

# Chile Copper Windfall Forces Hard Choices on Spending



Ian Salas/European Pressphoto Agency

Students demanded free bus rides and other benefits during a strike and protests in Santiago last summer.

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SANTIAGO, [Chile](#) — President Michelle Bachelet is learning the hard way that it really is possible to have too much of a good thing. Record prices for copper, Chile’s main export, have given her government a multibillion-dollar windfall but have also produced unexpected economic side effects and set off a sharp political debate about how to use the money.

Within Ms. Bachelet’s center-left coalition — mainly her Socialist Party and the Christian Democratic Party — pressure has been growing to apply the bonanza to the “equality agenda” she has promised. But the president and her cabinet have been hesitant to do anything that may undermine Chile’s reputation for cautious fiscal management.

Chile must apply the unanticipated revenue only “in an ethically and economically sound manner,” Paulina Veloso, Ms. Bachelet’s chief of staff, said in an interview. “You can’t spend a fortuitous bonanza the way you can permanent income.”

During the campaign that preceded her election as president last January, Ms. Bachelet, a former minister of health and of defense, pledged that her government would be even more committed to social investment than those of her predecessors. Voters took her at her word, and when signs of change had not appeared by midyear, hundreds of thousands of students took to the streets to demand an immediate overhaul of the education system.

“Chileans are patient, but one should never abuse that patience,” said Ricardo Ffrench-Davis, a prominent economist who wrote “Economic Reforms in Chile: From Dictatorship to Democracy.” “Ours is a country of great inequalities, and the perception of Chileans is that we need more social justice,” he said.

Driven largely by China’s seemingly insatiable demand for metals of all kinds, the price of copper quadrupled from 2003 through 2006, reaching record levels at midyear before falling to just under \$3 a pound at year’s end. That increase helped Chile build its foreign reserves and buttress its budget surplus, which in turn have been factors in the rise in the value of the peso against the dollar.

But that has made Chile’s exports relatively more expensive and less competitive, generating complaints from producers of wine, fruit and other items. Concerns that inflation could be fueled have also emerged, with suggestions — unpopular with consumers and businesspeople alike — that interest rates be raised to prevent an inflationary surge.

To reduce pressure on the peso, some of the windfall has been deposited in banks abroad, in foreign currencies. Some has been designated for an “economic and social stabilization fund” that “you draw on when you need it,” said Andrés Velasco, the minister of finance.

Part of the windfall is to help reform the privatized pension system. But Mr. Velasco argues that Chile should maintain discipline and not overspend or assume that the high copper price is permanent.

Unlike other Latin American countries, Chile “spends practically nothing on interest payments, because we have been able to reduce

public debt” and instead use the savings for social programs, Mr. Velasco. “This is very important and speaks of the payoff for fiscal responsibility.”

But that is not what many members of Congress want to hear. The Christian Democratic Party, for example, organized a commission that concluded that part of the price increase was in fact permanent and recommended more state investment in projects such as rural water supply, sports facilities in poor areas and programs for the elderly.

“This can be done,” said Mr. French-Davis, who was a member of the commission. “The Chilean economy continues functioning as if the price of copper were still 99 cents a pound. We need a stimulus. We don’t need to go into debt. We have the dollars; we’re awash in dollars.”

The situation has been further complicated by a law that guarantees the armed forces 10 percent of government revenues from copper. The statute has been on the books for decades, but it was made more generous during the dictatorship of Gen. [Augusto Pinochet](#) and has not been amended since democracy was restored in 1990.

Since the start of the decade, the Chilean military has gone on a buying spree, spending \$2.8 billion for weapons, ostensibly to modernize old equipment. The purchases, which have led to expressions of alarm in neighboring Peru and Bolivia, include 10 Lockheed Martin F-16 fighter planes acquired from the United States, eight frigates, two submarines and, most recently, 118 Leopard IIA4 tanks from Germany.

Two years ago, a study done by three international economic research bodies concluded that Chile spent more per capita on the military than any other country in Latin America: \$90.88 per inhabitant. According to recent estimates here, the copper law will result in the armed forces receiving nearly an additional \$1 billion in 2007, which must be used for “military acquisitions.”

In contrast, General Pinochet did not build a single hospital during the 17 years he was in power, María Soledad Barría, the minister of

health, said. The democratic governments that have governed Chile since his fall have tried, with notable success, to compensate for those and similar lapses in areas like housing, education and pensions. But as the income of Chileans has risen, so have their expectations.

The copper law's largess to an institution with an abysmal human rights record has infuriated "the penguins," as the young students are called in a reference to their uniforms. In the June strike that paralyzed the educational system, student leaders posted a placard on the Ministry of Education building here that listed all of the "toys" the armed forces have been able to acquire and then asked, "What about us?"

The minister of defense, Vivianne Blanlot, has been leading a commission to study ways to begin phasing out the law, and Congress is expected to tackle the subject in 2007.

"There are going to be changes," said Ms. Veloso, the presidential aide, but whether they will let more money be salted away or diverted to social investment is unclear.