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Trade Policy Review Body

TRADE POLICY REVIEW

CHILE

Report by the Secretariat

This report, prepared for the third Trade Policy Review of Chile, has been drawn up by the WTO Secretariat on its own responsibility. The Secretariat has, as required by the Agreement establishing the Trade Policy Review Mechanism (Annex 3 of the Marrakesh Agreement Establishing the World Trade Organization), sought clarification from the Government of Chile on its trade policies and practices.

Any technical questions arising from this report may be addressed to Mr. Raymundo Valdés (tel. 739 5346) and Mr. Arne Klau (tel. 739 5706).

Document WT/TPR/G/124 contains the policy statement submitted by the Government of Chile.

Note: This report is subject to restricted circulation and press embargo until the end of the meeting of the Trade Policy Review Body on Chile.

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SUMMARY OBSERVATIONS

(1) INTRODUCTION

1. Since its last Review in 1997, Chile has continued to reform and liberalize its already open trade and investment regimes. It has thus unilaterally reduced tariffs, streamlined customs procedures, ceased to apply capital controls, and floated the exchange rate. Inter-sectoral neutrality has remained a key feature of Chile's policies, as witnessed by an almost uniform applied MFN tariff, the absence of significant programmes to assist specific activities, and the granting of national treatment in government procurement and to foreign investors, in all but a few cases. Nevertheless, distortions might arise from the use of a price band system to protect a handful of agricultural products and of export support schemes. Sound policies help to explain the resilience of the economy in the face of various external shocks, although growth has been low compared with earlier years.

2. Chile has continued to show a strong commitment to the multilateral trading system, while also maintaining vigorous involvement in free-trade agreements (FTAs). In addition to the one FTA in force in 1997, Chile has signed seven new agreements, and is negotiating others. The growing number of FTAs is enhancing market access for some partners and increasing competition in Chile's economy. However, it has reduced the share of Chilean trade conducted under MFN conditions, is injecting complexity into its trade regime, may undermine the neutrality of economic policies, and may result in trade and investment diversion. Any resulting inefficiencies would be reduced if Chile carries on the unilateral liberalization of its economy, a strategy that has allowed it to achieve an enviable development record.

(2) ECONOMIC DEVELOPMENTS

3. Chile's economy has grown at an annual average rate of 2.4% since 1997. In 1999, the economy underwent its first recession since the early 1980s; growth resumed in 2000 but at lower rates than in previous years. A number of external shocks help to explain the sluggish GDP growth in recent years, including low copper prices, high oil prices, and contagion from financial crises in East Asia, Argentina, and Brazil; long-run factors may also be at play, including the slowdown of population growth. Per capita GDP stood at some US$4,340 in 2002.

4. A major development since Chile's previous Review is the adoption of a flexible exchange rate system in 1999. The Central Bank has been successful in lowering inflation, which fell to 2.5% in 2002. Since 2001, monetary policy seeks to achieve an annual inflation target of 2% to 4%, centered on 3%. With a view to reducing Chile's exposure to short-term capital flows and warding off appreciating pressure of the exchange rate, Chile applied controls on inflows of short-term capital until 1998, when it zero-rated the deposits to be lodged at the Central Bank. The FTA with the United States, signed but not yet in force, contains provisions on the transfer of capital.

5. Since 2001, fiscal policy aims to ensure medium-term fiscal stability, while permitting counter-cyclical measures in periods of slower economic growth. The authorities have sought to maintain a "structural surplus" equivalent to 1% of GDP, which since Chile's previous Review, has translated into modest fiscal deficits in 1999, 2001 and 2002.

6. Chile's external current account has posted a deficit in each of the past six years, except for 1999. However, the deficit has come down from its high 1996-98 levels, mainly because the trade balance switched into surplus in 1999. The deficit has been largely financed by FDI inflows, which have traditionally played an important role in Chile's economy; the mining sector has been the main magnet, although service activities have become major recipients in recent years.

7. Trade plays an increasingly important role in Chile's economy: the share of trade in *goods and services in Chile's GDP increased from 56% in 1997 to 66% in 2002. Chile's exports consist mostly of resource-based goods, with mining products, mostly copper, accounting for some 42% of merchandise exports and agricultural goods (WTO definition) for about 37%. Imports are dominated by a wide range of manufactured goods and crude petroleum.*

8. Chile's main export market is the European Union, followed by the United States and Japan. Chile's largest supplier is Argentina, just ahead of the United States and the European Union. Brazil and China are also important suppliers and have both increased their shares in Chile's imports.

(3) INSTITUTIONAL ENVIRONMENT

9. Chile is an original Member of the GATT and the WTO. The multilateral agreements form an integral part of Chile's legislation, with the status of ordinary law. Chile has been an active participant in the multilateral trading system; it took part in the extended negotiations on telecommunication and financial services and ratified the Fourth and Fifth Protocols to the GATS. Chile has been involved in eleven cases under the WTO dispute settlement system.

10. Chile's effort to further integrate into the world economy is also reflected in its participation in various regional and bilateral trade initiatives. Since 1997, Chile has entered into FTAs with Canada, Costa Rica, El Salvador, and the European Union, and expanded its agreement with Mexico. Further agreements, with the European Free Trade Association, Korea, and the United States, have been negotiated but had not entered into force as at mid-2003. In addition, Chile has partial scope agreements with all MERCOSUR countries, Bolivia, Colombia, Ecuador, Peru, and Venezuela, and participates in the negotiation groups of the Free-Trade Area of the Americas.

11. The increased number of Chile's preferential trade agreements are creating an elaborate system of different tariffs and rules of origin that could result in economic distortions. Applied tariffs vary across preferential agreements and product groups, generally as a result of the specific schedules of tariff reductions and the dates of entry in force of each agreement. The cost of these distortions, however, has not been quantified, and might be reduced by Chile's relatively low MFN border protection.

12. The investment regime grants national treatment to foreigners with only few exceptions. Investments made under the Foreign Investment Statute, a special voluntary investment regime, require authorization. Due to a long-standing privatization policy, there are very few state-owned enterprises left, but these include CODELCO, the world's largest copper producer. Since 1997, a number of seaports have been given in concession to private operators.

13. A draft law on miscellaneous WTO-related matters, sent to Congress in October 1999, was approved in August 2003. The bill aims to bring various individual provisions of Chile's legislation into line with the WTO Agreements; it contains provisions on customs valuation, technical regulations, taxation, and intellectual property. The bill also provides for the formal abolition of trade-related investment measures in the automotive sector.

(4) MARKET ACCESS FOR GOODS

14. Tariffs are Chile's main trade policy instrument. Chile grants at least MFN treatment to all its trading partners. The average applied MFN tariff has fallen from 11% at the time of Chile's previous Review, to 6% in 2003 Tariffs are applied at a generally uniform rate; exceptions include aircraft and vessels, which receive duty-free treatment, and a handful of agricultural goods (wheat and wheat flour, edible vegetable oils, sugar) subject to a price band system. Since June 2002, Chile has been applying a customs valuation system based on the WTO Customs Valuation Agreement.

15. In the Uruguay Round, Chile bound all its tariffs, most at 25%; a number of agricultural products are subject to a bound rate of 31.5% at the end of the implementation period. After the conclusion of the Uruguay Round, Chile pursued Article XXVIII renegotiations for sugar, resulting in an increase of the final bound rate to 98%, together with the introduction of Chile's single tariff quota. Closing the wide gap between applied and bound tariffs would increase the predictability of Chile's trade regime.

16. Tariff reductions under preferential agreements have also contributed to improved access to the Chilean market for partners. Duty-free access is offered to most imports from Canada, Costa Rica, El Salvador, Mexico, and the European Union. Preferential market access is also offered within the framework of partial scope agreements.

17. Irrespective of their origin and in accordance with the national treatment principle, imports are subject to domestic taxes, most notably a 18% value-added tax applicable on the c.i.f. value of imported goods. In addition, various goods, such as alcoholic beverages, jewellery, and vehicles, are subject to specific consumption taxes.

18. The use of non-tariff barriers appears limited. No import licensing system exists. Chile maintains various import restrictions and prohibitions, which apply equally to all trading partners, for reasons of health and environmental protection. It makes modest use of contingency measures; currently it imposes no anti-dumping or countervailing duties. Chile adopted domestic safeguard legislation in 1999 and has imposed seven measures since, some of which led to requests for consultation in the WTO.

(5) OTHER MEASURES AFFECTING TRADE IN GOODS

19. Chile has notified six support schemes involving subsidies. Since 1997, three of these schemes have been modified in order to bring them into line with the WTO Agreement on Subsidies and Countervailing Measures; the other three involve regional measures focusing on Chile's extreme northern and southern provinces. Two public export finance programmes are also in place. Since its last Review, Chile has streamlined export procedures, most notably by introducing a single export form. It does not apply export taxes or agricultural export subsidies.

20. As part of a broader project to reform and modernize the State, the Chilean Government has made efforts to increase transparency in public procurement, notably through the adoption of new legislation in July 2003 and the introduction of electronic tendering. Under this Law, national treatment is accorded to foreign suppliers. A new competition law is before Congress (mid 2003).

21. The WTO Agreement on Trade-Related Aspects of Intellectual Property Rights (TRIPS) became part of Chile's legislation through its ratification of the Marrakesh Agreement. Chile has undertaken legal and administrative reforms to facilitate the protection of intellectual property rights. New legislation on industrial property and copyrights is before Congress.

(6) SECTORAL POLICIES

22. As noted, economic policy is largely sector-neutral, notwithstanding special border protection for some agricultural goods provided through the price band system. Agriculture, fisheries and forestry remain crucial for employment and the generation of foreign exchange, Chile being one of the world's largest exporters of fruit, fish and fishmeal, and forestry products. Over the last few years, a certain diversification in agricultural production has taken place, including a shift from annual crops to fruit and vegetable production and stock-breeding.

23. Chile's highly productive mining sector generates more than 42% of merchandise export revenues, copper being its most *important single export product. Mining is also the most important recipient of foreign direct investment. Profits from CODELCO are an important part of government revenue.*

24. The contribution of manufacturing to GDP has declined in recent years, to about 16% in 2002. Manufacturing production and exports are based largely on the processing of natural resources. Chile is a net importer of all major categories of manufactured goods. Trade-related investment measures in the automotive sector were in place until their use was terminated with the entry in force of the FTA with the European Union in February 2003.

25. Services is the most important sector in the economy in terms of contribution to GDP and employment. Chile's foreign investment regime grants national treatment to foreign investment in services with only few exceptions, such as maritime transport. Foreign participation in Chile's services sector is substantial, most notably in financial services and telecommunications. Major legal reforms since 1997 include a new Bank Law, new legislation on capital markets, and the conclusion of a multilateral air transport agreement. Conditions for foreign participation in Chilean services sector are far more liberal than those implied by its GATS commitments; enhancing these commitments would thus increase the predictability of Chile's trade regime.