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## **The Chilean Economy and Job Market: The Impact of the Crisis in Specific Areas**

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# THE CHILEAN ECONOMY AND JOB MARKET: THE IMPACT OF THE CRISIS IN SPECIFIC AREAS

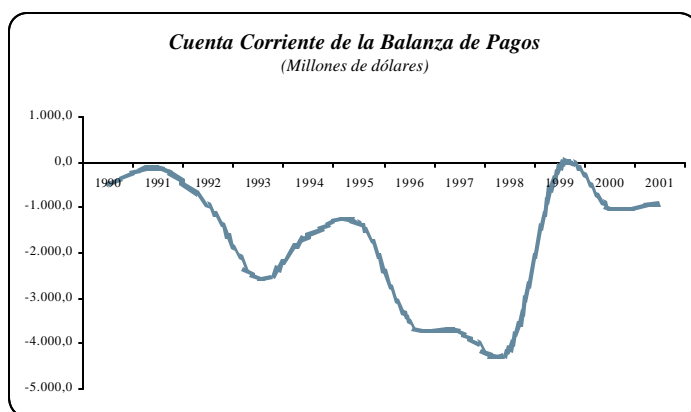
*Patricio Escobar S.<sup>1</sup>*

## 1.- Growth Prior to Crisis

In 1998, the Chilean economy reached the end of an extensive period of growth that began following the external debt crisis of the early 1980's. Subsequently, deep, neo-liberal, structural reforms were implemented. Indeed, the movement in this direction had begun years earlier, when, after the 1975 coup, the basic economic strategy that we live with today was initially outlined.

The current economic situation is directly linked to the balance of payments crisis that faced Asian economies in 1997. Nonetheless, this crisis simply triggered a problem that had been present for quite some time. Chile currently finds itself in the worst economic crisis in a decade with regards to its current account balance. This is due primarily to a significant trade deficit created during the 1990's.

GraphNº 1

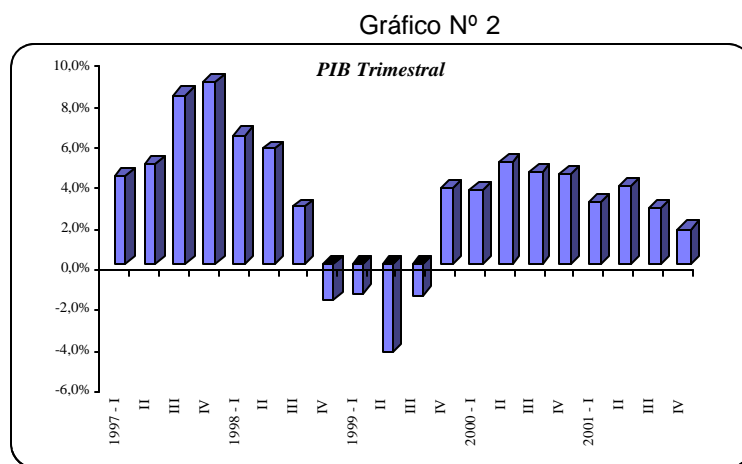


Fuente: Banco Central de Chile.

The adjustment policies followed by the economic authorities prompted a recession that lasted from the fourth quarter of 1998 to the third quarter of 1999, leading to an overall drop in the GNP of -1.1% for 1999. The performance of the current account, whose deficit in 1998 reached 6.3% of GNP, was somewhat tempered for most of the decade by

<sup>1</sup> *Investigador del Programa de Economía del Trabajo PET*

a positive balance in the capital account caused by significant investment in the primary sector, particularly in copper mining.



Fuente: Banco Central de Chile.

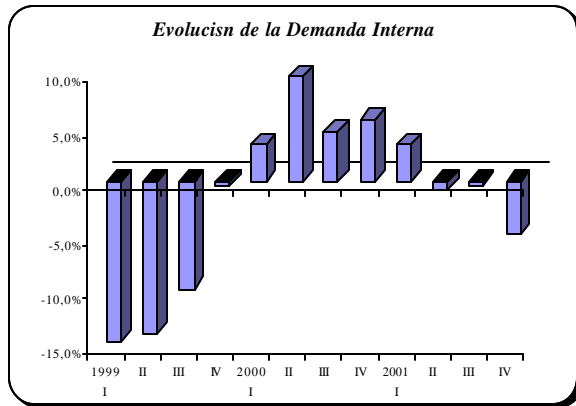
The gains by the Chilean economy during the 1990's not only distracted the authorities from the dangers of a large negative current account, but also contributed to a significant appreciation of the currency, which was ultimately responsible for the trade deficit in the final years of the last decade.

Given these conditions, the policy of implementing adjustment through raising interest rates drove the economy to contraction, where, along with production, internal demand dropped significantly. Added to this was a rise in unemployment and low expectations with regards to economic development and recovery. This economic situation precipitated the current one, in which a recovery from contraction and stagnation seems unlikely.

## 2.- A weak recovery that lead to the stagnation of 2001

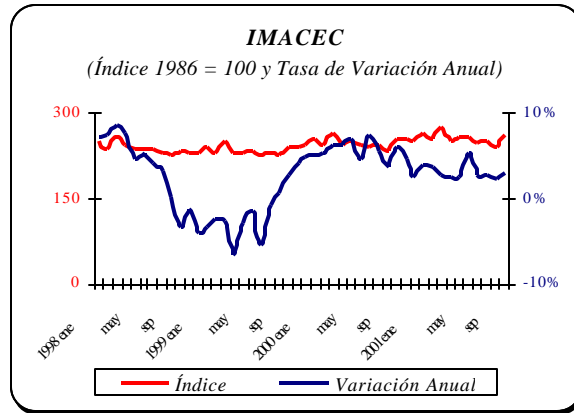
As show in Graph 2, economic production in 1999 began to show sings of recovery, reaching its peak at 5% in the second quarterquarter of 2000. The final result was that the economy had an overall growth of 4.4% that year. Nonetheless, from that point on we can see a marked deceleration, primarily in the performance of internal demand and the monthly general economic activity indicator (IMACEC).

Gráfico N° 3



Fuente: Banco Central de Chile.

Gráfico N° 4



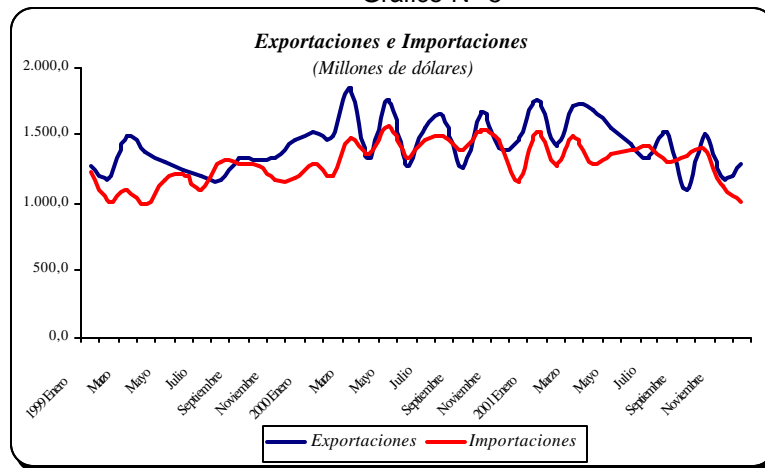
Fuente: Banco Central de Chile.

As with production, internal demand saw a recovery during 2000, growing at a peak annual rate of 9.7% in the second quarter. Nonetheless, alongside the drop in production, we see a deceleration beginning, turning to negative growth by the end of 2001.

The explanation for this performance can be found in several areas: the nature of the recovery, which was based on a fragile expansion of exports, the slowing of the United States and world economies, and an decline in the world price of copper.

The 4.1% growth in the US economy during 2000 sustained the worldwide economy but created an extremely fragile economic situation in Chile and other countries, given the economic factors outlined above. Thus, an overall growth of 4.4% in the Chilean economy did not prompt similar growth in other macroeconomic factors, namely investment and employment.

Gráfico N° 5



Fuente: Banco Central de Chile.

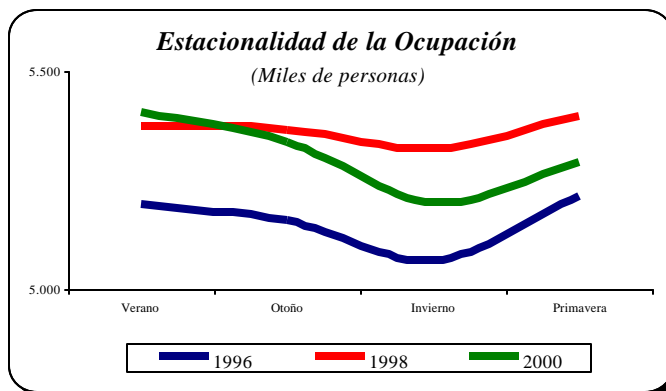
The current situation is one of dangerous deceleration. The fourth quarter of 2001 registered a 12.7% drop in exports and 15.7% drop in imports from the previous year, indicating the grave nature of the contraction facing internal demand. In the fourth quarter of 2001, internal demand had not changed at all from the previous year, and consumption had dropped by 1.5%

### 3.- The impact on the Job Market

It is apparent that effects of the economic contraction are seen primarily in the job market, showing that the cost of crisis is borne primarily by Chile's workers. We can look to both levels of employment and real salaries to see the true nature of the market and the economy.

An analysis of employment conditions demands that we first look at certain structural situations. The first is a significant change over the course of the year within the job market, most notably in the farming sector, which is labor intensive. The demand for labor in this sector is tied to the seasons in which there is the most farming, leading to an increased demand in the summer and a drop in demand during the winter. Naturally, given this situation, and the traditionally low wages given to these "temporary" workers, employment in this sector is quite unstable.

Graph N°6

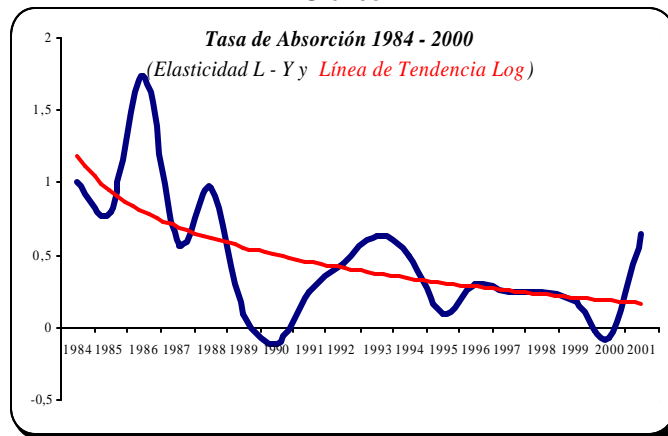


Fuente: Elaborado con datos del INE.

Graph 6 demonstrates the seasonal performance of this sector. 1998 showed a bit of an inversion of the normal trend due to the agricultural crisis. Nonetheless, the pattern is again found in 2000, indicating that, in Chile, unemployment reaches its peak during the winter season.

The second structural condition is in regards to a continuing drop in the absorption rate of the Chilean economy. This situation, which indicates that the economy is less and less able to generate jobs, creates serious doubts about the ability of the economy to recover and create permanent growth. Indeed, it hints at a persistent growth in unemployment.

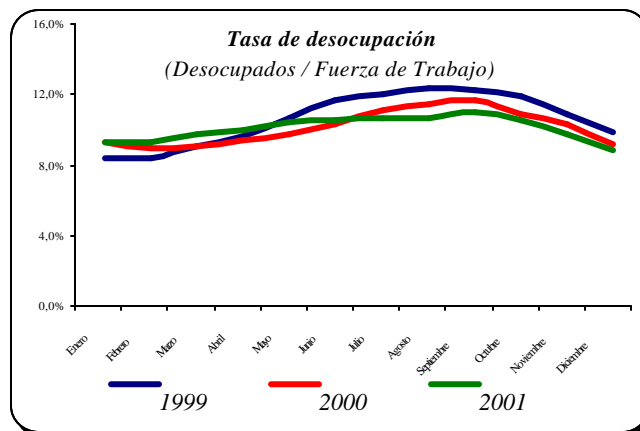
Gráfico N° 7



Fuente: Elaborado con datos del Banco Central de Chile e INE.

This problem of decreasing absorption rates is typically found in developed countries where technological innovation brings large increases in labor productivity, effectively reducing demand for labor. Nonetheless, the situation is somewhat distinctive in periphery economies. In our case, this decline in the rate of absorption is due mainly to the concentration of growth within highly capital intensive sectors that have a very low demand for workers relative to their output, such as mining. Under these structural conditions, alongside the deceleration and stagnation of the economy, we find the labor market in its present state.

Graph N° 8

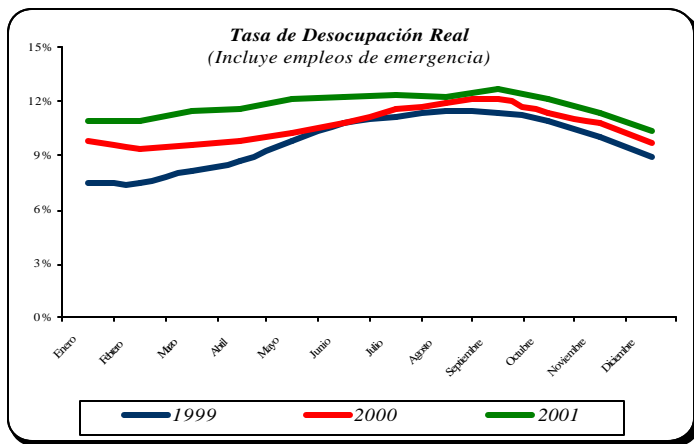


Fuente: Elaborado con datos INE.

In 2001 we can see that the unemployment rate is more rigid as compared to the traditional seasonal behavior. We can see that in 1999, the unemployment rate was above 10% for six consecutive months, and for four consecutive months in 2000. This past year, it was only above 10% for one month. These figures seem to indicate progress; nonetheless, this is simply an illusion.

Since 2000 the government has implemented emergency job programs for the unemployed. While these transitory jobs – cleaning up green spaces and repairing infrastructure – provide basic wages, they do not change the fundamental nature of the job market. In 2000, some 80,000 emergency jobs were created, and in 2001 that number rose to 150,000. Given the nature of the work outlined above, it is safe to realistically count these workers as unemployed. If we were to do this, the unemployment conditions change drastically.

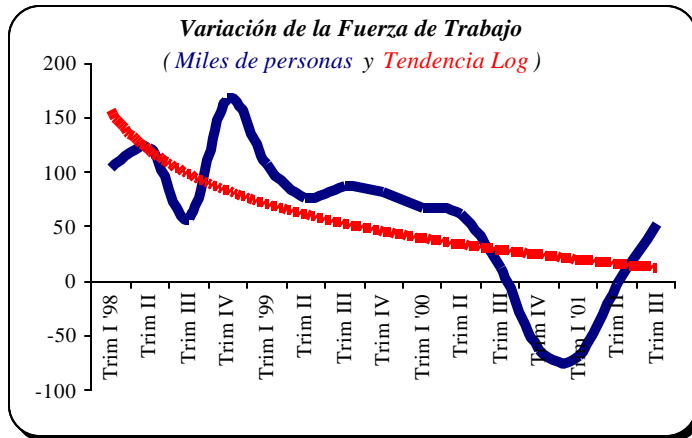
Gráfico N° 9



Fuente: Elaborado con datos INE.

Under these new conditions, the situation is inverted. In 1999 there are six months in which unemployment is in the double digits, rising to seven months the following year. In 2001, every month saw unemployment above 10%, and from May on, there was no month below 12%. If we examine more closely the components of the job market, work force, employment and unemployment, we can see important aspects that further demonstrate the fallacy of the official statistics provided by the government.

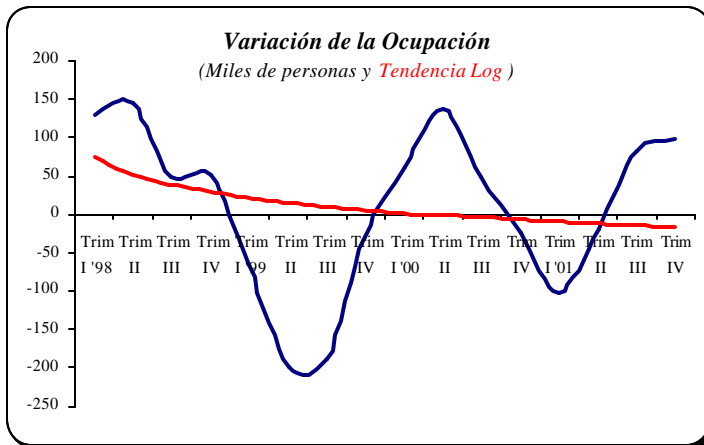
Graph N °10



Fuente: Elaborado con datos INE.

What is clear from a review of the behavior of the labor force is that declines in unemployment are more likely to reflect the national statistical survey's inability to identify long-term unemployment, than they are to be the result of decisions by the unemployed to voluntarily give up searching for work.

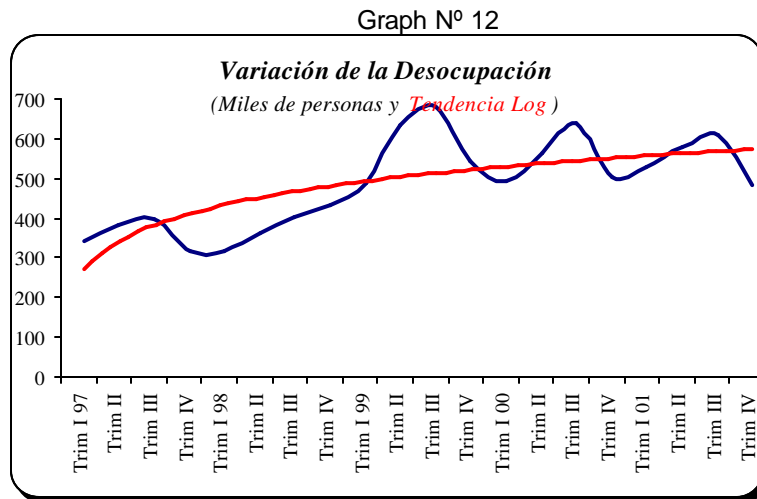
Graph N° 11



Fuente: Elaborado con datos INE.

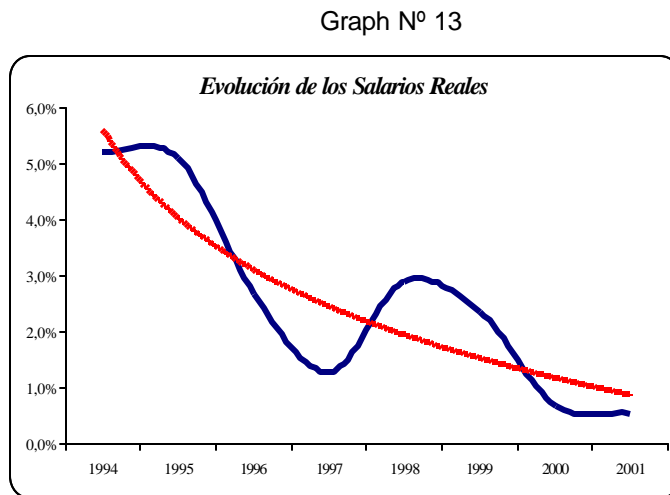
The statistics gathered by the government are flawed on several levels, then. Given the definitions outlined above for employed and unemployed, we can see that a large portion of those who are “employed” may simply have worked in various forms of informal jobs or underemployment, which can hardly be interpreted as normal employment. Overall, the graph shows a clear drop in the creation of employment, alongside the trend shown in Graph 7 with regards to economic absorption.

In summary, given the structural factors, and the flaws in the statistics outlined above, we can see that unemployment in Chile remains a serious problem. While the growth in unemployment may be decelerating each year, there are more and more people out of work in Chile every year. This is the fundamental problem of the current economic crisis.



Fuente: Elaborado con datos INE.

The employment crisis is exacerbated by the performance of real wages, which is related to the excess supply of unemployed workers. We can see the drop in wages in Graph 13, and the way in which it has correlated with the crisis of the past four years.



Fuente: Elaborado con datos INE.

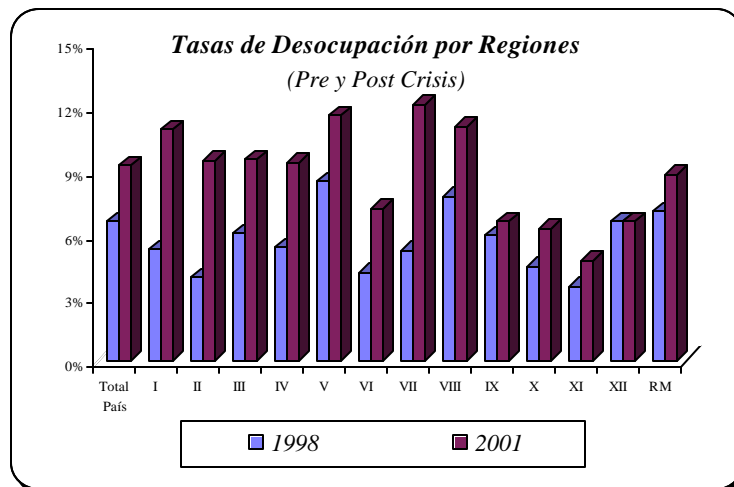
These factors indicate a particularly bad year for the Chilean economy. There is no evidence to suggest that 2002 will see any sort of recovery or positive performance. Indeed, everything indicates that the problems of 2001 will only deepen in 2002. This is partly due to the continuing US crisis, which has a worldwide effect and a particular effect on our region. The other factor that indicates no economic recovery is internal conditions.

The economic model applied in Chile will lead only to further contraction. Without major changes, there is no hope for recovery. Indeed, the standard neo-liberal reaction to crisis seems to be applied here as well: do nothing.

#### 4.- The regional situation in Chile

Unlike other countries in the region such as Argentina and Brazil, Chile is not a federal state –all power and resources are concentrated in the capital, Santiago. This situation has been a tense one since the birth of the nation in 19<sup>th</sup> century, when the reaction to independence by the dominant elite was to consolidate all the power in one place. During the 20<sup>th</sup> century there were various attempts to address the problems created by centralization. Nonetheless, these efforts failed under the pressure of attempting to consolidate the various interests of diverse regions. In the last quarter century an initial decentralization plan was adopted during the military dictatorship, whereby the country was divided into 13 regions, but it was quite limited and never effectively implemented. Perhaps reflecting the military's creativity and originality, these newly defined regions were given nothing more than a number to distinguish them.

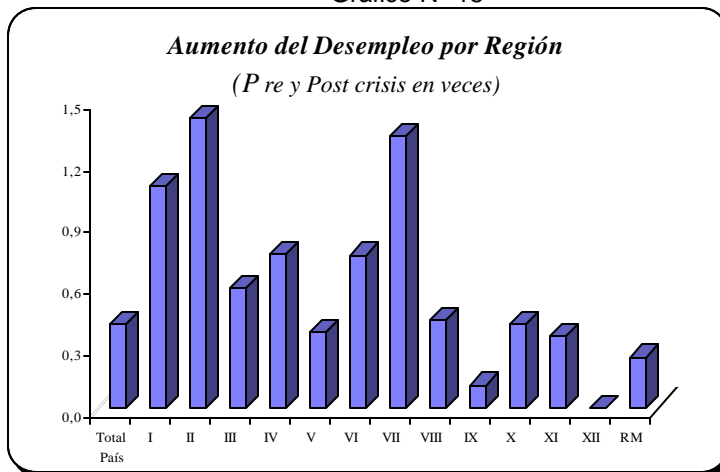
Gráfico N° 14



This distribution of territory, though, allows us to chart the effects of the current crisis throughout distinct parts of the country. The above graph shows each region's unemployment rate in 1998 as compared with 2001.

We can see that in region XII and region VII, there were drastically different situations, as the latter experienced virtually no change, while the former saw an almost tripling of unemployment. To get a better picture of this situation and understand the rise in unemployment, we can look at the following graph.

Gráfico N° 15



The regions in which the most impact was felt are precisely those that produce natural resources: in regions I and III, mining; in VI and VII, agricultural production; and, in regions VIII and XI, forestry. Conversely, in the metropolitan region (RM) and in region V there are primarily service activities, while cattle dominates region XII.

The drop in the price of copper has practically meant the death of the small and medium mining business, at a time when a world-wide slowdown has had a dramatic impact on agricultural sectors. These charts indicate, then, that those regions that suffered least were those that inherently differed from the general makeup of the national economy.

This disparity from region to region is related to internal differences in economic activities.. We can see this in the way that the traditional copper-production of region VIII suffered tremendously, throwing the region into a crisis only exacerbated by general economic troubles.

The prospects for the Chilean economy in 2002 are no brighter than those observed in 2001. We are under a monetary policy that is neutral in the face of crisis, where, despite repeated drops in interest rates, there are no solid signs of economic reactivation. Fiscal policy is counterproductive, only concerned only with maintaining a government surplus. Taken together, these policies will only postpone an economic recovery and the improvement of the situation in the labor market.

**Santiago, March 28, 2002.**