

# Chile is Losing Partner in Free Trade Agreements

By Hugo Fazio | December 14, 2005

Chilean President Ricardo Lago's signing of free trade agreements, particularly with the United States, has been one of his most noted accomplishments. Before signing each of the agreements, especially with the two largest world economies (the United States and the European Union), they were presented as key factors in increasing Chile's exports, and thus, economic activity and employment. The operating logic of this judgment was that since these were the two world's largest markets, exports would therefore substantially increase as markets theoretically opened up. However, after two years, the hopes and promises have not been realized.

In the period of January-August 2005, during which there was a large increase in Chilean exports because of foreign demand for these goods and a recovery in national demand, the predictions of export growth to the United States and the EU did not turn out to be comparable with the same months of the previous year. However, imports from these free trade partners skyrocketed.

In the first eight months of the last year of the Lagos administration, total exports grew 22.5%. Yet sales to the United States increased 15.5%, to the EU 11.5%, and to South Korea—with whom a treaty was signed at the beginning of the year—by 3.6%; all of these increases less than the overall increase. In contrast, with China—a country that Chile has not signed an agreement with—sales increased 46.2%, showing much stronger growth, along with other variables, among them economic expansion and the demand for raw materials as a result of accelerated industrialization. Chile continues to be fundamentally an exporter of raw materials.

Notably, imports from the countries with which agreements were signed grew spectacularly when the same comparison is made. Imports from the United States increased 54.9%, from the EU 44.0%, and from South Korea by 55.7%—all substantially higher than the 35.4% overall increase in imports. This data clearly shows which partners

have been the main beneficiaries of the free trade agreements.

In 2004, the first year of the U.S.-Chile agreement, similar results were seen. Chilean exports experience large gains, but export gains to the United States were lower than the usual growth in previous years. However, with imports from the United States the opposite occurred. Imports increased from the United States—the world's largest market—above the total percentage increase in Chile's imports.

The data for these two years show that the rate of growth of Chilean exports to the United States decreased, while the increase in imports intensified. The trade surplus in Chile's favor in bilateral trade, which in 2003 reached \$1,181.1 million and in 2004 continued to grow—although as a percentage imports increased more than sales—to \$1,654 million, from January to August 2005 it fell to only U.S.\$600.1 million. If that figure is projected across 12 months we can expect a surplus slightly over U.S.\$900 million. If this tendency continues, Chile could soon experience a trade deficit with the United States.

This change in bilateral trade was not unexpected. Chilean exports are mainly raw materials with little added value, which, before signing the free trade agreement,

Table 1

Balance of Trade per country, Jan.-Aug. 2005.

Source: Central Bank. Data stated as percentages of variation in relation to the same month of the previous year.

	Exports	Imports
National Total	22.5	35.4
United States	15.5	54.9
European Union	11.5	44.0
South Korea	3.6	55.7
China	46.2	39.9



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Table 2

## Balance of Trade Chile-United States 2004.

Source: Central Bank. In millions of U.S.\$ and percentages of variance in relation to the previous year.

	Exports	%	Imports	%
National Total	32,000.4	52.0	22,956.2	27.3
United States	4,820.4	25.4	3,166.4	34.0

entered the United States under reduced tariffs, a result of the U.S. tariff structure that concentrates protective measures in manufactured goods. Additionally, Chile had—before the agreement—industrial exports in the preferential tariff system, which allowed them to enter the United States without penalties. To the contrary, the United States was favored by an overall tariff reduction, which strengthened even more the already large difference between the two economies resulting from their differences in levels of production of goods and services, productivity, scientific and technological development, etc. As if that weren't enough, the United States did not give up any protective measures or subsidies. It was an unfair negotiation table that resulted in the accentuation of these differences.

### FTA Chile-United States and CAFTA: Uneven Relationships

The unequal relationship present in agreements with the United States became apparent again in the agreement approved by the United States in 2005 with five Central American countries (Costa Rica, El Salvador, Guatemala, Honduras, and Nicaragua) and the Dominican Republic: the agreement known as CAFTA. As in the previous agreement signed with Chile, its approval was gained by the White House by maintaining its anti-dumping mechanism and agricultural subsidies, but also, in the case of CAFTA, the United States established new restrictions that make the term “free trade” an oxymoron, placing restrictions on two of the strongest Central American industries: sugar and textiles. In the first instance, sugar, exports were limited to barely 1 % of the annual market for the world's largest economy. Basically, as the *Wall Street Journal* confirmed, “CAFTA promises slight relief for five Central American

countries and the Dominican Republic as it makes permanent a series of temporal preferences that the region already enjoys.” (July 29, 2005) At the same time, American pharmaceutical lobbies—who traditionally have an influence on the White House's decisions—gained protection against the production of generics even greater than in the United States. On the same note, as mentioned in the Human Development Report 2005 by the United Nations Development Programme (UNDP) “The United States gained many opportunities in market access for rice, to the extent that they obtained quotas temporarily tax-free, increasing annually 5%. More than a third of the rice exports of the United States will now enter tax free, in circumstances that formerly were subject to tariffs between 15% and 60%.”

CAFTA, from the American trade point of view, is unimportant. The six countries involved export to the United States in an entire year what Mexico sends in five weeks. At the same time, American exports to them reach U.S.\$17,000 million annually, equivalent to the annual exports of New Jersey. “CAFTA is a modest agreement between a whale and six small fish,” says *The Economist*. “The whale already admits 80% of the exports from the small fish without tariffs, and the Central American countries have already cut their tariffs from 45% in 1985 to 7%.” (August 3, 2005) The parties involved in CAFTA's approval in the United States gave it importance based on principle. The facts show that the benefits go to large corporations, which does not translate into protection for horribly-paid Central American workers. It is presumed that, as happened in NAFTA signed with Mexico and Canada, although on a smaller scale, it will induce American businesses to generate jobs in the signing countries, taking them away from the United States.

Table 3

## Trade Surplus Chile-U.S. 2003-2005.

Source: Central Bank. In millions of U.S.\$

Year	Exports	Imports	Surplus
2003	3,843.6	2,362.5	1,481.1
2004	4,820.4	3,166.4	1,654.0
2005	3,693.2	3,093.1	600.1

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## International Inequality

The Free Trade Agreements have evidenced how inequality is not exclusively a national but also international phenomenon. The 2005 Human Development Report by UNDP states that “success in world trade increasingly depends on the capacity to sell manufactured products with higher added value.” In Latin America, the document states, raw materials represent 72 % of Argentina’s exports; 83 % of Bolivia’s; 82 % of Chile’s; 90 % of Cuba’s; 64 % of Colombia; 88 % of Ecuador’s; 87 % of Venezuela’s; 78 % of Peru’s; and 66 % of Uruguay’s. In this aspect the region loses ground with developed countries, but also with Southeast Asia. “The comparisons between East Asia and Latin America show that in the production of goods with added value, Latin America has been losing market share,” says the report.

The UNDP report contradicts the idea, intentionally spread, that in international trade there are only winners. The countries that export raw materials very often suffer deterioration in their exchange, and for that reason should take advantage of stages such as Chile has experienced in past years, with a positive exchange, not obtained by only prioritizing fiscal surpluses. “When referring to development, some exports are better than others. The profit generated from petroleum and mineral exports can be bad for growth, bad for democracy, and bad for development,” concludes UNDP. The report also states that if Latin American countries continue as exporters of raw materials or products of low added value, the region could be delayed until the year 2177 to reach the current level of development in developed countries. In contrast, for China and India, who appear as economic powers with great potential in this century, raw materials represent only 9 % and 22 % respectively of their total exports.

The global trade regression is aggravated by the fact that the developed countries have large agricultural subsidies, special anti-dumping measures, and other trade barriers, all reducing the export capacity of developing countries and constructing barriers that have not been overcome by the successive meetings of the World Trade Organization. President Lagos, speaking at the United Nations world summit, mentioned that “anti-dumping is a mechanism applied unilaterally, that affects our growth.” He is right. The question is then, why he accepted the signing of trade agreements with the United States and European Union while leaving their anti-dumping measures, which grossly violate free trade, untouched. At the same time, he at first rejected agricultural subsidies, but by signing accepted them in the aforementioned agreements. Chile continues to suffer the negative consequences of both strategies

## Exporting Raw Materials

The process of opening the Chilean economy has led to profound changes in its productive structure. The export sector continues to grow, based on raw materials or products of low added value, while at the same time the production oriented to the national market is increasingly replaced by international imports. Industry loses ground as a percentage of the market. In 1996, manufacturing industries represented 17.5 % of total production, in 1999, the beginning of the Lagos government, it was at 17.4 %. In 2004, it fell to 17.1 % and it continues to fall. The free trade agreements tend to accentuate this tendency, as well as the diminishing role of the State, who therefore does not interfere with the foreign exchange market.

The effects on trade are the first concrete results of the agreement. Over time others begin to rear their heads, including in the social sector. Previous agreements signed with the EU and Canada limited themselves to the obligation of complying with internal labor standards, while in the agreement signed with the United States the obligations go much further, in a sector within which Chile suffers many setbacks. Chapter 18 of the agreement establishes a series of requirements that upon careful examination, Chile complies with very superficially. “Assuming the specific responsibilities in terms of worker’s rights,” says Diego Lopez, the legal labor specialist at the University Alberto Hurtado, “the Chilean State has acceded so that an important part of their credibility and stability in trade depends on the control of such rights, requiring efficient processes and guaranteed application of these rights, as well as budgeting for the costs of this compliance.” (October 3, 2005) These conditions are clearly not met. “Even though legislation exists on these topics,” recognizes the business newspaper *El Mercurio*, “compliance and budgeting are not as strict as is demanded of Chile. For example, workers’ health and security, even if it has improved, remains deficient.” (October 3, 2005)

The data speaks for itself. From January to April 2005, for example, the Metropolitan Health Organization evaluated 28 agroindustries, processing, and packaging operations in the Metro Area, citing 17 for insufficiencies in sanitary regulations and demanding of seven improvements in security measures. At the same time, seven were cited for pesticide poisoning.

In agriculture—Chile is an exporter of many agricultural products—labor rights are a farce. Legal measures prevent agricultural workers from using collective negotiation. A high percentage of workers don’t have contracts. The CASEN 2004 survey established that more than half of female temporary workers do not have contracts, leaving them without legal protection or health care. The problem is even worse in terms of work done by contractors.

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The possibility that sectors of the countries that import Chilean products will accuse the country of irregularities in terms of labor and environmental regulations is high. “Respect for workers’ rights is no longer an added value that one can optionally incorporate into business to assure profits or to differentiate oneself from the competition.” Daniel Lopez states, “It has become an indispensable condition to guarantee viability and stability of products sent abroad.”

## Intellectual Property and Chilean Development

As expected, the United States has progressively upped demands to comply with regulations regarding intellectual property which establish advantageous monopolies for groups that control specific scientific or technological advances. Chile is on the list created by the U.S. Trade Representative of countries being monitored for violations. The White House ambassador to Santiago, Craig Kelly, declared that this has had a negative influence on bilateral relations, insisting that Chile should rectify its said incompliance so that “Chile maintains its international prestige as a fair and responsible partner.” (September 29, 2005)

In the negotiations with the United States, the Chilean government was willing to make concessions in intellectual property in exchange for temporary benefits in trade issues, which as of now—as shown by the data on bilateral trade—have had a tiny real impact. “Regulations on intellectual property,” states the UNDP 2005 report, “are strongly linked to human development. They influence the conditions with which poor countries can acquire and adopt new technologies that they need to raise the quality of life and succeed in international trade. Any regulation of intellectual property should seek the balance between two objectives: creating incentives for innovation and the maximum

dissemination of the benefits of innovation.” The U.S.-Chile agreement provides a unilateral extension and expansion of patents for the United States. The agreements on Intellectual Property Rights of the World Trade Organization are headed toward accentuating the breach between technologically rich and poor countries.

The United States maintains all its existing restrictions while signing the agreement: anti-dumping mechanism, agricultural subsidies, and restrictions on labor movement. In contrast Chile was obligated to deepen its trade opening and capital movements, which aggravate economic inequalities. One of the most obvious results of this is seen in the large shifts in the exchange rate, now left absolutely to market variations. In the same tune restrictions on movement of labor persist. The agreement reduces drastically the role played by the Chilean State.

Particularly, shifts in capital are left completely open, which until now has had no negative side effects in terms of entrance and exit of resources in the short term, given that the country has basically maintained a margin in these movements. First, because of regulations—particularly the placing of short term capital—and later, after the Southeast Asian Crisis, because other countries in the region were seen as risky. As Joseph Steiglitz points out, “It’s an agreement with little benefit, among other things because it doesn’t allow the control of capital flows, a mechanism which Chile used in the 90s that contributed to its stability.” (October 2, 2004)

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*Hugo Fazio is an economist, university professor, and director of the National Center for Alternative Development Studies (CENDA in Spanish) <http://www.cep.cl/> in Santiago, Chile. He is a contributor to the IRC Americas Program [www.ircamericas.org](http://www.ircamericas.org).*

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Writer: Hugo Fazio

Editors: Laura Carlsen and Tom Barry

Translator: Katie Kohlstedt

Production: Chellee Chase-Saiz