

Declassified in Part - INHERITANCE 25V1
Sanitized Copy Approved for
Release 2011/10/31 : 
CIA-RDP85T00875R00160003


Declassified in Part - 
Sanitized Copy Approved for
Release 2011/10/31 : 
CIA-RDP85T00875R00160003


CIA/DER/IM 70-148 Doc/Ser.

~~Confidential~~

25X1



DIRECTORATE OF
INTELLIGENCE

Intelligence Memorandum

*The Chilean Economy: Allende's Inheritance
And Probable Actions*

~~Confidential~~

ER IM 70-148
October 1970

Copy No. 61

WARNING

This document contains information affecting the national defense of the United States, within the meaning of Title 18, sections 793 and 794, of the US Code, as amended. Its transmission or revelation of its contents to or receipt by an unauthorized person is prohibited by law.

GROUP 1
Excluded from automatic
downgrading and
declassification

CONFIDENTIAL

Foreword

The listing at the end of this memorandum is UNCLASSIFIED and may be removed for more convenient use.

CONFIDENTIAL

25X1

CENTRAL INTELLIGENCE AGENCY
Directorate of Intelligence
October 1970

INTELLIGENCE MEMORANDUM

The Chilean Economy: Allende's Inheritance
And Probable Actions

Introduction

On 24 October the Chilean Congress ratified the electorate's recent minority choice of a Marxist president who has pledged to create a "revolutionary, nationalistic, and socialist society." Scheduled to begin a six-year term on 3 November, Salvador Allende will be working with an economy where private enterprise already is weak and the government's role large. Moreover, Allende's Socialist-Communist coalition will inherit an economy strengthened in recent years by high copper prices and large investments in copper and other foreign-financed development projects. At the same time, the new administration will be confronted with rapidly rising popular expectations, sluggish output growth, a deeply engrained inflation mentality, and an economy badly shaken by the very fact of his election. This memorandum discusses the economy Allende will inherit, those factors favoring achievement of his economic goals, and those that will work against him.

Note: This memorandum was produced solely by CIA. It was prepared by the Office of Economic Research and was coordinated with the Office of Current Intelligence.

CONFIDENTIAL

25X1

CONFIDENTIAL

Chile's Mixed Economy

1. Chile is already a long way down the economic path Allende intends to follow. By almost any measure, the state's economic role is large and has been growing rapidly. Central government revenues equal 27% of gross national product (GNP) -- by far the highest proportion in Latin America, excluding Cuba -- and compulsory social security contributions increase this to more than 35%. Total public sector spending approaches one-half of GNP. Public expenditures make up 80%-85% of total fixed investment.
2. The government employs about 15% of the labor force and participates directly or indirectly in nearly every economic activity. Its role as a commercial producer of goods and services has increased substantially over the last three decades -- particularly during the Frei administration (1964-70), which expanded some state enterprises, created new industries, and nationalized various firms. The state now owns wholly or in part more than 90 enterprises, including most of the country's larger ones (see the attached unclassified listing). It dominates not only electric power, transportation, and communications but also the copper, steel, petroleum, chemical, and cellulose industries. Moreover, the government is the only major domestic source of medium- and long-term industrial credit. Thus, investment during the Frei years has gone mainly into the state-owned industries or into joint ventures with private foreign or domestic capital.
3. Chile's private enterprise system -- already distorted by three decades of rapid inflation and government intervention prior to 1964 -- thus has been further weakened during the six years of Christian Democratic Party (PDC) leadership. Although Frei and his more conservative supporters had hoped to maintain private investment while expanding the state's economic role, his government's policies actually strongly discouraged private initiative. Ever-increasing tax and wage bills squeezed profits, credit for private industrial expansion generally was tight, and investor confidence was eroded by increasingly vocal attacks on the capitalist system by PDC leftists as well as

CONFIDENTIAL

CONFIDENTIAL

openly Marxist forces. As a result, private industry almost certainly suffered net disinvestment in recent years.

Precedent of Frei's Moderate Social Revolution

4. Far-reaching social reform achieved considerable momentum under the Frei government. His administration gave a high priority to income redistribution and expanded social services to lower-income groups. The problem has been that the PDC program unleashed further economic demands and political pressures for radical change, and rapid reform itself had economic costs that limited capabilities. As a result, the gap between expectations and fulfillment widened considerably as Frei's administration neared its end.

5. Although the administration's agrarian reform program* fell far short of its goals, it markedly changed land tenure patterns in some key agricultural areas and had a revolutionary impact on attitudes regarding private property rights. As with industry, Frei failed in his intention to preserve private farmers' investment incentives. Despite his reassurances that efficient producers would not lose their property, the program proceeded as much in a spirit of vengeance as reform. It is doubtful that any sizable landowner without close PDC contacts felt safe from expropriation during the administration's later years. Moreover, implementing agencies have shown a marked preference for socialized agriculture, with the result that most if not all families settled are organized into communal farms.

6. The Christian Democrats did accomplish their basic goal of achieving a social "revolution in liberty," and the Presidential election -- in which two out of three voters chose markedly leftist candidates -- showed that most Chileans are not disposed to turn back. Large segments of the urban and rural poor participated in national life for the first time. Organized into unions,

25X1

CONFIDENTIAL

CONFIDENTIAL

cooperatives, and various community action groups, many were awakened to their economic-political potential. Although the PDC fostered their politicization, it clearly did not gain their full voting support, because social revolution brought political polarization as well. The incoming Allende administration nevertheless can, with some justification, view the 1970 election as a mandate for further and more radical change.

Economic Advantages Accruing to Allende

7. Among other economic advantages, the Allende government is fortuitously assuming power just as the large copper expansion program nears completion.* The largely US-financed program begun in 1967 involves an investment of about \$600 million and will increase the large mines' output from 650,000 short tons to almost one million tons in 1971. It also will more than double refining capacity and permit three-fourths of the expanded mining output to be refined domestically. In 1970, Chilean government tax and equity returns from the large companies' operations probably will be more than double their 1967 level and will average 85% of gross profits. If world copper prices average about 58 cents a pound** and output increases as planned,

* The Gran Minería (the three large mines owned and operated by Anaconda and Kennecott) accounted for 86% of Chilean copper output before their investment program was initiated in 1967. In addition to expanding these three mines and related refining facilities, the program involved opening two new mines -- one by Anaconda and the other by Cerro Corporation.



** Since mid-1966, Chilean copper has been sold at London Metal Exchange (LME) prices which averaged 69 cents a pound in 1966, 51 cents in 1967, 56 cents in 1968, and 67 cents in 1969. After holding strong at 74 cents a pound during the first half of 1970, LME copper prices began to decline and broke below the 50 cents level in mid-October. Despite [footnote continued on p. 5]

25X1
25X1

CONFIDENTIAL

CONFIDENTIAL

the large mines' copper exports will approximate \$1 billion in 1971.

8. Certain other industries are now considerably more developed and better able to meet Chilean needs than when Frei took office. Using its own resources as well as foreign aid, the government substantially expanded such industries as steel, petrochemicals, lumber, paper, and cellulose. Private foreign capital also has been encouraged to enter these fields, sometimes on a joint venture basis, and also to establish automotive assembly plants.

9. Allende will also inherit record-high foreign reserves. Thanks to prolonged high copper prices, foreign assistance receipts averaging nearly \$200 million annually, and capital inflow for copper development, gross reserves rose from \$90 million in 1964 to an estimated \$500 million in October 1970. To be sure, the public foreign debt considerably more than doubled during the same period and now approximates \$1.5 billion, but Allende already has signaled that repayment schedules will not be honored.

Major Economic Weaknesses

10. In deciding on the precise nature and timing of his initiatives, Allende presumably will take some account of other, less favorable economic circumstances. Chile's economic growth recently has been sluggish, averaging little more than 3% during 1967-70. Even without disruptive social change, accelerated growth would be hampered by inadequate investment during the Frei years. Rising public investment has been partly offset by declining private investment, and total investment has declined as a share of GNP. Indeed, by 1969, total fixed investment excluding the foreign-financed copper program was no higher than in 1964 -- itself a low year because of political uncertainties preceding Frei's election.

new additions to mining capacity in Chile and expected elsewhere in 1971, soft copper prices could prove to be temporary.



25X1
25X1

CONFIDENTIAL

11. The Allende government will inherit an economy wracked by rapid inflation -- a problem that has resisted stabilization efforts for more than three decades. The Frei government succeeded in slowing inflation during its first two years. But by 1967 the combination of rapidly rising real wages, greatly increased government spending, excessive monetary expansion, and stagnating output caused price rises to accelerate. Although the official consumer price index registered an average increase of 25% annually during 1967-69, current and constant price measures of private consumption in official national income accounts indicate the rate was nearer 33% -- and this perhaps is still understated. Inflation in 1970 could be considerably more than 40%.

12. The crisis of confidence in Chile since Allende's electoral victory on 4 September may cause serious difficulties for the new administration, at least in the short run. Sharply reduced consumer demand and inventory reduction by apprehensive dealers have caused widespread declines in industrial orders, sales, and production. Despite Chile's highly protective labor legislation, industrial unemployment could rise substantially in the next month or so as a result of bankruptcies. The Frei administration issued large amounts of new currency during the financial panic following the 4 September election to prevent commercial bank failures, and, because of continuing economic deterioration, it printed still more money in early October to cover a shortfall in government revenues and to maintain bank liquidity. The new administration will have to cope with the inflationary impact of massively increased money supply while trying to get the economy moving again.

Allende's Prospective Economic Actions

13. Allende and his Popular Unity Front have left no doubt that their basic goal is to establish a state-controlled socialist economy. The only question is how fast his government will move to eradicate capitalism and restructure Chilean society along socialist lines. Some disagreement is apparent within the Front on the

CONFIDENTIAL

CONFIDENTIAL

timetable and question of compensation for expropriated resources. It is reasonable to assume, however, that Allende will move as quickly as his administration's capabilities permit and offer as little compensation as possible.

14. Spokesmen for the Popular Unity Front say they want to form three broad economic sectors:

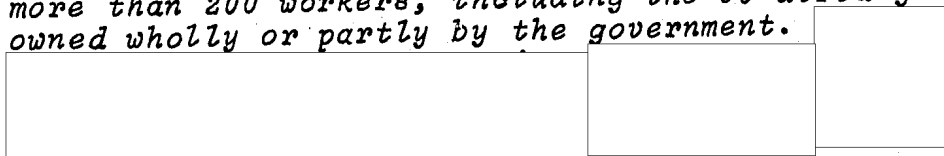
-- A dominant state sector of existing state enterprises and new ones to be expropriated -- notably the large copper, nitrate, iodine, iron ore, and coal mines; financial institutions, especially banks and insurance companies; foreign trade enterprises; marketing organizations; and all other activities that "condition economic and social development" (that is, all sizable producers of goods and services).

-- A private sector consisting of service establishments and other small enterprises, which also will be subject to state planning.

-- A joint state-private sector in which enterprises will give the government equity participation in exchange for loans.

Although Allende has been brandishing a list of some 160 large companies earmarked for early expropriation, he almost certainly will move first against the copper companies and banks.*

** The 160 companies represent a very large share of Chile's private industry, both foreign and domestically owned. A 1967 census indicated that there were only some 300 enterprises with more than 200 workers, including the 90 already owned wholly or partly by the government.*



25X1

25X1

25X1

CONFIDENTIAL

15. The government will face a delicate timing problem in establishing an elaborate state control mechanism. To minimize economic dislocation and avoid coalescing effective political opposition, Allende's administration will want to move promptly -- but not recklessly. Prompt action will be facilitated by the already extensive state apparatus, weaknesses in Chile's capitalist institutions, broad acceptance of socialist ideology, and -- perhaps most important -- the Communist Party's organizational abilities. Nevertheless, despite the intention to establish a planned economy as quickly as possible, Allende's advisers apparently have not yet drawn up detailed blueprints and seem at least temporarily awed by the prospect of assuming government responsibility in the midst of economic difficulties.

16. With few exceptions, Chile has sufficient expertise to operate the companies now wholly or partly foreign-owned. The copper industry, for example, relies largely on Chilean technicians and managers at the mines, and the Allende government should have little trouble in assuming marketing functions. It would have difficulty, however, in maintaining some technologically advanced operations and investment programs in such fields as telecommunications, unless West European and Japanese firms were willing to replace the US companies now involved. In any event, one of the Allende government's most serious problems will be holding onto indigenous skilled manpower. Post-election emigration already has involved some "brain-drain," and Allende apparently has drawn up plans to restrict it.

17. Agrarian reform will be markedly accelerated. Jacques Chonchol, a leading official in Frei's reform program and now a key figure in Allende's coalition, already has drawn up a 20-point program aimed at rapidly completing agriculture's transformation. All remaining large and medium-sized holdings will be expropriated and organized into large collective or state farms, and small farmers will be integrated into collectives or cooperatives. The state or state-controlled collectives will take over marketing. Terror tactics will probably minimize effective

CONFIDENTIAL

CONFIDENTIAL

landowner opposition. Perhaps the major constraint on Allende's agrarian actions will come from peasant groups with kulak tendencies.

18. Allende's counter-inflationary program includes nationalizing all activities required for economic growth and enforcing and expanding an already elaborate price control system even if private profits are squeezed severely. He may also use the orthodox Communist weapon of currency reform to sop up additional purchasing power pumped into the economy before and during the interregnum. Against the backdrop of previous administrations' failures in trying to slow price increases, Allende claims that a "people's government is the only one capable of reducing if not ending the scourge of inflation." But much depends on his budget, credit, and wage policies. Short-term difficulties in achieving price stability will be severe, particularly if the regime is unable to contain workers' demands for higher pay and other benefits expected from an Allende victory. And even in the longer run, unless aggregate supply and demand are brought into reasonable balance, Allende's controls would merely suppress continuing inflation and necessitate rationing, subsidies, multiple exchange rates, and other mechanisms designed to insulate the economy from reality.

CONFIDENTIAL

Productive Enterprises
with Chilean Government Participation

<u>Sector and Enterprise</u>	<u>Percent of Government Ownership</u>
A. Agriculture, Forestry and Hunting	
Servicio de Equipos Mecanizados (SEAM)	100.0
Sociedad Agricola CORFO Ltda. (SACOR)	100.0
Forestal Pilpilco S.A.	100.0
Hacienda Concón Bajo Ltda.	100.0
Industrias Forestales S.A.	50.0
Empresa Nacional de Semillas S.A. (ENDS)	100.0
Forestal Arauco S.A.	N.A.
Forestal Lebu S.A.	N.A.
B. Fishing	
Marco Chilera S.A.I.	84.7
Pesqueras Unidas Horizonte	55.0
Sociedad de Terminales Pesqueros Ltda.	99.7
Compañía Pesquera Arauco S.A.	100.0
Empresa Pesquera Tarapacá S.A.	98.5
Pesquera Coloso	39.8
Pesquera Guanaye	37.9
Pesquera Iquique	49.0
Pesquera Indo	47.4
C. Coal Mining	
Compañía Carbonera Colico Sur	99.9
Compañía Carbonera de Pilpilco	58.5
Compañía Carbonera Victoria de Lebu	99.9
D. Iron Mining	
Compañía de Acero del Pacifico S.A. (mine)	55.1
E. Copper Mining	
Empresa Nacional de Minería (ENAMI)	100.0
Sociedad Minera El Teniente S.A.	51.0
Compañía de Cobre Chuquicamata S.A.	51.0
Compañía de Cobre Salvador S.A.	51.0
Compañía Minera Cerro Negro	77.4

<u>Sector and Enterprise</u>	<u>Percent of Government Ownership</u>
Compañía Minera Chañaral y Taltal S.A.	84.2
Compañía Minera Tamaya	30.0
Empresa Minera de Mantos Blancos	5.7
Compañía Minera Maipú Ltda.	N.A.
Compañía Minera Carolina de Michilla S.A.	25.0
Compañía Minera Loica Ltda.	33.3
Compañía Minera Andina S.A.	30.0
Compañía Minera Exótica S.A.	25.0
Compañía Anónima Cuprífera de Sagasca	25.0
F. Other Mining Activities	
Empresa Minera de Aysén (EMA)	100.0
Empresa Nacional de Petróleo (ENAP)	100.0
Sociedad Geotérmica del Tatío	51.0
Sociedad Química y Minera de Chile S.A. (SOQUIMICH)	37.5
G. Food Products, Beverages & Tobacco Industries	
Pesqueras Unidas Horizonte S.A.	55.0
Marco Chilena S.A.I.	84.7
Industria Azucarera Nacional S.A. (IANSA)	96.6
Sociedad Lechera Nacional Ltda.	100.0
Empresa Pesquera Tarapacá	98.5
Cooperativa Agrícola y Lechera Osorno Ltda. (CALO)	60.0
Cooperativa Agrícola y Lechera Victoria Ltda.	100.0
Pesquera Coloso	39.8
Pesquera Guanaye	37.9
Pesquera Iquique	49.0
Pesquera Indo	47.4
H. Wood Products & Cork, Furniture, Paper & Cellulose	
Papelera del Pacifico	60.0
Impregnadora de Maderas S.A. (IMPREGMA)	76.7
Industria Celulosa Arauco S.A.	60.0
Industria Celulosa Constitución S.A.	66.7

Sector and Enterprise	Percent of Government Ownership
Laminadora de Maderas S.A.	21.7
Maderas y Sintéticos S.A. (MASISA)	17.0
I. Rubber Products, Chemicals, Petrochemicals and Coal Derivatives	
Empresa Nacional de Petróleo (ENAP)	100.0
Fabrica de Acido Sulfúrico S.A. (FASSA)	99.6
Sociedad Chilena de Fertilizantes (SOCHIF)	93.8
Compañía Sudamericana de Fosfatos S.A.	100.0
Petroquímica Chilena S.A.	100.0
Petrodow S.A.	30.0
Química Alquil S.A.	20.0
J. Non-Metallic Minerals, Primary Metals	
Compañía de Acero del Pacífico S.A. (Steel mill)	55.1
Vibrocret S.A.	30.5
Industria Nacional de Cemento S.A.	N.A.
K. Fabricated Metal Products, Non- electrical Machinery, Electrical Gear, Transportation Equipment & Others	
Astilleros y Maestranzas de la Armada (ASMAR)	100.0
Fábrica y Maestranzas del Ejército (FAMAE)	100.0
Maestranza y Fundición Antofagasta S.A.I.C.	100.0
Ransomes Chilena	60.0
Marco Chilena S.A.I.	84.7
Empresa Electrónica Nacional S.A.	80.0
Industria de Conjuntos Mecánicos Aconcaqua S.A.	80.0
Corporación de Radio de Chile S.A.	33.3
L. Construction	
Corporación de Mejoramiento Urbano (CORMU)	100.0
Corporación de Obras Urbanas (COU)	100.0

<u>Sector and Enterprise</u>	<u>Percent of Government Ownership</u>
Corporación de la Vivienda (CORVI)	100.0
Corporación de Servicios Habitacionales (CORHABIT)	100.0
Sociedad Constructora de Establ. Educativas	100.0
Sociedad Constructora de Establ. Hospitalarios	100.0
Sociedad de Construcción y Operaciones Agropecuarias (SOCOAGRO)	100.0
M. Electricity, Gas, Water & Sanitary Services	
Empresa de Agua Potable de Santiago	100.0
Empresa Nacional de Petróleo (ENAP)	100.0
Empresa Nacional de Electricidad (ENDESA)	100.0
N. Transportation	
Empresa Maritima del Estado (EMPREMAR)	100.0
Empresa Transport Colectivo del Estado (ETC)	100.0
Ferrocarriles del Estado (FF.CC.)	100.0
Línea Aérea Nacional (LAN)	100.0
O. Commerce, Warehousing, and Communications	
Empresa Portuaria de Chile (EMPORCHI)	100.0
Empresa Nacional de Frigoríficos (ENAFRI)	100.0
Empresa de Comercio Agrícola	100.0
Empresa Nacional de Telecomunicaciones (ENTEL)	100.0
Compañía Chilena de Teléfonos S.A.	0.3
P. Banking, Insurance and Real Estate	
Instituto de Seguros del Estado (ISE)	100.0
Banco del Estado de Chile	100.0

<u>Sector and Enterprise</u>	<u>Percent of Government Ownership</u>
Q. Servicios	
Estudios Cinematográficos de Chile S.A.	87.1
Hotelera Nacional S.A. (HONSA)	100.0
Empresa Nacional de T.V.	100.0
Empresa de Servicios de Computación (EMCO)	100.0
Sociedad Inmobiliaria de Exposiciones	38.6
Sociedad Inmobiliaria de Portillo S.A.	0.2
Sociedad Inmobiliaria San Cristóbal	48.8