

Chile

Status Index 9.2 (Democracy: 4.8 / Market economy: 4.4)		Management Index 7.6	
System of government	Presidential democracy	Population	15.4 mill.
Voter turnout	86.8 % (Parliamentary elections 2001)	GDP p. c. (\$, PPP)	9,190
Women in Parliament	10.1 %	Unemployment rate	9.1 %
Population growth^a	1.5 %	HDI	0.831
Largest ethnic minority	4.0 %	UN Education Index	0.89
		Gini Index	57.5 (1998)
Data for 2001 – if not indicated otherwise. ^a Annual growth between 1975 and 2001. Source: UN Human Development Report 2003.			

1. Introduction

In January 2000 Ricardo Lagos was elected president of Chile, narrowly winning on the second ballot, with 51.3 % to 48.7 % of votes cast over his conservative challenger, Joaquín Lavín. This was the third time since the end of the Pinochet dictatorship that a politician from the old opposition alliance, *Concertación de Partidos por la Democracia* (CPP), won a presidential election. Lagos' victory also set a precedent since the coup against Salvador Allende in 1973, by putting a socialist, albeit a moderate one with a social-democratic orientation, in Chile's highest office.

Upon taking office in March 2000 from his predecessor, Eduardo Frei Ruiz-Tagle, Lagos assumed the presidency of a country that, after 10 years of successful transformation and high, stable growth through 1998, for the first time was facing the consequences of a dramatic externally-induced economic crisis. The period covered by this report largely corresponds to the first half of Ricardo Lagos' six-year term.

This report on the status of transformation to a democracy and a market economy over the last five years (1998-2003) concludes that, despite the bump in the economic road from 1998 to 1999, Chile was able to continue its positive direction in political and economic transformation since 1990, and do so in an impressive manner.

This success prior to and after 1998, which was carried out against powerful resistance in the political arena in particular, is without doubt the result of the

successful management of the *Concertación* governments. In regard to almost all key performance criteria, the transformation broadened to the extent that Chile is close to the goal of a consolidated democracy with a market economy. At the halfway point of President Lagos' term, however, there remain a few key tasks in the areas of political participation and securing the social and long-term sustainability of Chile's economic development.

2. History and characteristics of transformation

Since it was founded in the 19th century, Chile has enjoyed a stable political system, which was also basically democratic during the 20th century. The collapse of democracy with Pinochet's coup against the government of Salvador Allende in 1973 initially represented a radical break with the country's political institutions. A few years later, it was followed by a similar rupture in its economic regime, which, like every other country in Latin America, was modeled along lines of a strongly regulated economy of import substitution.

In terms of democratization, Chile must be considered a latecomer, since in 1990 it became the last country in Latin America to return to democracy (except Cuba). In the transformation to a market economy on the other hand, Chile has been a pioneer. Since 1975, various generations of the "Chicago boys" converted the country under Pinochet's rule into a neo-liberal economic and social model. Thus Chile not only experienced the inverse sequence of transformation like most other countries of the third wave of democratization; but has also experienced a relatively long period of time between the two regime changes.

Chile's political transformation is strongly marked by the relative durability of Pinochet's authoritarian rule. At the zenith of his power, when the Chicago boys' project of "radical neo-liberalism" seemed to be taking hold, and the word about Chile's economic miracle was making the rounds, Pinochet had a constitution made to fit his conceit of a "protected democracy," which he had then legitimized by means of a (fraudulent) plebiscite in 1980. This constitution with its political schedule provided for in it survived the economic crisis and eventually formed the institutional framework for subsequent political developments. Among other things, it provided for a plebiscite in 1988 in order to reaffirm Pinochet's rule for another term until 1997.

This official game plan notwithstanding, the process of reorganizing and establishing opposition parties proceeded, without which there would be no explanation for Pinochet's defeat in the 1988 plebiscite. Yet in the end, the opposition had to accept Pinochet's schedule. Made up of center-left parties that came together under the leadership of Christian Democrat Patricio Aylwin in the *Concertación de Partidos por la Democracia*, the opposition subsequently won

the presidential and parliamentary elections in December 1989, after their victory in the 1988 plebiscite. But Pinochet and the Chilean political right retained their powerful position and managed to impose restrictive conditions on the Chilean transition, which then led to a defective democracy with “authoritarian enclaves.”

The development of democracy in the 1990s was marked on the one hand by a thorough but generally low-profile debate over these authoritarian enclaves, which included constitutional privileges of the military, appointed senators, and parts of the electoral system. On the other hand, the efforts of the *Concertación* governments, which have won all national elections since then, were aimed primarily at solidifying the democratic regime and therefore at achieving consensus with the parties on the right as well. This marked both the term of Patricio Aylwin (1990–1994) as well as that of his successor, Eduardo Frei Ruiz-Tagle (1994–2000), so only low turbulence was observed in the political realm.

Despite the threats still emanating from Pinochet, the democratic game grew increasingly stable, intermittently even allowing for agreements superceding political blocs, somewhat politely referred to as *democracia de los acuerdos*. Along with high institutional stability, the smooth political process and the relatively low level of conflict provided favorable prospects for meeting economic and social challenges step by step. While the Aylwin government provided the necessary stabilization of framework conditions, an almost “normal” political process ensued under President Frei so that an advanced degree of consolidation was reached by his term, despite remaining but diminishing authoritarian enclaves and an insufficient treatment of the Human Rights violations.

Pinochet’s arrest in London in October 1998 and its consequences further accentuated this development and led to a deeper legal and political confrontation with human rights violations. In addition, the Chilean military had also gone through a learning process, linked to a generational change as well, allowing for normalization of the relationship between civil society and the military. At the same time, the judiciary was noticeably strengthened through reforms of the judicial system.

Chile’s transformation to a market economy, going from the former socialist experiment under Allende to a model neo-liberal country, began in the mid-1970s with the ascendancy of the Chicago boys, a group of economic technocrats who largely held doctoral degrees from the University of Chicago. They gradually advanced to ministerial posts and other high government offices, with strong connections to the banking and finance sector.

The first phase of this radical neo-liberalism, which included an abrupt opening to the outside, deregulation, privatization, and uncontrolled capital flows, led to the demise of a classic rent-seeking society. It also managed to drastically reorganize the social insurance system reforming the pension and poverty policy, as well as the health care and educational systems. The first phase ended, however, in 1982 with Chile's greatest economic crisis since the Great Depression, intensified by the international debt crisis.

Nonetheless Pinochet succeeded in surviving the subsequent legitimacy crisis and, with the aid of a second generation of Chicago boys, was able to anchor a more pragmatic version of neo-liberalism that led to a rapid economic recovery from the depths, beginning in 1985. The learning process through which much of the opposition passed over the course of the 1980s was likewise important for the subsequent development of the transformation to a market economy. Although more heterogeneous than the Chicago boys, the Christian Democratic and Social Democratic politicians developed visions and programs for an economic and social regime that accepted the essential directions of market oriented reforms, while fitting them with a stronger, more viable social component.

The *Concertación* governments pursued this program, even as the process of socioeconomic reforms proved to be quite protracted, usually involving political bartering with the opposition. Years of skillful negotiations with segments of the opposition nonetheless succeeded, through a process of small steps, in solidifying the functioning of the market economy. This led to a greater international competitiveness, the strengthening of the private sector, a further opening of the economy to the outside world and the optimization of the regulation agencies especially in the areas of pension funds and the banking system.

Unlike the other Latin American countries, the Aylwin administration introduced measures to control speculative foreign capital inflows, and by these succeeded to enhance the country's financial stability. The economy's performance from 1990 to 1998, which included high macroeconomic stability, average economic growth of 8.3 %, a reduction of inflation from 27.3 % to 4.7 % and annual surpluses in the state budget, also reflects increasing solidity. Above all, however, individual reforms in the sociopolitical realm also succeeded, starting with the expansion of social expenditures through tax reform, and extending to revisions of labor legislation by successive adjustments to international standards. While developments here were slower to start, the basic high level of poverty was reduced by about half, and levels of employment and wages remained relatively high.

In 1997 Chile achieved the highest HDI numbers in Latin America, about the same level as Slovenia and surpassing the Czech Republic. The economic collapse in 1998–99 that followed the financial crises in Asia, Russia and Brazil

caused the demise of export markets, and a dive in prices for primary export goods. The effects of these crises were cushioned by rather unorthodox stabilization policies including budget deficits, loosening controls on speculative foreign capital and job creation measures; by 2000 the economy had taken a turn for the better again.

3. Review of criteria for democracy and a market economy

3.1 Democracy

In the transformation of its political regime, Chile has made further progress in some of the areas evaluated. Transformation deficiencies remain in the areas of elected representatives and military veto power, but these authoritarian enclaves have shrunk noticeably and no longer enjoy unqualified support from the opposition. While some indicators of democratic stability exhibit a certain stagnation, this does not affect the overall high stability of institutions, nor have they reached a level that would threaten the system as a whole.

3.1.1 Political regime

(1) *Stateness*: There are no stateness problems in Chile. There are no limitations on the state's monopoly over the use of force. The definition of citizenship and who qualifies for it are not politically relevant issues. All citizens have the same civil rights. Church and the state are separate; the political process has been secularized, though on some issues the influence of the Catholic Church is essential. A capable administrative system and public safety and order are guaranteed to a large degree.

(2) *Political participation*: Chileans enjoy universal suffrage and the right to campaign for elected office. Correct electoral processes are effective, without limitations. Like all other actors, the elected government observes the principles of an open and competitive electoral process. One remaining limitation is the procedure - controversial since 1990 - whereby nine of 47 senators are not popularly elected but rather are appointed by various state institutions.

Over the course of time, however, the political relevance of these authoritarian enclaves for the political parties has evaporated, since today not even the representatives of the military on the National Security Council can be viewed as unquestioning partisans of the political right. This outcome should be attributed to the responsible attitude of the actors, however, and this remains an institutional defect that is supposed to be reformed by the *Concertación*—again, under President Lagos—and which does not even enjoy the undivided support of the moderate right anymore.

These considerations also apply to the limitations on the effective power to govern. While there are still veto powers and political enclaves in the hands of the military, over the course of the years and especially after 1998, the year of both Pinochet's arrest in London as well as political and judicial disputes on human rights violations, these enclaves have increasingly eroded. More evidence of this trend can be seen in the statements at the end of 2002 made by General Juan Emilio Cheyre, supreme commander of the armed forces since March 2002, in which he disassociated himself from the Pinochet dictatorship with unusual firmness, as well as the appointment of Michelle Bachelet in 2002 to the office of defense minister. Bachelet is the first woman to hold this post in Latin America, and even more importantly, she is the daughter of a general who was tortured and murdered by Pinochet's henchmen.

Rights of political organization and communication can be exercised without restraint. Political and civic organizations can be freely established. Political activity on the part of unions is not subject to restrictions, but their collective bargaining rights are still subject to some provisions that do not meet international labor law conventions, despite recent reforms by the Lagos government. After years of debate, freedom of opinion and the press was strengthened in 2001 with the abolition of restrictive provisions ("insulting governmental authorities"). However, limitations result from the strong concentration of mass media which are dominated by two large groups.

(3) *Rule of law*: Under the Lagos government, the rule of law has been further strengthened in Chile. The *democracia de los acuerdos*, while still marked by political bartering, is not characterized by any infringement on the system of checks and balances among the executive, the legislative and the judicial branches.

The independence of the judiciary and the constitutional court exists almost without limitation, although it was subjected to a serious test by the Pinochet trial, which would have been almost unthinkable as recently as 2000. The outcome of the trial, cessation in July 2001 based on the ex-dictator's incapacity to take part for health reasons, was unsatisfying in terms of the rule of law—and it must be judged a last relic of the old enclave democracy. The trial had more the hallmark of a political trial, however, and its outcome also led to Pinochet's withdrawal from politics, including not taking his seat in the Senate, which he holds for life based on his previous position as president of Chile. Conversely, the flood of lawsuits against Pinochet and his former helpers, as well as the conduct of the judges involved, shows that the population's faith in the independence of the judiciary has grown.

Any general undermining of judicial control and review functions is not discernible. This picture is further supported by the limited extent of corruption, which plays a rather small role in society as a whole. Spectacular individual instances are not only appropriately denounced by the public, they are also prosecuted by the judiciary. Political office holders accept the processes of the judicial system, as was evident in particular in a case of corruption involving supporters of the Lagos government. A suspicious press also monitors the state's behavior to ensure that it is in keeping with the rules.

Civil liberties in Chile are to the greatest extent ensured; despite intermittent problems, there have been no more human rights violations during the democratic era. Major progress has also been made in the last five years in the political and judicial treatment of human rights violations. However, the self-amnesty law from 1987 still exists. Access to the judicial system has been improved for lower social strata as well through a specific program within the context of judicial reforms, although this is still insufficient in a Chilean society marked by great disparities.

3.1.2 Patterns of political behavior and attitudes

(1) *Institutional stability*: Chile is still living with a Constitution that was passed by the authoritarian regime and reformed in some sensible points during the transition in 1989. This means that the fundamental rules of the political game are not based on a broad consensus among politics and society but more or less on acceptance. Under these conditions, democratic institutions are to a high degree stable, notwithstanding the limitations posed by the authoritarian relics mentioned above.

These democratic institutions operate in accordance with their functional purpose and are effective and largely efficient. They are now accepted and viewed as legitimate by all relevant political and social actors, who also concur that, for instance, the reform of remaining authoritarian enclaves can only be accomplished by means of the procedures provided for in the constitution and thus, as a rule, through consensus.

(2) *Political and social integration*: Chile's political stability is closely tied to stable organizational patterns of political representation. While the effective number of parties represented in Parliament is apparently high at 6.25, Chile has a *de facto* two-party system since, under the current electoral system, parties are forced to stand for election in combined lists, reducing the effective number of parties to 2.03. Along with the parties in the *Concertación*—Christian Democrats (PDC) and Social Democrats (PS, PPD, PRSD)—there is also a coalition of the two right-wing parties, which includes the moderate RN and the UDI, the party closest to the forces of the old regime. There were significant shifts within the two

blocs during the last parliamentary elections in December 2001 but not between them.

In all, the party system is organizationally stable and sufficiently anchored in society, with stable connections to civil society. The degree of polarization is overall moderate when the parties not represented in Parliament are included, although comparatively high in relation to some issues, such as coming to terms with human rights violations. The degree of voter volatility is rather low when measured in terms of the two politically relevant blocs. Chile has a well-differentiated landscape of interest groups in which the associations representing capital play a particularly powerful role, along with the Catholic church.

The trade unions, which were weakened greatly under the dictatorship, have been able to achieve relative organizational stability under democratic governments, while the business associations were able to maintain their powerful position based on the economic strategy, which at its core did not change. Governments have been able to maintain relative equidistance between the two associational poles and have installed tripartite mechanisms for concerted action on important reforms, such as in the area of labor legislation. The ability of the state and social interest groups to cooperate is relatively high and, together with a functional party system, Chile enjoys solid structures that can mediate between the interests of society and the state.

In Chile, the approval of democratic norms and procedures is medium to high, 50 % to 60 %. It is still somewhat surprising that this figure has not risen more since the reinstatement of democracy, despite the successes of democracy and the market economy, and strong appreciation for the government's efforts. About one-third of the population expresses indifference toward democracy or autocracy, an attitude that is especially strong among the lower strata, while support for autocracy—at 25 %—remains strongest among the middle classes, the winners under the Pinochet dictatorship. In political practice, however, this pattern of political attitudes does not signify any questioning of the constitutional framework of democracy, even while Chile's political class does not enjoy any high standing, with the clear exemption of the president.

The organizational landscape of civil society continues to grow more differentiated; alongside numerous religious organizations, there is also a network of more than 80,000 associations; seen in relation to the size of the population, there are more than in France, for example. There is a willingness of civic organizations to cooperate and to engage in strategic negotiations, while greater governmental recognition of their role as policy initiators is required. Civic organizations contribute to broadening democratic attitudes and practices within Chilean society and represent a social force for political moderation.

3.2 Market economy

Chile has continued to make progress in transforming its economic regime. Transformation deficits exist especially in the areas of the social, ecological and long-term viability of the economic system.

3.2.1 Level of socioeconomic development

Chile enjoys a relatively high level of socioeconomic development. Measured by HDI, it is in the top group, just behind Poland, and the leading country in Latin America. The level of development provides most citizens with sufficient freedom of choice. This is distorted, however, by the high degree of inequality, such that fundamental social exclusion occurs through the extreme poverty (*indigencia*) of about 6 % of the population, a number that has stagnated since the mid-1990s. Throughout the evaluation period, Chile suffered no setbacks in regard to social disparities, the rate of poverty or income distribution, despite the recession of 1998–99. However, existing developmental imbalances among regions did not decrease noticeably in recent years either.

3.2.2 Market structures and competition

Chile possesses a model institutional foundation for market competition. Governmental policy is limited to general assurance and maintenance of the rules of the game, and to neutral organization of regulations consistent with competition, including control over monopolies and expansion of required intermediary institutions. The Frei and Lagos governments used the increasing consolidation of the economic regime for rather unspectacular expansion and complementing of reforms of the so-called first and second generations.

Foreign trade has been substantially deregulated, and the degree of openness of the economy continues to expand. By 2003, tariffs were reduced to 6 %. The state does not intervene in free trade, but rather supports the export orientation by means of a network of institutions linked to the economy. Chile enjoys a solid banking and finance system oriented on international standards. The finance sector is subject to its own supervisory agency, the SBIF, which monitors and applies the provisions of the banking act and provides a risk classification of financial institutions. Chile follows the norms of the Basle Committee on Banking Supervision on this but is even more conservative in provisions such as required

equity capital. Instead, the regulations on speculative capital inflows which had been useful for 10 years were eliminated in 2001 by the Lagos government.

3.2.3 Stability of currency and prices

The Frei and Lagos governments, together with the independent and highly professional central bank, have continued a consistent policy on inflation and exchange rates. Since 1990 inflation has been continuously reduced and has moved in a range below 5 % since 1998. In September 1999, in the course of the crisis at that time, the central bank replaced its previous exchange rate management policy, which floats within a set range based on a currency basket, with a free-floating exchange rate. Those governments' fiscal and debt policy was also narrowly aimed at stability. The budget deficit, which in the course of the economic crisis of 1998–99 was accepted for the first time since 1990, has now been reduced to zero again after the crisis subsided. Overall economic policy since the 1990s has been marked by highly disciplined maintenance of macroeconomic stability, in which the central bank and the government have worked together quite effectively.

3.2.4 Private property

Property rights and the regulation of property acquisition are sufficiently defined. The privatization of state enterprises that was initiated under the dictatorship continued under the Frei and Lagos administrations, although the accent shifted increasingly to participation of private capital in the public sector. The practice of issuing licenses for infrastructure measures previously carried out by the government has taken the same direction. They are now awarded to private investors through a transparent bidding procedure and then subject to government supervision (for example, road and bridge construction, ports, etc.). The goal is to overcome infrastructure bottlenecks that restrict the degree of international competitiveness of the Chilean economy.

3.2.5 Welfare regime

Since the drastic reforms of the early 1980s, Chile has had a welfare regime, which is liberal at its core; that is, individual and private responsibility have been institutionalized as the central regulative concept. On that basis, providential institutions meant to compensate for the risks associated with old age, illness, unemployment and disability are in part well developed but, due to social disparities, they do not come close to covering all risks for all strata of the population.

Characteristically, state measures to assist in fighting poverty are relatively strong, while the *Concertación* governments gave more emphasis to the aspect of integration in the overall social process of development. A recent example is the programme *Chile Solidario* which directly attends the 250.000 poorest families. Poverty was reduced from 38.6 % in 1990 to 20.6 % in 2000 through a combination of a targeted social welfare policy, higher state expenditures, and continuing economic growth, with the emphasis lying greatly on the latter.

In addition to considerable regional differences, poverty among the indigenous population is about 50 % higher. The government achieved further expansion of social insurance by introducing unemployment insurance in 2002, a unique step in Latin America, which not only guarantees monetary payments but also includes rights to continuing education and retaining health insurance.

Chile enjoys a relatively advanced and global health care system, but despite increased expenditures under democratic governments, it remains poorly equipped in many areas. Poorer strata of the population generally cannot avail themselves of the very well-developed private health care system for cost reasons. Improvement of access and quality are priorities of the present government.

Despite government reforms, the same distortions can be seen in the education sector. While expenditures for education have doubled since 1990 and Chile spends 7 % of its GDP on education and training, half of those expenditures are allocated to higher education or private schools. Improvements in equal opportunity for women can be seen but, at 33 %, the percentage of women in the labor market is still rather low, and their earnings average only about two-thirds those of men. Women's presence in public life, the media and politics has been growing, thanks not least of all to the activities of numerous women's organizations. Overall, however, and despite considerable progress, there is still not sufficient equality of opportunity in Chile.

3.2.6 Strength of the economy

After the crisis that led to the deterioration of fundamental economic institutions at the beginning of the period under examination, the governments' crisis management initially achieved macroeconomic stabilization. After a 0.7 % decline in growth in 1999, the GDP increased again the following year by 4.4 %. Due to negative global economic conditions, economic development slowed down again in 2001 and 2002 in the extremely export-dependent Chilean economy. After an interim recovery, developments in other macroeconomic data, especially unemployment and foreign direct investment, are only tentatively positive. Overall, the Chilean economy shows solid performance, although its growth

potential cannot be exhausted at the present time due to ebbing capital flows and low prices for its most important export goods.

3.2.7 Sustainability

On the part of society and legislation, environmental awareness greatly increased during the 1990s, but the neo-liberal growth strategy with all its considerations still dominates, and ecological concerns tend to remain subordinate. Legislative anchors for sustainable growth were most likely to be put in place when the negative impact for profits or health, such as setting ecological minimum conditions for export markets, overfishing of the sea and air pollution in Santiago became too apparent. Unfortunately, the still insignificant number of public initiatives do not stem the continued environmental damage in an economy that is still unilaterally aimed at the intensive exploitation of natural resources, resulting in deforestation and soil erosion, diminishing the number of fish species, polluting water from fertilizers and ore mining.

In regard to the viability of its economic growth model, Chile is no longer a typical developing country due to the learning process it has gone through, but despite high growth, it is also not a Latin American “tiger” because of the lack of technical and industrial skills. The educational system, a central factor in any sustainable race to catch up, still suffers from lack of modernity and from strata-specific segregation. This can especially be seen in the low performance in mathematics, reading and language. Chile has a differentiated system of public, subsidized private and purely private educational institutions at the primary, secondary and tertiary levels, which vary greatly in quality.

Despite a successful reform process, the public elementary education system is still in poor condition. People who can afford it send their children to private schools. The state’s educational expenditures have more than doubled since 1990; the percentage of private educational expenditures is relatively high. Consciousness of the importance of investing in research and development (R&D) has increased significantly, and funds reflecting that have increased greatly since the mid-1990s.

4. Trend

(1) *Democracy*: The development of democracy in Chile has continued to make progress in the last five years, as the authoritarian enclaves in the ensemble of democratic institutions, inherited from the Pinochet dictatorship, have been further weakened in practice. The military’s autonomy and the institution of

designated senators continue to exist and thus represent transformation deficiencies. Clearer progress in this point was achieved through more substantial coming to terms with human rights violations committed during the dictatorship. At the same time, existing institutional strengths were further consolidated and, in the area of the judicial system, expanded.

Progressive tendencies can also be seen in citizens' organizational opportunities, free activities of social organizations, freedom of the press and media and the enforceability of civil liberties. Mutual checks and balances among the executive, parliament and judiciary have been improved through a reform of the Supreme Court. Corruption remains limited; the courts' acceptance of actions against corrupt office holders has further strengthened the rule of law. Though a constitutional consensus still doesn't exist, the stability of fundamental constitutional institutions was also maintained, as was the relatively high institutional efficiency of the governmental system.

Due to the electoral system inherited from Pinochet and the given majorities, reforms to eradicate the authoritarian enclaves have not been possible, however. Parties' achievements in political and social integration continue to be a stabilizing factor in Chilean democracy, even if politicians' prestige is rather low. The landscape of civic interest groups and organizations is developing tentatively yet progressively, but forms an admittedly narrow basis for further development of social capital. On the other hand, the growth of a civic culture supporting democracy is advancing more slowly.

(2) *Market economy*: Chile's socioeconomic level of development as a middle income country with high human development did not change significantly during the period under examination. The fundamental indicators of development show a slight improvement of Chile's clearly above-average level of transformation during the period. This applies to indicators of sustainability as well, while stagnation of the Gini index at a high level shows no improvement in great income disparities. More improvements were achieved in the fight against poverty, although the extent of extreme poverty has stagnated in the meantime.

The institutional conditions for market economic activity, which were very solid at the start of the period, continued to improve. As is generally acknowledged, deficiencies in the economic and competitive regime are non-existent in Chile, but social disparities and continuing lack of guidance toward a growth model oriented on viable technological progress represents a transformation deficit. Measured by macroeconomic data, the overall economic development has lost a great deal of momentum compared with the period prior to 1998, due almost exclusively to external factors, however. In light of crisis conditions at the beginning of the period under study, these data reveal significant success of governmental development policy.

Table: Development of socioeconomic indicators of modernization

	HDI	GDI	GDP Index	Gini Index	UN Education Index	Political representation of women ^a	GDP per capita (\$, PPP)
1998	0.826	0.812	0.75	57.5	0.90	9.8 %	8,787
2001	0.831	0.821	0.75	n/a	0.89	10.1%	9,190

^a Percentage of female representatives in Parliament. Sources: UNDP, Human Development Report, 2000, 2002.

Table: Development of macroeconomic fundamentals (1998–2002)

	1998	1999	2000	2001	2002
Growth of GDP as a %	3.3	-0.7	4.4	2.8	1.8
Export growth in %	-8.7	5.1	11.9	-3.8	-
Import growth in %	-4.8	-19.8	16.0	-4.0	-
Inflation in % (CPI)	4.7	2.3	4.5	2.6	-
Unemployment in %	6.4	9.8	9.2	9.1	9.0
Budget deficit in % of GDP	0.4	-1.5	0.1	-0.3	-0.9
Current account balance in bn. \$	-4.1	-0.3	-1.1	-1.2	-0.5

Sources: CEPAL: *Balance preliminar* 2002.

5. Transformation management

5.1 Level of difficulty

At the beginning of the reporting period, the relatively advanced level of economic and social development, the existence of basic market structures, a very high educational level, lack of ethnic or religious conflicts, an efficient state administration, and the state monopoly on the use of force all offered good conditions for continuing the transformation. This was hindered, however, by greatly marked social disparities and, accordingly, socioeconomic progress that was too slow for major sections of the population. In regard to structural socioeconomic conditions that shape the political process over time, the level of difficulty of transformation should be viewed as low to medium.

Basic consensus on the rule of law, democracy, and the core rules of democratic play also existed prior to the evaluation period—but with the precise exception of authoritarian enclaves, which were designed by the former authoritarian rulers in such a way that they became stabilized over time, based on the strength of the political right. The deep split within politics and society over coming to terms with human rights violations has made and continues to make broadening and stabilizing democratic transformation more difficult.

Business climate conditions and the world economy were decidedly difficult during the period of study. While the Chilean transformation process since 1990 began with positive social and economic conditions on the one hand, but difficult political baseline conditions on the other, the transformation in the period from 1998 to 2003 had to be continued under economic conditions of crisis within the framework of a democracy whose foundations had been laid but remained deficient and unconsolidated.

5.2 Reliable pursuit of goals

The government of President Lagos, like the other democratic governments since 1990, has been able to set the necessary strategic priorities for Chile's continuing economic and political transformation. Its economic reform strategy was by and large aimed at economic stabilization with the cushioning of social costs, but did not succeed in all areas due to adverse world economic conditions. The only strategic shortcomings that bears mentioning would firstly be the technological and knowledge-based developmental path that was initiated but remained only marginally emphasized; and secondly the failure in reducing social inequality.

Obstacles also stood in the way of the political reform strategy, which continued to make use of windows of opportunity to deepen democracy but still had to fight blockades, especially from the right, from the business sectors and from the media controlled by them. Reform policies are nonetheless generally consistent and coherent; the individual elements are still aimed at realizing or broadening democracy and a market economy.

The unavoidable setbacks in individual areas have not led to a relativization of goals, while the performance in other, complementary areas is simultaneously improved, for example, by empowering the judicial system in issues of human rights violations despite political and military resistance against coming to terms with these violations. Politics are thus generally realistic in regard to available capacity, expectations of success, and the time span envisioned. The government also pursues an extremely reliable and predictable policy.

Social and economic actors, including citizens, can reliably calculate the foreseeable consequences of their decisions in regard to state actions, which applies to all relevant areas of action such as rule of law, macroeconomic conditions and physical security. To a large degree this applies to controversial issues as well, such as the reform of authoritarian enclaves, which can only be accomplished on a constitutional basis and with a broad consensus, as is widely recognized. In this matter the consensus in society regarding justice in human rights issues and constitutional reform is overwhelming, but the minority rights, the employers' federations and the media controlled by them are able to neglect this consensus and to defend impunity and constitutional immobility.

5.3 Effective use of resources

Like all the other democratic governments, the Lagos government has made generally efficient use of available human, financial and organizational resources. This applies to the use of governmental administrative personnel, budgetary assets, and administrative organization as well. The ratio between expenditures for personnel and governmental services provided has improved continuously, the amount of politically directed firing and new hiring of public employees has declined, and recruitment procedures are protected from political influence by appropriate regulations.

The national budget shows a relatively stable balance, state indebtedness is low, and effective auditing is in place. Budgetary planning and implementation is transparent, strengthened by the establishment of an expert commission and in cooperation with the IMF. Administration is clearly structured, and administrative organization facilitates effective management according to rational, professional criteria.

The government is generally able to realize its reform goals, even though this is often possible only as part of more comprehensive solutions, given existing political majorities, and thus often only over longer periods of time. The government provides public services which in some areas including property rights, workable markets and infrastructure are optimally tailored to the developmental requirements of the economy and society and thus favor developmental progress. However, in other areas such as health and especially education, bottlenecks are apparent which, while they have not distorted the path of development to date, are not sufficient for the future viability of socioeconomic development.

This image of effective use of resources is further supported by the limited extent of corruption and the efforts to strengthen transparency and combat corruption. Primary mechanisms to ensure public integrity are in place and are supported by

the government. Existing cultural resources, such as the willingness of some sections of society to assume responsibility and develop grassroots organizations, e.g. in the realm of social policy, are used effectively. Treatment of the traumatic events of the 1973 coup, which left deep scars on the political culture of Chile, remains ambivalent. On the one hand, it is used as a warning to moderate social conflicts, while on the other it is also exploited to block reforms.

5.4 Governance capability

The leading political actors within the Lagos government, as well as other governmental forces, have proven their ability to learn and have employed innovative measures in the place of ingrained policies, even though this has rarely been necessary. Some examples include the government introducing anti-cyclical measures to stimulate the economy, floating the exchange rate as a result of the economic crisis, and the *de facto* suspension of central bank controls on capital movements, though the latter might be a risk for the financial stability in the medium term. Overall, the government possesses sufficient political authority to realize its reforms.

As the most recent reform packages show, the government can also wring concessions from powerful political actors, such as business, who must assume part of the costs of reforms in accordance with its economic capacity. However, the business sector still remains very reluctant when it comes to progressive reforms and uses its strength to protect its own privileges. The distributive efficiency of markets in capital, goods and labor has been further stabilized under this government, even while the IMF has criticized growing rigidity in the labor market, especially by the established minimum wage. Fundamentally, the Lagos government has acted with great acumen in its choice of individual reform steps, tools, and strategies.

5.5 Consensus-building

As previous democratic governments have done, the Lagos government strives to achieve a broad reform consensus with other social actors, without giving up its reform goals. All significant political and social actors agree on the goal of reforms, democracy and a market economy, even while there is considerable variation in the vision implied in reaching those goals.

Just as his predecessors did, President Lagos has continued the politics of compromise in key reform realms. Anti-democratic forces with veto power still exist, but their impact is getting weaker. Although on the one hand the military still possesses a great deal of formal autonomy and sections of the political right –

especially of the more radical UDI – are on the other hand still able to prevent the completion of democracy, there are signs for a decline of the veto power. In particular, the military has been increasingly integrated into the democratic consensus, a process that has been favored by a generational change and by the government's utilization of more favorable political opportunities. This does not preclude the existence of representatives of the old guard within the Chilean military, who are especially interested in obstructing punishment of human rights violations.

The government was able to prevent the escalation of conflicts that could take structural shape within Chilean society, especially class social differences, regional disparities, and the human rights issue. It was only partially successful in reducing existing imbalances, however. Socioeconomic disparities have been barely reduced, but they were somewhat ameliorated by job creation measures and the introduction of unemployment insurance. Greater progress is discernible in the split in Chile over issues of punishing human rights violations, which has also contributed to greater openness to reconciliation.

5.6 International cooperation

Since 1990 Chile's political actors have closely targeted the use of international aid to the requirements of its transformation and demonstrated an ability to learn. In many areas of its reform policy, the Lagos government works together with international organizations such as the IMF, the World Bank, UNDP, the Interamerican Development Bank and the EU. The government has used international aid deliberately and efficiently in regard to economic reforms.

The role of external actors in the democratic transformation process was concentrated primarily within the areas of state and judicial reform during the reporting period. In regard to other regional powers and within the framework of regional and international organization, Chile has proven to be a reliable and cooperative partner. In its regional environment, the government was able to reduce existing differences with Peru and Bolivia. The Lagos government energetically and successfully continued to expand and deepen as many international cooperation agreements as possible, for example by signing further significant free trade agreements with the EU, United States and South Korea.

6. Overall evaluation

In regard to baseline conditions, status and evolution, and actors' managerial performance, this report comes to the following conclusions:

(1) *Baseline conditions:* In comparison to the situation in 1990 immediately following the Pinochet dictatorship, the democratic transformation had made further progress as of the beginning of the reporting period. Even before 1998, stateness was fundamentally assured, freedom of assembly and association as well as free and fair elections were guaranteed, checks and balances and especially an independent judicial system functioned, corruption was low, and there were no more human rights violations. In contrast, authoritarian enclaves remained intact, the military as an anti-democratic actor with veto power had not been neutralized, and punishment for human rights violations committed under the dictatorship had been achieved only in individual instances.

In regard to the transformation to a market economy, Chile enjoyed a stable market economic regime even prior to 1998 that provided the foundation for persistent growth until the externally induced crisis of 1998–99. Foreign trade was deregulated, the macroeconomic situation was stable, inflation low, privatization of state enterprises generally complete, the banking and financial systems very solid, and social welfare reformed and supported by the expansion of productive social policies. Deficiencies in education and health care remained, however, and, despite a striking reduction in poverty, the country is still marked by social and regional disparities.

(2) *Status and evolution:* The road traversed toward democratic transformation has been short. While political decision-makers did not succeed in abolishing authoritarian enclaves, they were able to weaken their effects. The military is beginning to increasingly distance itself from the Pinochet dictatorship and integrate into the democratic regime, there has been some progress in coming to terms with human rights violations, and the judicial system has been further consolidated. There are no discernible internal threats to democracy. Overall, the democratic transformation was qualitatively deepened, while still in slow steps.

The road traversed toward transformation to a market economy was also rather short, although it started from a high level. Here due weight must be given to the fact that economic crisis required restabilization of economic development, which was largely achieved. The framework structures of a market economic regime were improved as well. The transformation process continues, however, from an export economy based primarily on the exploitation of natural resources to a viable, knowledge-based export economy and, despite setting an initial course, it still requires substantial work.

(3) *Management:* The conclusion on the managerial achievement of essential transformation actors is positive. During the evaluation period, management of the economic and political transformation process maintained, in all regards, the high quality of previous periods. This also applies to the definitive elimination of authoritarian enclaves, which is yet to be accomplished. In view of the difficult

institutional and political framework conditions surrounding the passage of appropriate constitutional reforms, the use of favorable windows of opportunity to ameliorate these defects must be evaluated as a managerial success.

7. Outlook

This overall positive picture of Chile's transformation is highlighted by the judgment of numerous observers that the Chilean transformation has by and large succeeded. This transformational success is quite substantially the transformation achievement of "internal" actors. The key strategic tasks to be solved in terms of democratic and market economic reforms are 1) the elimination of authoritarian enclaves which affect participation and the effective power to govern, 2) the stabilization of patterns of democratic representation and attitudes, 3) establishing more justice concerning the human rights issues, and 4) ensuring the social, ecological and technological sustainability of economic development, including above all the elimination of the huge social inequalities.

In order to eliminate authoritarian enclaves, which formally requires constitutional reform and is thus difficult, favorable opportunities will have to be used, as they have been, to emphasize the enclaves' illegitimacy. A time line for reforms could be found in the presidential election campaign in 2005, in which most likely Joaquín Lavín from the till now blocking party UDI will run as the candidate of rightist coalition. A clever strategy could force him to support the necessary reforms for reasons of legitimacy. The generational change that has begun in the military can be directed toward further isolating the remaining "old guard" and thus ensure the *de facto* subordination of the military to civil authority even prior to constitutional reforms.

A more concise version could then also include the government's human rights policy, which has been left to the slow wheels of the law, rather successfully to date. A comparatively larger challenge is the pending transformation of the economy. While Chile has long since surpassed all other Latin American countries in the maturity and solidity of its economic formation, it must nonetheless use this favorable phase to set a course away from export-led growth and toward growth-led exports. This should be tackled during the remaining term of the Lagos government so that successive administrations will be bound to that process.