

# The Not-So-Boring Political Economy of Trade Policy in Chile

Nicolás Albertoni, Dorotea López, Milenka Montt, Felipe Muñoz, and Andrés Rebolledo

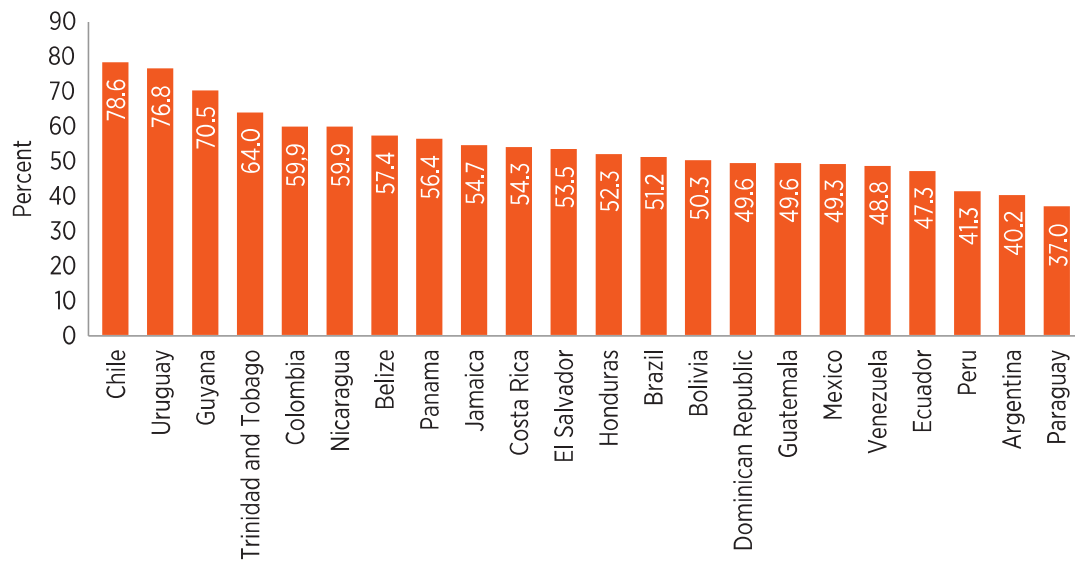
Chile's trade policy has been very active for the last 25 years, including implementing an open-economy strategy that adequately complemented unilateral instruments and conducting multilateral and bilateral trade negotiations, with the latter being fundamental to inserting the country into international markets and promoting growth and economic development.

Today Chile is among the countries in the world with the most extensive networks of trade agreements, with 26 in force with 64 countries that account for nearly two-thirds of the world population. The agreements cover more than 90 percent of Chile's foreign trade and almost 100 percent of its investment flows, which means that Chile has negotiated trade agreements with countries that account for 90 percent of GDP worldwide.

This result dates to a critical juncture in Chile's history: the end of the dictatorship and the beginning of democracy in the early 1990s. Although the trade policy at the time could have headed in different directions, including a reversal, it was decided to continue liberalizing policies that had begun in the 1970s and to resume historical ties with Chile's neighbors in the region and with the international community. The trade agreements, especially those signed with the Latin American countries, were conceived as the most appropriate way to resume international relations, which had been suspended or diminished during the 17 years of military government, and to bring more opportunities for Chilean products and services in international markets and greater liberalization of its local market.

This process of opening involved important productive and social adjustments that affected productive sectors that had to adapt, with the consequent political and economic challenges. The winning sectors that

**Figure 4.1**  
**Support for Free Trade Agreements in Latin America and the Caribbean, 2017 (percent)**



Source: Prepared by the authors based on data from the Latin American Public Opinion Project.

began to export became allies and drivers of greater trade opening. The consensus in Chile on these agreements is much greater than in other countries of Latin America and the Caribbean (over 80 percent, compared to the 53 percent regional average) (Figure 4.1), and it includes unexpected actors: labor unions as well as manufacturing industries that compete with imports.

The main hypothesis of this chapter is that Chile has succeeded in liberalizing trade policy for two main reasons:

1. The economic success associated with the trade opening implemented during the dictatorship brought about a change in the winning and losing economic sectors that facilitated greater openness within the framework of the free trade agreements (FTA). In addition, the experience of political actors in exile (in social democratic countries) who led the country after 1991 contributed to the continuity of trade policy in the democracy.
2. The partners with whom FTAs were negotiated were always more protected than Chile, so the relative gain of the opening was much more attractive for Chile. In addition, the opening was based on a strong institutional structure, with the accumulation of negotiating skills in both

the public and private sectors. The use of compensation mechanisms for the losers, especially in the agricultural sector, was very relevant.

The main research question for this chapter is, what are the main elements that explain why Chile implemented a consistent trade liberalization policy, especially in the period after the return to democracy? To drill down into this question, the chapter will examine the role of Chile's textile and footwear sector, Price Band System, and labor unions in the Chile-U.S. free trade agreement.

## 4.1. A Brief History of Chile's Trade Policy

### 4.1.1. Chilean Trade Policy, 1973–1990: Economic Liberalization

In the 1970s, Chile was not an exception among Latin American countries, pursuing like others a strategy of import-substitution industrialization. The strategy was based on the thesis of Raúl Prebisch and Hans Singer in which the economic goal behind import-substitution industrialization policies was to shift the imbalanced fixed structure of global trade under which poor countries exported primary commodities to the rich countries, which then manufactured products from those commodities and sold them back to the poorer countries. Chile's import-substitution industrialization policy toolbox included high tariffs and heavily regulated trade (tariffs averaged 105 percent and were highly dispersed).

The main difference between Chile and the other Latin American countries was that in the mid-1970s, under the dictatorship of Augusto Pinochet, Chile changed its development strategy from import-substitution industrialization policies to an open trade regime (export-oriented strategy). More specifically, in 1974, tariffs were slashed and replaced by a uniform and significantly lower tariff. Protectionist measures were significantly reduced, which was an important incentive to increase imports and exports. Between 1974 and 1981, exports of fruit, timber, and fish products grew to equal exports of copper in value.

In sum, starting in 1974, Chile unilaterally adopted an open trade regime characterized by low uniform import tariffs, a lack of exchange controls, and minimum restrictions on capital movements. By 1979, Chile's trade policy had become highly liberalized. A 10 percent uniform import tariff took effect.

Chile persisted with its policies in the 1980s. After a brief increase to 15 percent in 1982, the uniform tariff fell back to 11 percent. One of the effects of that liberalization was lowered cost of imported agricultural inputs and capital goods, which allowed the agricultural sector to become more competitive internationally.

### 4.1.2. Chilean Trade Policy, 1991 to the Present: Consolidation and Modernization

This second period was marked by the return to democracy in Chile. In this period of transition, the country faced a critical juncture when it was decided to continue the policy of opening, as will be discussed in detail in the next section of this chapter. By the early 1990s, exports had become the main source of economic growth, and the Chilean trade reform was winning praise from multilateral institutions and analysts of different ideological persuasions. Largely because of the boom in exports between 1986 and 1991, particularly the increasing growth in exports of fresh fruits and manufactured products, Chile experienced the highest rate of GDP growth in Latin America, with an annual increase of 4.2 percent.

The first democratic president, Patricio Aylwin (1990–1994), elected in December 1989, maintained most of Pinochet's foreign trade policies. This permitted Chile to enter into bilateral FTAs with several member countries of the Southern Cone Common Market (MERCOSUR) (Colombia, Ecuador, and Venezuela) and Canada. Aylwin decided to continue the liberalization process, and it was his administration that reduced import tariffs to a uniform 11 percent instead of 15 percent. Later, this tariff was dropped to 6 percent, and today it is 0.6 percent as a result of the trade agreement network.

In January 1995, Chile became a member of the World Trade Organization (it had been a contracting party to the 1947 General Agreement on Trade and Tariffs since March 16, 1949). This provided an international framework where Chile could start international trade expansion. First, Chile initiated its process of international trade negotiations through preferential trade agreements within the framework of the Latin American Integration Association (ALADI).

Between 2000 and 2003, the main step in Chile's trade policy was the negotiation and signing of an FTA with the United States and the European Union. This occurred within a democratic context, when Chile began to confirm politically that it needed trade openness to grow. An example is the Congress approving a bill in 1998 that lowered Chile's across-the-board import tariff (for countries with which it had no trade agreement) by a percentage point each year from 1999 until 2003. In November 2002, Chile signed an agreement with the European Union and in June 2003 with the United States. Two additional important agreements at the time were the FTAs with the European Free Trade Association (EFTA) and the Republic of Korea, both signed in 2003.

The period from 2003 to 2018 was marked by the negotiations of agreements with Asian countries, the consolidation of trade relations with Latin American countries, and Chile's participation in plurilateral negotiations.

Another relevant milestone in this subperiod was the creation of the Pacific Alliance in 2014.

## 4.2. The Institutional Framework behind Chile's Trade Policy

### 4.2.1. Public Institutions

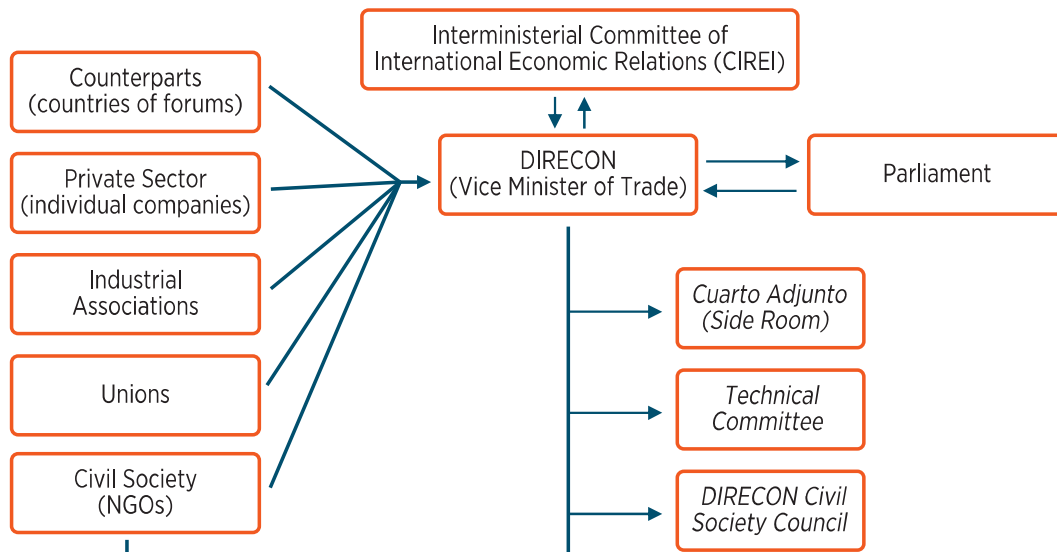
#### *Directorate General for International Economic Relations (DIRECON), Ministry of Foreign Affairs*

DIRECON was created on January 10, 1979, through Decree Law No. 53. It is a public entity under the Ministry of Foreign Affairs whose purpose is to implement and coordinate the policy formulated by the President of the Republic in terms of economic relations with the outside world, including collaboration with development of the country's exports.<sup>1</sup>

The Minister of Foreign Affairs and the Minister of Finance jointly appoint the head of this institution, which means there is a formal arrangement of double guardianship. This type of appointment shows the necessary relationship that must exist so that internal agreements can be reached. The trade policy ultimately is a combination of foreign and economic policy.

**Figure 4.2**

#### Trade Policy: Roles of the Directorate General for International Economic Relations (DIRECON)



Source: Prepared by the authors.

<sup>1</sup> DIRECON has 54 offices located in 45 countries.

DIRECON began to become a more socially and politically relevant actor in the negotiations with MERCOSUR and Canada. As a consequence, DIRECON took on greater importance in the growing social and political legitimacy of Chilean political constituencies and society. It was this feature that afforded it undisputed leadership in the conduct of trade policy in Chile.

### *The Trade Negotiations Committee*

The Interministerial Committee of International Economic Relations was created by Decree No. 419 of the Ministry of Foreign Affairs published on May 10, 1995. Its purpose was to advise on and make proposals to the President of the Republic regarding specific policies related to international economic negotiations. The committee is composed of the Minister of Foreign Affairs, who presides over it, the Minister of Finance, the Minister Secretary General of the Presidency, the Minister of Economy, Development, and Reconstruction, DIRECON (which acts as Executive Secretary), and other ministers when negotiations involve matters related to their competencies. The committee may also invite public officials, experts, academics, or representatives of the private sector related to the matters in question.

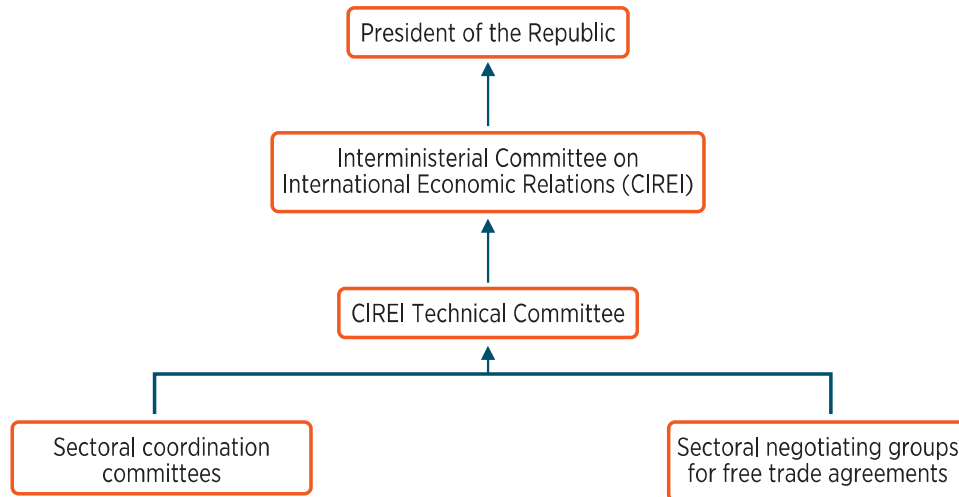
This committee is composed of two entities: a level of ministers and a technical committee chaired by the DIRECON General Director that summons the representatives the ministers call upon. An important element is that the representatives of the ministers on the technical committee do not need to have a formal position within the structure of the ministries (advisors with high decision-making capacity and political power).

There is a formal institutional link between these two subentities, since the general director of DIRECON is in turn the executive secretary of the inter-ministerial committee (at the ministerial level), which is why he reports on the progress and pending resolutions of the technical committee.

If no agreement is reached in the technical negotiation groups, the issue is raised to the Technical Committee of the Interministerial Committee on International Economic Relations (CIREI) for resolution (Figure 4.3). If this entity does not resolve the conflict between the positions of the different ministries or public agencies, the topic scales up to be addressed by the CIREI-Ministerial Committee. On the few occasions when the internal conflict has not been resolved at this ministerial level, it has been necessary that it be taken to the President of the Republic.

### *The National Congress*

In Chile, the role of the Congress is limited to the approval or rejection of international agreements signed by the government, without the right to modify

**Figure 4.3****Interministerial Committee on International Economic Relations (CIRED)  
Decision-Making Process**

Source: Prepared by the authors.

the content (Article 54, No. 1 of the Political Constitution of Chile). However, the influence of Congress on the country's trade policy is important, since governments always take into consideration the internal political viability of the treaties and internalize the preferences of members of Congress during the negotiations and in the process of discussing the treaty in order to ensure its approval. In fact, in the case of the MERCOSUR agreement, the compensations that the government implemented for the losing agricultural sectors is evidence of the importance of the Congress in trade policy.

All of the above has meant that processes of discussion of FTAs in Congress, in general, have been relatively comfortable, without many difficulties and with positive results in terms of the approval of agreements with broad majorities. (It should be noted, however, that this situation has been changing in recent years due to a new political force with representation in Congress that has an anti-trade perspective.) Table 4.1 shows the results of the voting on the main FTAs in the two chambers of the Congress.

In the course of the negotiations of Chile's network of trade agreements, a turning point in discussions with Congress was Chile's agreement with MERCOSUR. Despite being an agreement within the framework of the ALADI that legally did not require approval by Congress, the government decided to send the proposal for discussion and approval in Congress.

Obtaining approval from Congress on the agreement with MERCOSUR was complex because of the sensitivities of the agricultural sector and the

**Table 4.1**  
**Free Trade Agreements and Congress**

Agreement/Year	Votes in Low Chamber			Votes in Senate		
	In Favor	Against	Abstentions	In Favor	Against	Abstentions
MERCOSUR, 1996	74	26	3	36	3	1
European Union, 2002	107	3	1	41	1	1
Canada, 1997	78	21	10	34	6	3
United States, 2004	87	8	8	34	0	0
China, 2006	96	1	3	31	0	0

Source: Prepared by the authors based on information from [www.camara.cl](http://www.camara.cl), [www.senado.cl](http://www.senado.cl), and [www.bcn.cl](http://www.bcn.cl).

overrepresentation of the sector in the Congress. To gain approval, it was necessary to develop and commit to a support plan for the country's agriculture sector that, although not explicitly described as a compensation program, in practice operated as such.

Another milestone in the role of Congress in the approval of trade agreements was the FTA with the United States, which was the first agreement of much greater complexity that was negotiated in Chile. For this reason, it was agreed jointly between the government and the main congressional leaders to create a single, ad hoc commission composed of parliamentarians from the Chamber of Deputies and the Senate for discussion of all the issues involved.

#### 4.2.2. Main Actors of the Private Sector

It is important to point out that the definition of the private sector that was involved with trade policy and negotiations of the FTAs evolved over time, becoming broader and more complex as the thematic coverage of the FTAs widened. As explained in Estevadeordal and Robert (2001), "The expansion of what is traditionally understood by the private sector must be noted. Indeed, the inclusion of chapters on cross-border trade in services, investments, intellectual property, among other issues, requires the integration and consultation of representatives of activities that were previously mere observers of trade negotiations. Thus, for example, a chapter on services requires consultation with all professional associations."

The private sector also shared the advantages of Chile's free trade approach, even sectors traditionally reluctant to support trade liberalization, such as the textile and footwear sector.



An interesting aspect that came up in interviews for this chapter with leaders of business associations is the value assigned to establishing associations with broad representation of different productive sectors, thus avoiding atomization in representation and facilitating the dialogue with the government. (An example is ASOEX, which in Chile represents the entire fresh fruit export sector.) Such associations understand the role of the government in many functions of trade policy, as in the case, for example, of the phytosanitary area, which is fundamental for the international competitiveness of food sectors that are important to Chile's exports.

In contrast, during the 1980s, negotiations in Latin America focused on sectors where there was no local production, since the import-substitution approach still prevailed. In addition, before the 1990s, private representatives were members of official delegations and therefore participated in the official negotiating meetings. This approach changed with more governments became democratic, which meant that although the private sector was consulted, it was no longer part of official negotiating teams.

In Chile, in 1990, which marked the beginning of the broadest and most complex trade negotiations, teams of professionals were reinforced and other technical specialties that did not previously exist in institutions were incorporated into the negotiations, which contributed to the government taking leadership of the process.

In the case of the negotiation processes for FTAs, the private sector understood that it was necessary to reach a consensus-based national position, so private sector representatives accompanied the government and even occasionally collaborated with their public and private counterparts to address complex positions during the negotiation process. To the extent that the FTAs were successful for Chilean exporters, it was the private sector itself that encouraged and promoted the following negotiations.

### ***Cuarto Adjunto (Side Room)***

After the negotiation of the FTA signed between Chile and Korea, DIRECON implemented the participation mechanism called the "Side Room," which was originally composed of representatives of producer business associations and exporters of goods and services. This instrument has been fundamental to communicate progress of negotiations as well as to develop the consensus that allows for configuring national positions in the negotiations. This entity has been very active in recent years, even accompanying official teams during rounds of negotiations.

Starting in March 2014, at the beginning the second presidential term of Michelle Bachelet and during the last stage of negotiations on the Trans-Pacific Partnership (TPP), there was growing demand from the public for

information about the negotiations. A new, expanded version of the Side Room was implemented that was made up of representatives of nongovernmental organizations (NGOs), trade unions, academic institutions, and representatives of business associations, who were able to participate in specific aspects of the TPP negotiations. Subsequently, this entity was replicated for other negotiation processes of interest. It continuously developed and provided updated information on a specific website, highlighting the Trade in Services Agreement, modernization processes of bilateral agreements, and, more recently, the European Union and Pacific Alliance with Associated States. In short, the Side Room has served as an open space for information and discussion with civil society and the private sector about ongoing trade negotiations. As it has evolved, the Side Room is now made up of representatives from trade unions and associations, civil society, industry associations, producers and exporters, NGOs, foundations, small and medium-sized enterprises, academic institutions, and any other group that expresses its interest to the DIRECON negotiating teams within the framework of FTA negotiations.

A web platform has been created that contains information about the negotiation processes, including national negotiating positions (offers presented by Chile), a calendar of negotiation rounds, and reports of each negotiation round.<sup>2</sup> The minutes of discussions in Side Room meetings are also published.

### **4.2.3. Main Civil Society Actors**

During the first years of democracy, NGOs were oriented to domestic social and political issues and less to negotiations of trade agreements. NGOs became more vocal in their views during the process of negotiating the FTA with the United States and the European Union, expressing apprehensions about the benefits of trade agreements, with a particular concern about environmental issues.

Today there is more interest than ever on matters of trade and growing demands for more transparency and engagement entities. Behind this interest is an increasing distrust in the objectives and future results of current trade policies and agreements, and widespread awareness that these policies and agreements have impacts on the lives of people and the development of their countries.

In specific terms, today's FTAs and regional agreements are evolving beyond traditional disciplines, including next-generation issues that have begun to attract greater levels of public interest. In some instances, stakeholders have taken critical or defensive stances on issues such as the environment, health, intellectual property, and e-commerce, among others. One of the main problems related to this is the lack of access to information during the

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<sup>2</sup> The website is available at <https://www.direcon.gob.cl/cuarto-adjunto/>.

processes of trade negotiations. The configuration of new trade agreements has been characterized by what may be perceived as strict confidentiality in its negotiation processes. However, this may be in contrast with the need to provide greater transparency and information to domestic stakeholders and better communicate trade contents that are relevant for the common interest.

Providing greater transparency and enforcing communication channels is also essential to attain wider support for ongoing trade initiatives and new commitments, ensuring that these are widely beneficial for parties.

### 4.3. The Process of Negotiation and Interaction between Actors in the Decision-Making Process for Chile's Trade Policy

Table 4.2 systematizes what has been developed in the previous points and summarizes the main mechanisms through which institutional actors intervene and influence the development and implementation of the trade policy of Chile.

#### 4.3.1. Return to Democracy: Critical Juncture for Trade Policy

With the return of democracy, it was decided to apply a policy of continuity in trade liberalization, even deepening liberalization through multiple negotiations of FTAs based on the following concerns and developments, as discussed below.

**Table 4.2**  
**Institutional Actors in Trade Policy**

Actors	Main Objective	Channel of Influence	Instruments
<b>Executive</b>			
Directorate General for International Economic Relations (DIRECON)	Conduct trade policy	Press, executive, social media, congress	Publications, seminars, digital platforms, official minutes
Ministries and public services	Represent sectoral interests	Press, executive, social media, Congress	Publications, seminars, digital platforms, official minutes
Inter-ministerial Committee on International Economic Relations	Reach consensus on Chile's position on trade policy	Executive	Official minutes
<b>Legislation</b>			
Congress	Discuss and approve/reject trade agreements	Press, social media, Congress	Publications, digital platforms

*(continue on next page)*

**Table 4.2** (continued)**Institutional Actors in Trade Policy**

Actors	Main Objective	Channel of Influence	Instruments
<b>Private Sector</b>			
Industry associations (SOFOFA, ASOEX, ASILFA, CHILETEC, etc.)	Represent sectoral interests	Press, executive, social media, Congress	Ads, publications, seminars, lobbying, digital platforms
Chambers of Commerce	Represent sectoral interests	Press, executive, social media, Congress	Ads, publications, seminars, lobbying, digital platforms
<b>Other Stakeholders</b>			
Think tanks, academia, and NGOs	Participate in the negotiation process to influence the process in accordance with their interests	Press, executive, social media, Congress	Publications, seminars, lobbying, digital platforms, demonstrations, rallies
Civil society – Cuarto Adjunto	Channel the visions of its members	Executive	Official minutes
Consumer associations	Represent the interests of consumers	Press, executive, social media, Congress	Ads, publications, seminars, lobbying, digital platforms
<b>Counterparts from other countries</b>	Reach a convenient trade agreements	Press, executive	Official minutes
<b>Multilateral organizations</b>	Negotiate global trade rules	Press, executive	Official minutes, publications, seminars, digital platforms

Source: Prepared by the authors.

Note: “Digital platforms” refers to instruments such as Twitter, Facebook, Instagram, etc.

**Concern about Economic Performance**

The political and technical leaders responsible for developing trade policy during the first democratic government in 1990 paid special attention to the signals sent by the economic agenda. There was a conviction among those in charge of the process that the new government of President Aylwin would not be evaluated by his national reconciliation efforts, nor by advances in the respect of human rights, nor by social policies, as the public trusted that all of these issues would be addressed. However, there was uncertainty about economic issues such as what policies the new government would put in place. This was an area that citizens would pay particular attention to given

that the Pinochet dictatorship had set a good standard with its economic performance following the 1982 crisis against which the performance of the new coalition government would be measured.

Moreover, some political parties in the new coalition had been active supporters of the government of President Salvador Allende, which had faced big economic difficulties. Some of the interviewees for this chapter who were protagonists during the period of the new democratic government said they believed at the time that strategic economic decisions would be fundamental to determining the governability and continuity of the political coalition.

### *Ideological Changes and Correlation of Forces*

#### *Political Primacy of the Christian Democratic Party at the Beginning of the Democratic Transition*

One strategic political decision of the new government was that Chile would not go back to an import-substitution model, even among members of the government who had been involved in that model but would later become ministers close to President Aylwin. There was a strong presence of the Christian Democratic Party compared to left-wing parties that had just become legal again after the end of the dictatorship.

Alejandro Foxley, who was the Finance Minister of President Aylwin, said in an interview with a magazine of the time:

“Pinochet made the most important transformation of the Chilean economy in this century. He had the merit of anticipating the process of globalization that occurred a decade later, which all countries of the world were trying to incorporate. We must recognize his visionary capacity and that of the team of economists who entered that government in the 1973, with Sergio de Castro at the head....That is a historic contribution that will last for many decades in Chile and that, for those who were critical of some aspects of that process at the time, today recognize as a process of historical importance for Chile that has ended up being accepted practically by all sectors.”

#### *Socialist Renewal*

Another reason for the continuity of the economic and trade policies from the Pinochet regime was the renewed thinking of new political leaders who had been living in exile in Europe, which was already integrated with open markets under social democratic models in contexts of open economies. They understood that that model that could be reproduced in Chile

In this context, maintaining and deepening the opening of the economy to the world was a fundamental element of the policy of continuity of central aspects of the economic model. There was a conviction that Chile was doing well with the opening of its economy, so it was appropriate to maintain this policy.

### *Readjustment of Productive Sectors*

#### *Winners*

After the 1982 crisis, important export promotion measures were implemented, and there was a second export boom in the context of a depreciated exchange rate and public policies of incentives for non-traditional exports. In other words, this promotion of exports together with the opening of the economy made for growth and even created new export sectors that became new players in the private sector with influence on the authorities and an interest in maintaining access to cheap inputs and opening external markets via negotiations of trade agreements.

Tables 4.3 and 4.4 show the sectors that stood out as winners of this opening process both in the second part of the 1980s and during the 1990s, when the opening was deepened. These sectors coincide with some of the most active and main drivers of the opening and of negotiations of trade agreements.

#### *A Losing Sector: The Automotive Industry*

Some sectors lost competitiveness and disappeared from Chile as a result of the opening, so by the time they would have the opportunity to exert

**Table 4.3**  
**Exports of Goods, 1984–1989 (in millions of U.S. dollars)**

Product	1984	1985	1986	1987	1988	1989
Fresh fruit	293.6	357.3	478.9	608.5	586.2	544.4
Fresh fish	37.5	49.1	69.9	114.4	168.7	216.2
Fish flour	275.5	279.0	315.1	362.5	458.8	507.0
Canned fish	39.6	41.0	75.0	109.5	108.2	116.8
Canned fruit	15.2	16.2	27.8	34.2	47.7	75.3
Dried fruit	10.0	13.8	22.3	31.7	32.6	38.9
Bottled wine	7.2	8.5	10.3	13.9	17.9	28.2
Wood	116.3	112.0	135.0	217.3	310.8	350.8
Paper and cellulose	259.6	210.4	272.4	365.2	417.1	422.5
<b>Total exports of goods</b>	<b>3,650.6</b>	<b>3,804.1</b>	<b>4,191.2</b>	<b>5,302.5</b>	<b>7,054.1</b>	<b>8,078.4</b>

Source: Banco Central de Chile (1999).

**Table 4.4**  
**Exports of Goods, 1990–1998 (in millions of U.S. dollars)**

Product	1990	1991	1992	1993	1994	1995	1996	1997	1998
Mining	4,639.5	4,412.0	4,723.5	3,976.0	5,191.5	7,850.1	7,324.0	8,131.5	6,504.4
Fruit sector	756.7	984.1	1,005.0	869.5	975.9	1,172.4	1,266.1	1,283.6	1,261.3
Fish flour	379.7	464.6	538.4	363.7	449.2	627.7	608.3	549.6	345.8
Salmon	98.6	136.6	216.5	224.4	250.2	377.6	392.4	469.0	515.6
Drinks and tobacco	83.1	118.9	162.5	166.5	182.5	219.4	342.0	466.2	583.2
Celulose paper	423.2	445.6	684.4	617.1	923.6	1,542.2	1,008.9	967.9	972.0
<b>Total exports of goods</b>	<b>8,372.7</b>	<b>8,941.5</b>	<b>10,007.4</b>	<b>9,198.7</b>	<b>11,604.1</b>	<b>16,024.2</b>	<b>15,404.8</b>	<b>16,663.3</b>	<b>14,829.6</b>

Source: Banco Central de Chile (1999).

pressure for a reversal policy during the democratic transition, they were already gone.

One sector that lost with the opening of the Chilean economy was the automotive industry. The industry had an important presence in the local economy for almost 40 years, especially in certain regions of the country. However, many international companies closed their production plants during the 1970s and 1980. There was a time when companies such as Citroën, Ford, Fiat, Peugeot, Renault, Mini, and General Motors had assembly plants in Chile, but one by one they closed (Table 4.5).

### ***Free Trade Agreements: The Joining of Trade and Foreign Policy***

Accessing more markets under better conditions became a priority of the democratic government in order to diversify and provide incentives for the export sector to continue to expand. This put the export sector at the center of the economic growth, which led to a structural change in the country in terms of developing an export culture.

The Aylwin administration considered that an economy open to the world would have two great benefits: first, it would lead Chile to reinsert itself in markets and gain competitiveness of its products; and, second, it would improve the image of the country internationally. Both of these axes had been damaged during the dictatorship. It was necessary for Chile to reinsert itself in the international context in order to re-establish an economic, political, and socio-cultural exchange with the rest of the world after 17 years of ostracism (Cuellar 2013).

**Table 4.5**  
**Closing Year of International Automobile Production Companies in Chile**

Company	Plant Location	Closing Year of Production
Mini	Arica	1974
Ford	Arica y Casablanca	1975
Peugeot	Arica	1979
Citroën	Arica	1982
Fiat	Rancagua	1983
Renault	Arica, Los Andes	1991, 2004
General Motors	Arica	2008

*Source:* Prepared by the authors.

However, the opening of the economy in 1990 was done differently, negotiated within the framework of trade agreements so that the opening would be rewarded by markets open to Chilean exports—that is to say, a “reciprocal opening.” This is how a long history of trade negotiations began during the decade that focused on agreements with the countries of Latin America. This policy of international insertion, called “open regionalism,” was developed mainly by the Economic Commission on Latin America and the Caribbean (ECLAC) by several professionals who later became involved in the new Chilean government.

The trade agreements signed in the 1990s were also a foreign policy tool and the main instrument used in what was conceived as a return to the international community after 17 years.<sup>3</sup> One interpretation of the tariff reduction and opening of the economy that took place in the second half of the 1970s and into the 1980s comes from the interview with C. Mladinic: “It was carried out unilaterally because there was no other alternative given Chile’s isolation during the dictatorship. He [Pinochet] had no alternative, the conviction was to open up and that was the feasible modality.”

In short, it was in the 1990s that the foundations were laid for the trade policy model that Chile has today. As Ffrench-Davis (2018) explains, the decade “marked a new era for Chilean commercial insertion. The export dynamism was stimulated by a more integral policy that sought to combine the functioning of an open economy and the advance of processes of economic integration and trade liberalization, first with Latin America and then with various developed countries and other regions. All this was done in a context characterized by high internal investment and rising productivity.”

<sup>3</sup> Pinochet had traveled abroad only rarely.



## *Gap in Tariff Level*

The negotiations of Chile's FTAs were always asymmetric in terms of the degree of protection and tariff levels. Given the process of opening the Chilean economy, the partners with which the country negotiated always had an average tariff higher than that of Chile. That is, the relative concession of the partners was higher than that conceded by Chile (without considering relative market sizes). This situation helped certain sensitive sectors in Chile see an opportunity to increase their exports and be available to open the domestic market to foreign competition.

The fact that Chile was a market that was already open when it began its trade negotiations facilitated those negotiations and the concessions and tariff reductions that were granted to partner countries, while the gains obtained were relatively higher given the high level of protection of those markets. The more agreements that Chile signed, the more the tariff gap with partners was accentuated.

## *Institutional Aspects*

### *Primacy of the Economists*

Several interviewees for this chapter highlighted the importance of economists in the handling of the Chilean economy since 1990. Before 1990, the critique by economists opposed to the model installed by the Pinochet government questioned what they perceived as its naïve belief in the unregulated free market and the passivity of the state in the economy. In addition, they criticized the absence of a global conception of the development of the country. However, over time there was an important shift among opposing politicians and economists that would become fundamental for the consolidation of the economic model inherited from Pinochet. The economic and political debacle of the USSR and the countries of Eastern Europe prompted a profound reflection by Chile's leftist parties. Bureaucratic socialism ceased to be a reference point and market economies were once again viewed positively. Consequently, the concern for economic efficiency and the role of markets became incorporated into the thinking of the traditional left.

For the economists who came to occupy a fundamental role in programmatic processes in the new government, it was essential to resume growth and reduce macroeconomic vulnerability. This came from a sort of Neo-Keynesian consensus that implied a consensus to avoid past mistakes in episodes such as hyperinflation. That is, the priority was to keep the national accounts in order and at the same time design policies that encouraged entrepreneurs to export. There were reasons for their concern; inflation was at 20 percent when

the Aylwin administration took office, on top of high government external debt of 50 percent of GDP. Therefore, ensuring a period of economic expansion would allow wages to rise, generate jobs, and improve the quality of life.

The group of economists who came from ECLAC and who began developing the policy of open regionalism in the late 1980s postulated a combination of unilateral openness with trade agreements. In addition, the economists who had been working with the consensus had developed the conviction that growth in Chile was going to come through the export boom, and that this boom required a much more open economy.

Many economists trained at U.S. universities who began to take increasing leadership positions in Chile determined the nature of the transition. One of the milestones that marked the commitment of the model was maintaining an autonomous central bank, which was one of the most important institutional decisions. Another contributing factor to maintaining the open model was that economists from the Latin American Institute of Transnational Studies (ILET) did not question economic policy at the international level, that is, economic openness. This model was understood not just as pure liberalism, but also as having a social economic priority.

### *Constitutional Restrictions*

The 1980 Constitution, designed and promulgated during the dictatorship more than 30 years ago, continues to serve as a guideline for the country and reflects many of the liberal principles that still prevail in Chile. These include the protection of property rights, free markets, international economic insertion, freedom of work and association, the subsidiary role of the state, and an autonomous central bank. Enrique Correa, who served as a minister in the first democratic government, said, “We decided to reform economic policy and not change it, not replace it with another, but reform it. We gave support to a reformed market economy” (as quoted in Cuellar 2013).

The negotiated political transition that took place in Chile on the basis of the 1980 Constitution has been fundamental to Chilean policymaking (Boeninger 1997) and marked a change in the vision of the leaders of the coalition government who have been in power since 1990.

In the negotiation agreed on during the transition to democracy, the representatives of the consensus did not question the moorings of the economic model in the 1980 Constitution. As a result, the model was given a virtual go-ahead and later became an accepted and recognized model for the entire political class and its economists. The concepts of a non-interventionist state, the market as the sole allocator of resources, indiscriminate opening to the world, liberalization of the exchange rate, neutrality policies, an independent central bank, and the consolidation of Pinochet’s privatizations and social-targeting policies are accepted and have become the undisputed axes of national economic life.

### 4.3.2. Trade Policy Instruments

Table 4.6 presents some of the main instruments that were mainstays of trade policy during Chile's transition to democracy, starting in 1990.

#### *Flat Tariff*

A distinctive feature of the foreign trade policies implemented by the dictatorship in 1973 was the profound and unilateral liberalization of imports initiated in the first months of power. It was done with an intensity then unprecedented in other semi-industrialized economies; all selectivity was suppressed in a process that culminated in a uniform tariff of 10 percent for virtually all imports in 1979 (Ffrench-Davis 2018).

In 1990, there was a uniform tariff of 15 percent, which was then reduced to 11 percent in 1991. In November 1998, Law No. 19.589 was published, which gradually reduced the customs tariff from 11 to 6 percent from 1999 to 2003 and then reduced it further by 1 percent a year.

In parallel, on November 18, 1998, Chilean President Eduardo Frei Ruiz-Tagle participated in the annual meeting of the leaders of member economies of the Asia Pacific Economic Cooperation Forum (APEC) in Malaysia. During previous meetings held earlier that month, the Chilean position, presented by the Minister of Foreign Affairs, José Miguel Insulza, highlighted the country's interest in maintaining the forum as an entity of economic cooperation that allows for facing the complex crisis scenario and announced the tariff reduction plan that would reach 6 percent in 2003. This represented Chile's contribution to the commitments assumed in the Bogor goals of APEC.

**Table 4.6**  
**Trade Policy Instruments**

Instruments	Description	Effects on Trade Policy
Flat tariff structure	Flat tariff applied to imports of all products	Facilitates internal negotiation with the different productive sectors
Modalities of negotiation in bilateral trade negotiations	Mechanisms and procedures included in the market access negotiations, especially the different ways to reduce tariffs	Has an impact on the relationship with the different productive sectors and with other public agencies, both from the macroeconomic and sectoral perspectives
Compensations programs	Government programs applied to specific sectors to offset the potential negative effects of the tariff reduction included in the trade agreements	Contributes to the process of approval of trade agreements within both the government and Congress

Source: Prepared by the authors.

The economic rationale for applying a uniform tariff is to grant all the national productive sectors the same level of protection, heading off the administration of different levels of protection that imply tariff categories with higher and lower levels for imported products. The flat tariff has been a central instrument from the point of view of the political economy because it facilitated internal negotiations between the productive sectors in the liberalization process in Chile, both unilateral and bilateral.

The different levels of protection between productive sectors occurred *de facto*, and the flat rate structure began to be perforated after the tariffs applied to products and countries become different in each trade agreement. For example, the tariff applied to imports from Latin American countries was lower throughout the 1990s than the tariff applied to the rest of Chile's partners in Asia, Europe, and the United States. This discrimination began to disappear as trade agreements with these partners were also made to the point that, today, 95 percent of Chile's foreign trade is covered by this network of trade agreements, and the tariff is almost uniform again and close to 0 percent.

In summary, the political economy challenges of the opening in Chile were transferred to the trade negotiations and incorporated into the modalities to open the different productive sectors as part of the different trade agreements. Some interviewees for this chapter also pointed out that the adoption of the uniform tariff by Chile allowed for the implementation of a trade policy without sectoral distortions and with simplified administration procedures, which also contributed to the development of a more efficient tariff structure.

### ***Modalities of Negotiation in Bilateral Trade Negotiations***

#### ***Margins of Preference versus Residual Tariffs***

Negotiating trade agreements based on preferential margins corresponds to the ALADI tradition of the 1980s. This means that only a discount is applied to the tariff without consolidating the tariff reduction against future potential increases. The rationale of this modality is that it allows for preserving the value of what was negotiated when one of the parties changes its customs tariffs in the future. Preferential margins are well suited to the context of limited coverage agreements. Despite this, Chile and MERCOSUR agree on preferential margins that may even result, during the tariff reduction period, in a higher residual tariff when the importing country raises its tariffs *vis-à-vis* third parties.

Traditionally the Partial Scope Agreements of the ALADI covered a limited universe of products and preferences. Partial Scope Agreements generally had a limited duration. FTAs, generally in the form of Economic Complementation Agreements, radically changed both the scope (negotiations covered all

products) and the time dimension (they were of indefinite duration) (Jara 2005). These agreements and future ones were negotiated based on residual tariffs, that is, the tariff was consolidated, so future increases after the agreement was signed would not affect the reductions committed to in the agreement.

### *Free Trade Zone with or without Exceptions*

Another important element in relation to the modality of the negotiations refers to the configuration of the structure of the tariff liberalization schedules. Prior to the 1990s, negotiations in this area were based on the rationale of including positive lists of products for which tariffs were being reduced; that is, only those products explicitly identified had their tariffs eliminated.

After the first trade agreement signed a year after Chile's democratic transition in 1990, the logic of trade negotiations changed to a general principle that all products were included in the tariff reduction, except for what would be excluded, that is, outside the coverage of the tariff reduction for very specific and defined reasons. This modality also coincided with the sectoral non-discrimination approach that the country had taken.

The trade agreement with Mexico was fundamental to Chile's trade policy because for the first time the approach to negotiation changed, and the principle that guided the negotiation was that all sectors are opened, except only certain products for very justified reasons.

Jara (2005) explains this process:

“First it is defined that almost everything is linearly liberalized within an agreed period (four years). If an industry presents sensitivities in a well-founded manner, the reduction can be granted for a longer period (six years). Finally, it is established that a product can only be excluded from the liberalization program if it meets certain criteria. In these negotiations, four criteria are elaborated: (i) that there is a distortion in the counterpart market, such as subsidies, official prices; (ii) that they are products subject to the price band system; (iii) that there are products with high fiscal impact (tobacco and oil); and (iv) that there are sectors undergoing reconversion, such as some textiles. In this way, the private sector knows from the beginning what the rules of the game are and that they operate on the basis of relatively objective and politically acceptable criteria.”

In Chile's FTA signed with MERCOSUR and Canada, it was decided that there would be no products excluded from the tariff reductions, that is, there would be no exception lists. The only adjustment variable referred to the time-frame and modality of the tariff reduction. That is to say, these negotiations

pursued the creation of a free trade zone of wide coverage with 100 percent of the tariff universe subject to tariff reduction.

### *Compensation Policies*

#### *Support for Agriculture*

As a consequence of the approval of the Chile-MERCOSUR Economic Complementation Agreement in September 1996 and the tariff reduction in 1998, an agreement and a protocol of understanding were signed between the Chilean executive and the parliamentarians of various parties that committed greater financial resources to strengthen certain areas of work of the Ministry of Agriculture and other services to improve the competitiveness of the agricultural sector.

The agreement and protocol, which together were known as the “Commitment to Agriculture,” established that additional funds would be allocated to those agricultural subsectors that had more difficulties accumulating capital, incorporating new knowledge, improving productivity, and generating adequate levels of profitability due both to the trade liberalization in the MERCOSUR agreement and the unilateral reduction of five points in the general rate of the customs tariff between 1999 and 2004 at a rate of 1 percent per year.

In particular, within the framework of the discussion of the MERCOSUR Trade Agreement in Congress, parliamentarians representing agricultural areas conditioned their yes vote on the implementation of measures to support the sector to offset the negative effects that would result from the opening of agricultural products to competition, especially from Argentina. In 1995, the Ministry of Agriculture drew up a plan that laid the foundation for this compensation program and that later became a permanent policy over time and key to the subsequent internationalization and expansion of Chile’s agro-industrial exports.

The objective was a productive transformation of agriculture while alleviating the problems that affected the sector by committing the government to apply measures for adjustment.

It is interesting to note that the program also ratified and recognized that Chile supported trade liberalization. In a speech in 1995, the Minister of Agriculture emphasized that, “in the long term, the tendency that will prevail will be the free trade of agricultural products. This will be a long horizon for which it is necessary to prepare.”

That is why Chile’s position was not to leave products outside the tariff reductions, but rather for the negotiations to focus on the modalities of openness under which all products without exception would reduce their tariffs

to 0 percent, with the adjustment variable being the timeframe of this opening.<sup>4</sup> In the end what was accepted, according to an account at the time, was “a gradual transition for sensitive products. To this end, all the mechanisms accepted in the negotiations will be used to protect the interests of medium and small agricultural producers” (Ortega 1995).

The resources of the support program were allocated to training and education, strengthening information systems, research and technology transfer, investment in infrastructure, technical and financial assistance, and quality certification. Undoubtedly the most important measure, conceived by the government, was the “opening and consolidation of external markets as a main strategy that will put Chile on the threshold of development” (Ortega 1995).

With the MERCOSUR agreement the Fund for the Promotion of Agricultural and Livestock Exports was created, but support was also provided to farmers in the south of Chile who were most affected by the agreement. This support came for irrigation and recovery of degraded soils, for which the amount of resources surpassed that provided by the Export Support Fund (Table 4.7).

It is interesting to see how, in counterpoint with these resources, agricultural exports evolved over the 20 year period from 1996 to 2016 (Table 4.4).

**Table 4.7**  
**Agricultural Commitment Support, 1996–2006 (millions of U.S. dollars)**

Year	Agricultural Export Fund	Development of Irrigation	Innovation and Management	Recovery of Degraded Soils	Forestry Development	Health Improvement	Total Agricultural Commitment
1996	6.9	59.6	37.0	4.8	1.1	0	109.4
1997	7.8	86.3	45.0	13.7	1.4	0	154.2
1998	9.5	103.6	60.8	17.2	4.5	0	195.6
1999	11.6	102.7	73.2	29.8	2.1	1.7	221.1
2000	11.4	91.0	76.0	43.1	2.5	1.5	225.5
2001	11.2	86.1	81.7	49.2	28.0	4.3	260.5
2002	13.8	77.8	88.3	43.5	10.1	6.0	239.5
2003	12.7	63.3	85.2	42.1	8.0	8.0	219.3
2004	12.5	63.8	85.6	40.5	8.3	9.1	219.8
2005	12.5	68.8	99.4	41.9	8.2	12.1	242.9
2006	12.4	74.2	99.7	42.7	10.4	13.7	253.1

Source: ODEPA (2006).

<sup>4</sup> Tariffs on vegetable oils, sugar, and wheat flour were eliminated in years 15, 16, and 18, respectively.

## 4.4. Episodes

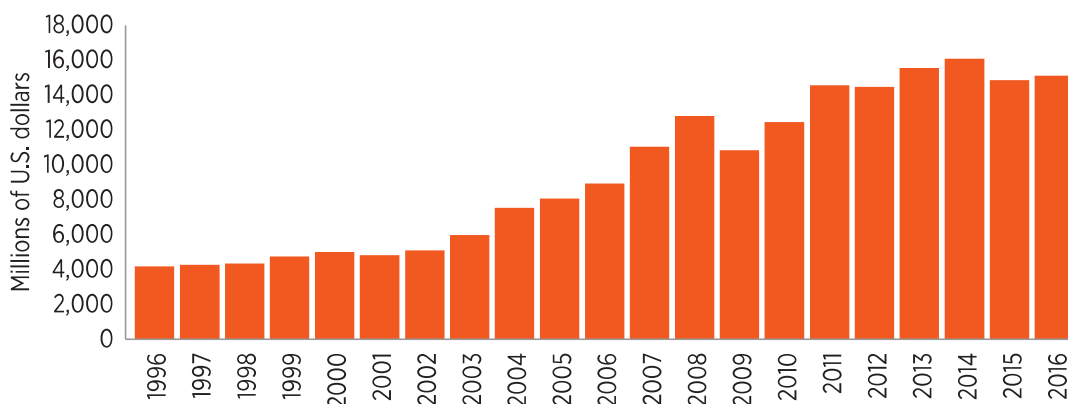
### 4.4.1. Textiles and Footwear

By the beginning of the 1990s, Chile had already experienced a profound opening of its economy that affected some commercial manufacturing sectors. Trade policy and signed agreements later deepened this process. Chile is not a producer of hydrocarbons or cotton as it does not have comparative advantages for those products. The textile and footwear sectors had to adapt to these new conditions of competition, redesign their business models, complement local production with commercialization of imported products, and focus on and specialize in niches where they were competitive in export markets. This process required public policies to support this transformation, along with an ongoing and frank dialogue, which was not always easy, with the companies and unions in the sector. In this, the explicit support of the majority of parliamentarians who shared this vision was important.

As a result of this policy, when Chile decided to negotiate its FTA with China in 2005, these sectors had already been exposed to international competition for more than a decade and were even exporting to previously unthinkable markets by taking advantage of new FTAs signed by Chile (Figure 4.4). This led to both sectors supporting the negotiation with China, which in turn also facilitated the parliamentary discussion of that FTA.

This was also the case of the textile and footwear sector in the negotiation of the FTA with the United States. These sectors were highly protected, with tariffs of around 40 percent. On the other hand, Chile applied equal tariffs of 6 percent. Table 4.8 presents some products that illustrate this situation.

**Figure 4.4**  
Chilean Agricultural, Livestock, and Forestry Exports, 1996–2016



Source: Prepared by the authors based on data from the Oficina de Estudios y Políticas Agrarias.



**Table 4.8**  
**Gaps in Tariff Levels between the United States and Chile (percent)**

Product/Tariff	United States	Chile
Pantyhose	16.3	6
T-shirts	16.3	6
Coats	16.2	6
Waterproof footwear with rubber and plastic top and sole	37.5	6
Footwear with a sole and rubber or plastic top with a value exceeding US\$12	20	6

*Source:* Prepared by the authors based on information in the Chile-United States Free Trade Agreement.

### *Footwear*

The footwear industry in Chile is represented by the Chamber of the Leather and Footwear Industry (known as Fedeccal F.G.), which is the institution that groups together Chilean companies in the sector. It was created in 1999 from the grouping of all trade associations of businesspersons, professionals, and technicians who constituted the entire sector in order to guarantee its protection and development, mainly in terms of protecting against import distortions.

During the military dictatorship, a social market economy was assumed and the sector, intensive in labor, was not prepared to face that challenge. Many decided to withdraw from the business association instead of thinking that this was precisely the moment that it should have been more united. The new model was applied “without anesthesia,” unlike, say, in Germany which prepared the country before a social market economy through education and capacity-building for innovation and competitiveness.

National production of the footwear sector grew under protectionist policies, reaching 24.7 million pairs in 1972. However, successive adjustments of the country’s economic policy and strong restrictions on demand strongly impacted the industry. Due to differences in productivity, costs, and export subsidies provided by governments such as Brazil, China, South Korea, and Taiwan Province of China, imports reached 4.4 million pairs by 1980 and rose to 9.2 million the following year (with an estimated internal consumption of 17 million pairs). Starting in 1986, the national industry began to recover thanks to an export initiative, some compensatory measures against imports of finished products, and the constant growth of the national economy; this stimulated the installation of new plants, especially for production of sports footwear.

With the arrival of democracy, the trade liberalization model was retained and opened Chile's borders even further. As shown in Table 4.9, since the beginning of the 1990s, imports of footwear have been growing rapidly. The Chilean market was opened to suppliers from ultracompetitive countries in Asia, such as China, Indonesia, Malaysia, and Vietnam. Exposed to this greater competition, Chile's footwear sector began to have concerns about technological development, innovation, and strengthening of competitiveness.

In 1994, the challenge for the sector was to harmonize private efforts with those of the state in searching for markets through trade agreements such as those with MERCOSUR and APEC, as well as obtaining information, macroeconomic stability, and protection against unfair competition (e.g., subsidized footwear from China). This would allow companies to plan their export effort and move to more developed stages of internationalization that would necessarily require increasing the professionalization of their executives and the incorporation of new technology.

For the technological development of the sector, entities such as the Corporación de Fomento de la Producción de Chile (CORFO) and ProChile provided support to learn about new technologies that were being developed abroad, participate at technology events, etc. The liberalization process radically changed the structure of the sector, as shown in Table 4.9.

The footwear industry today in Chile has been completely transformed by the opening process. The same shoe company in Chile can both export and import products to complement products manufactured in Chile. The sector is atomized, exporting mainly to Latin America. Large companies have reduced their numbers of workers due to technology.

In terms of trade negotiations, the sector has requested a set of flexible rules of origin and the possibility of accumulation of materials produced in the partner country in order to have more options to fulfill the rules.

**Table 4.9**  
**Chile's Footwear Industry, 1991 and 2017**

Item	1991	2017	Difference
Footwear production (millions of pairs)	35.7	5	30.7
Footwear imports (millions of pairs)	2.2	114.5	112.3
Footwear exports (millions of pairs)	6.1	0.31	-5.79
Number of workers employed in the sector	35,000	13,145	-21,855
Consumption per capita	2.4	6	3.6
Number of companies	1,000	491	-509

Sources: Banco Central; Dirección Nacional de Aduanas; SII; and Fedeccal F.G.

## *Textiles*

In the case of the textile sector, the depth of the liberalization before 1990 determined the position of the sector in the FTA negotiation process. The greater competition that local firms had to face from Chinese and Asian suppliers in general was not possible to counteract with the tariff level applied by Chile. The gap in the price of imported products with respect to domestic products was such that the only way to control the entry of these products was with the application of tariff surcharges that were applied during the 1990s, but only temporarily.

Therefore, FTAs signed by Chile were an opportunity to expand the sector's exports. By the end of 1990s the sector reached exports of US\$200 million. However, these flows then declined due to competition from Chinese products in export markets where Chilean products also flowed. Trade agreements opened markets for companies that became more efficient and survived the opening to imports. That is why the sector ended up supporting the FTAs.

The economic groups that owned the largest companies in the sector in the 1990s experienced expansion and diversification of their businesses. Many of them moved their main economic activity to other sectors such as real estate. For this reason, the influence of the textile association with the government and Congress waned. The tariff in the 1990s began to be irrelevant in terms of external competition, so the FTAs has less and less impact on the internal sector and rather were an opportunity to develop export markets.

### **4.4.2. Price Bands: Compensation Policy and the World Trade Organization Case**

The price band system was designed with the aim of stabilizing the domestic prices of certain agricultural products and avoiding sudden fluctuations caused by international prices. In that sense, the system sought to compensate agricultural sectors competing with imported products by giving them signs of price stability for their sowing and harvesting decisions.

Under the system, if international prices fell, domestic prices were maintained in a higher range and within the price band. Consequently, the compensation should be measured by the difference between the international price and the domestic price. In the case of wheat, when prices fell sharply, the band kept domestic prices higher, protecting the sector from more competitive producers and compensating it for this fall in international prices.

The protectionist measure that Chile maintained for years in certain traditional agricultural categories were price band systems that inversely correlated international prices of these products with the level of protection and surcharge

that imports had to pay upon entering the Chilean market. This instrument was questioned in the WTO, but above all, it was one of the elements more complicated to negotiate in the trade agreements. Keeping this instrument in force signified paying costs in these negotiations and losing advantages for other Chilean productive sectors in export markets. However, it was the only viable option to gain approval for the FTAs in the National Congress. In the Chile-MERCOSUR Trade Agreement (1996), this instrument was partially eliminated in the very long term and was accompanied by a support program for other agricultural and agrobusiness sectors for which the promotion and market opening programs of the FTAs were fundamental to their export growth. That process also facilitated the subsequent negotiation with the United States and the European Union that led to this instrument being completely dismantled.

In July 2003, the bill to modify the price band system applied to wheat, sugar, and edible vegetable oils was submitted to Congress. The modification to the instrument was made necessary as a result of a WTO Dispute Settlement Body resolution, in response to a claim by Argentina, specifically for cases of wheat and edible vegetable oils. The resolution determined that Chile should adjust its price band system to meet WTO rules, finding that the instrument had similarities with a variable tariff and with a minimum import price, both border measures not allowed under WTO rules. The resolution argued that the system was not transparent, not predictable, and discretionary.<sup>5</sup>

Adjusting the price band system to comply with WTO rules meant a substantial change in policy. Due to this, the system was thoroughly studied, and a wide discussion was initiated within the public sector and with the private sector on the modifications that could be included, always bearing in mind the limitations imposed by the WTO regulations.

As noted, the WTO ruling only referred to wheat and edible vegetable oil products, as claimed by Argentina, so there was no requirement to modify the instrument applied to sugar. However, modification of that instrument was also necessary, considering the high probability that the sugar band would later be questioned.

The adjustments to the price band system took into account the reduction on the tariffs for the products involved already included in the agreement with MERCOSUR, which specified that by 2015 the products would be in free trade conditions.

Therefore, the modification and its complementary provisions to comply with the WTO ruling constituted the policy that would be in force for the coming

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<sup>5</sup> The WTO said that Chile had the legal standard (Article 12 of Law 18,525) that determines the existence of the price band system but did not have any regulations detailing the application procedures.

years. In addition, the modification of the instrument and its application had to be transparent, predictable, and non-discretionary, as required by the WTO.

#### 4.4.3. Labor Unions and the Chile-United States Free Trade Agreement

The negotiation of the FTA with the United States marked the first time representatives from Chile's labor unions actively participated in the process. The agreement included a specific chapter on labor rights, which enabled progress on the enforcement of Chile's own labor laws. The labor unions in the region and in the United States had long been critical of these agreements. At first, this was also the case in Chile. However, after much dialogue and participation, the unions came to share the vision that open markets contribute to more and better jobs by expanding and diversifying Chilean exports. Finally, the Chilean unions provided great support in the negotiations. They publicly opposed the positions of the American Federation of Labor and Congress of Industrial Organizations (AFL-CIO) and then explicitly supported their approval in Congress.

The position of the labor unions has stayed the same since the Chile-U.S. FTA negotiations, which has facilitated the negotiation processes with other partners such as China, the European Union, India, and Korea. It has also helped to ensure approval of all of the FTAs with large majorities in Congress.

The main reasons for the position taken by labor union representatives in FTA negotiations were as follows (interview with D. Olivares):

1. A valuation of the benefits for economic growth and the employment of openness. There was a recognition that Chile had already determined the economic destiny of the country with its opening policy, that the country had changed, and that workers needed to participate in this opening and have a voice in it. Those who defended the FTA saw this moment as an opportunity to strengthen the union movement.
2. The political will of the President of the Republic and the evaluation that the FTA would inevitably be negotiated, so the intelligent decision for the unions was to get the most out of this process.
3. A fundamental commitment of transparency and permanent information from the negotiating team to the union leaders and the latter's participation in the negotiation process.
4. Including labor issues in the FTA was a positive step toward establishing standards to make labor legislation more binding, representing an opportunity for workers.
5. The Workers' United Center (CUT) made an effort to share with its bases the benefits of the FTA, implementing a dissemination mechanism for

sectoral unions not only in Santiago but in the country's regions. In particular, work was carried out with representatives from unions from sectors potentially affected by the FTA, such as textiles, metal mechanics, and agriculture.

6. The AFL-CIO, the largest union in Canada and the United States, opposed the FTA, maintaining that it did not comply with labor rules close to those in force in the United States. It also insisted that free trade reduced the number of jobs and working conditions in the United States (Cuellar 2013). However, among Chilean unions there was a conviction that these arguments responded to a protectionist position of defending jobs in the U.S. market, and that in fact the FTA would bring more investment to Chile and therefore more employment not only in Chile but in the United States as well.
7. Finally, the support of the international trade union movement was fundamental for CUT in Chile to support the FTA. Several associations of international workers valued the process of transition to democracy in Chile and supported CUT's role in this process.

#### 4.5. Conclusions and Challenges for Chilean Trade Policy

Today, Chile is the most open economy in Latin America. Tariffs are uniform and very low (6 percent, but de facto less than 1 percent) and the country has FTAs with countries that account for around 90 percent of world GDP. Chile does not apply nontariff barriers, and trade barriers that existed, such as price bands, have been eliminated as a result of multiple trade negotiations.

The opening of the Chilean economy began with a unilateral reduction of tariffs during the years of the Pinochet dictatorship. This deep and persistent policy brought about a change in the private actors, reducing the influence of competing sectors on imports and increasing the influence of exporters. Chile became increasingly competitive due to gaining access to cheaper imported inputs and at the same time gaining preferential access to many export markets. This scenario generated an interesting starting point for the negotiation of bilateral agreements because Chile's tariff concession was always significantly lower than the reduction that it granted in the export markets.

This policy forged a great national consensus around the benefits of the opening policy for the country. The consensus included actors that in other countries would be unexpected, such as labor unions, the textile sector, and some agricultural sectors that otherwise benefited from extensive compensation programs. The years of negotiations developed a strong institutional

structure with increasing transparency, and during which both public and private actors accumulated professional technical skills.

The focus of this chapter was to understand why Chile has formed a broad consensus around the benefits of free trade. This shared vision was fundamental in the implementation of Chile's international economic insertion strategy and its multiple negotiations of FTAs. The result of this can be seen in Table 4.1, which shows that the vast majority of FTAs were approved in the National Congress, often by wide margins.

However, today this reality is challenged because Chile's Congress is much more diverse than it has been in past decades, with a relevant presence of political forces that oppose free trade. This new scenario will make the next discussions of FTAs in the Congress much more complex, with the first test likely to be discussion of the Comprehensive and Progressive Agreement for Trans-Pacific Partnership (CPTPP).

The chapter identified the main reasons why Chile has applied a policy centered on bilateral and plurilateral trade liberalization in numerous international agreements. The chapter examined the main actors and instruments and how they interacted with each other. Several findings resulted from interviews conducted specifically for this chapter.

A fundamental reason behind Chile's trade policy is the strategic decision to continue the economic model of opening when democracy returned to the country in 1990. Although the emphasis of the policy was changed—with the opening implemented through negotiation with main trading partners and not unilaterally as was done during the dictatorship—the political and economic authorities remained committed to the benefits of trade liberalization policy. What followed was a long period of strong consensus that this policy was beneficial for the country. In short, Chile is a case study where ideology and economic interests coincided.

In this context, the trade policy instruments used by Chile were consistent with this liberalization process. The instruments included the application of the flat tariff, ambitious modalities in market access implemented in the negotiations of FTAs, and compensation programs that provided public goods to enable new exporter capabilities.

In the institutional field, the chapter highlights the roles of DIRECON in conducting trade policy and CIREI in the process of internal decision-making among the ministries and public agencies involved in trade negotiations. Concerning the Congress, its role was limited to approving the FTAs negotiated by the executive, so the challenge going forward is to strengthen its role in the future. Civil society has also been more active in recent years, and for this reason the Side Room has been institutionalized. This instrument has allowed for channeling the participation of many new

actors now interested in participating in the design and implementation of trade policy.

The episodes included in this chapter also help to understand in practical terms the mechanisms that have operated in the decision-making of trade policy in Chile, especially in the negotiations of FTAs during the last 25 years.

Finally, the chapter provided some lessons that will be useful in the current debate in Chile about the effectiveness of trade policy. Some important challenges that the country must face in the coming years are the following:

- Implementation of the new legal framework for DIRECON that approved its rank of Vice Ministry. How can the country take advantage of this new stage in order to reap better benefits from the network of trade agreements it has signed? This includes working to diversify exports that incorporate more added value and incorporating them into global value chains that today dominate international trade.
- Explore new governance in Chile's international economic relations. This might include, for example, combining into a single institution diverse functions such as trade negotiations, export promotion, promotion of foreign investment, promotion of the country brand, and tourism promotion.
- Given that the agreements are more "intrusive"—that is, they involve matters that have traditionally been the responsibility of national authorities—coordination among public agencies is a priority for implementation of trade policy.
- Current FTAs are evolving beyond traditional disciplines, including issues that have gained increasing public interest. In some cases, stakeholders have critical or defensive positions on issues such as the environment, health, intellectual property, and electronic commerce. In other words, the broader scope of trade agreements, including regulatory issues, imposes new challenges for a higher standard of transparency in these processes.
- This wide range of new issues being negotiated under trade agreements requires putting in place mechanisms that promote the participation of relevant stakeholders with specific knowledge and experience that can strengthen negotiating positions to achieve agreements that are satisfactory to the interests of each party involved.
- It is necessary to strengthen the role of Congress in the process of negotiating and approving FTAs. This includes the preparation of studies and the analysis of costs and benefits prior to any trade negotiations, along with evaluations of FTAs already in force, to benefit from lessons learned.