

**THE DEVELOPER'S DILEMMA
STRUCTURAL TRANSFORMATION, INEQUALITY
DYNAMICS, AND INCLUSIVE GROWTH**

Chapter: Chile

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Conclusions/ Summary

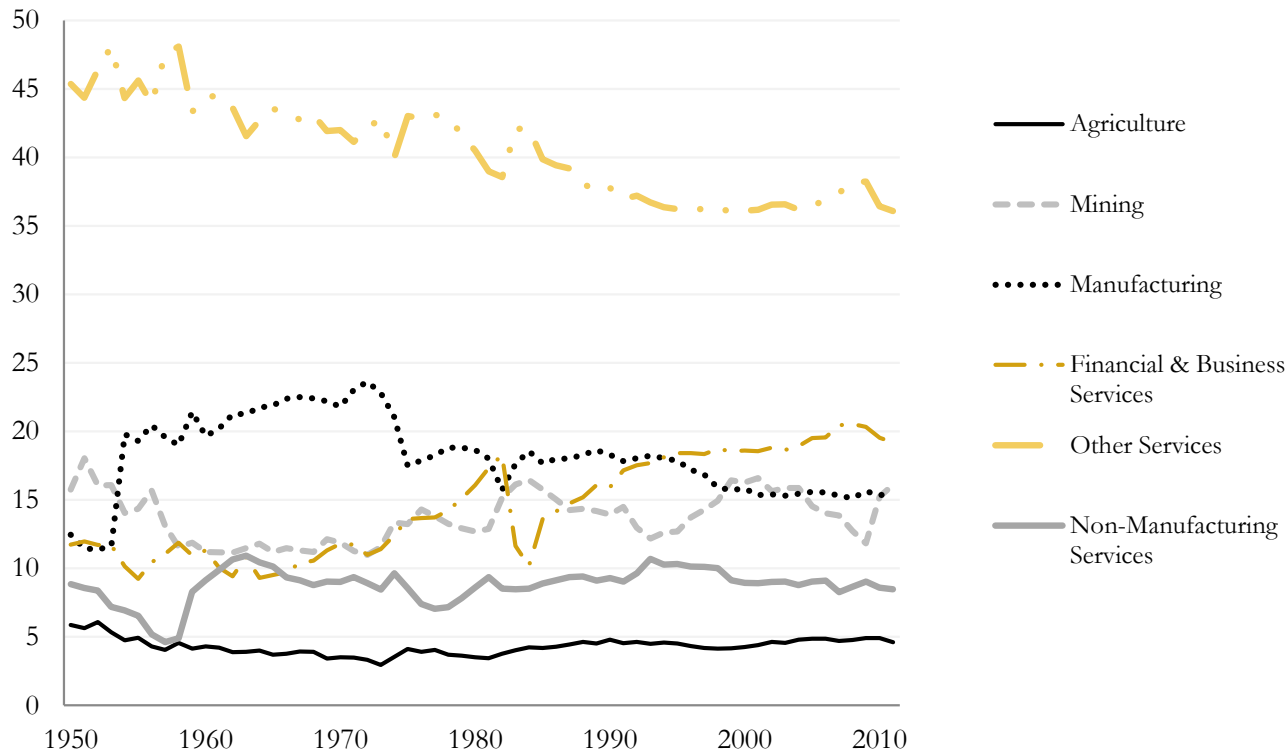
- The Chilean development strategy of the last three to four decades has given priority to aggregate economic growth, orthodox macroeconomic management and high profitability to foreign direct investment and big domestic business
- While income poverty has declined, access to quality social services is still problematic for the poor
- The country displays high indices of economic inequality and pressures on the environment after decades of resource-intensive growth
- decline in the value-added shares of manufacturing and agriculture and a rise in services, particularly finance and trade, hotels and restaurant with ups and downs in mining shares
- These trends are more accentuated for employment shares with the decline in relative employment generation in agriculture and manufacturing going directly to the services sector that accounts now for two-thirds of total employment in the economy
- A more balanced development strategy for Chile would require significant changes in its production structure away from the intensive use of natural resources and more towards knowledge-intensive sectors, a revival of manufacturing and clean production lines helped by a more environmentally conscious tax-system
- the reduction of high inequality and de-concentration of wealth would need important reforms in the tax system, the structure of markets, effective anti-trust legislation and the rebalancing of bargaining capacities between labour and capital that revert the enormous economic surplus currently appropriated by wealthy elites, enabling more inclusive growth

Economic history (before 1960)

- Commodity dependence:
 - Nitrate commodity cycle (1880-1930): Early 20th century nitrate accounted for 65-80% total exports, 40% of GDP. Nitrate taxes funded 50% of total public expenditure
 - Cooper cycle (1930 – to date)
- After the Great Depression (early 1940): attempt to switch from commodity-export-oriented growth pattern into an import substitution industrialisation strategy (ISI), aimed to reduce external economic dependency. Creation of new industries in the energy sector, iron and steel, sugar, and telecommunications. By the end of the 1950s, the manufacturing industry represented around 21 per cent of the Chilean economy
- 1950-1970 Cooper mining represented 55-65% of total exports (15-30% of fiscal revenues). In 1960 cooper mines started a nationalisation process (mixed property with American companies first). They were fully nationalised in 1973 (Allende's government)

Structural transformations: Changes in the Chilean Economic structure

Figure 1: Chile GDP share, %
Value added structure main sectors, 1950-2011



Source: Own elaboration, UNU-WIDER's World Income Inequality Database (WIID)

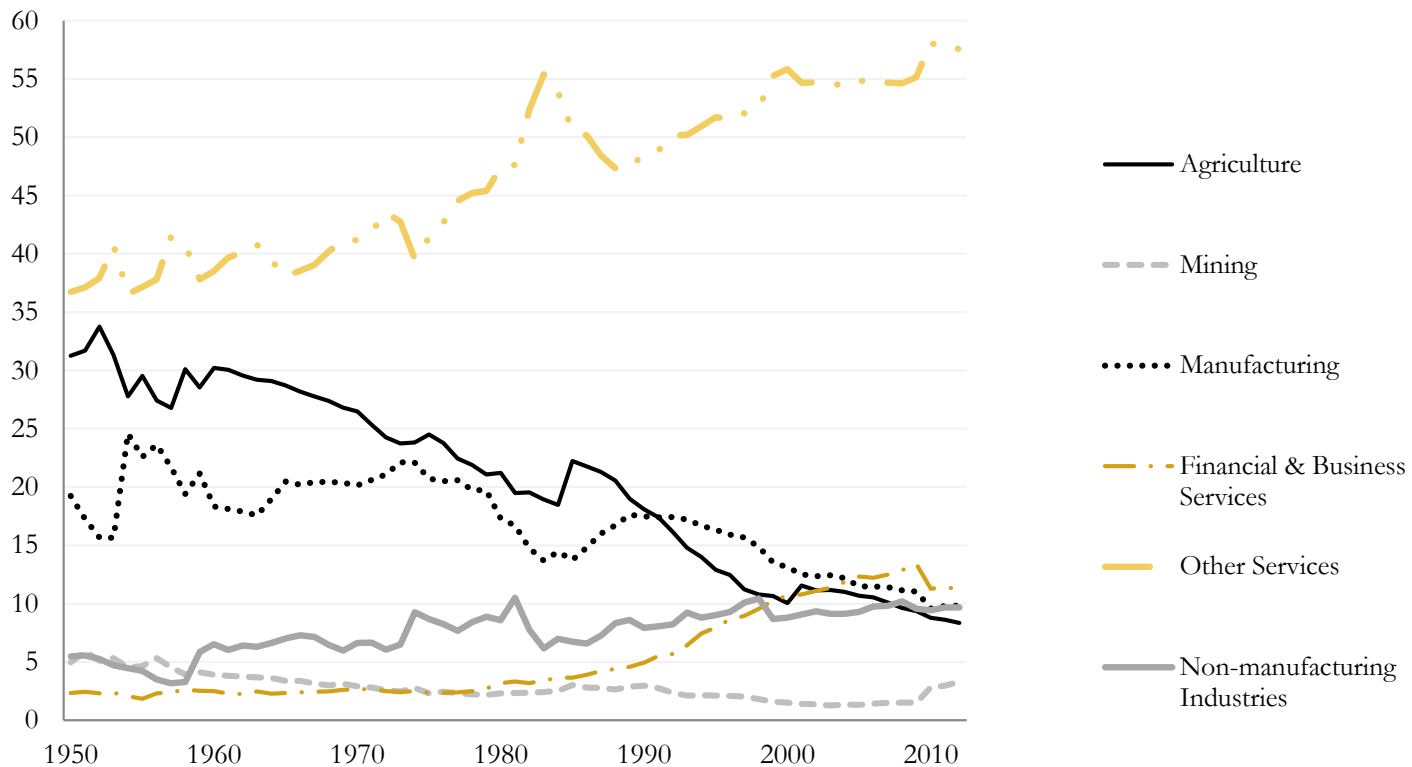
Changes in the Chilean Economic structure:

Two main trends

1. Growth of the service and financial sector as well as the mining sector. Services tend to be intensive in labour but not in technology, and mining is intensive in technology but requires fewer highly qualified workers
2. Early deindustrialization: shrinkage of the manufacturing sector. Industries such as textile, metal-mechanic, and shoe production sharply contracted with trade liberalisation in the mid-1970s and, later, with enhanced price competition from China and other East Asian markets.

Structural transformations: Changes in employment structure

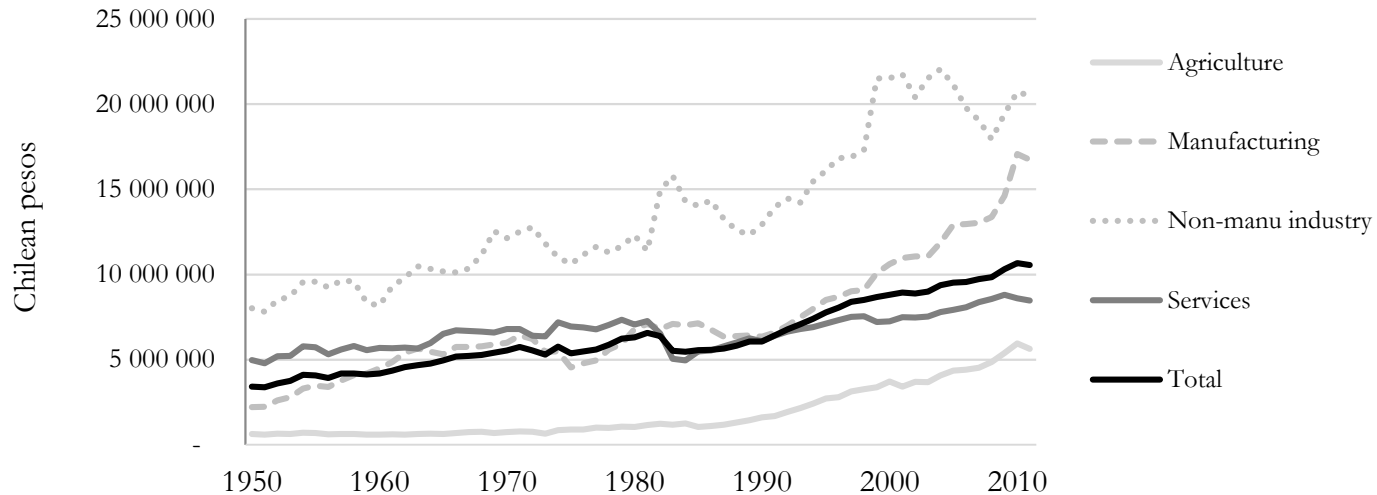
Figure 2: Chile Employment share, %
Sectoral shares in total employment main sectors, 1950-2011



Source: Own elaboration, UNU-WIDER's World Income Inequality Database (WIID)

Changes in sectoral labour productivity:

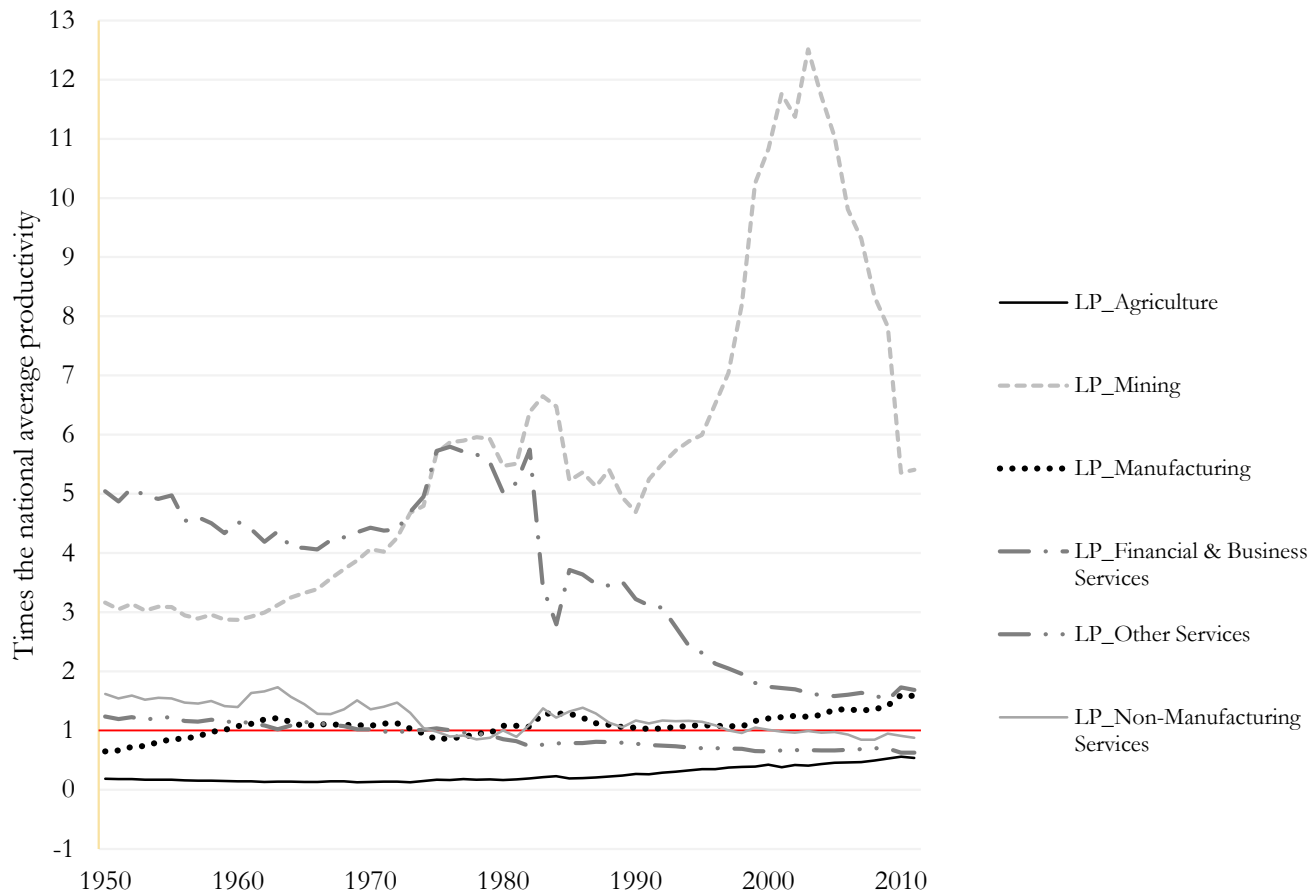
**Figure 3.1: Labour productivity
in local currency (Chilean pesos)**



Source: Own elaboration, UNU-WIDER's World Income Inequality Database (WIID)

Changes in sectoral labour productivity:

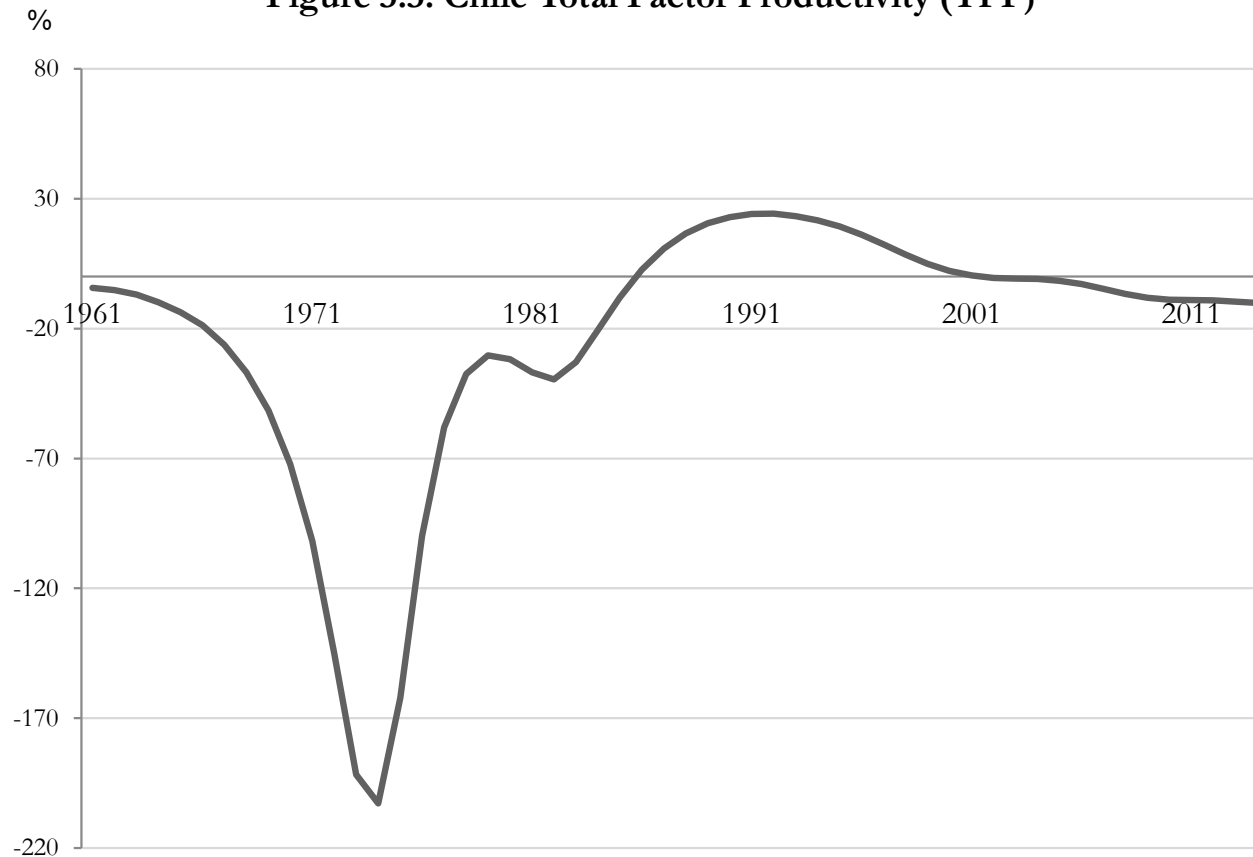
Figure 3.2: Evolution of Sectoral Labour productivity



Source: Own elaboration, UNU-WIDER's World Income Inequality Database (WIID)

Total factor productivity:

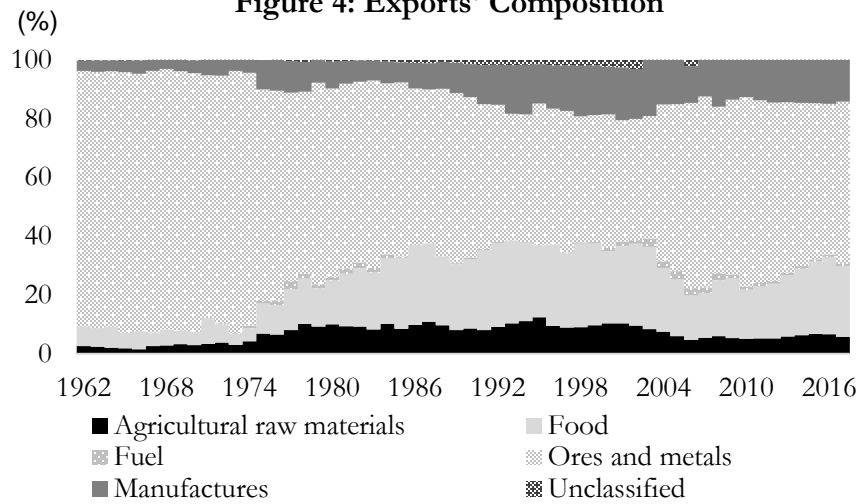
Figure 3.3: Chile Total Factor Productivity (TFP)



Source: Own elaboration, UNU-WIDER's World Income

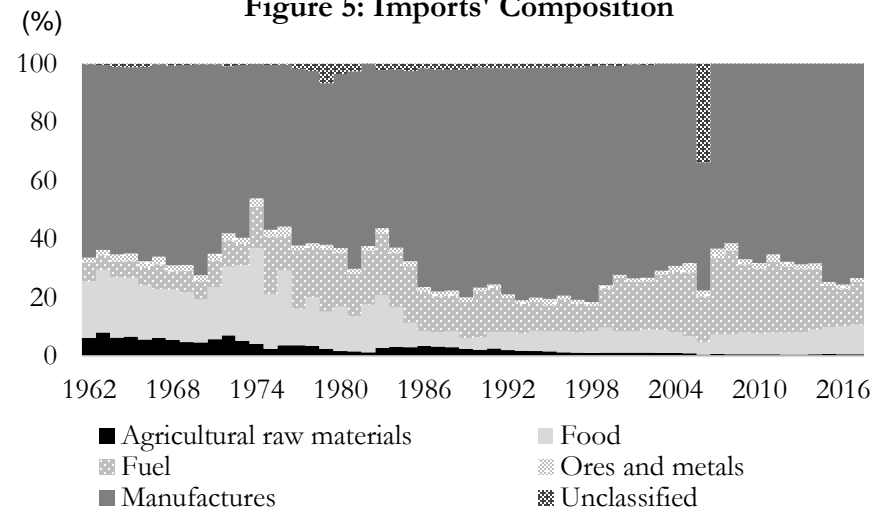
Trade structure

Figure 4: Exports' Composition



Source: Own elaboration, UNU-WIDER's World Income Inequality Database

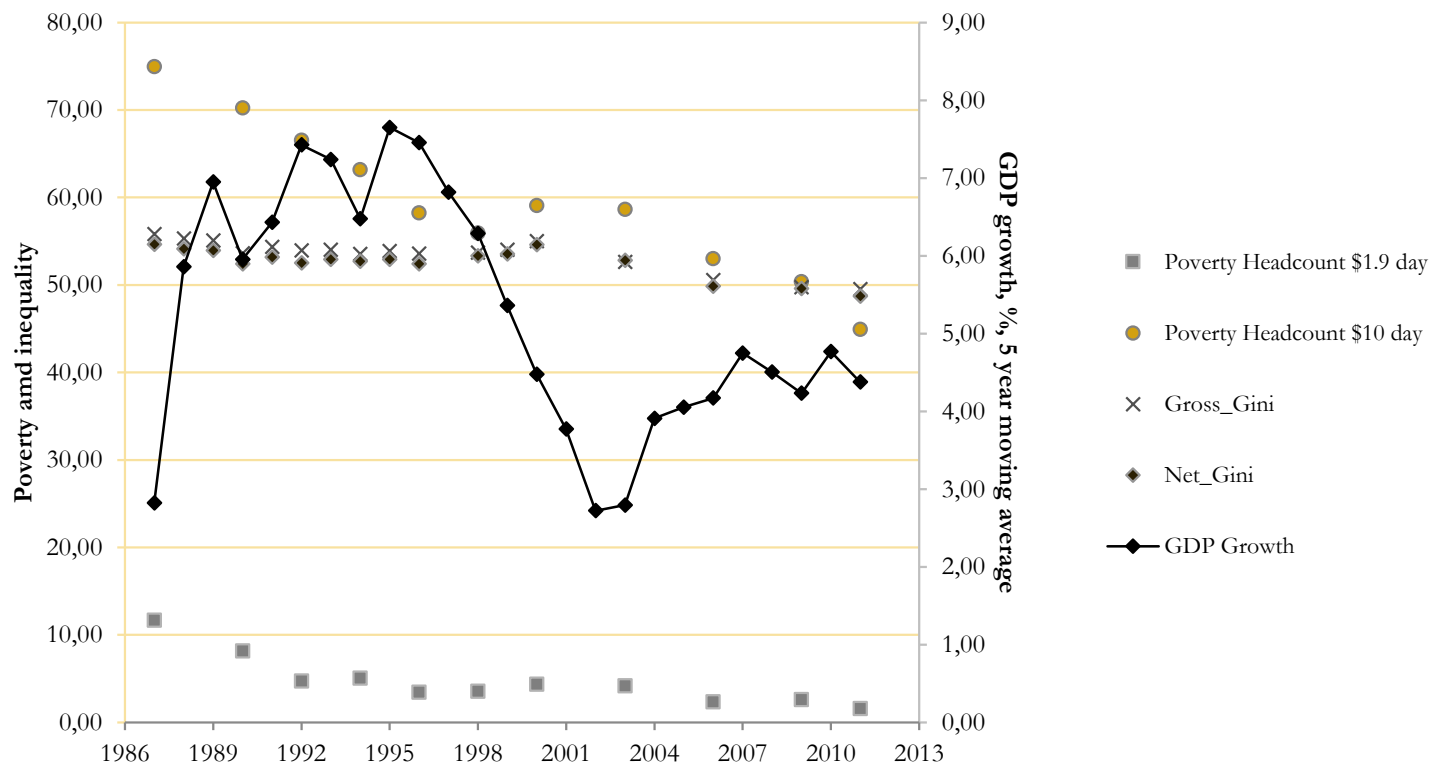
Figure 5: Imports' Composition



Source: Own elaboration, UNU-WIDER's World Income Inequality Database

Trends in income inequality, employment and inclusive growth

Figure 6: GDP Growth, Poverty and Inequality



Source: Own elaboration, UNU-WIDER's World Income Inequality Database

Trends in poverty:

- Income-measured poverty (headcount ratio) fell from near 45% in 1987 to 8.6% in 2017. Only 2.3% extreme poverty
- Strategies to reduce poverty: mainly aggregate economic growth complemented by subsidies targeted to the poor
- Per capita income increased from around US 4,500 dollars in the late 1990s to US 25,000 dollars in 2018

Trends in inequality:

- Less successful reduction in inequality, only six percentage points between 1980 and 2017
- Gross and net Gini follow similar patterns suggesting that tax redistribution is very limited in the country
- An important source of inequality in Chile is high-income shares at the top of the distribution (concentrated specifically in the top 1 per cent). The relationship between the richest and the poorest decile is 35.6 times in 2011 (Gammage et al., 2014)

Growth and Employment Generation

Quantity and quality of the employment

- Employment grew less than the economy in periods of high growth:
 - ▣ Average GDP growth rate of 5.5% between 1990 and 2016
 - ▣ Average employment growth rate of 2.5% during that period
- 40% of the rise in occupation has been driven by contracts of less than 30 hours per week
- Between 2000-2009, the economy grew at 4.6% and the real wages only at a 0.9%
- 51% of workers had short term contracts (less than three years) in 2014. While in more developed countries a short term contract is a vehicle to permanent jobs, in Chile only 36.8 per cent lead to permanent jobs

Policies used to shape ST, inequality and inclusive growth

From mid-1970

- Early deindustrialisation:
 - Tariff reductions and elimination of non-tariff trade barriers
 - Absence of explicit industrial policies
 - Exchange rate devaluation
 - Privatisation of public enterprises
- Trade union weakening
- Market oriented social policies:
 - For-profit providers operating in the education sector, health, housing and pension-fund management

Post-Pinochet democratic period:

- Independent Central Bank (From October 1989)
- Fiscal rule to increase fiscal spending according to expected long term values of growth and terms of trade in 2008
- Economic and Social Stability Fund and a Pension Reserve Fund (2008)

Political economy of Structural Transformations

Post-Pinochet democratic period:

- Privatisations done during dictatorship period were not revised, and new privatisations were made
- Democratic governments maintained the private provision of education, health and the capitalisation pension systems. However some public programmes in health and education have increased the role of the state in these areas
- Job stability and labour rights have been affected by the weak bargaining power of labour due to de-unionisation, outsourcing and fragmentation of labour unions. However some legal practices such as having multiple-tax identification numbers have been forbidden
- Tax reform in 2014 increased moderately corporate income taxes and reduced deductions from corporate taxation to personal taxes for form-owners

Future trajectory of the ST–inequality–inclusive growth

- Diversification of the economy, in terms of activities and markets (reduce mineral dependency)
- Changes in the current composition of growth is not an easy task (mining and services)
 - ▣ Low investment in R&D
 - ▣ Moderate value-added intensity of the export bundle
- OECD Productive Transformation Policy review suggests increase an “update” of the country’s development strategy, increasing factor productivity growth, reducing territorial concentration of production, increasing value addition in services, and reducing over-reliance on mining
- Future trends in inequality and the prospect for more inclusive growth also remain uncertain