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PAUL N. ROSENSTEIN-RODAN

Why Allende Failed

*The downfall of Allende had nothing to do with socialism.
It was caused by poor leadership, poor planning, and
a lack of economic realism.*



The death of Salvador Allende was a threefold tragedy. It was a tragedy because it has been taken as a breakdown of socialism, and socialism is a great, perhaps the greatest, ideal of this century. It was a tragedy because it has been taken as proof that socialism and democracy are incompatible, that only a dictatorship can impose socialism, but the Chilean experience offers no proof of that. And it was the personal tragedy of a man whose hopes and dreams had been shattered, ending in suicide or murder.

Salvador Allende died not because he was a socialist, but because he was an incompetent. After he took office, he accomplished a major redistribution of income that dramatically increased demand, but he did nothing to increase production to satisfy that demand. Instead, he printed money. A breakdown was inevitable, and the resulting inflation not only destroyed the income redistribution that had taken place, but lowered real wages below the level of 1970.

It is not inherent in socialism to be inefficient.

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Russia is also a socialist society, but it does not increase its money supply by 10 percent every month. Any undergraduate economics student would have known better. The question is why the economists in the Allende government allowed such obvious mistakes. The answer is that the program of the Allende government was not well worked out. The ends and means were not coordinated or made compatible. The party was not prepared or perhaps did not expect to win and to govern in 1970.

Historical perspectives

In September 1970, in a field of three, Salvador Allende Gossens won the presidential election by a slim margin over the runner-up, Jorge Alessandri. Because no candidate received an actual majority, the election went to the Chilean Congress. There Allende's election was confirmed after a period of uncertainty and agitation and, most important, after Chile's president, the immensely popular Eduardo Frei, assumed a posture of nonintervention. (By Chilean law, Frei was not allowed to succeed himself.)

The election of a Marxist president signaled a decisive move to the left in Chile, but the events surrounding the election must be put in historical perspective. Chile is politically the most developed country in Latin America. It has evolved a form of parliamentary democracy, an efficient and independent civil service, a substantial middle class, and a lively labor movement. It also has the good education system required for modern development. Moreover, there are ample natural resources and enough good land to assure an adequate food supply and, if properly managed, even some agricultural surplus for export. Per capita income is the third highest in Latin America. Traditionally, at least, the army had been apolitical and, traditionally, there were no political prisoners.

What distinguishes Chile, however, is not only a vocation for freedom and respect for the law, but also a growing stratification of social forces: army, church, trade unions, gremios, and the student movement. Since 1920, there has been a continuous historical trend—accelerated in 1964 by the Frei government—toward increasing diversification of Chilean society and a corresponding change in political power. Participation increased rapidly. In 1958, 850,000 persons voted in the presidential elec-

tion; by 1970, the number of voters had risen to about 3 million. Growing participation was accompanied by a movement toward the left and the increasing polarization of political groups.

Allende's first year

In the first year following Allende's election there was great division. Twenty percent of the people were in a state of revolutionary euphoria; 10 to 20 percent experienced a spasm of violent (un-Chilean) hatred; and the remaining 60 percent seemed paralyzed by shock. The middle and upper classes lived in a *fin de siècle* mood: tomorrow we die. Instead of saving, everybody spent. One had to phone to find a seat in a luxury restaurant. Santiago almost became a swinging town whose ambience was reminiscent of the unreal atmosphere that pervaded Vienna in the midst of the despair and doom of the 1920s. During the first few weeks there was a run on the banks, a flight of capital, and an emigration of many technicians. (Chile was unique among the Marxist countries in allowing complete freedom of emigration.) For a short while, there was even a peculiar capital flight on four legs as masses of cattle were driven over the Andes into Argentina.

The panic subsided gradually and the Allende economic program began. It consisted of a short-run policy, which was Keynesian, and a long-run policy of transition to socialism, which was vaguely Marxian. The short-run program had three objectives: a substantial redistribution of income, full employment, and stabilization of prices. There was a recession in Chile in 1969-70, with some unemployment and considerable unused capacity. The Keynesian policy assumed that by raising wages substantially (they were raised on the average by 50 percent), the increased demand would lead to the absorption of excess capacity and the recovery would therefore be, in a way, self-financed. According to the plan, the main actors of the Allendista demonology—the imperialists and the landowners—were to be properly squeezed and eviscerated. Money, considered only a bourgeois veil, was increased at an unprecedented pace of 10 percent per month and price controls were imposed.

There is a story of a Chinese bandit general occupying a province who called in thirty bankers and told them: "Tomorrow you deliver \$10 million in bank notes." The bankers said: "General, the entire

money circulation in our province is only \$30 million. If we increase it by \$10 million, the quantity theory of money says that prices will rise by 30 percent." "Quantity theory, eh," said the General. "Tomorrow you deliver \$10 million. If prices rise 10 percent, ten of you will be hanged. If prices rise 20 percent, twenty of you will be hanged. And if prices rise 30 percent, all thirty of you will be hanged." Prices did not rise.

Unfortunately the story is apocryphal and Allende was not a Chinese warlord. After a considerable redistribution of income, the increased purchasing power indeed led to a great increase in demand, and to an increase in production and employment which, if it could have been sustained, would have made the first year of Allende an economic triumph. Industrial production was increasing at a rate of 11 to 12 percent. Unemployment, in spite of the fall in private investment, was almost halved, and economic well-being undoubtedly improved.

It is not only obvious now, but should have been then, that this desirable state of affairs could not possibly have been sustained. Excess capacity in industry may have been 30 percent, but it was not equally distributed among the goods for which demand was increasing. Moreover, there certainly was no excess capacity in agriculture, and radical measures of agrarian reform, whatever the long-run structural effects, were more likely to reduce than to increase agricultural production. Thus, food imports had to be more than doubled. Many of the supplies necessary for the production of other goods were scarce and also had to be imported. The government paid for these imports with the \$400 million in foreign exchange reserves it had inherited. The excess inventories which had accumulated during the 1969-70 recession were also consumed. A fixed low exchange rate accelerated the depletion of foreign exchange resources. It would have been a simple arithmetical exercise to calculate that foreign exchange reserves and inventories would be exhausted within one or two years. The fundamental need was for an increase in national production and, after the initial absorption of excess capacity, only an increase in investment could provide that.

The squeeze and reduction of profit in private enterprise led to decapitalization in the private sector and a fall in private investment. The redistribution of income to the lower income classes was not accompanied by any measure designed to increase





the savings of the workers, which would have provided funds for investment. Last but not least, the price policy of public enterprises and of enterprises nationalized under the Allende government kept prices low, vastly reducing investment funds in the public sector. Output and employment increased, but investment fell by 20 percent in 1971. Further improvement in income distribution and growth became impossible, and it was only a question of time before the gains already made in the redistribution of income would be more than lost.

Fidel Castro correctly pointed out that "Marxism is a revolution of production; Allende's was a revolution of consumption." During his first year, Allende won the battle of consumption but lost the war by not fighting the battle of production. The reliance on income redistribution without provision for increased savings has more in common with populism than with Marxist socialism. If the redistribution of income had been half of what it was, and had it been coupled with other measures, it might have been sustained. As things were, it led to a foreseeable growing scarcity of goods.

The expropriations

Production was also hindered by the nationalizations. Under Allende the nationalization of Chilean enterprises proceeded partly by buying up all the banks (paying for them and for subsequent expropriations with freshly issued money), partly by nationalizing big industrial enterprises, and partly by invoking a 1932 law which allowed the government to take over an enterprise whenever a strike or a breakdown would be against the public interest.

Taking over the banks is not the main point. Whether or not it is a nationalized banking system does not matter half as much as what that banking system is made to do. The nationalization of the banks enabled Allende to prescribe credit irrespective of credit worthiness—or any other consideration. A policy that directed the banks to operate efficiently would have had a completely different outcome.

The question of compensation is complex. For example, copper is Chile's main source of foreign exchange. Had the Allende government promised

adequate compensation for nationalization of the copper mines, Chile would have been able to run the mines more efficiently and to open new mines. It was a matter of just a few people: the emigration of two dozen experts meant that the plans to expand production were never implemented. These experts, most of whom were Chilean, are now employed in Australia and elsewhere by the same companies they worked for in Chile. The international experts later brought into Chile from Russia and Japan were unfamiliar with Andean conditions, and their advice was useless. (I do not know whether it was a matter of increased intelligence or decreased hormone count, but U.S. policy during this time was extremely unobtrusive and to some extent surprisingly nonaggressive.)

Adequate compensation to the multinationals could have been something like an annual payment over forty years at a 3 percent rate of interest. Or the payment could have been in newly issued bonds. In either case, this sort of settlement amounts to a confiscation of 30 to 50 percent, an amount which is internationally acceptable. There was another solution (which in my opinion will be used increasingly in both socialist and underdeveloped countries). Chile could have agreed to a joint venture, in which a multinational sells—and the accent is on sell, not surrender—50 percent of the assets of its local subsidiary to the host country. Several multinationals have arranged joint ventures in Yugoslavia, and the Fiat co-production agreement to produce automobiles in the Soviet Union is another possible form.

Expropriation of the copper mines reduced Chile's major source of foreign exchange but, even more important, expropriation resulted in less production. The intervenors and the new managers of "socialized" enterprise were even less competent than the effete and monopolistic private entrepreneurs. The volume of production fell, and with it disappeared any surplus that might have been used for investment.

The case of agriculture is instructive. Chilean agriculture was characterized by the conventional inequality: a small percentage of large units controlled a high percentage of cultivation. But there were two types of large landholdings: those that were intensively cultivated and those that were not. In the first case, redistribution may have had socially positive effects, but the impact on production was

negative. Under Eduardo Frei, agrarian reform was based on a productivity principle which forced the redistribution of land not intensively cultivated. That kind of reform should have a beneficial effect on production. For example, under the normal sharecropper's agreement, the tenant pays rent equal to 40 or 50 percent of the crop. It does not pay the tenant to cultivate more intensively—to invest in fertilizers, insecticides, or tractors—because half the increased product then has to be paid to the landlord; but it does not pay the landlord (often an absentee) either, because half his investment returns will go to the tenant.

Under Allende's program, holdings above 250 acres were to be expropriated. For those farms already intensively cultivated, the effect on production was negative. Even this type of reform, if properly managed, could have been positive on balance. But seizures were completely haphazard, and many were illegal. Frequently the small and medium-sized farms, not just the large estates, were expropriated. Orders had been given to the police never to interfere, with the result that these completely arbitrary confiscations created uncertainty among those whose land was supposedly not to be seized. These people farmed two-thirds of Chile's land, and the effect of the uncertainty on production was enormous.

The failure of Chilean agriculture to produce as much as it should have, given the quality of soil, was partly due to the policies of the past. The heavy protection of industry raised industrial prices to very high levels relative to those in agriculture. These domestic terms of trade discouraged investments that would have made agriculture more productive: the more bushels of wheat you have to sell to buy a ton of fertilizer, the less you buy. Under Allende, food prices were intentionally kept low. At first the government tried to keep industrial prices down, too. But the increases in the money supply made that impossible, and the terms of trade between agriculture and industry worsened.

In the mining sector, nationalization was a popular and emotional issue. But viewed functionally, the Allende program was a disaster not only because Chile could not open new mines but because production broke down in the old mines. Allende's government failed to induce labor discipline. The very same workers who loyally demonstrated with slogans of "El gobierno es la mierda, pero es el nuestro" (the government is terrible but it's ours) said: "Now

we have our government, let's celebrate." On Mondays absenteeism ran 20 percent. Thus the nationalizations failed in part because of the labor movement. The trade union mentality in Chile (and elsewhere) is not concerned with an equitable income distribution within the working class. The average wage of the copper miners in Chile was three and a half times the average for all workers. Nonetheless, they were the first to strike for a wage hike, which would only have increased the income differentials. Trade unions were once an instrument of progress against the exploitation of workers, but this is a matter of the past.

Allende's third year

If after the first or even the second year, Allende had said: "We have established the basis of social justice and we are building a new socialist society; the coming year must be a year of consolidation," he could have saved the situation. Lenin was not a bourgeois, yet he proclaimed the New Economic Policy (NEP) in Russia. Something similar was needed in Chile, but it didn't happen. In Allende's third year the inflation accelerated, and for obvious reasons. The most active full employment activity was printing bank notes. Most of this additional money supply went to cover deficits in badly administered nationalized enterprises and to sustain an increasing consumption that was in the long run unsustainable. There was no investment. The foreign exchange reserves were gone, spent on consumer goods and food rather than on important machinery, equipment, or material for production and investment. Inventories—spare parts and raw materials—were used up. The economy slowed to a standstill and then lost ground. Queues formed. People waited six or seven hours a day to get bread. Workers took a day off to spend in the queue; half of what they got, they sold in the black market—and their profit was more than a day's wages. The impact on production can be easily imagined. There was a complete breakdown of labor discipline. Inflation reached one percent a day. In this inflation the redistribution of income which had taken place during the first year was in fact more than canceled. Moreover, as is typical in such an inflation, the worst elements in society were making inflationary profits. It was not only economically inefficient, it was also morally unbearable.

The collapse came with the truckers' strike. Those drivers employed by large firms had benefited from

Allende's initial reforms, but many of the truckers were small, self-employed entrepreneurs. The strike began as a normal collective bargaining dispute, but rapidly acquired a political tone. The lower middle class was entering into a revolutionary euphoria of its own. The truckers wanted guarantees that the expropriations would not be applied to them. Eventually, their goal became Allende's resignation.

It was not just the lack of adequate planning or the inefficiencies of democratic Marxism that caused Allende's downfall. It was also his personal leadership. Being a revolutionary is like being in love. The characteristic of people in love is that they do not believe that anybody else in their lifetime has also been in love. So they do not learn from other people's mistakes and repeat all the same errors. This was eminently true of Allende and may now be true of the junta generals. One of the reasons why the truckers' demands escalated was that Allende had been adroit in making legalistic interpretations and giving promises that were never kept. In the end Allende's word was no longer good. On top of that, he was sentimental. He could have announced an NEP after the first year or so, but he refused to twist the arms of his own party members who opposed it. To do so, he said, would be a betrayal. If one feels that way he should write a poem about it, not serve as president of a republic.

A few words about the structure of political parties are needed here. The Communist Party was moderate and conservative. Its motto was that socialism cannot be built overnight. The Allende party, however, was different. It consisted of three sections: more than one-third were old-fashioned, well-meaning individuals of the Left, rather like Leon Blum's French Socialists of the 1930s, who discussed problems in highly intellectualized style and could be members of the existentialist clique at the Café de Deux Magots in Paris—out of date and obsolete, but charming, cultured, and nice; one-third were Castroites; and one-third were a mixture of Trotskyites and Maoists with Don Quixote notions of *la revolución* for its own sake. The radical groups comprised the extreme Left. It was a remarkable achievement of Allende that, using the Chilean myth of the presidency, he managed to keep the coalition of the Popular Front, and indeed the most difficult part of it—his own party—in some semblance of cooperation. However, by August 1973 Allende's power was gone. My estimate is that had a plebiscite been held

then, at least 60 percent would have voted for a new government. The people almost wished for a military coup.

The generals

Despite the excesses of the Chilean generals—and there is reason to fear these days for the state of human rights in Chile—I still suspect that their concept of the ideal leader is not Mussolini or Franco but de Gaulle. They have all read the memoirs of de Gaulle, they know what he did for France in the 1950s, and they admire him. Fundamentally, however, the Chilean generals (unlike the Peruvian or Brazilian ones) never planned to govern the country permanently. They are critical of the shortcomings of their society (both under Allende and before) but have no clear, positive ideas of what to do about it.

There is widespread agreement that Chile needs a new constitution. The present one incorporates the worst features of the Fourth Republic in France. There is need for a synchronization of various elections (for the presidency, the legislature, and so forth) and a strengthening of the executive to provide something halfway between that of the Fourth

and Fifth French republics.

It should, however, be voted by a specially convened constitutional assembly or a referendum, not proclaimed by a lawyers' committee appointed by the junta. Moreover, de Gaulle never banned the Communist Party. The banning of communist, socialist, and other political parties which together represent more than one-third of the population may prove counterproductive. The banning of all other political activity—if sustained—points the wrong way and is a bad omen. Chile is not Brazil; its political consciousness is more deeply rooted. True, the growing exacerbation of political factionalism since 1967 was inflammatory. A change in the system is necessary to reduce the political tensions, but the change requires subtle methods. Long vision and magnanimity by government, entrepreneurs, and workers are needed to restore the most important goal: social harmony. In the intermediate period, it may be that political activity must be suppressed; but this should be only a transition period. In the long run, in a good society every man has the right to hold a wrong opinion. In every society it is always an elite minority that governs; but in a good society it governs by persuasion rather than by coercion.

