

## Chile fights to stay top of class

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By Jude Webber in Santiago

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Rich in copper and with enviable macroeconomic stability, investment-grade credit ratings and dramatic poverty reduction in the past two decades, Chile has become used to being top of the South American class.

Now, as Peru and Colombia emerge as the continent's high growth stars, Santiago has started to hear the depressing words "could do better".

Inflation has soared to a 12-year high, official growth expectations have been revised downwards and exporters - whose copper, salmon, fruit, cellulose and wine benefit from free trade deals with 58 countries - say the dollar's weakness against the Chilean peso is hurting their ability to compete abroad.

"We are growing less than we'd like and less than we could," said Felipe Morandé, dean of the economics faculty of the University of Chile.

But do not write Chile off yet. Investment is flooding in - the country nearly doubled its inward investment in 2007, according to new UN figures - and cautious husbanding of the revenues from record copper prices means the government has \$20bn (£10bn, €13.5bn) in public funds and is spending 8-9 per cent of GDP a year in areas such as education, housing and health.

The government has also pulled off a feat that has eluded many rich countries with ageing populations: a landmark overhaul of its already much copied private insurance system, promised by President Michelle Bachelet as her first priority when she took office nearly two years ago.

The reform, which takes effect in July and will cost \$130m for the remainder of 2008, rising to 1.1 per cent of GDP by 2025, will boost payments to old people on tiny pensions, offer incentives to young people to start saving for their retirement and pay mothers who give up work 1½ years in contributions for every child - important in a country where only just over a third of women have jobs.

"In spite of the fluctuations of the world economy, in spite of instability as a result of the financial crisis, in spite of unprecedented high oil prices and problems with imported gas supplies, the Chilean economy continues to grow at a steady pace - 5.2 per cent in 2007," says Andrés Velasco, finance minister.

"It's very hard to quarrel with that, it's a very respectable growth rate," he told the Financial Times.

The economy had been expected to grow up to 6 per cent in 2007 and inflation was also more than double the central bank's target range, although prices were in line with expectations when energy costs and food prices, which soared after increases in international prices and severe frosts, were stripped out.

"Five to six points of inflation last year came from food or energy," José De Gregorio, central bank governor, said.

"This is not relaxed monetary policy but unanticipated shocks, and in order to bring inflation back to target, avoiding undesired spillovers to other prices, we have been tightening."

Eduardo Engel, Yale economics professor, says Chile's fiscal management has been "far more responsible" than that of its peers, meaning less severe falls in growth rates when the commodities boom finally ends. Indeed, he reckons that at the current pace Chile is on course to catch up with southern European per capita income rates by 2020.

"I don't think Chile will have any problems in the next two years . . . on the macro side there's no problem. All the problems are microeconomic and public management," says Juan Andrés Camus, managing director of financial services group Celfin Capital.

However, despite this progress, Ms Bachelet has struggled.

Her four-year term has been marred by the botched introduction of a new transit system in Santiago and protests over education and mining strikes dented her popularity with disgruntled voters who want a bigger slice of the nation's prosperity.

The ruling Concertación coalition has lost its majority in Congress and this month the president reshuffled her cabinet for the third time.

The latest cabinet, with a trusty veteran in the key interior ministry, is widely seen as a sop to other parties in the Concertación, which has governed Chile since the return of democracy in 1990. "I think she gave in [to parties in the Concertación] because she doesn't want to be responsible for losing the election," said Marta Lagos of polling group Latinobarómetro.

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