

Chile

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If Australia does go down the Argentina road it should meet Chile coming up. Jose Pinera, one of the econocrats responsible for Chile's economic and political recovery, visited Australia at the invitation of BHP and the Institute of Public Affairs. He is neither a politician nor a general but an economist, businessman and proselytizer on behalf of the market economy. He talks with passion and eloquence about success in Chile.

Plainly something unusual has happened in Santiago. By next March Chile will have rejoined the ranks of the democracies and Australian capital---BHP, Bond, Fletcher Challenge and Western Mining---is going to Chile. Democracy is not the norm in Latin American and Australian capital, even of the more speculative kind, is not yet fleeing to Venezuela, Ecuador or Argentina.

One important Chilean lesson is that legality, legitimacy and civil rights tend not to survive gross economic mismanagement---Venezuela, still a democracy, provides current demonstration of the same point. In Chile, during the virtual civil war between the Cuban-backed communists and the junta, civil rights were violated. The security forces are still high-handed and oppressive. Now, however, emerging prosperity for ordinary people has opened the way for democracy. A social democratic party is likely to win the coming election---"Its Time".

For fifty years before the Pinochet rule, Chile's economic growth had been only 1.5% per annum. With a rising population this meant that living standards fell. By 1973 the economy, including the labour market, was highly regulated. Government ownership dominated key industries. Trade was stifled by tariffs averaging 100% and rising to 1000%. This meant that exports were few and concentrated. Inflation was 600% and unemployment and the resultant poverty were serious.

All this is being changed. Inflation is down to 11-12% and economic growth is excellent. The junta has deregulated, freed trade and privatised. And the Social Democratic opposition, although it finds plenty to complain about, is promising not to reverse the economic reforms.

Dr Pinera's story starts with generals who were as ignorant of economics as generals tend to be. Individual voluntary actions which make both parties better off are alien to the military mind. Conflict cannot be prosecuted successfully by voluntary transaction---the privates would individually declare peace. But generals are intelligent and Pinochet's generals recognised their own ignorance. To overcome it they consulted with groups---businessmen, lawyers, the many US-trained economists and others. One might say that they held a series of "summits".

These meetings produced nothing worthwhile, so the generals started asking members of the groups individually. Then they discovered that the lawyers did not not agree with each other---lawyers, like generals, understand only zero-sum games and compulsion. The businessmen were worse: each pushed his own interest which, of course, was someone else's cost. The economists, on the other hand, were being asked pretty basic questions about the fundamentals of their discipline. Economists generally agree on the way individuals en masse behave in markets and how wealth is created---so the generals got much the same advice from each. Chile was in such a mess that optimal policy, not tempered by political judgement, was recommended and often accepted. So long as they stuck to economics, the generals, except for a short panicky period in the middle, tended to accept the economists' advice.

First came trade reform. Tariffs were reduced to a flat 15% on everything. There are no exceptions and the government makes no favourites. In 1973, Chile, with five other small Latin American States, belonged to the Andean trade pact. She was making 20 different models of car but not many people could afford them, and exports were 12% of GDP. Today, Chile has left the Andean Pact and opened its economy to the world. Trade is now 28% of a much larger GDP. And, although most cars are made in Japan, many more people own them. In the period 1973-1987 the number of different products exported rose from 412 to 1343; the number of exporting firms from 208 to 2780. Free trade works.

Chile had a corporatist labour market---not unlike our own. She now has a substantially deregulated labour market in which over 5000 unions with voluntary memberships negotiate with individual employers. Except in 30 companies producing essential services, strikes are legal. Workers and bosses may employ arbitrators, whom they must pay, but "pendulum arbitration" is the norm. After one month's negotiation the arbitrator must choose whichever of the two final positions he thinks, in all the circumstances, is most reasonable. He cannot split the difference, therefore parties can win only by being reasonable. After a month of being reasonable, differences become so small that the biggest question becomes: why pay an arbitrator?

Like Australia, Chile had an unfunded pension system. Except that the very poor are helped by the government to pay their premiums, this has now been privatised. Above a minimum, people may invest as much as they like in individual accounts

with one of several competing funds. Subscribers may change funds. They may retire early on a smaller pension. When they retire they may re-invest their capital in funds that disburse equity and interest or they may buy an annuity.

There is much more to Jose Pinera's story---the IPA has it on video. Even if some allowance should be made for Pinera's patriotic enthusiasm, Chile's story is exciting, full of hope and relevant to Australia. By chance, I have heard Dr Pinera three times. On each occasion he was asked: "What will happen when Chile becomes democratic?" Pinera scorned the idea that it was easier to convince a general than a democratic politician---both are slaves to the views they hear. The key element, he said, was not a military regime but understanding that had reached its critical mass.

Chile went to the abyss and saw itself becoming another Cuba or Albania. Do we also have to travel all the way to the abyss and if we do, when we get there, will we behave like Argentina or like Chile?

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