

# Latin American Countries Stuck in the Field of Development Theory: A Case Study of Chile

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## ABSTRACT

This manuscript conducts a nuanced exploration of the ramifications associated with the adoption of neoliberal development theories in Latin America, with a particular emphasis on the Chilean experience. It delves into the comprehensive implementation of neoliberal reforms under the auspices of the Washington Consensus during the 1970s, charting the trajectory of Chile's economic hardships, its subsequent period of growth, and the enduring challenges of socio-economic inequality and insufficient social welfare systems. Despite Chile's transformation into one of the region's most affluent countries, the analysis exposes the intricate relationship between economic advancements and the overarching well-being of society. The widespread protests in 2019 against entrenched neoliberal policies serve as a poignant critique of the tangible disconnect between macroeconomic success and the populace's quality of life. Through this case study, the paper advocates for a recalibration of development theories to equally value human rights and social progress as indispensable counterparts to economic prosperity, proposing a more integrated framework for sustainable development.

## KEYWORDS

Neoliberalism; Development Theories; Chile; Washington Consensus; Economic Growth; Social Welfare; Income Inequality; Latin America; Socio-Economic Impact; Public Demonstrations.

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## 1. INTRODUCTION

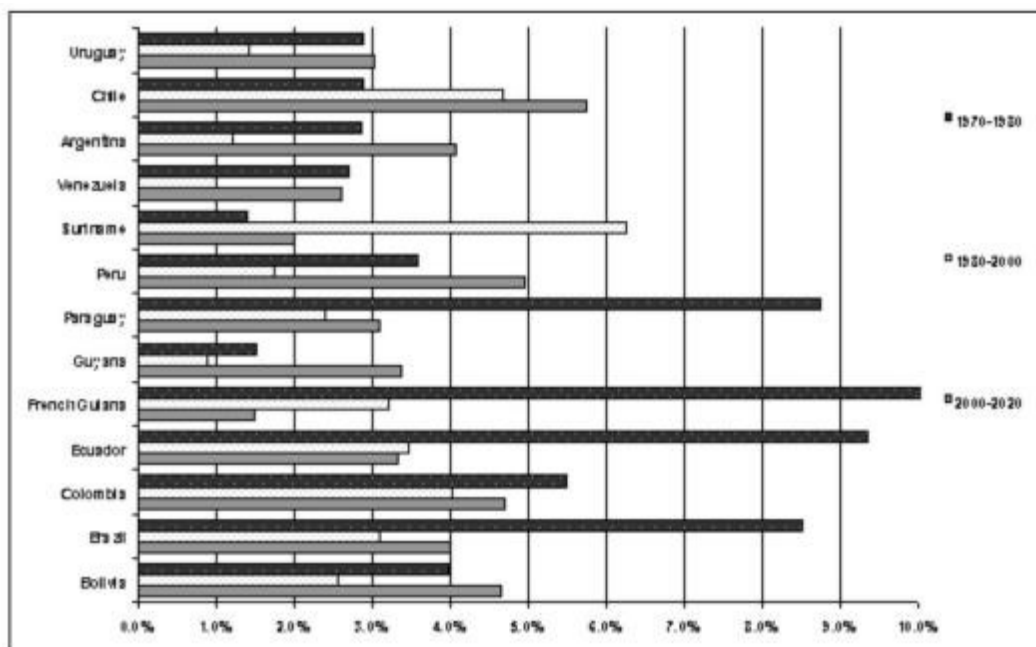
Latin America, a continent full of sadness, is continuously contested by foreign powers and has never taken control of its own destiny. (Diamond, 2017) Whether as a distinctive tribal nation during the early period or as a rapidly developing civilization empire during the late period, Latin America has always been one of the most brilliant pearls in human history. However, external powers, including the early Spanish Empire, the late United States or the Soviet Union, are always trying to influence the independent development path of this continent. (Weyland, 1996).

As a arena of great powers, Latin America is affected by the extreme political ideology of the powerful countries outside the region and various economic policies derived from it. Therefore, to a certain extent, Latin America has actually become a testing ground for various development theories where numerous development theories have taken root and been put into practice. As one of the Latin American countries with the deepest degree of international integration, Chile chose a development path with typical Washington consensus color under the influence of neo-liberalism guiding ideology in the 1970s. Thus, the research on Chile's economic development can provide some case support for developing countries in the region in adopting neo-liberalism development theory. (Davis-Hamel, 2012).

## 2. ECONOMIC REFORMS AND THEIR SOCIO-ECONOMIC IMPACT IN CHILE: A NEOLIBERAL EXPERIMENT

The development of neo-liberalism in Chile has experienced typical stage characteristics of neo-liberalism over the past decade, especially the characteristics of the first stage. In September 1973, General Pinochet came to power through a coup and started to take over a country experiencing large fiscal deficits and large debts. (Grandin, 2006) At that time, in the context of economic globalization, the globalization project led by the United States had a broad market in Chile. (Berger, 2005) Nonetheless, this process is actually two-way. Historical data explain that the reason why the Washington Consensus has a wide market in South America is that several countries in the region were ruled by populists and authoritarian governments.

Also, what Peru Fujimori's "self coup" or Argentina's Menem and Chile's Pinochet reform have in common is that the leaders have more centralized control over the government, which plays a significant role in fundamentally reforming economic policies. Therefore, it is not so much that the leaders of Latin American countries chose neo-liberalism as that neo-liberalism found its own way.



**Figure 1.** Historical and projected average annual growth in real GDP from 1970 to 2020-South America

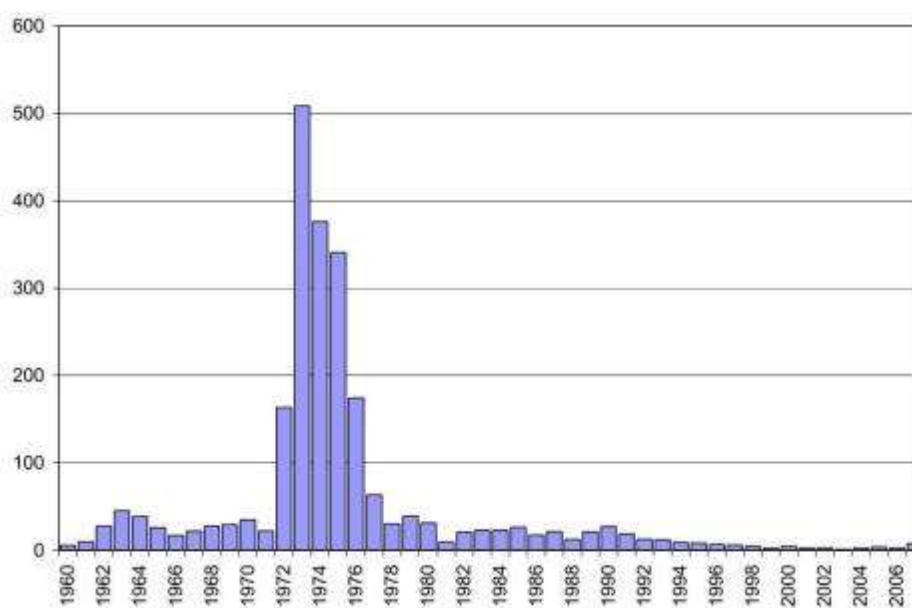
Source: World Bank (1994, 1999a and 1999b), IMF (2000) and CIA.

In Chile, in order to pay off the debt as soon as possible and ensure the normal operation of the government, General Pinochet chose to rely on a group of "Chicago disciples" who accepted and understood the western market economy theory to carry out the first neo-liberal reform in trade, finance, social security, labor and other important fields of Latin America. The guiding ideology of these reforms is: "Once the rule of market forces is established, resources will be reallocated (at no cost) to the export industry with comparative advantages, thus driving both exports and the rapid growth of the entire national output." (Agosin, 1998) On the advice of the "Chicago Disciples", the military government began to adopt the "shock therapy" and attempted to borrow loans from the IMF. Also, the government cut the national expenditure by 27%, reduced tariffs significantly and lifted restrictions on foreign investment. (Harvey, 2011) Furthermore, General Pinochet made a very wise decision to withdraw Chile from the alliance formed with its neighbors and to promote regional industrialization. Under the influence of reformism, some radicals believe that any economic integration in Latin America will be more beneficial to foreign investors than local investors, and

support the withdraw from the economic integration alliance. In fact, Chile has become an important import of cheap goods into Latin America.(CHEW & DENEMARK, 1996).

After the start of the reform, it experienced pains in the 1970s, such as a 13% drop in GDP, a 28% drop in industrial output, and a sharp drop in purchasing power to only 40% of that in 1970, (IMF. Western Hemisphere Dept., 2008)and these were objective side effects of following the Washington Consensus. The government entrusted most of the state-owned enterprises and public affairs to foreign capital and private capital, which caused tens of thousands of government staff to be laid off.(Peet & Hartwick, 2015).

Meanwhile, the opening of foreign trade and the adjustment of the financial system also made the inflation at this stage reach a very alarming height. What's worse, the inflation has led most Chileans to live a passive and low-quality life for a long time. Even 20 years later, Chileans' income and life have not improved significantly with the development of the country's economy.



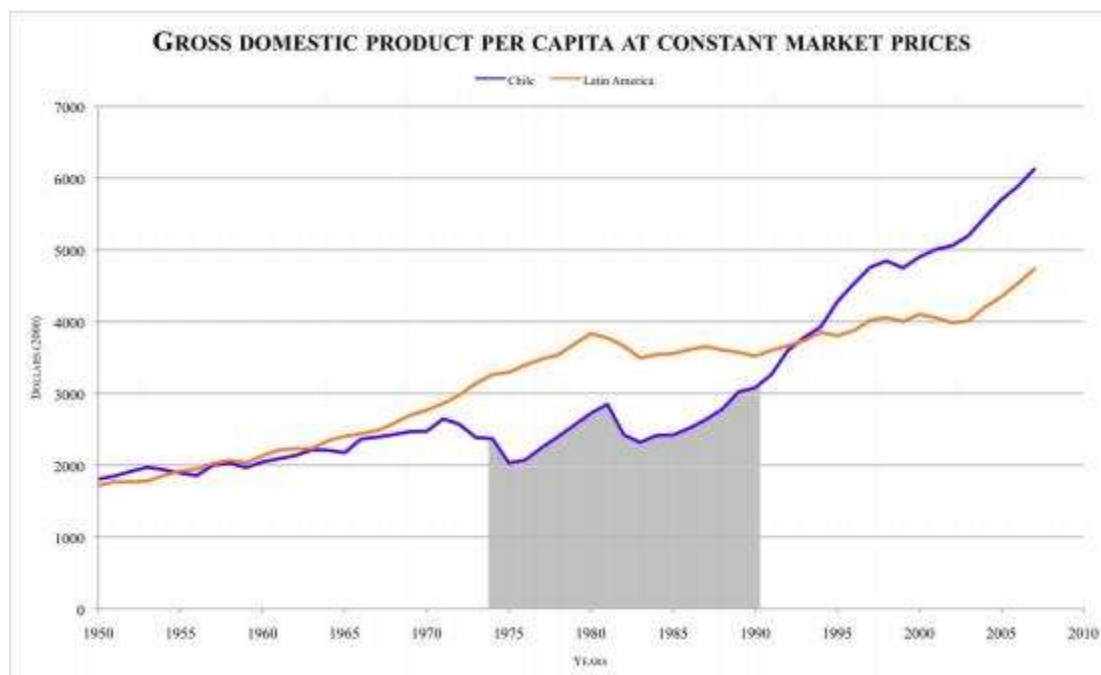
**Figure 2.** Chile:Inflation rate 1960-2007(in percentage per year)

Source: Three Decades of Neoliberal Economics in Chile Achievements, Failures and Dilemmas  
 Andrés Solimano

Chile's economy did not begin to rebound until 1978. After the transformation of economic liberalization and political authoritarianism, Chile achieved the goal of economic growth of 32% in just four years, which was actually achieved by the influx of foreign capital. However, the military government had already been overwhelmed by short-term victory and implemented the fixed exchange rate system with the US dollar in June 1979. The essence of this behavior is to gain the trust of foreign investors. Nevertheless, the Chilean government neglect an economic problem, that is, the dollar is hard currency and the peso is soft currency. Once the inflation rate of the peso is lower than the inflation rate of the dollar, Chile will be in serious danger of borrowing. Thus, as a result of the huge fluctuations of copper price around the 1980s, Chile experiences a two-year economic recession after the foam burst in 1982.

In the 1980s, most third world countries and colonial countries fell into economic recession due to the oil crisis. They found that their economic situation was even more fragile than that in colonial period. This period of time was even called "the lost decade" by other Latin American countries. (Leys, 1996)However, after a short recession in the early 1980s, Chile further implemented the disciplines in the Washington Consensus and gave the Central Bank more power, which enabled Chile to achieve strong economic growth in the late 1980s. Until 1992, Chile's unemployment rate

dropped significantly, and the average GDP growth rate reached an amazing 6.2%, and it entered a period of rapid growth in the 1990s. It even crossed the threshold of \$10000 per capita income defined by the "middle-income trap".(Bosworth et al., 1994).



**Figure 3.** Chile (blue) and South America (orange) GDP per Capita (1950-2010). Source: Angus Maddison, Historical Statistics for the World Economy: 1-2003

It is believed that the Washington Consensus actually plays a essential role in this stage. Chile has indeed ended high inflation and resumed growth under the guidance of neo liberalism. However, this guiding ideology, which makes economic data look good in form, fails to make any significant contributions to poverty alleviation and development. For example, the World Bank, hoped that Chile could go further in combating poverty, especially increasing public spending to promote primary health and education.(Williamson, 2000) However, the Chilean government did not follow the expectations of the World Bank. Instead, it chose to privatize most of the social security services, such as the privatization reform of pensions in 1981. The main content of this reform is that the insured can receive 70% of the salary before retirement. However, according to OECD data, until 2017, the amount of this retirement salary in Chile has not exceeded 40% before retirement. If calculated according to the proportion in 2018, the final pension that the insured can receive is only one third of the minimum wage, far less than 70% of the pre-insurance publicity. This is the possible significant negative impact of New Freedom's attention to the reform process. Excessive attention to the country's own economic growth will lead the country to reduce its intervention in the social security system related to the national economy and the people's livelihood. Actually, the Chilean people at the middle and lower levels do not get much benefit from the important distribution link of social security, and the attention even produces large-scale social problems, such as protest marches and urban public security.

Moreover, because neo-liberalism excludes state intervention and government guidance, the unrestrained private capital, driven by the instinct of pursuing profits, focuses on the copper mine development industry with low risk and high return. As a consequence, it solidifies Chile's fragile and single industrial structure. At the same time, under the requirements of the Washington Consensus, the Chilean government has weakened its control over the macro financial field, which makes Chile's financial risks gradually recede on the uncontrollable road. (Stiglitz & Chang, 2001)These risks are also reflected in the difficulty in controlling inflation. Although this is the main macroeconomic malady of Latin American countries under the background of the Washington

Consensus, this malady can be addressed by further strengthening the construction of the market economy.

Even after Pinochet stepped down, his successors were generally neutral or left-wing populists, but they did not abandon the free market economic policy created by Pinochet. At the same time, the neo-liberalism imposed no restriction on the market and capital, leading to the widening gap between rich and poor as well as severe polarization. Besides, all resources inclined fully and systematically to capital rather than labor. The failure of neo-liberal reform to provide a fair and balanced social policy to solve the problem of economic inequality had led the Chilean populist government, which boasted of left-wing or progress, to coming to power and re-adopting policies and programs to strengthen the role of the state (Martin Jacques, 2016), including the return of state-owned enterprises and the implementation of a more powerful and broader anti-poverty plan. (Lang et al., 2018) This, to some extent, declares that the combination of right-wing populism and neo-liberalism is difficult to adapt to the development of the new era.

### 3. CONCLUSION

In October 2019, the largest demonstration took place in Chile in which people held flags and shouted the slogan "not 30 pesos, but 30 years" to protest against the rise in subway ticket prices. This has forced us to rethink what neo-liberalism and the Washington Consensus have brought to Chile's development in the past 30 years, whether it is the growth of the country's economy or the improvement of people's lives?

While these development ideas objectively helped Chile recover from the economic crisis and become one of the richest countries in Latin America, does the development of a country really mean that people's lives and rights will be developed along with it? In fact, the people's income did not get much improvement and the democratic process even stagnated or even regressed, which are the inevitable side effects of the use of neo liberalism. (Hickel, 2016).

To adopt what kind of development theory depends on very complex internal and external conditions as well as historical and realistic factors. Although neo-liberalism and the Washington Consensus had played a positive role in the development Chile, countless development theories were selected or abandoned in Latin America and the interests of the people were not really developed or, more precisely, ignored in the process of implementation. Therefore, we hope that people's rights and lives can take a higher priority in the guiding ideology of development and be truly practiced in the process of development no matter what kind of development theory the country adopts.

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