1999 Country Reports on Economic Policy and Trade Practices
Released by the Bureau of Economic and Business Affairs
U.S. Department of State, March 2000

CHILE

Key Economic Indicators

(Billions of U.S. Dollars unless otherwise indicated)

	1997	1998	1999
Income, Production and Employment:			
Nominal GDP 2/	77.1	79.6	79.5
Real GDP Growth (pct) 1/	7.1	3.3	-2.7
GDP Growth by Sector (pct) 1/ 2/			
Fishing	8.1	5.0	-1.3
Agriculture	2.1	1.4	-0.3
Mining	8.1	3.0	13.3
Manufacturing	9.5	4.0	-3.2
Construction	8.2	3.0	-10.2
Services	35.5	18.0	-1.9
Government	5.3	6.0	1.3
Per Capita GDP (US$) 1/	5,300	5,100	5,000
Labor Force (000s) 1/	5,380	5,851	5,854
Unemployment Rate (pct) 1/	5.3	6.0	11.0
Money and Prices (annual percentage growth):			
Money Supply (M2) 2/	21.7	10.5	6.0
Consumer Price Inflation (pct) 1/	5.6	4.7	2.4
Exchange Rate (Peso/US$) 1/	419	465	543
Balance of Payments and Trade:			
Total Exports FOB 4/	16.9	14.9	8.5
Exports to U.S. 5/	2.7	2.9	1.5
Total Imports CIF 4/	18.2	17.4	7.2
Imports from U.S. 5/	4.3	4.0	1.5
Trade Balance 4/	-1.3	-2.5	1.1
Balance with U.S. 5/	-1.6	-1.1	0.0
Current Account Deficit/GDP (pct)	5.2	5.2	0.0
Total External Debt 1/			
Private Debt	21.6	26.0	28.3
Public Debt	5.1	5.7	5.9

Debt Service Payments/Exports (pct) 1/	20.1	24.9	36.0
Fiscal Deficit/GDP (pct) 1/	0.0	0.0	0.5
Gold and Foreign Exchange			
Reserves (US$ billions) 1/	17.8	15.3	15.0
Aid from U.S. (US$ millions) 5/	0.3	0.3	0.3
Aid from All Other Sources	N/A	N/A	N/A

1/ Central Bank of Chile, November 1999 Monthly Information Bulletin
2/ Central Bank of Chile, August 1999 Monthly Information Bulletin
3/ Includes electricity, gas, and water generation
4/ DIRECON
5/ U.S. Department of Commerce, International Trade Administration Statistics

1. General Policy Framework

Chile's economy suffered a sharp recession from November 1998 to late 1999, following a decade of over 7 percent average growth. A fall in exports (mainly due to the Asian economic crisis) coupled with a striking spike in short-term interest rates in the fourth quarter of 1998, pushed Chile into 11 consecutive months of negative growth between November 1998 and October 1999. Unemployment rose to 11.5 percent in August 1999, marking 16 months of rising unemployment, before falling to 11 percent in November. Exports of primary products such as copper remain strong; copper exports have risen an average of 20 percent in value over 1998 figures despite lower prices that prevailed for much of 1999. Chile's credit rating remains investment grade, and direct foreign investment has increased to record levels despite the recession. Growth is projected at approximately 5 percent in 2000 as domestic demand slowly comes out of a slump and vibrant exports continue in the context of international economic recovery.

The government of Eduardo Frei (1994 to March 2000) has continued Chile's policies of macroeconomic stability and export orientation. The calendar year 1999 budget will register Chile's first deficit in 10 years, but the Finance Ministry insisted upon and won passage of a 2000 budget that features 3.3 percent nominal growth, basically flat when considered in context of 3-4 percent predicted inflation. While the GOC has expressed concern over too-rapid, uncontrolled capital inflows prior to the 1998-99 economic crisis, it has continued to loosen capital restrictions. Following legislative changes in 1997, foreign banks have invested heavily in the Chilean market (particularly in 1999). Foreign insurance and finance companies are also dominant in the health and pension industries, owning most of the market leaders. The Government of Chile has privatized some ports through concessionary contracts. Bid documents have been released for the privatization of water and waste water treatment facilities.

In September of 1999, Chile's independent Central Bank dropped the exchange-rate band system that governed its exchange rate policy. This is a major change from previous policy, which sought to keep the peso/dollar rate within pre-set parameters. The Central Bank maintains its policy of balancing growth and inflation via short-term interest rate policy and intervention in the currency markets, but has pledged to use those tools sparingly.

The 1998-1999 contraction is showing definite signs of abating at the close of the year, but has left unemployment at 11 percent, nearly twice the average level seen in the 1990s. Domestic demand is still depressed, following a contraction of 8.5 percent in the third quarter of 1999 versus the third quarter of 1998. Chilean exports to Latin America remain sharply lower. 2000 is expected to bring renewed growth to the Chilean economy. Private and government economists generally agree that growth should reach approximately 5 percent annually, with steam picking up in the 3rd and 4th quarters. Commodity prices are expected to rise internationally, boosting the already strong performance of the copper and mining sector. Unemployment should gradually fall from its peak of 11.5 percent to the 8-9 percent range by mid-2000. Chile’s current trade surplus should continue in the mid-term, as domestic demand recovers from a sharp 13 percent decline and exports rebound. The small current account surplus will, in all likelihood, disappear, and Chile will revert to its traditional deficit; policy-makers are committed to seeing it remain at a much lower level than seen prior to the recession.

2. Exchange Rate Policies

The Central Bank moved to a freely floating exchange-rate system from an exchange-rate band in September 1999. The peso promptly devalued by 5 percent within six weeks before stabilizing and recovering somewhat. The Central Bank’s short-term interest rate is currently 5 percent, and the Central Bank and Treasury Ministry are committed to holding it there at least until growth solidifies in 2000.

Over the last several years, the Central Bank has gradually reduced restrictions on foreign-exchange outflows. In 1995, it lifted the requirement that exporters remit some of their foreign currency earnings through the inter-bank market. A legal parallel market operates with rates almost identical to the inter-bank rate. The value of the peso versus the U.S. dollar has fallen almost 18 percent in 1999 in real terms (473 pesos to the dollar in December 1998 to 547 in December 1999), given roughly equivalent rates of inflation.

3. Structural Policies

Pricing policies: The government rarely sets specific prices. Exceptions are urban public transport and some public utilities and port charges. State enterprises generally purchase at the lowest possible price, regardless of the source of the material. U.S. exports enter Chile and compete freely with other imports and Chilean products. Chile's trade agreements with Mexico, Canada, Mercosur and Central America give exporters from those countries significant competitive advantages -- virtually all Mexican and Canadian exports enter the Chilean market duty free. Import decisions are typically related to price competitiveness and product availability. (Certain agricultural products are an exception. See section 5.)

Tax policies: An 18-percent value-added tax (VAT) applies to all sales transactions and accounts yielding over 40 percent of total tax revenue. There is a 10 percent tariff on virtually all imports originating in countries with which Chile does not have a free trade agreement, down from 11 percent in 1998. Tariffs are programmed to drop to 9 percent in 2000, and to keep falling by one percentage point per year through 2003, at which point tariffs will stabilize at 6 percent. Computers enter Chile duty-free as a result of the Information Technology Agreement. Personal income taxes are levied only on income over about $6,000 per year. The top marginal rate is 45 percent on annual income over about $75,000. Profits are taxed at flat rates of 15 percent for retained earnings and 35 percent for distributed profits, with incentives for business donations to educational institutions. Tax evasion is not a serious problem.

Regulatory policies: Regulation of the Chilean economy is limited. The most heavily regulated areas are utilities, the banking sector, securities markets, and pension funds. No government regulations explicitly limit the market for U.S. exports to Chile (although other government programs, like the price-band system for some agricultural commodities described below, displace U.S. exports). In recent years, the government has introduced rules permitting private investment in the construction and operation of public infrastructure projects such as toll roads. The "privatization" of Chilean state-owned ports, which consists of granting long-term concessions for the operation and management of ports, is proceeding as projected. The three most important state-owned ports have already granted concessions: Puerto Valparaiso, Puerto San Antonio, and Puerto San Vicente/Talcahuano. The Ports of Arica and Iquique are undergoing the bidding process. The due date to present technical offers is January 27, 2000, and concessions will be awarded by February 2000. These five ports account for approximately 30 percent of the total cargo transferred in Chilean ports and almost 80 percent of the cargo transferred at state-owned ports; much of Chilean exports is accounted for by copper and mineral exports that leave via private loading facilities. Bid documents have been released for the privatization of water and waste-treatment facilities.

4. Debt Management Policies

Due to Chile's vigorous economic growth and careful debt management over the last decade, the magnitude of foreign debt no longer constitutes a major structural problem. As of November 1999 Chile's public and private foreign debt was $34.2 billion, or 43 percent of GDP (In 1985, the debt-to-GDP ratio was 125 percent.) Public-sector debt has remained low the past four years, reaching $5.9 billion in 1999, or 7.4 percent of GDP, reflecting 10 years without fiscal deficits. In 1995, the government and the Central Bank prepaid over $1.5 billion in debt to the International Monetary Fund (IMF).

5. Significant Barriers to U.S. Exports

Chile has a relatively open economy and is a member of the WTO. However, many agricultural commodities are subject to strict phytosanitary requirements and restrictions. Beginning in January 2000, the uniform Chilean tariff rate will decline to 9 percent and will be reduced by one percentage point per year to reach a rate of six percent in 2003. The uniform rate applies to all goods except for used goods, which are subject to a 16.5 percent tariff. Chile has free-trade agreements that will lead to duty-free trade in most products by the early 2000's with Canada, Mexico, Venezuela, Colombia, Ecuador, Peru, Bolivia, the Mercosur bloc, and the Central American nations of El Salvador, Nicaragua, Honduras, Guatemala and Belize. Chile is also an active participant in negotiations for the Free Trade Area of the Americas (FTAA). Tariffs also are lower than 10 percent for certain products from member countries of the Latin American Integration Association (ALADI).

The 18 percent VAT is applied to the CIF value of imported products plus the 10 percent import duty. Duties may be deferred for seven years for capital goods imports purchased as inputs for products to be exported. Duties may be waived on capital goods to be used solely for production of exports. (See section 6.) Automobiles are subject to an additional tax known as the luxury tax. Legislation was approved in August 1999 that increased the value of imported vehicles above which the luxury tax applies from approximately $10,000 to $15,000. Automobiles that have a CIF value over $15,000 pay an 85 percent tax on the value of the vehicle over $15,000. This tax discourages sales of larger and more expensive vehicles, including many U.S.-made automobiles. Despite these taxes, sales of U.S.-brand vehicles are rising.

Another tax with the effect of discouraging U.S. exports is a prejudicial excise tax on distilled liquors that compete with domestically produced liquors. In late 1997, the legislature passed a law to gradually modify, but not eliminate, the discriminatory taxation faced by imported liquors. The European Union won a WTO panel appeal over Chile's discriminatory liquor taxation, and the Government of Chile must bring its law regarding taxation of distilled spirits into compliance with WTO disciplines. The U.S. was a third party observer to the panels.

Import licenses: According to legislation governing the Central Bank since 1990, no legal restrictions are imposed on licensing. Import licenses are granted as a routine procedure for most products. Imports of used automobiles and most used car parts are prohibited.

Investment barriers: Chile's foreign investment statute, Decree Law 600, sets the standard of treatment of foreign investors to be the same as that of Chilean investors. Foreign investors using DL 600 sign a contract with the government's Foreign Investment Committee guaranteeing the terms and tax treatment of their investments. These terms include the rights to repatriate profits immediately and capital after one year, to exchange currency at the official inter-bank exchange rate, and to choose between either national tax treatment at 35 percent or a guaranteed rate for the first ten years of an investment at 42 percent. Approval by the Foreign Investment Committee is generally routine, but the committee has rejected some "speculative" investments. In late 1997, the government modified its DL 600 policy to restrict investment entering under the law's provisions to projects worth more than $1 million. In addition, projects of more than $15 million are now routinely vetted with the Central Bank to identify possible "speculative" flows. Associated external loan financing in excess of the value of direct foreign investment flows cannot enter under the provisions of DL 600 (i.e., to enter free of deposit provisions, foreign loan leveraging cannot exceed a ratio of 1:1).

Investment not entering Chile through DL 600 can enter under Chapter 14 of the Central Bank Regulations. Under Chapter 14, investors can be required to deposit a certain percentage of the value of capital inflows in a non-interest-bearing Central Bank account (known as the "encaje") for as long as two years; through mid-1998, the required deposit was 30 percent for one year. Responding to increasing risk premiums charged by creditors and a substantial decline in foreign financial capital flows as a result of the global financial crisis, the Central Bank reduced the requirement to zero in August 1998, but did not abolish the policy. The purpose of the policy had been to limit speculative flows and thus to help stabilize the value of the Chilean peso. When in effect, the encaje applies to inflows of foreign capital into stocks, bonds, bank deposits, as well as real estate, none of which in the view of local authorities increases the Chilean economy's productive capacity or improves technology. There is no tax treaty between Chile and the United States (although negotiations are underway), so profits of U.S. companies operating in Chile are liable to taxation by both governments. However, U.S. firms generally can claim credits on their U.S. taxes for taxes paid in Chile.

Firms may invest without using DL 600 or registering with the foreign investment committee by bringing capital in through foreign exchange dealers or private banks under Chapter 14. Few firms have used this means of investment, as it subjects funds to the encaje and lacks the guarantees provided by the contract with the foreign investment committee.

There are some deviations, both positive and negative, from the nondiscrimination standard. Foreign investors receive better than national treatment on taxation, as they have the option of fixing the tax rate they will pay at 42 percent for ten years or paying the prevailing domestic rate, which is at present lower. There are also examples of less than national treatment.

D.L. 600 allows the Central Bank to restrict the access of foreign investors to domestic borrowing in an emergency in order to prevent distortion of local financial markets. The Central Bank has never exercised this power.

Other examples of less than national treatment are certain sectoral restrictions on foreign investment. With few exceptions, fishing in the country's 200-mile Exclusive Economic Zone is reserved for Chilean-flag vessels with majority Chilean ownership. Such vessels also are the only ones allowed to transport by river or sea between two points in Chile ("cabotage") cargo shipments of less than 900 tons or passengers. The automobile and light truck industry is the subject of trade-related investment measures.

Oil and gas deposits are reserved for the state. Private investors are allowed concessions, however, and foreign and domestic nationals are accorded equal treatment.

Services barriers: Full foreign ownership of radio and television stations is allowed, but the principal officers of the firm must be Chilean. A freeze in force since the early 1980s on the issuance of new bank licenses means that investors, foreign and domestic, have to acquire existing banks. The Government of Chile promulgated banking reform legislation in December 1997 that, inter alia, established objective criteria for issuing new bank licenses.

Principal non-tariff barriers: The main trade remedies used by the Chilean government are surcharges, minimum customs values, countervailing duties, antidumping duties, and import price bands and safeguards. A significant nontariff barrier is the import price-band system for wheat, wheat flour, vegetable oils, and sugar. When import prices are below a set threshold, surtaxes are levied on top of the across-the-board 10-percent tariff to bring import prices up to an average of international prices over previous years. Because of low international wheat and sugar prices this year, the price-band system imposed import duties well above Chile’s WTO bound rate of 31.5 percent. As a consequence, the GOC announced the use of safeguards to legalize the lack of compliance with its WTO bound tariff rate. Domestic beverage manufacturers have complained bitterly about the high duty on sugar. Imports of U.S. wheat, while subject to import duties of nearly 40 percent will be at near record levels in 1999.

Animal health and phytosanitary requirements: Chile has been slow to recognize pest-free areas in the United States, delaying the export approval for many U.S. fruits and vegetables to Chile. Chile has begun to publish its regulations and allow for a public comment period on proposed rules changes. Most import permits are issued on a case-by-case basis, thereby lending to uncertainty and possible discriminatory treatment. Procedures and tolerances for testing imported chicken for the presence of salmonella present such a severe commercial risk that local importers are reluctant to import such products. Chile's unique beef grading and labeling requirements deter the trade from considering the importation of beef cuts from the United States.

Government procurement practices: The government buys locally produced goods only when the conditions of sale (price, delivery times, etc.) are equal to or better than those for equivalent imports. In practice, given that many categories of products are not manufactured in Chile, purchasing decisions by most state-owned companies are made among competing imports. Requests for public and private bids are published in the local newspapers and will soon be published on the Internet.

6. Export Subsidies Policies

Chile offers a few non-market incentives to exporters. For example, paperwork requirements are simplified for nontraditional exporters. The government also provides exporters with quicker returns of VAT paid on inputs than other producers receive. In 1997, Chilean subsidies became the focus of a countervailing duty investigation by the Department of Commerce of Chilean salmon exports to the United States; on June 22, 1998, the countervailing duty determination was found to be negative.

The most widely used indirect subsidy for exports is the simplified duty drawback system for nontraditional exports. This system refunds to exporters of certain products a percentage of the value of their exports, rather than refunding the actual duty paid on imported inputs to production (as is the case in Chile's standard drawback program). All Chilean exporters may also defer tariff payments on capital imports for a period of seven years. If the capital goods are used to produce exported products, deferred duties can be reduced by the ratio of export sales to total sales. If all production is exported, the exporter pays no tariff on capital imports.

In 1998, the Chilean congress replaced earlier forestry-sector subsidy legislation with a new law that will be directed mainly toward assisting small farmers. Planting costs will be subsidized by as much as 90 percent for the first 15 hectares and 75 percent for the remainder in the case of small farmers. A maximum of $15 million dollars yearly will be destined for this purpose. Special land-tax exemptions will also be part of the program. Under the previous law, the combined subsidy costs incurred during 1997 totaled $7.7 million, down from $15.3 million in 1996.

7. Protection of U.S. Intellectual Property

Chile's intellectual property regime is basically strong. However, deficiencies in the intellectual property regime have kept Chile on the USTR Special 301 watch list since 1989. Chile belongs to the World Intellectual Property Organization. In late 1999 the Chilean Government submitted draft legislation to the Congress to attempt to bring Chile into compliance with its WTO TRIPS commitments.

Copyrights: Piracy of video and audio tapes has been subject to criminal penalties since 1985. Chilean authorities have taken enforcement measures against video, video game, audio, and computer software pirates in recent years, and piracy has declined in each of these areas. In the mid-1980s, the software piracy rate was believed to be around 90 percent; it is currently estimated at roughly 55 percent, believed to be the lowest rate in Latin America. The decline is in part the result of a campaign by the U.S. and international industry, with the cooperation of Chile's courts and government, to suppress the use of pirated software. Greater access to authorized dealers and service has also helped to reduce the rate of piracy. Industry sources say that penalties remain low relative to the potential earnings from piracy and that stiffer penalties would help to deter potential pirates. Copyright protection is generally the life of the author plus 50 years.

Trademarks: Chilean law provides for the protection of registered trademarks and prioritizes trademark rights according to filing date. Local use of a trademark is not required for registration. As with the licensing of other intellectual property privileges, contracting parties may freely set payment rates for use of trademarks

8. Worker Rights

a. The Right of Association: Most workers have a right to join unions or to form unions without prior authorization, and around 12 percent of the work force belongs to unions. Government employee associations benefited from legislation in 1995 that gave them many of the same rights as unions, although they may not legally strike. Reforms to the labor code in 1990 removed significant restrictions on the right to strike. Those reforms require that a labor inspector or notary be present when union members vote for a strike. In late 1999, the Government of Chile narrowly failed in pushing through Congress reforms to Chilean labor laws that encouraged greater collective bargaining.

b. The Right to Organize and Bargain Collectively: The climate for collective bargaining has improved, though unions still face difficulties. Sector-wide collective bargaining would be permitted under legislation proposed by the Government of Chile and narrowly defeated in the Chilean Congress. The process for negotiating a formal labor contract is heavily regulated, a vestige of the statist labor policies of the 1960's. However, the law permits (and the Frei government has encouraged) informal union-management discussions to reach collective agreements outside the regulated bargaining process. These agreements have the same force as formal contracts.

c. Prohibition of Forced or Compulsory Labor: Forced or compulsory labor is prohibited in the constitution and the labor code and is not practiced.

d. Minimum Age for Employment of Children: Child labor is regulated by law. Children as young as 14 may be legally employed with permission of parents or guardians and in restricted types of labor. Some children are employed in the informal economy, which is more difficult to regulate. The Chilean government estimates that roughly 50,000 children between the ages of 6 and 14 work. Most of these children work in the countryside, and many of them work with their parents.

e. Acceptable Conditions of Work: Minimum wages, hours of work, and occupational safety and health standards are regulated by law. The legal workweek is 48 hours. The minimum wage, currently around $190.00 per month, is set by government, management, and union representatives or by the government if the three groups cannot reach agreement. Lower-paid workers also receive a family subsidy. The minimum wage and wages as a whole have risen steadily over the last several years. As a result, poverty rates have declined dramatically in recent years from 46 percent of the population in 1987 to 21.7 percent in 1998. Currently 11 percent of salaried workers earn the minimum wage.

f. Rights in Sectors with U.S. Investment: Labor rights in sectors with U.S. investment are the same as those specified above. U.S. companies are involved in virtually every sector of the Chilean economy and are subject to the same laws that apply to their counterparts from Chile and other countries. There are no special districts where different labor laws apply.

Extent of U.S. Investment in Selected Industries -- U.S. Direct Investment Position Abroad on an Historical Cost Basis **--** 1998

(Millions of U.S. Dollars)

Category		Amount
Petroleum		18
Total Manufacturing		845
Food & Kindred Products	162	
Chemicals & Allied Products	294	
Primary & Fabricated Metals	39	
Industrial Machinery and Equipment	14	
Electric & Electronic Equipment	(1)	
Transportation Equipment	(1)	
Other Manufacturing	204	
Wholesale Trade		342
Banking		627
Finance/Insurance/Real Estate		3,429
Services		212
Other Industries		3,659
TOTAL ALL INDUSTRIES		9,132

(1) Suppressed to avoid disclosing data of individual companies.

Source: U.S. Department of Commerce, Bureau of Economic Analysis.