system

of developmental state policies with limited socialist provisions and how did these policies commence a political divide within Chile? Why was Allende unable to cure the political divides commenced under the Frei administration and why was his presidency marked by high inflation rates, food shortages, and general instability during the last year of his presidency? Why was Pinochet forced to impose a neoliberal economic model during his first years in the presidency and why was he forced to reverse most of these policies during the Latin American debt crisis? Most importantly: Why was the mixed system of neoliberal and industrial policies successful in generating the most economic growth?

The analysis will argue that the switch to the developmental state model after the Great Depression was mainly due to the increasing vulnerability to external shocks that resulted from the existing free market policies. Eduardo Frei was able to implement a series of industrial policies that provided domestic businesses with the necessary economic incentives to build a manufacturing base that was able to compete in the international arena. These policies were continued under the Allende administration but the prominence of socialist measures in the embodiment of land reforms and social provisions was extended and the growing political divide between conservative and liberal parties forced Allende to enact a series of reforms that caused economic instability. When Pinochet took power, he was forced to implement a neoliberal model in order to secure the financial and diplomatic support of the United States and institutions such as the World Bank and the IMF. However, most of these policies were removed when the Latin American debt crisis exposed the vulnerability of an economy that was too open for trade in the agricultural sector. The resulting instability from this crisis generated a series of civil unrest and terrorist attacks that forced the Pinochet administration to impose an economic model of mixed neoliberal and industrial policies.

This mixed system was able to provide the necessary incentives for domestic and international investors to resume their economic activities after the debt crisis, as well as the support of international loans from the IMF and the World Bank. The incentives provided by the strong role of the government enabled the copper, fishery, and other natural resource industries to regain their competitive edge in the international markets. The neoliberal reforms that were kept were used to privatize inefficient industries and assured the continued support of international banks.

The analysis starts with the theoretical explanation of the three political economic models that were predominant in the different phases that comprised the years of 1930-1989. The analysis then commences its exploration of the policy reversals that were common during these years. The first switch occurs after the Great Depression from an economic model that relied on free market policies before the Great Depression to a developmental state model that comprised a stronger role of the government in its promotion of economic efficiency and incentives for domestic industries. The analysis then transitions to the exploration of the details of the Frei presidency as he solidified a system in which developmental state policies were predominant in increasing industrial efficiency, but were also combined to a limited degree with socialist policies that created a divide between the conservative and liberal parties.

The examination then moves on to the administration of Salvador Allende, a presidency that implemented a series of reforms meant to transition Chile into a socialist era but that unfortunately built upon the existing political divides and culminated in a military coup on September 11, 1973. The Pinochet dictatorship is what followed the Allende administration and it was a dictatorship that had to rely on the complete overhaul of the existing economic system in

order to gain the necessary external support from the World Bank, IMF, and US banks. The overhaul of the existing economic system relied on the complete monopolization of power, the abolition of political freedom, and authority on the part of the military dictatorship.

This monopoly was achieved by means of political repression and state terrorism and it enabled the dictatorship to establish a neoliberal economic model. The economic transformation of Chile during the Pinochet years was divided into three phases: 1973-1975, 1975-1981, and 1981-1989. During the first phase, the dictatorship was in charge of conducting widespread privatizations and dismantling all of the social provisions that had been in place since the Frei and Allende administrations. During the second phase, the dictatorship implemented a variety of neoliberal policies under the guidance of a group of technocrats known as the Chicago Boys. During the third phase, due to the increasing unpopularity of the regime and renewed terrorist attacks by the opposition, Pinochet was forced to make some changes to the existing economic model that relied mainly on neoliberal policies. These policies had made Chile vulnerable to external shocks such as the Latin American crisis of 1981 and had failed to generate economic growth. Thus, the new economic system was one that relied on mixed industrial and neoliberal policies. This system generated the most economic growth, increase in revenues and wealth, and efficiency in production.

The analysis of the neoliberal and industrial policies during the Pinochet era provides an insight into the economic models that generated consistent economic growth in Chile. Although Chile is often hailed as the epitome of the success of the neoliberal model commenced during the Pinochet era, economic growth in Chile was in fact initiated and fueled by a mixed system of industrial and neoliberal policies that enabled Chile to become one of the countries with the highest economic growth rates in Latin America. The organization will be divided into the

following sections: theoretical discussions, from the free market policies to the developmental state, the 1964 presidential elections and its implications, the Allende presidency, and the Pinochet dictatorship.

II. Theoretical Discussions

In order to fully comprehend the statements being presented regarding the economic strategies and development in Chile during the years after the Great Depression, the Allende presidency, and the Pinochet dictatorship, a series of theories and concepts must be clearly defined. The section will not only elucidate the theoretical concepts behind the economic planning and decision-making from the 1920s-1990s, it will also illustrate the ambiguity and the overlapping of these diverse theories in their applications and effects throughout the different political regimes that pervaded in Chile. Table 1 shows the different types of policies that have been predominant between 1900 and 1990 in an effort to elucidate the policy reversals and intersections evident during this time.

Table 1. Governmental Policies in Chile from 1900-1990

	Type of Policy	Actual Application
1900-1930	Free Market	Free Market
1930-1970	Industrial and Socialist	Industrial
1970-1973	Industrial and Socialist	Socialist
1973-1981	Neoliberal	Neoliberal
1981-1990	Neoliberal and Industrial	Mixed

Source: Author's findings

The economic and political discussion during these years will revolve around three concepts: developmental state theory, socialist theory, and neoliberal theory. Throughout the

presentation of the economic analysis, the reader will become aware of periods in which these economic frameworks were all present and periods in which one or two of these frameworks were predominant. In the discussion of the developmental state theory, a distinction will be drawn between the East Asian developmental state and the Latin American developmental state as they did differ in their application in the latter stages. “The developmental state¹ relies on industrial policy² as its main tool for the achievement of economic development through the state-led macroeconomic³ planning of the economy that relies on market forces” (Cypher and Dietz, 2009, p. 20). Although the economic process is led and nurtured by the state with a stronger role during its initial stages, this does not mean that the state owns the companies it helps become efficient. The developmental state must undergo a series of phases in order to become economically efficient and competitive in the international arena through a system known as import substitution industrialization (ISI), the first stage of the ISI was implemented by East Asian countries and Latin America between the mid 1960s through the 1980s.

The first stage is known as the Easy ISI. “The Easy ISI stage relies on the surplus of labor in the countryside to fuel the industrial sector of the economy” (Ibid, p.178). The government first identifies the industries that can become profitable and protects them through the imposition of tariffs⁴ and aids them in the acquisition of credit and loans at low interest rates given by national banks. The objective is to develop specific industries so that they can become internationally competitive once the tariffs are removed.

¹ An economic model proposed in the early 1960's that advocates for a stronger, more autonomous state role in the conduction of the economy through industrial policies. The model has been associated with the economic growth of the East Asian economies starting in the mid 1960's

² Policies implemented by the government of a country in an effort to strengthen the domestic manufacturing base by offering economic incentives such as tax breaks and preferential credit allocation in an effort to prepare the domestic economy for international competition with an educated entrepreneurial class

³ A branch in economics that deals with the performance, decision-making, and behavior of the economy as a whole, rather than individual markets.

⁴ A tax on imports paid on a particular class of goods.

As long as there is a surplus of labor, the wages remain the same, and the industries take advantage of the cheap labor in order to reduce the cost of producing goods. The goods being produced during this stage are low value added manufactured goods⁵ that can be easily produced by a labor group that does not possess advance skills and technical expertise (Ibid, p.188).

Even though these industries took advantage of the cheap labor and the preferential credit allocations, they were still producing at a higher cost than the international industries that were importing the same goods, thus the necessity of tariffs. However, tariffs could not be kept in place permanently because they caused consumer and deadweight losses⁶ to become predominant since consumers had to pay a higher price than the market price and the quantity exchanged (actually bought) was reduced. The necessity to remove tariffs and bring these industries into a competitive arena brings us to the second stage. The second stage of the ISI is where the East Asian and Latin American economies differed:

Whereas the East Asian economies recognized the necessity to remove tariffs in order to prevent permanent consumer and deadweight losses as well as the necessity to transition into the production of intermediate goods only after specific industries had faced international competition and had been successful in selling their goods efficiently, the Latin American economies including Chile ignored these realities. The LA economies

⁵ Goods that do not require skilled human capital in order to be produced. Examples include sodas, textiles, and paper goods.

⁶ The losses that are incurred whenever there is a decrease in the quantity exchanged in the market for a good and/or an increase in prices for the same good. These losses often come as a result of government interventions such as tariffs, price ceilings, and price floors.

immediately transitioned to the production of intermediate goods⁷ and kept the tariffs in place (Ibid, p. 195).

This strategy led to a series of failed economic policies because the industries had not faced international competition and due to this, the market was unable to determine which industries were the most efficient in producing quality goods at a low cost. Instead these companies continued under the protection of tariffs that not only imposed a cost to the government but to consumers as well.

Because the industries were not exposed to the full forces of the market, they were unable to develop an entrepreneurial class that possessed the sufficient skills to manage an industry as well as to provide its workers with the proper technical training to start producing intermediate goods that required an educated workforce. These industries were also forced to import expensive machinery with the money that they were earning from the agricultural sector. Thus, these policies created a balance of payments crisis⁸ because the economy was relying on cheap agricultural goods that were less profitable and more volatile than industrial goods (Ibid, p. 197).

Hence, this is why the developmental state model was less successful than it was in the East Asian economies, however this does not mean that the entirety of the industrial policy failed in Chile, as will be examined in the latter sections.

The second theoretical concept that will be analyzed is the socialist state and its corresponding socialist policy. “Socialism is a political and economic theory that advocates that the means of production, distribution, and exchange should be owned or regulated by the

⁷ Goods that require a skilled human capital in contrast to low value added manufactured goods. These goods are in turn used as inputs for final goods. Some examples are steel and car engines.

⁸ Also known as a currency crisis. A situation that occurs when a nation is unable to pay for essential imports and/or service its debt repayments

community as a whole. This social ownership is often equated with state ownership as well as cooperative enterprises” (Mises 2009, p.15). However, in the discussion of the Chilean socialist economic framework and policies, the focus will be on the state ownership of industries and banks in order to fuel economic growth.

A socialist economic system is aimed at the production and distribution of goods that directly satisfy human needs and demands rather than for private profit. Decisions are taken on a basis of a political hierarchy that conducts policies in the name of the collective group in terms of re-allocation of resources and welfare distribution. The main objective of socialist policies is to provide the community with a more equitable distribution of the earnings made by industries that are often collectively owned enterprises or state owned enterprises (Ibid, p. 45).

Thus, this method of distribution goes against the resource allocation mechanisms of the market that are determined through the price mechanism. Socialist policy does require extensive state intervention and it should not be confused with industrial policy that relies on the market mechanisms to determine which industries are more efficient in order to aid them through preferential credit, loans etc. Socialist policy does not rely on this mechanism and:

Entails policies such as the nationalization of banks and industries as well as the imposition of welfare projects, and the empowerment of trade unions and collective organizations. These welfare policies such as wage negotiations with trade unions and the nationalization and governmental control of banks goes against the free market theory that advocates the market to be the most efficient resource allocator (Fleming 2007, p. 63).

Thus, although industrial policy does involve state-led macroeconomic policy, it still relies on the market for its efficiency and direction, unlike socialist policy.

The third theoretical concept that will be analyzed is neoliberal theory. Neoliberalism arose as a response to the failure of embedded liberalism⁹ after World War II, a system that had relied on Keynesian¹⁰ economics and was unable to correct the balance of payments crisis¹¹ that governments around the world were facing in the 1960s. “Neo-liberalism as a theory calls for the construction of a better world based on individual rights and freedom, rights that can be secured only by private property rights and the freedom of the market to be guided by its invisible price mechanism¹²” (Harvey 2005, p. 33). Yet, as neoliberalism calls for individual rights, it also demands for the commodification¹³ of everything including labor.

Neoliberalism was presented as the solution to the failure of embedded liberalism yet it can also be described as a maneuver for business elites to prevent further state intervention in their corporate profits in the face of the rise of increasingly socialist regimes such as that of Sweden in the 1960's. David Harvey¹⁴ views neo-liberalism “as a project to restore class power as neoliberalism in practice without state intervention allows for the massive accumulation of

⁹ A term for the global economic system as it existed from the end of World War II to the 1970s. The system was set up to support a combination of free trade with the freedom of states to enhance their provision of welfare and to regulate their economies to reduce unemployment.

¹⁰ An economic theory stating that active government intervention in the marketplace and monetary policy is the best method of ensuring economic growth and stability.

¹¹ During the 1960's almost all of the major industrialized nations were suffering from a currency crisis that resulted in an increase in debt, loss of purchasing power, and the consequent inability to pay for existing debts. This resulted in a variety of currency wars where industrialized nations devalued or overvalued their currencies in order to gain a competitive edge in exports and thus gain more revenues for the domestic economy. The crisis resulted in the abolition of the Gold Standard and the transition to a floating currency system where the currencies around the world were no longer fixed or pegged to gold.

¹² A term coined by economist Adam Smith in his 1776 book "An Inquiry into the Nature and Causes of the Wealth of Nations". The invisible hand is essentially a natural phenomenon that guides free markets through competition for scarce resources and ensures the most efficient allocation of resources.

¹³ The transformation of goods and services, as well as ideas or other entities that normally may not be considered goods, into a commodity.

¹⁴ Distinguished professor of Anthropology and Geography at the City University of New York. Wrote the prominent book “*A Brief History of Neoliberalism*” in 2005.

capital in the upper echelons of society, especially those who are vital parts of the financial sectors of the most industrialized countries” (Ibid, p. 100). “Neoliberal policies include liberalization,¹⁵ privatization, de-politization, monetarism,¹⁶ and deregulation¹⁷. These practices are geared towards limiting the government’s intervention to securing that the conditions for neoliberalism are optimal” (Mudge 2008, p. 7).

Through these policies and the limitation of the government’s role in the economy, neoliberalism promises the most efficient system in the production of economic growth and makes no promises regarding the equitable distribution of profits and a decrease in factors such as unemployment. Another important point of analysis is the difference between neoliberal theory and neoliberal application, a point that will be especially emphasized during the economic analysis of the policies during the Pinochet Era. “Although neoliberal theory emphasizes the government’s limited role in the conduction of the economy, it needs the government to intervene whenever there is an economic crisis” (Przeworski 1992, p. 22) such as the Latin American debt crisis of the 1980’s (explained in the later sections). “The countries that have adopted a neoliberal economic framework have often been forced to undergo a series of structural reforms that have created widespread unemployment and an unequal income distribution as well as sometimes even negative economic growth” (Breneck, Peck, Theodore, 2010, p. 33).

¹⁵ The removal or reduction of restrictions or barriers on the free exchange of goods between nations. This includes the removal or reduction of both tariff (duties and surcharges) and non-tariff obstacles (like licensing rules, quotas and other requirements).

¹⁶ A set of views based on the belief that inflation depends on how much money the government prints. It is closely associated with Milton Friedman, who argued, based on the quantity theory of money, that the government should keep the money supply fairly steady, expanding it slightly each year mainly to allow for the natural growth of the economy.

¹⁷ The reduction or elimination of government power in a particular industry, usually enacted to create more competition within the industry.

Now that the theoretical concepts have been introduced, it is easy to understand how the different theories and applications can overlap in their effects and how their application may not be explicitly categorized as neoliberal, industrial, or socialist policy but rather as a mix of these various elements in a variety of areas in the economy and in society as a whole. Institutions such as the World Bank, the IMF, and scholars such as Milton Friedman¹⁸ and Hernán Buchi¹⁹, have claimed that the Chilean economic miracle of consistent economic growth during and after the Pinochet Era is a result of the neoliberal reforms that were implemented during the Pinochet Era. Scholars such as Naomi Klein²⁰ (2007) and David Harvey (2005) negate this statement by presenting evidence that illustrates that Chile's political and individual freedoms were eliminated once Pinochet came to power partly in order to institute neoliberal reforms that resulted in the creation of negative economic growth and generated widespread unemployment and debt crises. Was Chile's economic miracle based solely on neoliberalism or was it based on a mixed economic system of the theoretical and practical concepts reviewed in this section? Did neoliberalism generate growth as neoliberal theory promises? Was neoliberalism detrimental to Chile's economy and society? Was neoliberalism a vital factor for the political survival of the Pinochet regime? All these questions will be addressed in the following sections.

¹⁸ An American economist and statistician best known for his strong belief in free-market capitalism. Milton Friedman strongly opposed the views of Keynesian economists, encouraging governments to minimize their involvement in the economy by reducing taxes and ceasing inflationary policies.

¹⁹ A Chilean economist and politician. He served as Minister of the Treasury under the government of Augusto Pinochet between 1985 and 1989.

²⁰ A Canadian author and social activist known for her political analyses and criticism of corporate globalization. Author of the "The Shock Doctrine" where she talks in detail about the psychological and economic exploitation Chilean citizens endured during the Pinochet dictatorship.

III. From the Free Market policies to the Developmental State (1919-1930s)

Chile's economic and political history since World War I have been mixed and often conflicting as political elites and economic technocrats have strived to find a perfect system for the achievement of political unity and economic growth.

After World War I and before the Great Depression of the 1930s, the Chilean government imposed a series of economic reforms that sought to increase foreign investment, privatize national industries, and advocate for the further implementation of the free market philosophy; efforts similar to those experienced fifty years later during the Pinochet dictatorship (Collins and Lear, 1995, p. 21).

Once the Great Depression gathered pace and intensified after the stock market crash of 1929,²¹ the Chilean government realized that the economy's over-exposure to the world economy through import dependency and foreign direct investment²² among other free market policies, had placed Chile in an increasingly vulnerable position. Thus, once Chile recovered from the loss of imports and investment of the 1930's, it became a pioneer in Latin America as a "developmental" nation.

The objective of the transition from free market policies to developmental state policies was to lessen Chile's dependency on foreign imports, diversify and direct its economy away from its main export markets (mainly mineral resources such as copper and coal), and lessen the country's vulnerability to world swings. The wave of privatizations that had taken place during the years between World War I and the Great Depression had re-directed revenues from the government to international elites and had caused serious

²¹ A severe downturn in equity prices that occurred in October of 1929 in the United States, and which marked the end of the "Roaring Twenties." The crash of 1929 did not occur in one day, but was spread out over a two-week period beginning in mid-October.

²² An investment made by a company or entity based in one country, into a company or entity based in another country.

distributional inequalities. Chile's industrial policies sought to reduce these inequalities (Ibid, p. 40).

Thus, Chile started to transition from a system of free-market policies to a developmental state system, a system that recognized that the government could play a fundamental role in promoting economic development and social equity. Table 2 illustrates the changes experienced in GDP, exports, and tariffs in the transition from free market policies to developmental state policies. The table illustrates the drop in GDP as a result of the Great Depression and its effect on natural resource exports that were highly vulnerable to world price swings. The table shows the decline in exports in copper and nitrate as well as an increase in tariffs due to the implementation of industrial policies as part of the developmental state model to build a strong manufacturing base.

Table 2. Chile: GDP, Exports, and Tariffs, 1928-1940
(1926=100)

	GDP	Total Exports	Nitrate	Copper	Average Tariffs
1928-1929	124	134	136	187	117
1930	106	93	96	122	136
1931	84	69	40	80	140
1932	71	26	17	33	80
1933	87	38	15	57	137
1934	105	63	22	95	176
1935	111	60	32	91	179

1936	117	71	32	106	177
1937	133	112	36	223	162
1938-1940	138	89	42	176	154

Source: Diaz, Lüders, Wagner (2003)

Within this system, the government came to recognize that the decisions taken in the private sector were not always the most efficient ones, sometimes the public sector had to actively intervene and conduct monetary²³ and fiscal²⁴ policy actions in order to encourage economic growth. Hence, until the adoption of neoliberal reforms in 1973 by the Pinochet dictatorship, Chile advocated a mixed system in which the private sector remained predominant and the government played an active role in intervening during recessions and in maximizing economic growth. Consequently, “the government started investing large sums of money in infrastructure projects and in private and public enterprises considered vital for economic development and diversification” (Ibid, p. 44). The government extended credit policies and protective policies in order to encourage the formation of a diverse industrial base in textiles and manufacturing that produced goods that were in high demand in the domestic market and decreased the demand for imports. Socialist policy was also implemented when social services were expanded and the government invested heavily in the provision of education, housing, social security, and health services. Unfortunately, proper agencies were not established to oversee the management of these programs and the government was reluctant to increase taxes on the population in order to finance them.

²³ The actions of a central bank, currency board or other regulatory committee that determine the size and rate of growth of the money supply, which in turn affects interest rates.

²⁴ Government spending policies that influence macroeconomic conditions. These policies affect tax rates, interest rates and government spending, in an effort to control the economy.

During this time, the country also became increasingly politicized as a variety of political parties struggled to grasp different constituencies such as urban workers, farm workers, women, etc. The political system came to be characterized by left, center, and right-wing coalitions.

The political factionalism increased when Chile faced a developmental crisis²⁵ that started in the early 1960s and culminated in the destruction of the industrial and socialist policies that had preceded the Pinochet dictatorship. The expansion and diversification of the industrial domestic base as well as the provision of social services had been largely financed by budget deficits,²⁶ deficits that contributed to a surge in inflation²⁷ (Cypher and Dietz, 2009, p. 6).

Although the economy had become somewhat diverse, “it was still overly dependent on copper (80 percent of the total exports) and these companies remained under US ownership. The agricultural sector remained under the tight grip of landowners that were reluctant in adopting any reforms that kept the sector from becoming stagnant” (Ibid, p. 10). It is precisely during these years of economic chaos that political factionalism and opposition reached their peak.

IV. The 1964 Presidential Elections and its Implications

The 1964 presidential election was especially significant because it was the first election that created deep and serious political divides between the political parties of Chile, especially between the moderate right Christian Democrats and the leftist Popular Unity party. The corresponding candidates were Eduardo Frei and Salvador Allende. With the support of large

²⁵ An economic crisis that started in the presidency of Eduardo Frei. It arose due to the increasing debt incurred by the amount of loans that were being provided in order to finance the industrial policies and strengthen the manufacturing base. This debt lead to the government to incur a series of budget deficits throughout the Frei administration

²⁶ A financial situation in which the government has more money going out through lets say imports than money coming in through lets say exports

²⁷ The rate at which the general level of prices for goods and services is rising, and, subsequently, purchasing power is falling.

sums of money from the CIA and the members of the moderate right and the ultra conservative parties of the right, Frei was able to win the election. “From 1964 to 1970, the objectives of President Frei were to limit government interventions, reduce foreign influence, implement an agrarian reform, and despite the budget deficits and debt problems that the government had, expand social services such as housing and education” (Collins and Lear, 1995, p. 91). In an effort to reduce foreign influence, Frei bought “51% of the stock shares of the copper industry, but the substantial tax breaks Frei gave the U.S. mining companies allowed them to continue to take out enormous profits” (Ibid, p. 123). The leftist groups were hostile to these policies since they advocated the complete expropriation of foreign owned enterprises.

The Frei administration was limited in reducing foreign influence because they continued to accept much needed loans from the United States in order to finance their continuous budget deficits. Frei’s administration also intervened in the agricultural sector and sought to reduce the power that landed elites held. “In 1964, huge estates comprising a mere 7 percent of Chilean farms controlled over 80 percent of agricultural land, a pattern prevailing since colonial times” (Ibid, p. 136). Frei gave rural workers the legal right to form labor unions, engage in collective bargaining, and conduct strikes. Once rural workers gained these rights, political parties became increasingly interested in incorporating them into their constituencies. Thus:

In 1967, Frei implemented an agrarian reform that put limits on the size of agricultural holdings and attempted to establish worker cooperatives on these expropriated lands. In this matter, Frei based bitter opposition from the parties of the right that opposed any reform that appeared to be socialist, and even from the parties of the left that claimed that the agrarian reform was not working fast enough or as efficient as it needed to be in order to re-distribute land in a more equitable manner (Cypher and Dietz, 2009, p. 16).

The events and reforms of the Frei administration have been singled out, because it is important to clarify various misconceptions that are held by the general public in the analysis of the Allende administration that followed Frei's administration in 1970. Although Allende's administration was plagued with economic chaos during the last two years of his presidency, much of this was a result of the economic and political instability that existed due to the nature of the country's political factionalism and the policies that preceded him. Allende was also not the first Chilean president who implemented industrial and socialist policies. As previously discussed, Chile became a pioneer in the implementation of developmental policies in Latin America after the Great Depression and the administrations since then also implemented socialist policies that were aimed at providing social services. Also, the political fragmentation and instability that was partly responsible for the military coup that led to the deposition of Allende in 1973, was not only generated during the Allende administration but rather commenced in the early 1960s with the developmental crisis and was heightened by Frei's policies that disturbed both the conservative and left-wing parties.

V. The Allende Presidency

A. Political Factionalism and Instability

Allende came to power in a very hostile political and economic situation. The country was:

Dependent on imports and foreign loans and had a significant amount of internal debt due to the provision of internal loans, credits, and social provisions that were financed on the basis of budget deficits. He also had to deal with an agrarian reform that was stalling and

making rural families and leftist parties increasingly militant and impatient. The country's major export-industries, with the exception of the copper industry (Frei had purchased 51% of the stock shares), were still under the control of foreign investors that were reluctant to expand their existing industries because of the high rate of inflation and political instability (Ibid, p. 27).

When he assumed power, Allende's main objective was to pursue a "peaceful and democratic road to socialism," an objective that created even greater political hostility both in the parties of the right and the left. The Popular Unity (UP) party itself was severely fragmented. The two main parties that formed the UP were the Communist party and Allende's Socialist party but the party was composed of a variety of other groups such as the Independent Marxists, Trotskyists, Anarcho-Sindicalists and Guevarists. These groups varied in their political radicalism and many of them were not in agreement with Allende's "peaceful" road to socialism. Thus, many of the actions taken by the Popular Unity party during the Allende presidency were not directly approved by Allende (such as those in the rural areas that will be mentioned later). They were in fact a product of the miscommunication and disagreement among policies between the various groups of the Popular Unity.

Besides disunity in his party, Allende also faced other elements of political instability that came to be associated with his party. The Movement of the Revolutionary Left (MIR) and the Marxist Revolutionary Vanguard (VRM) were movements that came to be associated with Popular Unity simply because the members that composed it were part of the political left. In 1968, the MIR established a polemical newspaper that was called *The Rebel (El Rebelde)*. Throughout Allende's presidency, the newspaper printed various revolutionary manifestos that encouraged the peasants and the dissatisfied urban lower classes to take over landed estates and

factories. “The MIR actively opposed the theory of a peaceful way to socialism because its members believed that a peaceful way politically disarmed the lower classes. The MIR also believed that unless the working class took arms, the owners of factories would try to suppress the working class through totalitarianism or through civil war before ceding power.” (Collins and Lear, 1995, p. 31).

The problem was that, although Allende was not associated with these groups, he could not distance himself from them, because these groups had attracted a broad constituent base. In 1971, the MIR became increasingly militant, when it started encouraging peasants to engage in violent confrontations and take land by force as well as engage in work stoppages in the industrial belts. Allende repudiated these actions and asked the peasants to wait for the legal expropriations to take place. “On June 29, 1973, the military organized what is now widely known as *El Tancazo*. A series of generals of the army took over the main squares of Santiago and blocked the streets with tanks while they engaged in mutiny. When the government failed to respond harshly enough, the members of all the leftist parties and organizations knew that a coup was impending.” (Ibid, p. 23).

Once Allende realized that the country’s political fragmentation was too unstable and that the coalition of the Popular Unity could fall apart, he tried to reach a compromise with the Christian Democratic (DC) party, because it was a moderate right-wing party. The Christian Democrats refused to compromise, because they believed that once Allende’s term was over, the DC leader Patricio Aylwin would be elected. The Christian Democratic party was also an unstable and divided political party. The DC was registered in 1957 and it relied on middle class Christian support tired of traditional parties. The DC advocated for a “Third Way”, a political platform that was neither socialist nor capitalist. The problem was that the Third Way was

interpreted differently among leaders of the party and this was a constant cause of disagreement and instability, which ultimately led to a high degree of factionalism. “When Allende was first elected in 1970 and Popular Unity remained strong, various members of the DC defected and joined Popular Unity, rendering the DC an ultra conservative party” (Cypher and Dietz, 2009, p. 12). This switch weakened the DC and made the remaining conservative members reluctant, when it came to negotiating with Allende during the final years of his presidency to preclude a coup.

The most vehement and effective opposition to Allende’s presidency was the Association of Entrepreneurs (AE) who were themselves backed up by international investors with US support. “These entrepreneurs represented the large industries and worked through channels such as the Confederation of Product and Commerce in order to introduce policies that conflicted with the government” (Ibid, p. 9). For example, as will be discussed later, one of the policies that Allende implemented in 1970 during the first months of his presidency was to freeze prices and raise wages. The entrepreneurs decided to stop producing once these policies were implemented and contributed to the scarcity of several goods that characterized the latter years of Allende’s presidency. Yet, the issue in which Allende faced more disunity from within his party was that of land reform.

B. Land Reform

The land reform program that Frei had instituted in 1967 had fallen short of its objective and had furthered divided the country into the political right and left. Allende’s objective was to continue the expropriation of big estates, but he was unable to do so at a faster pace, because he faced strong opposition from Congress. “Even though only about 25% of Chileans lived in the

countryside and rural areas accounted for only 8% of the Gross National Product²⁸ in 1970, Allende found it strategically necessary to propose an efficient plan of land reform” (Steetland 1997). Allende carried out this plan for two reasons: the food shortage crisis²⁹ and the need to gain support from politically uncommitted sectors of Chile.

“The food shortage crisis commenced when inflation skyrocketed during the Frei administration and Chileans lost purchasing power and were unable to continue importing foodstuffs.” (Ibid) Chileans were heavily dependent on imports because the government had relied on mineral resources as their main export revenue and had funneled all the government resources into this area while neglecting the domestic agricultural market. Allende was also forced to find ways to co-opt the rural peasants because he came into power at a time of political hostility from both left and right wing parties as well as from the foreign investors that were dissatisfied with the climate of uncertainty and political instability.

When Allende first came to power in 1970 and for the duration of his presidency, Congress was dominated by the Christian Democrats and by the parties of the right. “These political groups in Congress ordered Allende to sign a statute of guarantees that obliged Allende to promise that he would respect the right of private education, the monopoly of arms, the chain of command, and the non-political character of the armed forces” (Collins and Lear, 1995, p. 82). Once Allende took office he tried to accelerate the pace of land expropriation and the Christian Democrats accused him of violating the statute of guarantees and creating a social area of property and expropriation. Allende also went beyond his executive powers when he took over factories because the factory owners had refused to continue producing at the current prices and

²⁸ An economic statistic that includes GDP, plus any income earned by residents from overseas investments, minus income earned within the domestic economy by overseas residents.

²⁹ A crisis in Chile during the first year of the Allende presidency that arose as a result of a significant rise in inflation and the consequent loss of purchasing power and the inability of citizens to import the same amount of foodstuffs.

wages. Opposition from Congress increased even more when radical groups such as the MIR decided to publish communist manifestos and encourage peasants to take land by force.

Even though the Chilean Congress staunchly opposed Allende on the issue of land reforms, he was still able to sign some resolutions that accelerated the land reform process and affected over half of the country's irrigated land by 1973. Another issue with the patterns of expropriation was that Allende refused to work through peasant councils in order to establish worker cooperatives on expropriated land, and this caused the alienation of various peasant groups that started to firmly oppose Allende's policies.

The new minister of Agriculture Jacques Chonchol instituted the most famous land reform resolution on January 1972. The minister promised to expropriate all estates that were larger than eighty basic hectares. By the end of 1972, no farm exceeded these limits and the conservative right, businessmen, and landed elites started to look for the support of the US government in order to mount an opposition against Allende's policies (Steetland 1997).

Yet, the policies that generated the greatest opposition from the entrepreneurs, businessmen, and foreign investors were the socialist policies that led to serious economic decay in the industrial belts of Chile.

C. Socialist Policies and Economic Decay

Allende's main objectives in the economic sector were to improve Chile's export earnings, diversify exports, redistribute income, increase production and national consumption, and raise living standards. "A 1968 study showed that the top fifth of the Chilean population captured over half of national income, while the bottom fifth wound up with less than 5 percent"

(Politzer 1989, p. 10). When Allende came to power he was also concerned with finding ways in which he could raise his popularity since the Frei administration had caused the country to become deeply divided along political and economic lines.

On November 1970, in an effort to co-opt the leftist supporters that were dissatisfied with the Popular Unity, Allende froze prices and gave factory workers wage hikes, much to the dissatisfaction of the capitalist elites and business owners. “During 1971, The short-term economic results of Minister of Economics Pedro Vuskovic's expansive monetary policy were unambiguously favorable: 12% industrial growth and an 8.6% increase in GDP, accompanied by major declines in Chile’s long-endemic chronic inflation (down from 34.9% to 22.1%) and unemployment (down to 3.8%).” (Collins and Lear, 1995, p. 53). However, in the long run, by 1972, manufacturers refused to produce at fixed prices and either stopped producing or sold their products on the black market. When the number of manufacturers doing this increased, scarcity of goods became commonplace and long lines in supermarkets as well as people rushing to spend their income as soon as they received it became ordinary. With the increasing scarcity of goods, the people in need of social assistance increased and the government was forced to finance its social programs through deficit spending³⁰ and printing money, contributing further to a rise in inflation. Congress was also strongly opposed to any tax reform, so the government had a limited revenue base for its social programs. “The annual inflation rate climbed to 150 percent by mid-1973 and to even higher levels in the months leading up to the September coup³¹. The average Real GDP³² contracted between 1971 and 1973 at an annual rate of 5.6% (“negative

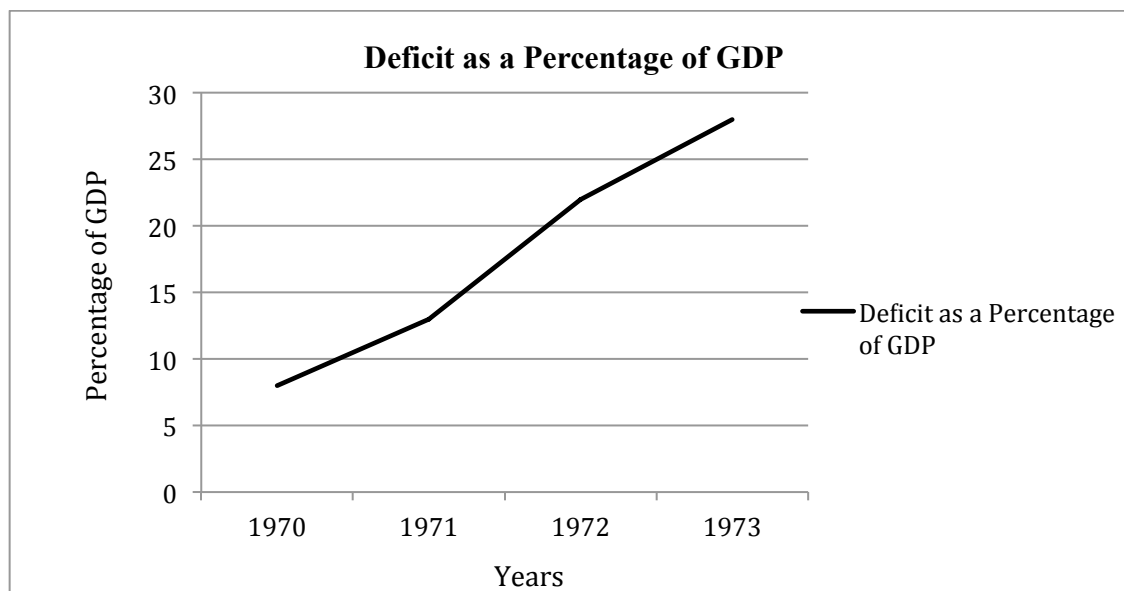
³⁰ When a government's expenditures exceed its revenues, causing or deepening a deficit. This excess spending needs to be financed through borrowing, likely from foreign governments.

³¹ A military coup carried on by the Chilean Armed Forces against president Salvador Allende on September 11, 1973.

³² An inflation-adjusted measure that reflects the value of all goods and services produced in a given year, expressed in base-year prices.

growth"), and the government's fiscal deficit³³ soared while foreign reserves³⁴ declined" (Angel and Pollack, 1993, p. 113). Figure 1 illustrates the increase in deficit spending as a percentage of GDP due to the expansion of social services under the Allende administration. Figure 2 shows the decline in foreign reserves. This decline prevented the government from purchasing the same amount of imports as during the Frei Administration and directly affected the ability to import machinery to build a strong manufacturing base as part of the continuation of Frei's industrial policies.

Figure 1. Chilean Deficit as a Percentage of GDP 1970-1973

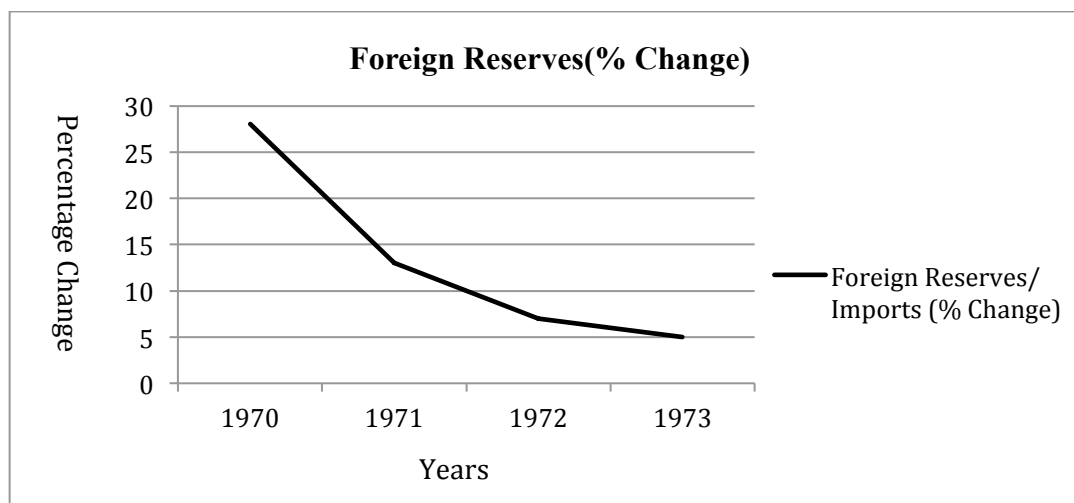


Source: Pontifical Catholic University of Chile

Figure 2. Percentage Change in Chilean Foreign Reserves/Imports 1970-1973

³³ When a government's total expenditures exceed the revenue that it generates (excluding money from borrowings). Deficit differs from debt, which is an accumulation of yearly deficits.

³⁴ A foreign currency held by central banks and other major financial institutions as a means to pay off international debt obligations, or to influence their domestic exchange rate.



Source: Pontifical Catholic University of Chile

On November 1970, Allende implemented an emergency plan for the construction of 120,000 residential buildings despite the fact that the country's economy was running on budget deficits. Allende also granted part-time workers the rights to social security and granted amnesty to political prisoners. "In early 1971, he raised the wages in real terms for blue collar workers by 37% - 41% and 8% - 10% for white collar workers. A year later, blue collar wages rose by 27% in real terms" (Cypher 2004, p. 16). These policies culminated on October 1972 when truckers, small businessmen and students took to the streets and organized strikes for twenty-four consecutive days. These groups protested against either the frozen prices and rising salaries or the lack of sufficient government provisions in the face of growing scarcity. The strikes became even more common, when the copper industry suffered from a global change in prices in 1971 and 1972. "Shares in the copper industry fell from 66 dollars in 1970 to 49 dollars in 1971 and 1972" (Collins and Lear, 1995, p. 189)

In order to gain a greater percentage of export revenues and decrease foreign holdings in the country, Allende completed the nationalization of the copper industry that Frei had commenced. The Popular Unity government broke the private monopoly in the banking sector

when it bought all three of the country's largest banks and many industries controlled by family conglomerates. "The problem is that these policies created a deeper political divide because it was done against the opposition of the center and the right-wing parties and utilizing a 1932 resolution that allowed industries to be temporarily requisitioned in the public interest" (Cypher 2004, p. 31). The climate by 1973 was increasingly unstable, massive sums of money were illegally converted by businessmen into dollars and deposited in offshore banks, merchants hid away goods and sold them at a high price on the black market, and business people stopped producing and investing. During 1973, Chile also experienced an enormous brain drain as lawyers, doctors, and entrepreneurs emigrated to the United States and Western Europe.

The tensions between the Chilean and the US-government reached their peak when the 1932 law allowing the government to requisition and nationalize foreign owned industries was passed. The Nixon administration cut off all aid and credit programs to Chile and used its power within the World Bank and the Inter-American Bank to cut off loans. "During the six-year Frei government, U.S. economic aid had totaled \$1.2 billion; during the three years of the Popular Unity government, the total dropped to \$68 million, of which \$33 million was military aid" (Angel and Pollack, 1993, p. 58). The middle class became increasingly wary of Allende's socialist goals and played into the hands of the right-wing media that started comparing Allende's government with Fidel Castro's³⁵ dictatorship in Cuba. Although the climate of inflation and scarcity was chaotic, as Gonzalo Martner, Allende's Minister of Planning commented a few years after the coup as follows "Many people repeatedly refer to the economic chaos of the last year of the Popular Unity. Yet the drop in production in 1973 was 6 percent, while under Pinochet both in 1975 and 1982, it was as bad as fifteen percent. The problem was

³⁵ A Cuban communist revolutionary and politician who was Prime Minister of Cuba from 1959 to 1976, and President from 1976 to 2008 after a coup against democratically elected president Fulgencio Batista.

not simply one of economic production but the manipulation of information and fear” (Lomnitz and Melnick, 1991, p. 29).

Thus, the Allende administration was torn between its goals of structurally readjusting the economy in order to decrease inflation and encourage investment and that of gaining the support of the poorer classes while fighting off opposition both domestically and internationally. Unfortunately, these goals were self-contradictory. In order to maintain the support of the poorer classes, Allende had to continue funneling government revenues into the government programs that were in charge of granting those in need with service provisions. This prevented his administration from reducing inflation because it had to finance these programs by running up budget deficits and printing more money. These actions also precluded the Popular Unity administration from creating a climate of confidence in which investors would not be afraid that the value of their investments could turn to nothing overnight.

As Allende continued to support the poorer classes by expropriating land, taking over factories, raising wages and freezing prices, and nationalizing industries, he lost the support and gained the fervent opposition of groups that belonged to the moderate right, conservative right, and foreign governments such as the United States and investors from abroad. These groups were in charge of organizing demonstrations, economic sabotage, destabilization policies and violent actions. Allende was forced to remain true to his socialist promises despite the country's inability to remain in that course. Hence, Allende's policies ostracized a significant number of political and economic sectors in the country. “In collusion with the US government and the CIA, the entrepreneurs and businessmen decided to collaborate with the Chilean army in what ultimately led to a coup against the Allende administration in the early morning of September 11, 1973” (Politzer 1989, p. 92).

D. The September 11 Coup

As previously illustrated, the coup occurred due to a combination of causal factors that had been present ever since the economic and political instability of the 1960s developmental crisis and the Frei administration. Allende's peaceful road to socialism was far from peaceful as members of the leftist parties and organizations took land by force and members of the conservative parties engaged in economic sabotage and congressional deadlock. On top of these factors, the business and entrepreneurial classes halted production and investment, while the armed forces engaged in mutiny and strikes. These factors arose from the inflationary and deficit spending economic policies of Frei and were further aggravated, when the Allende administration was pressured into spending more on government programs in order to keep hold of its main constituent base (urban workers and rural peasants). The US government and US investors were eager to find ways to curb Allende's power as their profits kept falling and their investments became unstable. Allende knew that unless he was able to achieve a coalition that would broaden his constituent base and increase political stability and unity, he would be the victim of a coup.

In early 1973, Allende approached the leader and future presidential candidate of the Christian Democratic party, Patricio Aylwin in order to form a coalition.

Aylwin was confident that he would win the next presidential elections and he refused to form a coalition, forcing Allende to establish the ninth cabinet in less than three years. Meanwhile, the Chamber of Deputies (the lower house of Chile's bicameral Congress) passed a regulation (mainly a statement) castigating Allende for his condoning of the

illegal seizure of productive property and the arming of extremist groups such as the MIR (Cypher 2004, p. 10).

During the first months of 1973, the Allende administration was also forced to deal with a massive popular strike by many groups in the transportation industry such as the Independent Truckers Association that were fearful that Allende would take over the transportation industry as he had done with so many other industries through nationalization.

On June 29, 1973, Colonel Roberto Souper surrounded the La Moneda presidential palace with his tank regiment but failed to depose the Allende government. “This coup had been planned by the *Patria y Libertad* (Nation and Freedom) paramilitary group and was followed by a general strike by the copper miners of *El Teniente*.³⁶ In late August 1973; 100,000 women congregated at Plaza de la Constitución protesting inflation and increasing shortages of food” (Angel and Pollack, 1993, p. 66). Also, on August 22, 1973, the Chamber of Deputies accused Allende of unconstitutional acts and called upon the military to enforce constitutional order. In this instance, the Chamber of Deputies passed a 81-47 resolution with the support of the Christian Democrats and the ultra Conservative parties that asked the President of the Republic, the ministers of the state, and members of the Armed and Police Forces to put an immediate end to breaches of the constitution. The resolution accused the socialist government of Allende of the following:

Ruling by decree, refusing to enforce judicial decisions against its partisans, ignoring the decrees of the Independent General Comptroller’s office, usurping control of the National Television Network, allowing socialist supporters to assemble armed, supporting more

³⁶ The biggest copper mine in Chile

than 1,500 illegal takings of farms, illegal repression of El Teniente miners strike, and illegally limiting emigration (Archivos de la Camara de Diputados Chilena, 1973, p. 22).

Allende responded by stating that the Chamber of Deputies had not obtained the necessary 2/3 Senate majority to accuse Allende of abusing his powers and to ask the armed forces to take action in restoring constitutionality. Allende also argued that the legislature was usurping the power of the executive and illegally calling for a coup against a democratically elected government that had respected the constitution. Not only was Allende fervently opposed by Congress, he was also opposed by businessmen, entrepreneurs, and foreign governments.

The Association of Entrepreneurs started organizing themselves in late 1972 and started engaging in economic sabotage in collusion with the business elites and the monetary support of the US government through the CIA. The coup is suspected to have been planned during the early months of 1973, a variety of factors seem to validate this suspicion. “First of all, the composition of the high command of the Armed Forces and the police had to be changed three times in the months prior to the coup. These changes culminated in the appointment of Augusto Pinochet³⁷ as the head of the Chilean Armed Forces” (Lomnitz and Melnick, 1991, p. 76). Chile had not been at war since the Pacific War³⁸ (1879-1883), “so when the troops were ordered to take over the streets of Santiago and attack the presidential palace, they had a unique opportunity to use all their weapons and tactics with no restrictions and extreme gusto” (Cypher 2004, p. 12).

³⁷ Army General and dictator of Chile between 1973 and 1989. He was forced to give up power during a plebiscite in 1989 to the Concertación government

³⁸ The War of the Pacific was fought in western South America, between Chile and a united Bolivia and Peru, from 1879 through 1883. It arose because of a dispute over the mineral-rich Peruvian provinces of Tarapaca, Tacna, and Arica, and the Bolivian province of Antofagasta.

Yet, even though the institutions of the armed forces and the police had officially agreed to carry out the coup, there were many members from within that supported the legitimacy of the Allende government. The director general of the Carabineros (police force), Jose Maria Sepulveda adhered to his belief in the legitimacy of Allende's government and on the day of the coup, he retreated to the presidential palace to accompany Allende. Others simply did not participate in the coup by being absent from work or refusing to fire at the palace. These defectors, if captured, would later be victims of repressive measures under the Pinochet regime.

“On September 11, 1973 at 700 a.m., the Navy captured the city of Valparaíso, stationing ships and marine infantry in the central coast and closing radio and television networks. The Air Force bombed the rest of the network stations by 800 a.m. Allende went into the presidential palace with his bodyguards believing that only a small section of the navy had revolted” (Ibid, p. 21). Those commanders of the armed forces that were unaware of the impending coup and loyal to Allende had been identified and their cars and telephones had been sabotaged so that they could not communicate and warn Allende of the impending danger. The leadership of the armed forces was as followed: the leader of the Navy was Jose Toribio Merino, Augusto Pinochet was the General of the Army, Gustavo Leigh was the General of the Air Force, and finally, Cesar Mendoza Duran was the head of the Carabineros (civilian police). These Generals did not respond to any of the phone calls that Allende placed during the day. “At 830 a.m. the armed forces declared control over Chile and declared that Allende was deposed. Allende remained hopeful that some factions of the armed forces were still loyal to him and decided to stay in the presidential palace. By 900 a.m., the armed forces wrested control of all the regions in Chile except the capital city of Santiago” (Ibid, p. 27). At this point, Allende gave his farewell speech,

stating that he would not resign. Soon after, Pinochet ordered the infantry to advance into the presidential place with the support of the Air Force.

A violent confrontation ensued between Allende's bodyguards and those who had remained loyal to him and the armed forces.

At 230 p.m., the Armed Forces were finally able to take control of the Presidential Palace and Allende was dead. Minutes before, Allende dismissed the last of his supporters and spoke the following words before committing suicide: These are my last words and I have the certainty that my sacrifice will not be in vain. I have the certainty that at least, it will be a moral lesson that will castigate felony, cowardice, and treason (Ibid, p. 29).

The months after the coup under the Pinochet regime would prove to be the most politically repressive in the history of Chile. Thousands of political opponents and suspected defectors would disappear, many would be tortured and all would live in a state of paranoia for the years to come. Political stability and unity would come at a price, mainly at the price of freedom of association and speech. The economy would experience a revolutionary transformation and would have cycles of negative growth, unemployment, and inflation similar or worst to those of the Allende administration followed by temporary cycles of positive growth that would barely match or fall behind to those of the first years of the Allende administration. Nevertheless, the Pinochet regime would be successful in exploiting the memories of the last year of the Allende administration to its favor, reminding the Chilean citizens of the long lines, the food shortages, the uncertainty, the unending inflation, and the political division; a memory that would justify the systematic repression of thousands of Chileans over the next decade.

IX. The Pinochet Regime

A. Political and Economic Goals for the New Era

The residents of Chile that had supported the September coup had high expectations for their future government. The military junta assumed power with limited political aims; these aims were to eradicate the climate of political instability and disunity left by the Allende administration in order to transition Chile to a democratically elected government. The presidency of the junta was also to be rotated every six months until the country was stable enough to hold popular elections. However Pinochet's aims differed from those of Gustavo Leigh, Jose Toribio Merino, and Cesar Mendoza Duran.

Pinochet sought to revolutionize the political and economic spheres of Chile and create a system of order and discipline with absolute popular loyalty to the military government.

On the day of the coup under the direction of Pinochet, the military junta proceeded to dissolve Congress and declare a state of emergency in which political and individual freedoms were to be suspended (Angel and Pollack, 1993, p. 39).

At the core of his political and economic aims was the necessity to extirpate all opposition in the form of both political parties and popular dissidents.

Once the opposition had been eradicated, Pinochet had the ability to institute a series of revolutionary reforms that did not need the approval of any of the other governmental branches without running the risk of strikes, revolts, and general anarchy. Pinochet was also highly adept in co-opting the different branches of the armed forces in order to prevent a coup from occurring. He achieved this objective by raising salaries, prolonging pension benefits, and appointing generals of the armed forces to key governmental posts. "With the fear of political repression and threat of assassination, the judiciary branch merely acted as a rubber stamper and refused to take cases that dealt with the abuse of authority on the part of the military junta and its agencies by

stating that the judiciary was not responsible for resolving political cases” (Ibid, p. 69). Pinochet was also dexterous in the art of psychological manipulation. Chile remained under a state of emergency with suspended liberties for almost a year, sufficient time to eradicate almost all of the opposition without facing popular unrest. “As soon as he assumed power on September 11, Pinochet declared Chile to be in a state of civil war, a war against those who had shattered Chile’s economy and had fragmented its political unity” (Cypher 2004, p. 3). For a while, he convinced the Chilean citizens that previous laws had to be broken and an iron fist had to be employed in order to prevent Chile from returning to the times of food shortages, unregulated inflation, and financial instability.

In the economic realm, Pinochet sought to extirpate all signs of communism and socialism from the Chilean economic institutions and policies. Thus, he instituted a neoliberal system, a system that did not hold the government to be responsible for the provision of social welfare and the creation of economic equity and that in theory promised economic growth and efficiency. Neoliberalism had gained prominence in the industrialized countries of the United States and Great Britain, and its implementation would enable Pinochet to secure the diplomatic support of the industrialized Western nations and international institutions such as the IMF and the World Bank. Neoliberalism would also enable Pinochet to secure the necessary loans to commence the economic reforms necessary to move away from Allende’s socialist state. Neoliberalism did not promise more than economic growth and economic efficiency and it disregarded the effects that growth would have on redistribution, wages, unemployment, and social equity. The reforms executed to implement the model came to be known as the shock therapy of structural adjustment reforms.³⁹ In order to institute these policies that would

³⁹ Reforms implemented in 1975 in Chile that induced a severe depression. It involved a sudden and dramatic change in national economic policy that turned a state-controlled economy into a free-market one. Characteristics of

transform the entire economic system that had prevailed since the Great Depression, Pinochet found it necessary to extirpate all possible opposition through a series of brutal repressive policies and institutions.

B. Iron Fist and State Terrorism: Political Repression during the Pinochet Regime

Once the military junta had established a tight grip over the presidential palace, had dissolved the National Congress, declared a state of emergency, and a state of civil war; it had all the tools in its power to conduct the systematic repression of thousands of Chilean citizens that were suspected of being disloyal and critical of the military junta. “During the first three weeks after the coup, Pinochet proceeded to neutralize the opposition in the radicalized state technical university, in the industrial sectors where workers had been dependent on the socialist policies of Allende (wage hikes and frozen prices), and in the shanty-towns of the capital inhabited by the majority of the urban working class” (Steetland 1997). The declared state of civil war allowed the junta to draft a military edict that ordered troops to kill in action any civilian that was part of the opposition. “A curfew was established in order to prevent civilians from organizing after the daylight hours and also to conduct abductions during the night without being noticed. The curfew was set to commence at 6pm and was heavily enforced, various underage civilians were killed for violating curfew hours” (Angel and Pollack, 1993, p. 78).

The systematic abuse of power and violence caused a mass wave of emigration to Latin American and European embassies by refugees who sought political asylum in fear that they would be branded as part of the opposition and assassinated. “In 1973, 4,000 people were

shock therapy include the ending of price controls, the privatization of publicly owned entities and trade liberalization. Shock therapy is intended to cure economic maladies such as hyperinflation, shortages and other effects of market controls in order to jump-start economic production, reduce unemployment and improve living standards.

granted safe conduct documents by the military government but after 1973, they became hard-lined and no documents were granted as security around the embassies increased” (Ensalaco 1999, p. 40). The National Stadium is symbolic of the Pinochet era, because it served as an internment and torture camp where “as many as 50,000 prisoners were taken during the first couple of weeks after the September coup” (Ibid, p. 43). The regime was supported by the US government who in its effort to eradicate all traces of socialism (which was equated with communism), provided monetary and diplomatic support in order to prevent Chile from associating itself with the Soviet Union during the Cold War.

Pinochet’s main objective was to institute a reign of terror that allowed him to become firmly established in power and revolutionize the economic and political spheres of the country towards a government with a high centralization of power and an economy that promoted economic growth and no responsibility towards socialist goals. However, it was not long before the embassies became worried about the political instability and repression during the first months after the coup and it did not take long for families to summon and inform humanitarian organizations of the volatile state of the country.

Organizations such as the International Red Cross and Amnesty International tried to gain access into the country and into areas such as the National Stadium and urban shantytowns in order to assess the state of political chaos. The government delayed their entrance in December 1973 by establishing the National Executive Secretariat for Prisoners (SENDET) which was put in charge of answering inquiries related to political prisoners by both desperate families and humanitarian organizations (Ibid, p. 78). However, SENDET was an agency without authority that relied on the orders of the military junta.

The methodical torture was not only limited to nationals, it was extended to all those foreigners that had travelled to Chile to promote the Marxist doctrine. These were among the first taken to interrogation camps where they were often tortured and disappeared. “The interior ministry was reporting that up to 13,000 foreigners were in Chile. Chile’s UN ambassador was claiming that as many as 3000 of them were in Chile as armed mercenaries prepared to stage an uprising, a number were killed and thousands were jailed” (Ibid, p. 86)

The junta also sought to extirpate all the policies related to land reform and it cooperated with landowners in the assassination of hundreds of peasants who had benefited from the land reform programs of the Frei and Allende administrations.

In the city of Concepcion, over 200 people were killed and 589 were imprisoned and they did not even engage in active opposition against the Army or Navy. They were targeted because the University of Concepcion had been the birthplace of the MIR. The Fugitive Law of 1973 was one of the hallmark policies that enabled the junta to mask the assassinations of innocent people under a frame of legality. The law stated that the troops had the right to kill any suspected member of the opposition that attempted to escape the authorities (Ibid, p. 110).

This law was used by several generals and officers to stage prisoner escapes and claim that the prisoners had tried to escape. One such general was General Sergio Arellana Stark, a general who travelled around the country with a military delegation identifying and murdering socialist supporters by staging escape plans. The members of this delegation would later become key officials of the Directorate of National Intelligence (DINA) (see below).

According to the Rettig report, a report drafted by a governmentally organized committee that sought to evaluate the extent of the human rights abuses incurred during the Pinochet Era and published in 1991:

More than 1,260 Chileans were killed from September 11 until the end of 1973. Tens of thousands were arrested and detained without charge. Agents of the Pinochet regime would murder 600 Chileans over the next three years. What had been indiscriminate repression during the first months became state terrorism conducted in a permanent state of siege that ended only in 1977. Repression became more discriminating and methodical, torture techniques were improved, fewer bodies were being delivered to the Medical-Legal institute, more were being disappeared to conceal crimes and inflict psychological terror (Ibid, p. 115).

On top of all these repressive policies, Pinochet made sure that the junta gained more power over Chile's future and governmental institutions. "In 1973, he drafted and instituted decree law number 1 that stated that the junta had supreme rule over the land and decree law number 5 that stated that the junta would exercise all executive, legislative, and constitutive powers" (Angel and Pollack, 1993, p. 117). Pinochet also proceeded to ban all political parties including those that were not leftist such as the Christian Democrats, and soldiers were appointed to key positions such as mayors and governors. Pinochet solidified his power when he changed the constitution in 1980. "The new constitution was drafted and subject to a national plebiscite that was successful in gathering 67% of the popular vote, however the vote was not democratic because army officers and troops were stationed at the ballot posts ready to abduct those who

voted against it, and the citizens who counted the votes were hand-picked by the government” (Cypher 2004, p. 9).

The constitution gave Pinochet the right to declare a state of siege when there was an internal disturbance provoked by rebellious forces already organized or being organized whether openly or underground. He also conferred on himself the authority to promulgate laws by stating that decrees had the same power of constitutional amendments. Pinochet also eliminated the constitutional tribunal that had existed to resolve controversies between the legislative and the judicial branch. The constitution also allowed Pinochet to appoint the senators in Congress and established strong barriers against amendments. However the constitution also provided a concession point and that was that his eight-year term would be followed by a plebiscite on the continuance of his rule through 1997, a provision that provided the means by which the opposition would eventually remove Pinochet. The junta chose not to dissolve the judicial court because it needed to appear to be legitimate in the eyes of the international community and because the court was acting as a rubber stamp institution under the president of the Supreme Court, Enrique Urrutia Manzano, who refused to take political cases and was happy that Allende had been removed from power, since he had feared that Allende was resolute in dissolving the judicial court. Urrutia in fact stated that military commissions in times of war were by their nature not within the supervision that was entrusted to the court. The International Court of Justice responded by stating that although Chile was in a state of war, the actions of the military junta were in violation of the 1949 Geneva Conventions.

In November 1973, the junta created what would be the most politically repressive institution of the government: the Directorate of National Intelligence (DINA). “Under the leadership of General Manuel Contreras, the DINA became an independent agency in 1974 and

was given the power to conduct searches and arrests but its main goal was to assassinate the members of the opposition. The DINA established various offices and sites around the country that would become infamous for torture” (Ensalaco 1999, p. 57). The DINA was also responsible for spying on army activities in an effort to discover whether army generals were planning a coup or any sort of opposition to the military junta. The main targets for the DINA were the members of the MIR and, in an effort to accelerate the pace of their eradication, Pinochet instituted a law modeled after the Nazi Night Law⁴⁰ in 1974. This law gave the army troops the right to abduct people at night without any warrants and assassinate them rather than bring them to trial. The second biggest targets were the Communist supporters who were also victims of abduction and torture. Even forensic pathologists covered up the crimes and the nurses did not report prisoners that were brought to the hospital for fear of retaliation.

Under international pressure by humanitarian organizations, the DINA was dissolved in 1977, but since the agency was independent of the government the international courts could not link the agency’s actions to the military junta. In 1977, when the junta was dissolved, all effective opposition had been eradicated and Pinochet was no longer in need of this intelligence arm. The DINA was replaced by the National Center for Information (CNI), essentially an agency that continued to conduct spying activities.

Pinochet not only secured power over the political sphere of Chile but also over the junta itself. “In July 1978, Pinochet ousted Air Force commander Gustavo Leigh from the junta and the armed forces because Leigh was the most powerful potential political rival he had and Leigh believed that the junta should prepare to hand over power to a democratically elected government” (Angel and Pollack, 1993, p. 77). The only way that the junta could oust a member

⁴⁰ A law that was imposed on every occupied country by the Nazis during WWII, starting with France in 1944 that allowed German soldiers to abduct any suspected members of the opposition of any country.

was to have a unanimous vote under medical pretexts. Thus, the junta members declared Leigh to be mentally unfit to perform his duties and had him placed under house-arrest and later under the supervision of the government for the duration of the Pinochet regime.

The years of political repression under the Pinochet regime gave rise to a variety of grassroots and humanitarian organizations that sought to both denounce the violation of human rights and protect the people from further human rights abuses. One of the organizations established was the Committee for Cooperation for Peace In Chile in 1973 that helped foreign nationals and captured Chileans, and was run by priests until it was dissolved by the government and replaced in 1975 by the Vicariate of Solidarity that provided legal assistance, filed habeas corpus for victims, and documented human abuses. This would become useful later especially during the drafting of the Rettig report in 1991. The Foundation for Social Assistance of the Christian Churches secured safe conduct documents for those seeking asylum and provided psychological treatment for traumatized victims. The Association of Families of the Detained continues to this day demanding to know what happened to their loved ones.

Other organizations established were: The Association of the Families of the Executed for Political Reasons, the Chilean Human Rights Commission established in 1978, the Commission for the Rights of the People established in 1980, The National Commission Against Torture established in 1982 that revealed that physicians had been involved in torture and sought to denounce this as well as the several torture practices employed, and the Sebastian Acevedo Movement against Torture. By 1985 some 15 human rights groups were active in Chile. Partnerships between NGO's and International Organizations also developed as NGOs supplemented the necessary information to denounce human rights abuses.

In 1983, the Latin American region was suffering from a general debt crisis and Chile was especially hard hit (the reasons for this will be explained later). During this time, the opposition groups started to gain strength and momentum and organized themselves into groups that conducted strikes and terrorist activities.

On May 11, 1983, the Copper Workers Union called for a general strike to protest the harsh effects of the economic downturn and the regime's economic policies in general. From that day until 1986, the government experienced a total of 14 days of strikes, all of which were brutally put down. On November 1984, Pinochet used sweeping emergency powers from the 1980 constitution to call a state of siege and raid shantytowns, put down activists, intimidate labor unions, and violently quell protests (Ensalaco 1999, p. 23).

In 1984, government sponsored vigilante groups began to appear. Priests were harassed and abducted in shantytowns and human rights activists were raped and murdered. The CNI was heavily involved in the wave of repression and intimidation and the corps of Carabineros also took part in the harassment. The MIR had also started to conduct guerilla warfare and staged a series of robberies, bombings, and assassinations aimed at army offices and Carabineros. "The wave of these terrorist incidents increased from 15 in 1977 to 222 in 1981" (Ibid, p. 26).

At the same time, Pinochet secured international monetary and diplomatic cooperation in order to launch his program of economic reforms.

The Nixon administration's aid package provided Pinochet's regime with up to \$52 million in commodity credits. In 1974, Chile had agreed to pay North American corporations for losses incurred during the Allende presidency. The US and Chile reached a bilateral agreement with respect to debt payments. Efforts by congressional

democrats to block or reduce aid levels to Chile to punish the junta for its human rights practices were met with opposition by the executive branch and the Congress (Ibid, p. 33).

Reagan was also a strong supporter of Pinochet, as he believed the military regime had prevented Chile from becoming communist. Yet, not even all of the aid from international institutions and foreign governments prevented the Pinochet regime from instituting a series of economic reforms that became detrimental to economic growth, unemployment, health, education, and the distribution of wealth. The economic system that Pinochet chose to revolutionize Chile provided Chile with periods of economic growth and recessions that either did not match or barely matched the economic growth during the Allende years. The implementation of the system itself changed over time as key economic advisers and Pinochet himself came to view the necessity of combining social welfare and industrial policies with neoliberal plans.

C. 1973-1981: Neoliberalism and Its Reign over the Chilean economy

Neoliberalism could not have gained prominence without the hand of political authoritarianism. Thus, even though neoliberalism in theory promised individual freedoms in the market, it could not have survived without the iron fist of Pinochet's regime. The implementation of neoliberalism entailed a complete overhaul of a system of social welfare and industrial policies that had predominated since the Great Depression. This economic change also entailed a great deal of suffering for the Chilean citizens as they saw a rise in unemployment, a drop in wages, an increase in internal debt and fierce international competition that crippled domestic

entrepreneurs. Thus, between the years of 1973-1981, Pinochet's dictatorship became dependent on the economic system of neoliberalism.

Pinochet was in need of an economic system that distanced itself from socialist policies and enabled him to gain the good will of international institutions such as the IMF and the World Bank as well as the United States. Those economic advisors and economic scholars that took advantage of the Chilean conditions to conduct their economic experiments were in need of a political system that gave no room to democracy, where economic decisions would be able to be implemented overnight without the fear of anarchy or political instability. International lenders and capitalist countries such as the United States and Great Britain were content with the idea of a Chile that would institute the economic reforms necessary to move away from socialism in a Cold War era. Hence, between 1973 and 1981, Pinochet was able to take advantage of these conditions to overturn many of the socialist policies instituted during the Allende and Frei presidencies. Yet even during this period, when neoliberal policies reigned over Chilean economic policy, certain industrial and socialist policies remained in place. An analysis of the neoliberal turn and the policies kept in place that were contradictory to the neoliberal system is what follows.

When Pinochet first came to power, the doors opened for a variety of economic scholars and policy makers that had been ostracized during the time of Allende's peaceful road to socialism. Table 3 illustrates the names and positions of the renowned Chicago Boys, economists that had been mostly trained at the University of Chicago and took positions of power in order to implement the neoliberal model during the Pinochet regime.

Table 3. Names and Positions of the Chicago Boys (1975-1990)

	Name	Position
1975-1977	Jorge Cauas	Minister of Finance
1977-1982	Sergio de Castro	Minister of Finance
1976-1979	Pablo Barahona	Minister of Economy
1978-1980	Jose Piñera	Minister of Labor and Pensions
1985-1989	Hernán Büchi	Minister of Finance
1982-1983	Alvaro Barón	Minister of Economy
1975-1981	Juan Carlos Méndez	Budget Director
1975-1981	Emilio Juanfuentes	Economic Advisor to Central Bank
1982-1983	Sergio de la Cuadra	Minister of Finance
1978-1980	Miguel Kast	Minister of Planning
1987-1989	Martín Costabal	Budget Director
1980-1990	Juan Ariztia Matté	Private Pension System Superintendent
1988-1990	Maria Teresa Infante	Minister of Labor

Source: Klein, Naomi (2007)

Among these were “the renowned Chicago Boys⁴¹, a group of thirty Chileans that had been mostly trained at the University of Chicago between 1955 and 1963 under the guidance of economist Milton Friedman and took positions of economic planning and leadership under the Pinochet regime such as finance, health, and city planning ministers” (Bortzutzky 2000, p. 93). Milton Friedman was a leader of the Chicago School of Economics and a soon to be Nobel Prize winner in 1976. He opposed Keynesian theory and was a proponent of full-fledged neoliberalism and everything it entailed such as free markets and limited government intervention. During the

⁴¹ A group of young Chilean economists, most of who were trained at the University of Chicago under the guidance of Milton Friedman that directed the Chilean economy between 1975 and 1981 under posts such as the Minister of Finance and Minister of city planning.

first months of the dictatorship, Pinochet had no concrete economic plan, but he became acquainted with the neoliberal model.

Pinochet invited Milton Friedman and the Chicago Boys as key economic advisers to his regime in late 1974, an alliance that would remain untouched until 1981. According to Sergio de Castro, one of the Chicago Boys and Pinochet's economic and finance minister, "a fascist-like system was required to introduce economic liberty because it provided a lasting regime; it gave the authorities a degree of efficiency that was not possible to obtain in a democratic regime; and it made possible the application of a model developed by experts and that did not depend upon the social reactions produced by its implementation" (Ibid, p. 106). Thus, "The Chicago Boys mission was to legitimize the coexistence of economic liberalism with political authoritarianism. The dictatorship gave the neoliberal technocracy an unlimited scope of action, to restructure the foundations and workings of the Chilean economy, and the state-ization of politics" (Angel and Pollack, 1993, p. 72).

The argument used for the necessity of neoliberalism was that a neoliberal system would enable Chile to achieve a greater degree of economic efficiency and that the former development model was inefficient and incapable of solving the country's economic problems. The dictatorship guaranteed that the economic policies would benefit the nation as a whole without any discrimination; these policies would look after the general interest even though the neoliberal theory itself did not promise anything more than economic growth. Hence, it is with this argument that they justified the extreme concentration of political power, the existence of socio-political repression and the inherent contradiction that a system that promoted economic liberty needed the hand of political authoritarianism for its survival. However, this does not mean

that the relationship between the entirety of the armed forces and the neoliberal economic advisors was free of tensions.

When the Chilean Armed Forces came to power:

They came to power with an outlook that was not only anti-Marxist and anti-labor but also anti-politics. They viewed themselves as professionals who wouldn't dirty their hands in the sordid business of politics. The Chicago Boys shared this anti-political outlook, and would give it ideological coherence. Presenting themselves as experts in economic science, they appealed to the Armed Forces' own ideal of apolitical professionalism. What was wrong with Chile, they argued, was, in a word, politics. And so the economists and the soldiers joined hands in an alliance of technocrats (Ruess 1999, p. 10).

However, the relationship between the military officials and the Chicago Boys regarding economic policy was not free of tension. The military ministers believed that a degree of industrial and social welfare policies had to remain in place whereas the Chicago Boys wanted a complete overhaul of the previous economic system. "Tensions also grew between the DINA and the Chicago Boys since General Manuel Contreras, the head of the DINA, had economic ideas that were more in common with industrial policy than with free markets" (Ibid, p. 12). However, once the DINA was abolished in 1977 due to international human rights pressure, the path for the Chicago Boys was clear of opposition and they gained complete prominence in the economic realm.

In March 1975, the Chicago boys had held an economic seminar that received national media attention. Here they had proposed a radical austerity program called "shock treatment" to solve Chile's economic woes. They invited some of the world's top economists to speak at the

conference, among them Chicago professors Milton Friedman and Arnold Harberger⁴².

Unsurprisingly, they gave the proposal their highest praise. “The plan called for a drastic reduction in the money supply and government spending, the privatization of government services, massive deregulation of the market, and the liberalization of international trade” (Ibid, p. 17).

Once the DINA along with Contreras had been removed and the military ministers had increasingly lost power in the face of Pinochet, the Chicago Boys administered their shock treatment in 1975. “They devalued the currency, reduced public expenditure and greatly increased effective interest rates, triggering a major recession. They also increased privatizations and slashed tariffs. The resulting economic contraction and trade liberalization destroyed Chile's industrial sector, the lifeblood of the working class, further undermining the dictatorship's opponents.” (Ibid, p. 17). The post-1973 widespread privatizations increased the power of a select group of businessmen who acquired ownership shares at bargain prices due to the regime's impatience in de-nationalizing the vast majority of the Chilean industries that had been nationalized under the Frei and Allende administrations. Table 4 illustrates the decrease in tariffs and the consequent increase in openness experienced during the neoliberal turn from 1973-1989.

Table 4. Average Tariff and Openness for Chile, 1973-1989

	Average Tariff	Openness
1973	94.0	29.6
1974-1979	35.3	45.6
1980-1982	10.1	44.3

⁴² A US economist graduated from the University of Chicago and John Hopkins University known for the proposition of the “Harberger's Triangle” (deadweight loss), widely used in welfare economics

1983-1985	22.7	47.9
1986-1989	17.6	57.5

Source: French-Davis, 2005

Notes: Average Tariff Given in Percentage, Openness calculated as (Exports+Imports)/GDP

In short, the Chicago Boys' plan included privatizing welfare and social programs, deregulating the market, liberalizing trade, rolling back trade unions, and they did this in the absence of democracy. This was not solely the Chicago Boys' plan; it was also formulated by the International Monetary Fund and the World Bank, who made the program a precondition for future loans to Chile. "The debt, devastation, inequality and exploitation that the IMF and World Bank brings to Third World countries in the name of neoliberal development is another story in itself. Chile remains the worst example" (Leiva and Petras, 1994, p. 51). In fact, as previously mentioned, the shock treatment induced a severe depression that would prevent the Chilean economy from recovering until 1978 with a surge in growth that only equaled that of Allende's presidency in 1971.

During the period from 1978-1981 that the Chicago Boys called the economic miracle, the economy grew by 6.6 percent a year. The Chicago boys lifted nearly all restrictions on foreign direct investment, creating an almost irresistible package of guarantees for the foreign investor with extraordinarily permissive treatment. Foreign investment and loans came pouring into Chile, with loans alone tripling between 1977 and 1981. Of the 507 state enterprises set up before or during Allende's presidency, the Chicago boys would eliminate or privatize all but 27. However, when you take both the recession and the recovery into account, Chile actually had the second worst rate of growth in Latin America between 1975 and 1980. Only Argentina did worse. Also, between 1977 and 1981, 80 percent of Chile's growth was in the unproductive sectors of the economy, like

marketing and financial services. Much of this was speculation attracted to Chile's phenomenally high interest rates, which, at 51 percent in 1977, were the highest in the world. (Ibid, p. 59).

In GDP terms, the initial effects of introducing free market policies in 1975 was a shock-induced depression which resulted in:

National output falling by 15 percent, wages sliding to one-third below their 1970 level and unemployment rising to 20 percent. This meant that, in per capita terms, Chile's GDP only increased by 1.5% per year between 1974-80. This was considerably less than the 2.3% achieved in the 1960's. The average growth in GDP was 1.5% per year between 1974 and 1982, which was lower than the average Latin American growth rate of 4.3% and lower than the 4.5% of Chile in the 1960's. Between 1970 and 1980, per capita GDP grew by only 8%, while for Latin America as a whole, it increased by 40%. Between the years 1980 and 1982 during which all of Latin America was adversely affected by depression conditions, per capita GDP fell by 12.9 percent, compared to a fall of 4.3 percent for Latin America as a whole (Rayack 1986, p. 64).

However, by far the hardest hit group was the working class, particularly the urban working class. "By 1976, the third year of Junta rule, real wages had fallen to 35% below their 1970 level. It was only by 1981 that they had risen to 97.3% of the 1970 level, only to fall again to 86.7% by 1983. Unemployment, excluding those on state make-work programs, was 14.8% in 1976, falling to 11.8% by 1980" (Ibid, p. 78). The main objective of the Chicago Boys regarding the labor sector was the total overhaul of the existing labor laws by eliminating collective bargaining, allowing for the massive dismissal of workers, increasing the length of the labor day

to 12 hours, and eliminating the labor courts. The irony is that as workers got laid off and wages were reduced in order to decrease the costs industries were incurring, demand contracted because workers were no longer able to purchase the same amount of goods. This contraction hurt the business community that started producing more goods for exporting and less for consumption. This led to an increased concentration of income and wealth in the hands of the business elites.

Table 5 illustrates the declining labor conditions suffered by workers during the Pinochet regime; collective bargaining levels were zero, when the Chicago Boys were in power as labor unions were stripped down. The table also illustrates the minimum wage hikes during the Allende presidency and the consequent slashed wages during the Pinochet regime. Overall, workers were better off in 1970 than in 1990. The trend since the Pinochet regime has been to finance the export base through declining wages.

Table 5. Labor Market Indicators for Chile, 1970-1990 (All numbers represent %)

	Collective Bargaining	Real Average Wage Growth (per year)	Real Minimum Wage Growth (per year)	Unemployment Rate
1970-1973	26.1	-5.1	35.3	4.7
1974-1979	0.0	0.9	-9.2	13.7
1980-1990	13.4	1.3	-0.7	14.7

Source: Cortázar, 1997

Notes: Collective Bargaining represents percentage of wage earners covered by collective agreements

The neoliberal economic planners also had the objective of diversifying exports away from the nationalized copper industry and the natural resource industry but as will be explained later, their dependence on copper and natural resources increased because these industries were the only ones that could finance the massive economic reforms that were employed between 1975 and 1980.

During the late 1960`s and 1970`s, Chilean trade was characterized by extreme dependence on copper, as it constituted between 70 and 80% of total exports. The introduction of trade liberalization policies and other export promoting reforms in the mid 1970`s began a significant process of export diversification. By 1980, dependence had been diminished but still accounted to 45% of the exports and maintained itself like that throughout the 80`s. Also, between 1980-89, Chile`s percentage of non-communist world mine production increased from 17.7 to 22.7 percent. (Angel and Pollack, 1993, p. 122).

Monetary policy was geared towards cutting spending and devaluating the Chilean peso, making exports more attractive in the international arena at the cost of higher prices for imports in the face of a shrinking internal consumer market and declining wages. Thus, the regime was successful in reducing costs and “by 1982, the average costs of production had fallen to 42 cents a pound.” (Ibid, p. 146). Although the copper industry became nationalized, Pinochet was interested in attracting foreign direct investment in order to expand the national production of copper. Pinochet passed the investment law of 1977 that gave substantial credit and interest rate offers to international investors. However, at the time there was an international perceived instability of the Pinochet regime (due to the human rights abuses) and Pinochet failed to attract sufficient investment into this area.

The increase in poverty and unequal income distribution also developed into one of the main problems that the dictatorship had to deal with, problems that until today plague Chile`s economy. “Figures for those covered by government subsidies for the extreme poor in 1975, estimated that the population of extreme poverty as opposed to poverty, defined as without income to meet its basic subsistence needs, less than 20,000 pesos for month, was 31% of the

population” (Ibid, p. 138). In order to determine which families or individuals were suffering from poverty, the regime established a measuring system known as FICHA (the measurement for social stratification). This measurement was widely criticized because it did not rely on income levels to determine poverty but rather on things such as ownership of house appliances. The regime also provided subsidies rather than investment in human capital, a system that created dependency and did not encourage the acquisition of skills. Thus:

The Pinochet government leaves a mixed legacy in the field of poverty alleviation. On the one hand, the government effectively provided for the basic needs of the poorest during severe economic crisis, no small achievement when one considers the record of other countries in the region. On the other hand, its narrow vision of social welfare policy in conjunction with its disdain for participatory institutions resulted in a safety net that reached the poorest for the first time yet at the same time stigmatized them. Those who participated in government programs became an underclass of sorts, dependent on government subsidies without making progress in improving their capacity to meet their own basic needs (Lazzara 2009, p. 8).

The neoliberal planners were also concerned with the movement away from the agricultural dependence to an economy that would be centered more on the production of manufactured goods. “In a normal pattern of structural transformation, manufacturing’s contribution to GDP should rise from 15-36% as the economy moves to a higher level of GNP per capita, this didn’t happen in Chile where the share of agriculture rose and the industry and manufacturing shares fell substantially. Chile’s share of food and agricultural market value added increased from 17% of GDP in 1970 to 27% in 1986” (Leiva and Petras, 1994, p. 101).

The planners also failed to technologically innovate in certain industries, set up sufficient infrastructure and encourage dependence through foreign direct investment, while failing to provide incentives for local industries and entrepreneurs to diversify as had been done under Frei's and Allende's administration through credit allocations and tariffs under the a framework of industrial policies. Instead, the fierce international competition from abroad led to the destruction of a variety of local industries and the discouragement of domestic entrepreneurs to invest in the internal economy.

The neoliberal model was also instituted in the health and pension sectors. In these two areas, structural problems were created and continue to exist, because the regime created a two-fold system of public and private provision that was and continues to be characterized by an inefficient and underfunded public sector and an overpriced private sector. Thus, the reforms instituted during the Pinochet era created a profound polarization in the provision and quality of services according to individual incomes. In comparison to the social spending during the Frei and Allende administration:

Existing programs were either abolished, heavily cut back or simply left to erode in circumstances of spiraling inflation. This retrenchment of social policy was part of the shock therapy program through which the regime rapidly curbed state expenditure, cutting it by one-quarter by 1981. In terms of social spending, by 1979 it had recovered slightly but still stood at 83 percent in real terms of the 1970 level. This was manifested in marked decreases in the value of average pensions, hospital beds per person and per capita health and education spending (Huber 1996, p. 40).

The regime encouraged the creation of private service provision of key social services on a for-profit basis in order to introduce the market's price mechanism into these sectors. This included a compulsory privatization of social security and the creation of dual systems of health and education in which private enterprises would compete with each other and the state to provide services to paying customers. "The retreat of the state from service provision was juxtaposed with a correlate movement away from a commitment to providing basic services as social rights to an emphasis on the freedom of choice of the user" (Taylor 1998, p. 14). The citizens of Chile were then free to choose between the most individual affordable options. Yet, the private system discriminated against those with previous conditions and against certain job groups that were associated with risk-related injuries. The private system was not affordable for any but the upper echelons of society and the public system fell to disrepair as medical provisions became scarce and the best doctors decided to transfer to the private health system. The changes implemented in the pension sector were similar:

The reform entailed a rapid privatization of the pension system with workers obligated to place a requisite thirteen percent of their monthly salaries in an individual account with a private pension fund of their choice. The latter, known as the *Asociación de Fondos de Pension* (AFP), proceeded to collect a two percent administration charge and then invest the remainder in a regulated fashion, with investments predominantly directed towards domestic bonds and equities. Future pensions are therein tied to the performance of the investments made by the AFP (Ibid, p. 20).

This reform changed the relationship between employer and employee and replaced it with a relationship between the individual and the private pension company. This reform was

implemented in order to free firms from the burden of social security provision and, simultaneously, increase the flexibility of the labor market. The reform aimed to enable firms to hire and fire workers without considerations of pension stipends and, therein, remove one of the distorting factors acting upon the price of labor. However, it did not free the state from considerable expenditures, as “the continued commitment to maintaining the remnants of the old system plus ensuring the state minimum pensions means that pension provision remains the major component of state social spending. In 1998 it amounted to 40.8% of public social expenditure, a figure that corresponds to 6.11% of GDP” (Ibid, p. 33).

It is important to note that even though neoliberal reforms predominated in the economic realm between 1973 and 1981, the regime still found it necessary to maintain certain industrial policies in order to conduct the economic reforms that the Chicago Boys desired to implement.

Chile's economic performance has been mixed, and its successes owe more to state intervention than to the invisible hand of the free market. In fact, it would be hard to find any major sector of the economy that did not owe much of its existence to state intervention, an intervention that continued in a variety of forms under the nominally neoliberal Pinochet dictatorship. Most of the credit belongs to the state: most of the strategies such as new product development, risk capital, technical training/advising, marketing, quality control, and many of the personnel involved in the new Chilean miracle were products of the old, and much derided, state interventionism of the ISI era (Cypher 2004, p. 18).

Many of the industrial policies were kept because military officers in the upper ranks of the dictatorship were “developmentalists” and believed that the state had an important role in

helping certain industries become efficient and successful in the international arena. Chilean state production in 1974 had become characterized by high costs, declining production and exports. The military government had distinct problems in formulating policy towards the copper sector. On one hand, the economic teams within the military government were intent on privatizing all nationalized companies. On the other hand copper continued to constitute Chile's main strategic sector and important sections within the armed forces were vehemently opposed to denationalization. "The Pinochet government reacted in three ways: it decided to maintain copper as a nationalized sector due to strategic significance, international relations were normalized by an agreement on terms of compensation with US companies, and a radical policy of rationalization was implemented which included cost cutting and profit maximization" (Huber 1996). Given that CODELCO was controlled by the state, it came to make a substantial contribution to the fiscal budget. "Between 1975 and 1980, CODELCO's payments to government increased fourfold, from \$244.9 million to \$1,006.6 million in 1980" (Angel and Pollack, 1993, p. 61).

CODELCO was heavily exploited during the 1970's, the strategy went as follows: if CODELCO's production exceeded the forecast, the extra revenues would go to the state treasury and if it failed to meet the forecast, CODELCO had to borrow externally to meet the quota. The Pinochet regime found it politically and economically difficult to privatize CODELCO. However, the regime did not allow CODELCO to expand, it was restricted to production in its existing lands: *Chuquicamata, El Teniente, Andina and El Salvador*. "However the industry still accounted for 45% of the exports throughout the 1980's and the effort of the government to minimize its importance over time failed" (Ibid, p. 73). On top of their direct involvement,

CORFO introduced forest management techniques, provided credits and subsidies, financed projects for technological development and labor training, and fostered the development of the allied paper, cardboard, and wood industries. “CORFO also created an affiliate, the Forestry Institute, which launched a marketing and information campaign designed to promote forestry exports, while carrying on massive reforestation programs and introducing new tree varieties” (Cypher 2004, p. 16).

The same story holds for the fishing industry, as well as for most of the developments in fresh produce and processed food. *Fundación Chile*, a public-private agency designed to develop firms in new areas where private capital would not invest then sell them to the private sector, was responsible for most of this diversification. “*Fundación Chile* began in 1976, with the assistance of a prominent economist, Raúl Saez, who had headed CORFO for many years. Like many of the military officers in the highest ranks of the dictatorship, Saez was contemptuous of the Chicago School neoliberals” (Rayack 1986, p. 27). The dictatorship also created Pro-Chile in 1974 to assist the private sector in locating and selling to foreign markets. Today, many of the activities of Pro-Chile are coordinated with support programs fostered by CORFO. Through its Export Promotion Fund, Pro-Chile has co-financed export projects, “providing up to 50% of the necessary capital, often using funds obtained from or through CORFO. In yet another instance of state intervention, the government facilitated a boom in the private mining sector from the 1980s by allowing the mines to operate essentially tax-free” (Cypher 2004, p. 17).

Even during the years of 1973-1981, when the Chicago Boys were in charge of implementing a neoliberal system and overhauling the industrial and socialist policies that had existed ever since the Great Depression, vital industrial policies remained in place. The economic shock therapy that was implemented in 1975 not only induced a severe depression, it

also caused a negative growth rate to be seen until early 1988 when the economy started recovering and matched that of Allende's growth rate until 1980. It was during that time that Latin America experienced a severe debt crisis that hit Chile the hardest due to its vulnerability to world swings and trade openness, policies that came as a result of the neoliberal turn. It was during this crisis that the Chicago Boys prominence and power in the economic realm was lost and the Pinochet regime recognized that certain industrial policies that had been removed had to be re-instituted in order to prevent Chile from suffering from external shocks such as those experienced during the debt crisis. Thus, from 1981 until the end of the Pinochet dictatorship in 1990, the government enacted a series of reforms that armed Chile with a balanced system of industrial and neoliberal policies, a system that enabled Chile to recover from the second depression in less than a decade and finally enabled Chile to achieve greater economic growth than that experienced during the first year and a half of the Allende administration.

D. 1981-1990: Latin American debt crisis and reformulation of economic policy along industrial and neoliberal lines

The Latin American crisis that would commence in late 1981 and would intensify throughout 1982 was a testament to the flawed neoliberal policies of the late 1970s. In conjunction with a regional external shock, the debt crisis exposed the weaknesses of a system that provided limited social provisions for its citizens and overexposed the economy to external economic swings. The crisis arose from a conglomeration of factors including a worldwide economic recession that commenced in 1973 and increasing oil prices due to the Middle-Eastern

conflict⁴³ between Israel and Palestine. “These factors contributed to a credit crunch⁴⁴ that prevented Latin American countries from gaining access to much needed loans for development projects and increased the interest rates on existing loans. With increasing interest rates, debt payments increased making it harder for borrowing countries to pay back their existing loans” (Ibid, p. 33).

During this time, Latin American countries also started to experience high rates of inflation and their purchasing power decreased and prevented these economies from investing in machinery to build up their manufacturing base. With inflation rates soaring, foreign direct investment decreased as international lenders and investors became skeptical about the profitability, return on investment, and security of their assets. While the dangerous accumulation of foreign debt occurred over a number of years, the debt crisis began when the international capital markets became aware that Latin America would not be able to pay back its loans. “This occurred in August 1982 when Mexico's Finance Minister, Jesus Silva-Herzog declared that Mexico would no longer be able to service its debt” (Pastor 2012, p. 31). This announcement generated a wave of speculation⁴⁵ from international lenders and institutions and contributed to even greater interest rates and credit crunching. In the wake of Mexico's default, most commercial banks significantly reduced or halted new lending to Latin America, and since the majority of the Latin American loans were short term, refinancing requests were rejected. Thus, these short-term loans were due immediately and, starting with Mexico, a wave of Latin American countries started defaulting on their loans.

⁴³ The Yom Kippur War, Ramadan War, or October War, also known as the 1973 Arab–Israeli War and the Fourth Arab–Israeli War, was a war of aggression fought by the coalition of Arab states led by Egypt and Syria against Israel from October 6 to October 25, 1973.

⁴⁴ An economic condition in which investment capital is difficult to obtain. Banks and investors become wary of lending funds to corporations, which drives up the price of debt products for borrowers.

⁴⁵ The act of trading in an asset, or conducting a financial transaction, that has a significant risk of losing most or all of the initial outlay, in expectation of a substantial gain.

In order to avoid financial panic from ensuing and generating greater civil unrest and waves of speculation, the banks had to somehow restructure the debts; this usually involved new loans with very strict conditions, as well as the requirement that the debtor countries accept the intervention of the International Monetary Fund. Several strategies were implemented to slow and end the crisis. “The IMF moved to restructure the payments and reduce consumption in debtor countries. In conjunction with the World Bank and the US, the IMF also encouraged policies that promoted open markets and pushed for debt relief, once they realized that countries would not be able to pay back in full the large sums they owed” (Krueger 2007). The effects of the Latin American crisis were widespread throughout the different sectors of the economy, wages dropped as productivity lagged and workers were laid off. Investment decreased as international and domestic investors grew wary of the profitability of their investment in light of rising inflation rates. Poverty increased as incomes dropped and purchasing power deteriorated and Real GDP rates dropped substantially. Although all of the Latin American countries suffered from the effects of the crisis, Chile suffered more than any other; this was mainly due to certain neoliberal policies that had been implemented by the technocratic Chicago Boys.

Chile was the Latin American country with the greatest degree of trade openness and reliance on foreign direct investment. Thus, it was more vulnerable to economic world swings as well as to international investments in the economy. “When the crisis hit, Chile’s overdependence on mineral and resource based exports (copper being the main one) made the Chilean economy particularly vulnerable to world swings” (Krueger 2007). As international investors saw the value of their assets decline as well as the growing atmosphere of insecurity as protests and domestic terrorist attacks took hold of Chile in 1982, they halted further investment

and even caused some of their existing ones to be withdrawn. Chile's 1982 crisis was even worse than the self-induced depression during the 1975 shock therapy. "Real wages dropped sharply, falling in 1983 to 14 percent below what they had been in 1970. Bankruptcies skyrocketed, as did foreign debt. By the end of 1986 Gross Domestic Product per capita barely equaled that of 1970" (Rayack 1986, p. 54).

Productivity started to lag behind those of other Latin American countries and in order to keep the economy's competitive edge in the export base, companies continued to decrease wages and with the high levels of unemployment, workers had no choice but to continue to accept declining wages. "Between 1980 and 1988, the real value of wages grew only 1.2 percent while the real value of the minimum wage declined by 28.5 percent. During this period, urban unemployment averaged 15.3 percent per year. In other words, after nearly 15 years of free market capitalism, real wages had still not exceeded their 1970 levels" (Rayack 1986, p. 91). Table 6 serves as an indicator to the increasing income inequality and concentration of wealth experienced during the Pinochet regime as most of the major industries were owned by a handful of powerful firms.

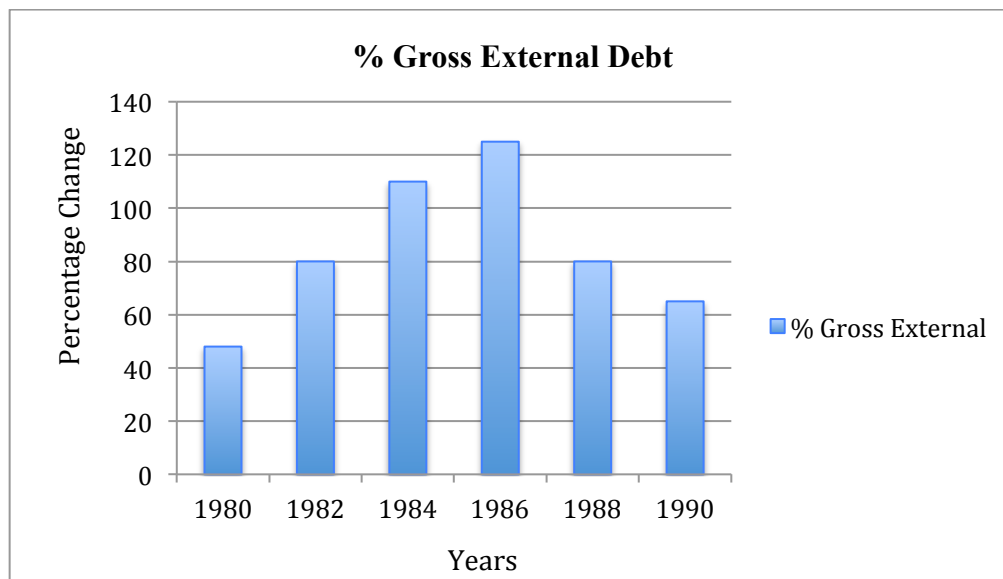
Table 6. Main Chilean Industries Concentrated in a Handful of Firms

Industry	Number of Firms	Industry Share (%)
Paper, cellulose	2	90.0
Chemicals	2	71.4
Wine and Beverage	2	70.2
Forest Products	5	78.4
Food	6	67.3
Fish Products	6	51.1
Mining	7	97.1

Wood	7	78.6
Agriculture	8	80.6

Source: Oscar Muñoz, 1986

Figure 3 Chilean Percentage of Gross External Debt 1980-1990



Source: Central Bank of Chile

The relative wealth created during these years in the mid to late 1980's did not trickle down to the working class but instead accumulated in the hands of the rich. "In the last years of Pinochet's dictatorship, the richest 10 percent of the rural population saw their income rise by 90 per cent between 1987 and 1990. The share of the poorest 25 per cent fell from 11 per cent to 7 per cent" (Green 1991, p. 12). Figure 3 serves as another indicator of the declining economic conditions experienced during the debt crisis as the amount of loans needed to be repaid accumulated and the government was forced to continue asking for more loans to pay the existing ones at higher interest rates.

The policies of the Reagan administration also contributed to the severity of the debt crisis as he continued to push for laws in Congress that limited the liquidity of the US financial system. “Reagan also became worried of his international image as a supporter of right wing autocrats and he launched project “Democracy” in June 1982 creating the National Endowment for Democracy that was in charge “of directing 1.6 million dollars to the opposition in Chile” (Ibid, p. 12). The US was also part of a multilateral effort to pressure Pinochet to accelerate the pace of reforms both in the economic and in the political sector:

Commercial lending declined from about 3.3 billion in 1981 to about 750 million in 1985, multilateral lending increased from only 13 million to 1.1 billion over the same period. Blocking multilateral development aid brought tremendous pressure on Chile, given its heavy reliance on it, and it transmitted a clear message to Pinochet to quicken the pace of reforms. It also dissuaded him from maneuvering to become the sole candidate in the upcoming plebiscite that would take place in 1989 (Ensalaco 1999, p. 44).

With decreasing loans and credit, the Chilean Central Bank encountered a balance of payments difficulty and the uncertainty during this period brought back strikes and terrorist violence intended to depose Pinochet. On May 11, 1983 the Copper Workers Union called for a general strike to protest the harsh effects of the economic downturn and the regimes economic policies in general. These protests lasted for a total of 14 days and were brutally put down by the regime. “In 1984 government sponsored vigilante groups began to appear. Priests were harassed and abducted in shantytowns, human rights activists raped and murdered” (Green 1991, p. 14).

Workers were left hopeless as their social provisions were stripped down, unions lost power, and wages continued to decline. “Widespread unemployment has the effect of driving down wages, as unemployed workers compete for a limited number of jobs, accepting even sub-poverty wages to get them. As might be guessed, such high unemployment also reduces a nation's productivity, which is largely why Chile's growth record compared so poorly to its neighbors ” (Arellano 1988, p. 33). Table 7 illustrates the declining labor conditions during the debt crisis and even after as the export sector continued to be financed on the basis of declining wages. Table 8 also illustrates the inequality that arose as a result of the declining power of the labor unions, as blue-collar workers earned only a small percentage of what white-collar workers and employers earned. Chile had also been one of the countries along with Mexico that had borrowed the most from abroad. Chile had borrowed heavily as part of its neoliberal reforms and efforts to overhaul the economy and impose an export led economy.

Table 7. Evolution of Real Wages, revised index, 1980-1987 (In percentage terms)

Year	Average Wage	Minimum Wage
1980	95.0%	97.7%
1981	105.0	102.3
1982	110.3	101.2
1983	91.1	79.3
1984	86.5	69.5
1985	80.0	64.7
1986	81.5	60.3
1987	81.2	55.5

Source: Meller, 1990

Table 8. Relative Average Earnings to Blue Collar Workers by Periods in Great Santiago, 1957-1990

	White Collars	Own-Account	Employers
1957-1963	2.943	2.154	6.539
1964-1969	2.954	2.073	7.827
1970-1973	2.841	1.929	6.379
1974-1981	2.770	2.204	8.820
1982-1986	3.196	2.070	9.541
1986-1990	3.452	2.281	13.060

Source: Aguirre, 2000

In order to finance these reforms, Chile had relied on the IMF and US support from such presidencies such as the Reagan administration. Hence when the crisis hit, Chile was one of the countries with the highest external debt in Latin America. In conjunction with rising interest rates and the inability to finance short-term loans, Chile found itself in a difficult position. Thus, as stated before, unemployment rose and wages declined and “by 1983, Chile's economy was devastated, with unemployment soaring at one point to 34.6 percent, far worse than the U.S. Great Depression. Manufacturing production plunged 28 percent. The country's biggest financial groups were in free fall, and would have collapsed completely without a massive bailout by the state. The Chicago boys resisted this measure until the situation became so critical they could not possibly avoid” (Ibid, p. 44). Chile was no longer the paragon of financial stability and in an effort to preserve Chile’s international image, the IMF offered loans to help Chile out of this situation but under strict conditions, “Chile had to guarantee her entire foreign debt — an astounding sum of US\$7.7 billion. The total bailout would cost 3 percent of Chile's GNP for each of three years. These costs were passed on to the taxpayers. It is interesting to note that when the economy was booming, profitable firms were privatized; when those firms failed, the costs of bailing them out were socialized” (Ibid, p. 56).

The switch to a mixed system of neoliberal and industrial policies arose from the necessity to calm the civil unrest that resulted from the effects of the Latin American crisis. Opposition groups such as the MIR started conducting a series of terrorist attacks in the main cities of Chile and the workers started organizing popular strikes as they saw their wages decline and inflation skyrocket. In the face of increasing opposition, Pinochet saw the necessity to enact a system that would overhaul some of the neoliberal policies that had made the economy increasingly vulnerable as well as to return consumer and investor confidence to the economy while maintaining the provision of loans from the World Bank and the IMF.

This analysis does not state and does not intend to demonstrate that all neoliberal reforms were overhauled after the lessons learned during the Latin American crisis or that all neoliberal reforms were detrimental to the economy. In fact, one can observe that the economy continued to benefit from declining wages in order to maintain its competitive edge. The unions were still weak relatively to their power during the Allende and Frei years and wage negotiations as well as workers benefits were non-existing. The economy still relied on the mining and resource based sectors of the economy despite promises to shift the economy towards a more industrialized sector.

The health, education, and pension reforms were also kept in place, in each of these areas, public and private sectors competed with each other for the provision of these services, often excluding those that were on the lower end of the income distribution. These reforms contributed to a lack of medical expertise, supplies, proper schools, high schools, and pension systems in the public sector, excluding the majority of the impoverished population. However, the government did overhaul certain neoliberal reforms that had been put in place before the Latin American crisis, and the Chicago Boys' prominence and reign over the economy was

destroyed as the government sought to establish a mixed system of neoliberal and industrial reforms. The copper industry is perhaps the biggest example of this mixed system. The copper industry as has been previously discussed was owned by the state and it provided preferential incentives for those who wished to invest in it, however it was also characterized by a strong private sector that relied heavily on market forces to determine prices and the amount of investment allowed to maintain the copper industry vibrant.

During the shock therapy reforms, most of the banks in Chile had been regulated and a lot of the social provisions meant to provide people with poverty alleviation programs had been curtailed. After the debt crisis, the government removed these reforms.

Domestic banks were deregulated in the late 1970s but reregulated with vigor in the early 1980s. Poverty had increased enormously during and in the wake of the UP's and the 1975 disastrous economic policies, and it decreased only as a result of the state-led stabilization policies, structural reforms, and targeted social programs of the Pinochet period. Major state expenditures for direct action social programs targeted to the poorest of the poor were initiated in the middle 1980s, not after 1990. Poverty levels, as high as 50 percent in 1984, were reduced to 34 percent by 1989. They continued to fall after 1990 to 15 percent in 2005 (Packenham and Ratliff, 2007, p. 93).

These emergency employment programs included tasks such as garbage collectors, street sweepers, and janitors. The programs rarely matched the minimum wage and became increasingly necessary due to the declining productivity and laying off of workers that had occurred during the debt crisis. Even though these programs were only meant to provide a temporary source of employment until the economy was stabilized, they represented a strong role of the state in the conduction of the economy and provided people with some income to survive

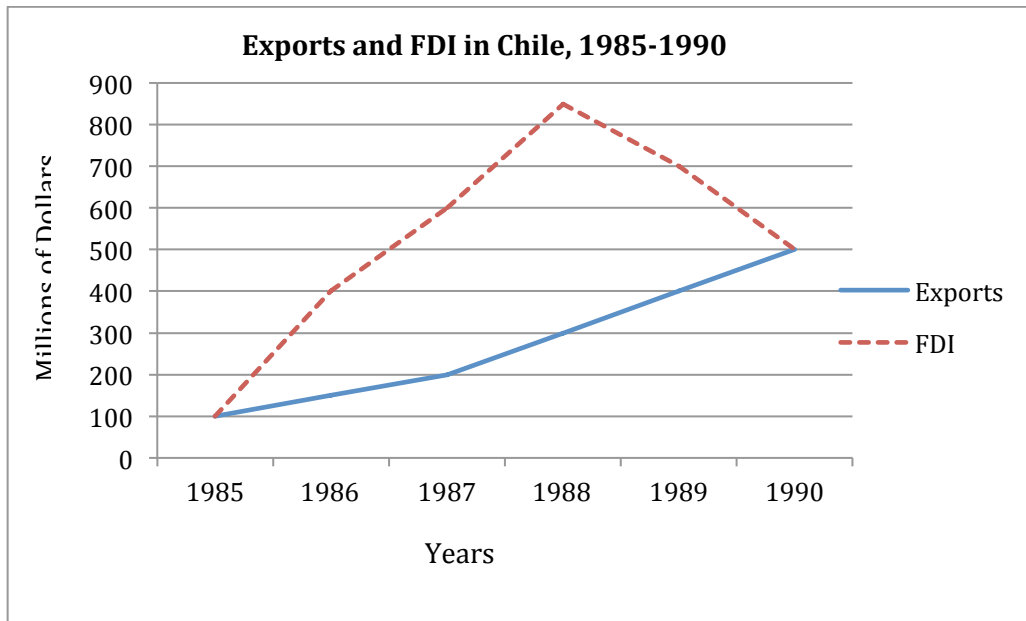
those harsh times. Policies in which the state had a strong role in providing people and companies with economic incentives were also extended to the mining, forestry, and trade sectors.

To promote exports in the forest sector, the government introduced legislations like Decree 701, which “subsidized between 75 to 90 percent of forest company costs, and freed the companies from taxes. This mechanism encouraged the big companies to substitute native forest with pine and eucalyptus and channeled 96 percent of the subsidies to the big farmers; only 4 percent has gone to small farmers. As a result of these policies, Chilean exports in forest products increased 1,600 percent” (Larrain 1999). Even though the government failed to significantly reduce the overdependence on resources, it did provide international and domestic investors with the much needed incentives such as tax breaks to return investor confidence after it had declined due to the high inflation rates and climate of insecurity of the early 1980s. The state also had a strong role in the implementation of protective tariffs and capital controls that would prevent Chile from being as vulnerable as it was during the debt crisis to economic swings.

The use of capital controls was widely criticized by the IMF as they continued to advocate for policies that promoted trade openness as a path to achieve macroeconomic equilibrium. “Thus, even though the IMF’s influence was strong in the management of the Chilean economy, the state still had a strong role in the sectors that it believed were vital to Chile’s achievement of economic stability” (Larrain 1999). Figure 4 shows the results of the reinstatement of industrial policies in an effort to provide incentives to increase exports as well as to increase investment after the debt crisis had reduced investor and consumer confidence. Figure 5 illustrates the GDP levels of the years that comprised the Frei, Allende, and Pinochet

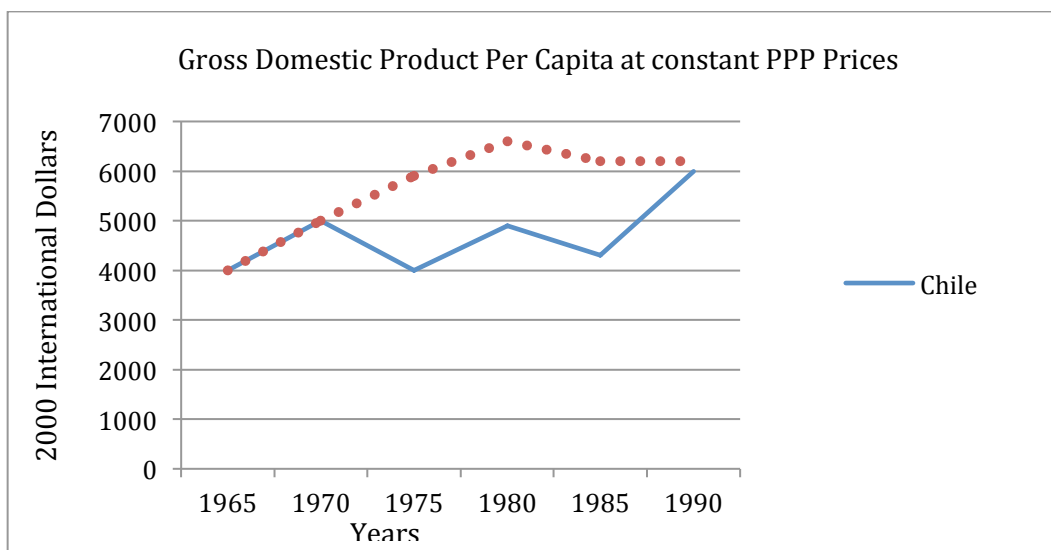
administrations. The figure indicates that the growth during the first years of the Allende administration was not outmatched until the late 1980s when the administration established a mixed economic system of industrial and neoliberal policies.

Figure 4: Exports and FDI in Chile between 1985 and 1990



Source: Banco Central de Chile

Figure 5. Chilean GDP Per Capita at constant PPP prices, 1965-1990



Source: Central Bank of Chile

The Latin American debt crisis served as an eye-opener to the realities of some of the flawed economic policies imposed during the early 1970s in the wave of privatizations and during the late 1970s in the shock therapy reforms imposed by the Chicago Boys. These policies had been aimed at removing the role of the state in every sector of the Chilean economy. However, the government soon became aware of the importance of the state in the correction of flawed economic policies and in the provision of social protections and economic incentives during recessions. Once the government reached this realization, it started implementing a mixed system of neoliberal and industrial policies, overturning some neoliberal policies that had exposed the economy to volatile swings and re-introducing some of the industrial policies that had provided international lenders and domestic investors with the necessary incentives to make economic innovations and maintain investment and consumer confidence.

As previously illustrated, these mixed policies started being implemented shortly after the debt crisis reached its peak in Chile, in late 1982. Once these policies were solidly put in place Chile started to experience a boom in GDP and other economic growth variables. “After enduring a deep recession from 1982 to 1985 (unemployment reached 20% in 1982), Chile's economy more than bounced back. Between 1987 and 1998, per capita income grew by 88%” (Cypher 2004, p. 19). In 1987, the Pinochet regime was finally able to surpass the GDP indicators that had been present during the first two years of the Allende era. The mixed system of industrial and neoliberal policies had finally achieved the objective that the Chicago Boys had so desperately tried to achieve. Although the economy was still far from being perfect (unemployment was still high, the export industry relied on low wages, and poverty was still widespread) the government was finally able to achieve the economic growth necessary in order to begin the drafting of propositions in order to address the remaining economic problems.

XIII. Conclusions

The political economic history of Chile has been marred by policy failures and reversals due to either the climate of domestic instability or external shocks that have especially affected Chile during the periods characterized by high degrees of trade openness. External shocks such as the Great Depression and the Latin American debt crisis have provided the existing administrations with the necessary momentum to enact a series of policy reforms that are geared towards providing a greater degree of social protections and providing domestic and international investors with the necessary incentives to resume their confidence in the economy and continue to invest in vital industries. These external shocks were followed by the enactment of industrial policies and a limited degree of socialist policies aimed at providing a safety net in the areas of emergency employment programs, healthcare, pensions, and poverty alleviation measures. Thus, external shocks have demonstrated the necessity of a mixed system that is not solely focused towards the efficiency of the market system but also on the protection of the well-being of the citizens.

In terms of economic growth, the analysis of the years between 1930-1989 has also shown that a mixed model of neoliberal and industrial policies is better than one dogmatic model. Before the Pinochet dictatorship, the models that were predominant were the developmental and socialist models. During the Frei administration the developmental model was the leading model but this model was also coupled with a limited degree of socialist policies such as the partial nationalization of the copper industry and the initiation of the land reforms, policies that were intensified during the Allende administration. This mixture enabled the Frei administration to strengthen the domestic manufacturing base and attract international investors

through the provision of economic incentives such as credit allocation and tax breaks. However, Frei's limited socialist measures created a divide between the conservative and liberal parties in Chile.

During the Allende administration, the socialist model was the leading model but this model was also coupled with a limited degree of industrial policies. Although Allende completely nationalized the copper industry and was forced to accelerate the pace of the land reforms by members of his own party, he also kept the credit allocation and tax incentives intact for industries that had not been nationalized. Unfortunately the climate of political fragmentation, rampant inflation, and decreasing investor confidence gave the military the necessary tools and arguments to conduct a coup and depose Allende. Yet, even though the last year of the Allende presidency was chaotic, the Pinochet administration that followed matched the economic growth of the Allende presidency until the late 1980's. This reality was due to a variety of reasons, mainly because the first phase of the Pinochet dictatorship (1973-1975) had relied on heavy privatizations without any clear economic direction and the second phase of the dictatorship (1975-1981) had relied on the overhaul of most of the existing industrial and socialist policies that had provided investors with the necessary incentives, and citizens with the necessary social protections to enable economic growth to occur.

During the 1981 debt crisis, the Pinochet administration found it necessary to conduct a series of reforms to the existing neoliberal model. This was due to the climate of increasing civil unrest and terrorist attacks on the part of the opposition caused by declining economic conditions, increasing poverty and income inequality triggered by the debt crisis. The re-introduction of industrial policies and the retrenchment of some of the neoliberal policies, enabled the Pinochet administration to regain investor and consumer confidence, to maintain the

loans received from the IMF and the World Bank, to generate levels of economic growth that finally surpassed those of the Allende years, and to increase the revenues and wealth received from exports to levels that had never been seen before.

Although the analysis addressed the factors that enabled Chile to achieve greater economic growth with a mixed model of industrial and neoliberal policies rather than with one dogmatic model, it does not attempt to explain which model was the most effective in improving overall living conditions. In fact, between the years of 1930-1989, poverty increased and although wealth and revenues increased, and the efficiency in domestic production increased between the years of 1981-1990, these earnings were not distributed in an equitable manner. Throughout these years, Chile was always among the top in Latin America in terms of the proportion of the population living under the poverty line and of the unequal income distribution. The imposition of a neoliberal model involved a strong sacrifice on the part of the Chilean citizenry, as they were forced to live under the iron fist of the Pinochet dictatorship, a dictatorship that enacted politically repressive measures and used its monopoly on power and authority in order to methodically conduct assassinations and abductions to maintain a regime without visible opposition.

The Pinochet legacy is not one without psychological trauma. Yet, this regime also provided Chile with the necessary regime to be able to experiment with the different economic models that were predominant between 1930-1990. The experimentation with these different models culminated in the adoption of a mixed system of industrial and neoliberal policies that generated a consistent rate of economic growth yet failed to decrease the poverty and inequality levels. Thus, when the plebiscite of 1989 removed Pinochet from power, there were still a variety of issues that needed to be addressed and became part of Pinochet's legacy. The export markets

in mineral and natural resources were still dependent on the ever-decreasing wages and poor labor conditions of workers and the economy was still over-dependent on mineral and fishery resources and failed to diversify into a more industrial base. The economy was also characterized by a detrimental public/private divide in the areas of pension, health, and education. The public sector in these areas was lacking in medical supplies, educated personnel, teaching supplies, and pensions that did not depend on stock market swings.

The political system was also in need of freedom of speech and organization in order to promote an environment for further consumer and investor confidence. These factors would need to be addressed in the administrations that followed. To this day, Chile remains the country with the biggest unequal income distribution in the world yet it has been able to maintain a consistent economic growth rate ever since the late 1980's. The Chilean history between the 1930s and 1990s serves as a true testament to the co-dependence and co-existence of a variety of economic and political models that are vital for the achievement of economic growth and stability in a developing country.

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