1. In accordance with its terms of reference, the Committee has conducted the consultation with Chile under Article XVIII:12(b). The Committee had before it a basic document for the consultation (BOP/45), a decision of the Executive Board of the International Monetary Fund, dated 6 January 1965 (see Annex II) and background documentation supplied by the Fund as mentioned in paragraph 4 below.

2. The Committee also consulted with Chile concerning Chile's request for an extension of the decision of the CONTRACTING PARTIES of 27 May 1959 which waived, subject to specified conditions, the provisions of paragraph 1 of Article II to the extent necessary to allow the Government of Chile to maintain certain surcharges. The Committee is presenting a separate report on that subject to the CONTRACTING PARTIES although the consultation was conducted with both objects in mind.

3. In conducting the consultation, the Committee followed the Plan for consultations under Article XVIII:12(b) recommended by the CONTRACTING PARTIES (BISD, Seventh Supplement, pages 97-98). The consultation was completed on 8 March 1965. The present report summarizes the main points of the discussion.

Consultation with the International Monetary Fund

4. Pursuant to the provisions of Article XV of the General Agreement, the CONTRACTING PARTIES had invited the International Monetary Fund to consult with them in connexion with this consultation with Chile. In accordance with the
agreed procedure, the representative of the Fund was invited to make a statement supplementing the Fund's documentation concerning the position of Chile. The statement, which was designed to serve both for the regular consultation and for the consultation concerning the waiver, was as follows:

"The Fund invites the attention of the CONTRACTING PARTIES to the Executive Board decision of January 6, 1965 taken at the conclusion of the last consultation with Chile under Article XIV of the Fund Agreement and to the background material prepared in connection with that consultation. Also on January 6, 1965 the Fund approved a stand-by arrangement with Chile authorizing drawings up to the equivalent of $36 million in the next twelve months.

"Chile's balance of payments was in approximate equilibrium in 1964, with a small increase in monetary reserves about offset by an increase in import arrears. Net reserves, however, remain at a substantial negative figure. In addition, sizeable debts have been accumulated on account of the compulsory deferment of import payments for 120 days and on account of arrears beyond this deferment period. It is not anticipated that net reserves will rise significantly in 1965. The general level of the various restrictive and import surcharge measures currently applied by Chile does not go beyond the extent necessary at the present time to achieve a reasonable rate of increase in its monetary reserves.

"With respect to alternative measures to restore equilibrium, the Fund invites attention to the decision taken at the conclusion of its recent Article XIV consultation with Chile. The Fund has no additional alternative measures to suggest at this time."

Opening statement by the representative of Chile

5. In his opening statement, the text of which is contained in Annex I to this report, the representative of Chile traced the history of Chile's efforts to establish a system of international trade regulations consistent with
Chile's obligations under the General Agreement. He recalled how fluctuations in the price of copper, Chile's principal export product, have at times hampered these efforts, as was the case in 1957-58. The earthquake of 1960 had also added enormously to Chile's burdens, and tax revenues have been inadequate, partly because of an outmoded tax structure and partly for administrative reasons, not to mention the fact that inflation itself hampers the collection of taxes at appropriate levels. A principal difficulty has also been inflation, all the more difficult to control as Chile has been engaged in an effort to promote industrialization and raise domestic living standards. The representative of Chile then explained that the new Government which took office in 1964 had addressed itself to these problems and had worked out comprehensive plans for reform of the tax administration which might enable Chile to remove the surcharges on imports and also contribute to controlling inflation. Up to now the lack of a working majority in Congress has hampered implementation of plans but late news indicated that the Government would no longer have difficulties on this score. For the immediate future, however, both the fiscal situation and the severe shortage of foreign exchange require that the surcharges continue and that they be used so as to limit imports to bare essentials. It is hoped, as a result of all the measures envisaged, to hold inflation to 25 per cent during 1965 and to reduce it to 15 per cent in 1966 and to 10 per cent in 1967. As consideration has meantime been given, within the General Agreement, to permitting less-developed countries having balance-of-payments difficulties to use surcharges as an alternative to, or in addition to, other restrictions on imports the representative of Chile hoped that it would be possible to extend Chile's waiver to the end of 1966.

Balance-of-payments position and prospects

6. Members of the Committee expressed sympathy with Chile's efforts to achieve internal stabilization. One member mentioned aid which his country was giving to Chile for this purpose. The representative of Chile noted that Chile's difficulties are well described in the Fund documentation. As there explained, a position near equilibrium in the balance of payments had been achieved in 1964, but there will also be need for continued capital inflow to cover Chile's deficit on the current
account. Also heavy accumulated external public debt created a need to arrange some deferment of payments. Payments of $30 to $40 million due in 1965 have been deferred. Multilateral negotiations on the public debt had recently been concluded in Paris, but the amount which Chile will be required to pay will also depend on bilateral negotiations with creditors which are still in progress. In general outline, the arrangement agreed upon is that Chile would pay 70 per cent of the public debt, with maturities of principal falling due in 1965 and 1966, including accumulated guaranteed commercial arrears, over a period of five years beginning after an initial grace period of three years. It was clear that theoretically it might be appropriate for Chile to use drastic fiscal measures to overcome inflation, but this would involve too great social costs. Consequently, the Government would do what it could internally and at the same time maintain a realistic exchange rate, promote exports by an array of administrative and credit measures, while maintaining strict control of imports.

7. A member of the Committee noted that it appeared that Chile would benefit greatly by the introduction of international arrangements to stabilize primary product prices, including copper. The representative of Chile agreed that a stable and remunerative price for copper would, if also favourable to the development of consumption, be of great benefit, especially as increased copper output is to be a prominent feature in Chile's development plans, along with plans to process more of the mineral locally. He noted, however, that this is by no means Chile's only need; as higher living standards for Chile's growing population imply a need for substantial growth of the economy.

8. Question was raised whether there were not some danger in Chile's programme that restriction of imports would lead to the development of new industries not necessarily suited to Chile's economy and that these might even attempt to export. In response to this and other questions concerning the development of Chilean exports, the representative of Chile said that Chile plans to effect a 78 per cent increase in exports over the next five years. The principal source of increase will be mineral products, of which it is hoped to export production
valued at $793 million in 1970 instead of $502 million as estimated for 1965. An increase in agricultural products exports from $30 million to $50 million will also contribute to the increased total. In the area of industrial products, an increase of exports for $50 million in 1965 to $185 million in 1970 is planned, principally in metallurgical products, products of the fisheries industry and the pulp and paper industries. Exports of products of the fisheries industry are to increase from $35 million to $70 million, and the paper and cellulose industries from $10 million to $50 million. To help effect these increases in exports, Chile has already negotiated with a number of private mining companies arrangements looking toward a doubling of Chile's output within the next four to five years; Chile has also adopted and will keep a realistic exchange rate and will implement various measures of export assistance, including better credit facilities. And, to ensure a net improvement in the balance of payments, imports will continue subject to very strict control.

9. In response to a question concerning export promotion measures, the representative of Chile added that besides the measures already mentioned, there would be tax rebates to promote exports, a new Foreign Trade Institute which would endeavour to promote exports and which would study such matters as quality standards, market research, advertising, etc., loans and credits to industries such as the fisheries were also contemplated. Finally, he said, special efforts would be made to develop LAFTA market, especially as LAFTA has up to now proved more effective in bringing imports into Chile than in promoting exports by Chile to its trade partners. However, he emphasized, this trade was too small a proportion of the total to affect the overall payments to any great extent. In assessing Chile's export programme, he said, it was essential to bear in mind that the export projections he had cited had been prepared on a conservative basis.
Alternative measures to restore equilibrium

10. There was general interest concerning Chile's efforts to increase internal taxation and other steps being taken to combat inflation. The representative of Chile stated at the outset that in his country it was impossible, for political and social reasons, to attempt an abrupt cessation of inflation. Instead, the Government envisages a gradual approach, improving at the same time the relative position of agricultural prices. For 1965 the target is to hold price increases to 25 per cent. This cannot be done by reduction in the Government's expenditures on development, which must increase for social and economic reasons. There should, however, be some possibility of reducing expenditure for current operations and the tax reform already in effect and a new tax on net worth proposed by the Government will greatly increase the revenue side of the budget. Also, certain tax exemptions are being re-examined and tax administration and implementation is being improved in order to obtain better yields. It should be pointed out that the external deficit, a consequence of the internal one, is not much greater than what the Committee of Wise Men set up by the Alliance for Progress considered necessary for Chile at this stage of its development policies.

11. A question was asked as to what developments there might be to report concerning what the Fund decision had described as the critical importance of pursuing restrained credit and wage policies; in particular it was noted that an important decision concerning adjustment of wages was scheduled to be taken early in 1965 and the question was asked whether anything was known about the outcome. The representative of Chile indicated that it was the Government's position that both publicly and privately employed workers were entitled to a wage increase equal to the amount of inflation in the past years, estimated at 38 per cent, and that legislation will provide for holding wage increases to that level in private contracts as well as in contracts with the Government.
12. With respect to the "prohibited list", it was asked whether goods in this category were really completely barred or whether the term meant that a licence was required to enter such goods. The representative of Chile indicated that, with some exceptions, goods not figuring on the permitted list are actually banned. Exceptions concern non-commercial imports, imports of scheduled products from LAFTA countries and imports into the so-called free zones located in sections of the country relatively remote from the main centres of population. He explained that there were also some goods which were listed as subject to deposits of 10,000 per cent. These might be described as effectively prohibited except when the Central Bank in specific cases waives the deposit requirement. Imports into the free zones were exempt from surcharge, but the goods may only be shipped into other parts of Chile from there after processing. Imports by large mining companies are also exempt from surcharge, as are imports by State enterprises.

13. A subsequent enquiry sought an explanation of the rationale of the exemption from surcharge of imports by these companies, of government agencies and of imports made under deferred payment arrangements or coming from LAFTA countries. The representative of Chile explained that such imports are controlled to a considerable extent in other ways. State enterprises may import only goods needed to carry out approved plans, and the imports of the copper companies, which operate under special exchange arrangements are reviewed by an agency which attempts to confine imports to goods not obtainable in Chile. All such imports are subject to licence. None of these cases involved discrimination between countries.
14. The policy of favouring the free zones was also questioned as possibly
tending to build up industry in locations in which it could not survive without
assistance, as for example might be the case with the auto-assembly industry
of Arica. The representative of Chile acknowledged that opinions differ in
Chile on this policy, but that such development is in fact in accordance with
laws in force at the present time.

15. A member of the Committee inquired what was the present status of the
proposal to switch to the Brussels Tariff Nomenclature and whether any changes
might result from adoption of that change. The representative of Chile replied
that the bill was awaiting action in the Congress and that the Government
desired to see it enacted. In answer to a further question, it was explained
that at the "projecto" stage, where the bill still is, there has been no action
by the Congress. The Government has not pressed for action up to now because
it did not have sufficient votes to ensure passage of the bill without crippling
amendments. When the Congress meets again in May, this situation may be
different, in which case progress will likely be made.

16. A number of questions were asked about the working of the prior deposit
and surcharge system. The representative of Chile explained that until recently
the system had been to require prior deposits in dollar bonds, in an amount
representing fixed proportions of the c.i.f. value of the proposed import.
Importers usually had to pay a rent for the use of such dollar bonds. More
recently, the bond deposit was replaced by a payment in Chilean currency of an
addition to the import surcharges already in effect and equivalent to the finan­
cial cost of renting the bond. Furthermore, in order to retain its power to
reimpose import deposits, if necessary, according to Chilean legislation, the
Central Bank requires the deposit of the surcharge at the time of the registration
of a new import and this amount is afterwards transferred to the Government.

17. Another recent change was made effective on 15 January 1965 when the
Central Bank was empowered to reject all applications for imports of any class
of goods if the applications in a given month exceed by more than 5 per cent the
average monthly importation of that class of goods over the past twelve months.
This power is optional with the Bank and, to ensure non-discriminatory operation, the Bank may only choose between granting all applications and rejecting all.

18. The question was asked how Chile justified, in economic terms, the exemption of one group of countries from charges and prior deposits levied on balance-of-payments grounds, especially as the exempted countries did not have a common monetary system with Chile. The representative of Chile replied that, unlike the situation in some countries where surcharges are used as a substitute for devaluation, Chile's surcharges and advance payment requirements could not at this stage be classed as pure balance-of-payments measures. Until the new schedule of duties came into effect, these charges were also acting to some extent as protective measures. When the new arrangements are fully in effect, a part of the present charges will disappear, but part will also remain and at that time Chile will have to renegotiate its obligations. It would be impossible to answer the question, in other words, except with respect to an individual product as the combination of the two elements varies. Vis-à-vis LAFTA countries, both elements have been removed entirely.

General

19. Members of the Committee indicated that, while they appreciated Chile's difficult situation, they had received complaints from traders that Chile's requirements were exceedingly complex, particularly on the matter of documentation required to effect imports. They hoped that Chile might be able to take this problem into account. The representative of Chile replied that he believed the system as now in force since 15 January might prove somewhat less complex.

20. The Committee thanked the representative of Chile for the information he had supplied, and he, in turn, promised that the views expressed by the Committee would be brought to the attention of his Government.