Economic Analysis

Lessons from Chile: Market and State must complement each other

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In the last thirty years, Chile has experienced an economic miracle. It went from having a GDP per capita 50% lower than that of Mexico in 1974 to one 47% higher in 2022. In that period, it went from being a country in the middle of the table in Latin America to being, without a doubt, the most advanced economy in the region.

Not only was this significant economic growth observed, but there were also great social advances. The population living in poverty went from more than fifty percent in the mid-1980s to only six percent in 2017. In addition, schooling increased significantly, as did access to health. Progress was even made on the issue of inequality, a chronic problem in Chile: the Gini coefficient, which indicates less inequality the closer it gets to zero, went from 0.56 in 1987 to 0.44 in 2020.

Despite all these advances, beginning in 2019, Chile experienced enormous protests and social discontent, which led to the election of Gabriel Boric and the process of promulgating a new Constitution. How can these protests have occurred in the Latin American country that has experienced the most remarkable economic and social progress in the last half-century? This is the question posed by the economist at the University of California, Los Angeles, Sebastián Edwards, in a magnificent recently published book called "The Chile Project. The Story of the Chicago Boys and the Downfall of Neoliberalism." It is a complete and fascinating economic history of Chile written, it seems to me, objectively, and that leaves essential lessons for Mexico.

The Chicago Boys are a group of Chilean economists trained at the University of Chicago who played a decisive role in designing the economic policies implemented during the Pinochet dictatorship (which, of course, was characterized by its violations of human rights). These economists eliminated price controls, partially opened the economy to international trade, privatized companies, stabilized public finances, deregulated the economy, and granted autonomy to the central bank. All this resulted in a stabilization of the economy and higher growth. However, crucial mistakes were also made, such as maintaining a fixed exchange rate that resulted in a real overvaluation of the currency and aggressive bank deregulation. These two factors led to a substantial economic and financial crisis in 1982.

What is interesting about the Chilean case is that when democracy returned and center-left parties united in the Concertación came to government, they decided to continue with the policies of economic liberalism, although with greater emphasis on social policies. In fact, it was really until the arrival of the Concertación governments that Chile achieved high growth rates with substantial advances in social matters. So why did the social outbreak occur? Edwards mentions several factors. The new pension system stands out. It changed from a pay-as-you-go one, in which the value of the pension was previously defined, to one of individual accounts in which the amount obtained in retirement would come from the savings and their returns. Contrary to what the reform's promoters predicted, pensions were clearly lower than those of the previous system, which generated social discontent. On the other hand, Edwards points out that, although inequality decreased, it remained high, supporting a feeling that the game's rules weighted in favor of the elites

What lessons does Chile leave for Mexico? First, growth is a necessary but not sufficient condition to achieve social welfare. Inequality matters. Some of the Chicago Boys argued that as long as poverty decreased, inequality didn't matter. The Chilean case shows us that social cohesion depends on not having excessive levels of inequality. Another lesson is that markets are the most efficient mechanism for producing goods and services in most cases. Still, some essential services, such as health, education, and pensions, cannot be left exclusively to the invisible hand.

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