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CHILE

Key Economic Indicators

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

	1998	1999	2000 (proj)
Income, Production and Employment:			
Nominal GDP 1/	73.1	67.7	71.7
Real GDP Growth (pct) 1/	3.9	-1.1	5.6
GDP Growth by Sector (pct) 1/			
Fishing	2.4	1.7	5.0
Agriculture	6.5	-1.3	3.0
Mining	7.4	16.2	4.5
Manufacturing	-1.5	-0.7	7.5
Construction	0.7	1.7	10.0
Services	5.8	-1.2	6.0
Government	1.4	1.4	1.4
Per Capita GDP (US$) 1/	4,900	4,485	4,717
Labor Force (000s) 1/	5,851	5,934	6,000
Unemployment Rate (pct) 1/	6.2	9.0	8.3
Money and Prices (annual percentage growth):			
Money Supply Growth (M2) 1/	19.1	9.1	7.2
Consumer Price Inflation (pct) 1/	4.7	2.3	4.6
Exchange Rate (Peso/US$, annual average) 1/	460	509	540
Balance of Payments and Trade:			
Total Exports FOB 1/	14.9	15.6	18.3
Exports to U.S. 2/	2.5	3.0	3.2
Total Imports CIF 1/	17.4	14.0	16.9
Imports from U.S. 2/	4.0	3.0	3.3
Trade Balance 1/	-2.5	1.6	1.4
Balance with U.S. 2/	-1.5	0.0	0.1
Total External Debt 1/	31.7	34.0	36.0
Private Debt	26.0	28.3	30.4
Public Debt	5.7	5.8	5.6
Fiscal Deficit/GDP (pct) 1/	0.0	1.5	0.5
Current Account Deficit/GDP (pct) 1/	5.7	0.1	2.0
Debt Service Payments/Exports (pct) 1/	21.2	27.7	25.4

Gold and Foreign Exchange Reserves (US$ billions) 1/	15.9	14.7	14.4
Aid from U.S. (US$ millions)	0.3	0.3	0.3
Aid from All Other Sources	N/A	N/A	N/A

1/ Central Bank of Chile.
2/ U.S. Department of Commerce, International Trade Administration Statistics.

1. General Policy Framework

Chile's economy is recovering strongly from the recession it suffered in 1998 and 1999. Growth of 5.6 percent is projected for 2000. Exports are leading this growth while consumer demand has lagged expectations. The official projection of year-end unemployment is 8.3 percent versus 9 percent at year-end 1999. Exports of primary products have strengthened substantially. Rising copper prices have driven a 4-percent increase in the volume of copper exports to a 30-percent rise in their value (copper represents 40 percent of Chile's foreign exchange earnings) and an 18-percent rise in the value of total exports over 1999 figures. Chile's credit rating remains investment grade, and direct foreign investment remains solid and in line with long-term trends (although it is likely to reach only about half of 1999's record levels, which had doubled prior year figures due to large scale mergers and acquisitions). Growth is projected at approximately six percent in 2001 as domestic demand increases and vibrant exports continue. Chile is an active participant in negotiations for the Free Trade Area of the Americas (FTAA), and recently announced the start of bilateral negotiations of a free trade agreement with the United States.

The new government of Ricardo Lagos (March 2000-2006) has continued Chile's policies of macroeconomic stability and export orientation. The calendar year 1999 budget registered 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, austere when considered in the context of 4.6 percent projected inflation. While the Chilean government 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.

In September 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, but has left unemployment in the double-digits for much of 2000, nearly twice the average level seen in the 1990s.

Domestic demand is still depressed, despite recovering much of the ground lost in the recession. Chilean exports have grown 18 percent in the first nine months of 2000 and are expected to remain strong. Commodity prices are expected to continue to rise internationally, boosting the already strong performance of the copper and mining sector. Unemployment should gradually continue to fall from its peak of 11.5 percent in October 1999 to the 8.5 percent range by late-2000. Chile’s current trade surplus should continue in the mid-term based on strong export growth and despite domestic demand recovery. The small current account surplus will, in all likelihood, disappear, and Chile will revert to its traditional deficit; policymakers 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 Central Bank’s short-term interest rate is currently five percent, and the Central Bank is committed to holding it there at least until economic recovery takes hold. Over the last several years, the Central Bank has gradually reduced restrictions on foreign-exchange outflows other than reporting requirements. A legal parallel market operates with rates almost identical to the inter-bank rate.

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 below).

Tax policies: Forty percent of total tax revenues are generated by an 18-percent value-added tax (VAT), which applies to all sales transactions. There is a 9 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 eight percent in 2001, and to fall by one percentage point per year to reach six percent in 2003. 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, with three of the five major ports already privatized. 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, fiscal responsibility and careful debt management over the last decade, the magnitude of foreign debt no longer constitutes a major structural problem. As of October 2000, Chile's public and private foreign debt was $35.7 billion, or 49 percent of GDP (in 1985, the debt-to-GDP ratio was 125 percent). Public-sector debt has remained low the past five years, fluctuating between $5 and $6 billion and representing 7.7 percent of GDP in 2000. 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 2001, the uniform Chilean tariff rate will decline to eight percent and will be reduced by one percentage point per year to reach a rate of six percent in 2003. The uniform rate (9 percent in 2000) 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 2000s 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 nine percent for certain products from member countries of the Latin American Integration Association (ALADI). In December 2000, Chile and the United States announced the beginning of negotiations for a bilateral U.S.-Chile Free Trade Agreement.

The 18 percent VAT is applied to the CIF value of imported products plus the 9 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 below). There is an additional luxury tax of 85 percent on the CIF value of automobiles in excess of $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 by March 2001. The United States 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 (DL) 600, sets the standard of treatment of foreign investors to be the same as that of Chilean investors. DL 600 investment is generally direct investment. 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. In May 2000 the Central Bank eliminated the one-year residency requirement on capital entered under Chapter 14, which consists essentially of portfolio investment.

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 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.

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.

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 nine percent tariff to bring import prices up to an average of international prices over previous years. Domestic flour millers and beverage manufacturers continue to complain bitterly about the high duties on wheat and sugar. Imports of U.S. wheat are expected to be down in 2000.

Sanitary and phytosanitary requirements: Chile has improved its recognition of pest-free areas in the United States, but delays on export approval for many U.S. fruits and vegetables continue to hamper increased sales to Chile. On a positive note, Chile recently granted market access for California avocados and walnuts. Chile has begun to publish its regulations and, in some cases, allows a public comment period on proposed rules. 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 effectively preclude imports of U.S. beef. Chile's livestock products law requires first-hand Chilean inspection of every U.S. establishment wishing to export to Chile. Products affected include red meat, dairy and pet food. Chile's recent rule on imported salmonid eggs requires a 60-day pre-notification period followed by a 120-day quarantine, severely deterring imports 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 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.

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 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. Legislation intended to bring Chile into compliance with its WTO TRIPS commitments is pending in the Chilean Congress.

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 50 percent, believed to be the lowest rate in Latin America. The decline is in part the result of a campaign by the United States and international industry, with the cooperation of Chile's courts and government, to suppress the use of pirated software. 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.

b. *The Right to Organize and Bargain Collectively:* During the last decade, the climate for collective bargaining has improved, though unions still face difficulties. Sector-wide collective bargaining is not allowed. The process for negotiating a formal labor contract is heavily regulated, a vestige of the statist labor policies of the 1960s. However, the law permits 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 15 to 18 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. The majority of these were males from single-parent households headed by women.

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 $175 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 ten years (except for 1999). Poverty rates have declined dramatically from 46 percent of the population in 1987 to 21.7 percent in 1998. In a 1999 government survey of 1,247 companies and 79,532 workers, 45.3 percent of the workers earned less than two minimum wages. Only one third of the workers stated they had received wage increases in 1999 versus 47 percent in 1998.

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—1999

(Millions of U.S. dollars)

Category		Amount
Petroleum		33
Total Manufacturing		1,323
Food & Kindred Products	192	
Chemicals & Allied Products	231	
Primary & Fabricated Metals	(1)	
Industrial Machinery and Equipment	20	
Electric & Electronic Equipment	(1)	
Transportation Equipment	(1)	
Other Manufacturing	195	
Wholesale Trade		365
Banking		656
Finance/Insurance/Real Estate		3,404
Services		211
Other Industries		3,893
TOTAL ALL INDUSTRIES		9,886

(1) Suppressed to avoid disclosing data of individual companies.
Source: U.S. Department of Commerce, Bureau of Economic Analysis.