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McNamara Papers

Contracts
Chile (1968-1971)

 **Archives**  **1771002**

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Contacts with member countries Chile - Correspondence 01

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WBG Archives

CHILE

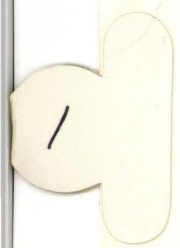
CHILE

1. 4/15/68 Rafael Moreno, President of the Agrarian Reform Corp. of Chile
Fernando Irarrazabal, Adviser
- 5/23/68 Dr. Raul Saez, President, ENDESA (Government Development Finance
Organization); former Minister of Finance
2. 7/15/68 Ambassador Domingo Santa Maria
3. 11/7/68 Andreas Zaldivar, Minister of Finance
Carlos Massad, President, Central Bank of Chile
Sergio Molina, Executive Vice President, Corporacion de Fomento
de la Produccion
Carlos Figueroa, Undersecretary of Agriculture
Edgardo Boenninger, Director of the Budget
Ambassador Domingo Santa Maria
4. 2/6/70 Maximo Pacheco, Minister of Education
Ambassador Domingo Santa Maria
- 6/18-19/70 International Meeting on Development Policy:
(Heidelberg)
Enrique Iglesias
- 12/21/70 Ambassador Domingo Santa Maria
5. 2/23/71 Pedro Vuscovic, Minister of Economy
Alfonso Inostroza, President, Central Bank
Ambassador Orlando Letelier
- 6/29/71 Sergio Gutierrez-Olivos, former Ambassador of Chile
6. 8/6/71 Orlando Letelier, Ambassador of Chile
7. 9/13/71 Ambassador Nathaniel Davis
8. 10/1/71 Mr. Knapp's meeting with the Chilean Delegation
Mr. Alter's meeting with the Chilean Delegation
9. 4/14/72 President Salvador Allende Gossens
(Santiago) Americo Zorrilla Rojas
Ambassador Orlando Letelier
- 6/12/73 Alfonso Inostroza, Governor of the Bank
Javier Urrutia, Alternate Governor
10. 11/27/73 Ambassador Heitmann (Courtesy call)
11. 12/17/73 Raul Saez, Economic Advisor to Government of Chile
- 1/31/74 Fernando Leniz, Minister of Economy (at Reception at Embassy)

CHILE

-2-

12. 7/19/74 Raul Saez, Minister for Coordination
13. 2/21/75 Jorge Cauas, Minister of Finance
Ambassador Walter Heitmann
14. 5/7/75 Jorge Cauas, Minister of Finance
Ambassador Manuel Trucco
- 6/12-13/75 Jorge Cauas, Minister of Finance
(Paris-Dev.
Cte.)
- 1/6-10/76 Jorge Cauas, Minister of Finance
(Dev.Cte.,
Kingston)
15. 6/14/76 Cardinal Silva, Archbishop of Santiago
Raul Paiva Casali, President of the Foundation for Development
Ivan Radovic, Aide to the Cardinal
Jaime Bellalta, Aide to the Cardinal
16. 3/30/77 Jorge Cauas, Ambassador to the U.S.
17. 12/3/79 Sergio de Castro, Minister of Finance



INTERNATIONAL BANK FOR
RECONSTRUCTION AND DEVELOPMENT

INTERNATIONAL DEVELOPMENT
ASSOCIATION

INTERNATIONAL FINANCE
CORPORATION

OFFICE OF THE PRESIDENT

3/24

To Mr. Alter

Jerry, for your files
re the alleged com-
mitment to Morocco.

Rnew

cc Mr. Knapp

May 24, 1968

Memorandum of Meeting held in Mr. McNamara's
office on Monday, April 15, 1968 at 2:00 p.m.

Present: Mr. Robert S. McNamara
Mr. Rafael Moreno, President, Corporation of
Agrarian Reform, Chile
Mr. Fernando Ibarrazabal, Adviser to Mr. Moreno
Mr. Luis Escobar, Executive Director for Chile

This was a courtesy call. Mr. Moreno told Mr. McNamara that he had been instructed by President Frei of Chile to try and see the new President of the World Bank in order to convey President Frei's greetings, explain what is being done in Chile in the field of land reform, and, finally, express the hope that Mr. McNamara would be able to visit Chile in the near future.

Mr. Moreno was enthusiastic and optimistic about what has been achieved, even though he recognized explicitly that the accomplishments fell short of the original goal established by President Frei and the Christian Democrat Party in their program of "Revolution in Freedom". He gave some details of how the program is actually being implemented, and asked whether the Bank would be willing to consider helping Chile to continue with the land reform plan. Mr. McNamara answered that the Bank has a great interest in agricultural development, has been granting loans for this purpose, and, consequently, would look favorably on projects which met its lending policy standards.

Luis Escobar

INTERNATIONAL BANK FOR
RECONSTRUCTION AND DEVELOPMENT

INTERNATIONAL DEVELOPMENT
ASSOCIATION

INTERNATIONAL FINANCE
CORPORATION

OFFICE OF THE PRESIDENT

Mr. McNamara:

Mr. Chaufovier has had an extensive talk with Mr. Moreno.

Another meeting between Mr. Moreno and Projects Department is scheduled for Tuesday.

Mr. Moreno was not free for a luncheon to be given by Western Hemisphere Department next Tuesday.

fyio.

ABS Apr. 12

OFFICE MEMORANDUM

TO: Mr. Robert S. McNamara

DATE: April 12, 1968

FROM: Luis Escobar

SUBJECT: Land Reform - Chile

Mr. Rafael Moreno, President of the Agrarian Reform Corporation of Chile, is in Washington. Today, he had a meeting with the World Bank's Western Hemisphere Department and will see them again on Monday morning. After that, at 11.30 a.m., he will be received by Mr. Aldewereld.

As you know, land reform is one of the pillars of President Frei's program of "Revolution in Freedom" and Mr. Moreno is here to study the kind of support that could be obtained from different financial organizations. He told me that he would very much like to talk to you, even if only briefly, on Monday or Tuesday.

*Monday
1 PM
4 PM*

INTERNATIONAL BANK FOR
RECONSTRUCTION AND DEVELOPMENT

INTERNATIONAL DEVELOPMENT
ASSOCIATION

INTERNATIONAL FINANCE
CORPORATION

OFFICE OF THE PRESIDENT

April 11, 1968

To: Mr. Robert S. McNamara

You may know Ed Korry, the exceptionally capable U.S. Ambassador in Chile--formerly in Ethiopia. When I received the attached letter I asked Mr. Gerald Alter, Director, Western Hemisphere Department, to take this matter on with the thought that he would try to arrange for a meeting or a luncheon which you could attend.

I now find that Alter is leaving town, with the result that Mr. Moreno--highly regarded by Ed Korry--will not, in all probability, receive adequate attention.

Inasmuch as Korry believes it would be useful if you met Moreno, I thought I would invite your attention to the facts.



G. D. Woods

Attachment

INTERNATIONAL BANK FOR
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INTERNATIONAL FINANCE
CORPORATION

OFFICE OF THE PRESIDENT

4/11/68

GDW:

Mr. Alter's secretary advises Mr. Peter Reitter (Western Hem. Dept) talked with Mr. Perry Shankle (Chilean Desk - State Department), and that a meeting or lunch in WESTERN HEMISPHERE DEPARTMENT will be arranged for Mr. Moreno.

S

4/11/68



DEPARTMENT OF STATE

Washington, D.C. 20520

April 5, 1968

Mr. George Woods
World Bank
1818 H Street N.W.
Washington, D. C. 20043

Dear Mr. Woods:

Ambassador Korry has cabled from Chile to request that we pass on to you the following message:

Rafael Moreno, Head of the Land Reform Corporation of Chile (CORA) will be in Washington April 10-17. Moreno is young, vigorous, articulate and a trained agronomist. He received a Master's Degree in Economics at the University of Illinois and is a force behind one of Latin America's most interesting reform programs. If it is at all possible, I believe it would be mutually very useful for Mr. McNamara at IBRD to meet this arch-type of progressive, dynamic, young Latin reformer. For your information, Moreno has become an enthusiastic supporter of the kind of ideas that I recently discussed with you concerning a more compatible arrangement for the use of private enterprise funds from the developed nations.

Ambassador Korry asked that we extend his best wishes. Also, in accordance with his request, we are sending a copy of this letter to Mr. John Reilly in Vice President Humphrey's office and Mr. William Bowdler of the White House.

Sincerely,

A handwritten signature in blue ink, appearing to read "Wm Broderick", written in a cursive style.

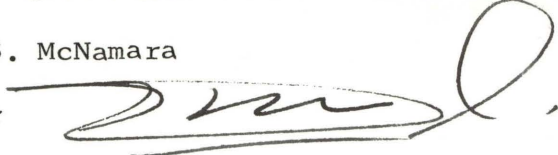
William Broderick
Deputy Director
Office of Bolivian-Chilean Affairs

cc: Mr. John Reilly
Mr. William Bowdler

OFFICE MEMORANDUM

TO: Mr. Robert S. McNamara

DATE: July 3, 1968

FROM: Luis Escobar SUBJECT: Luncheon in honor of the new Ambassador from Chile,
His Excellency Domingo Santamaria

Mr. Domingo Santamaria, the new Ambassador from Chile, arrived in Washington last Friday and has already presented his credentials to President Johnson. I am arranging a lunch for him to meet the highest officials of the Bank and the Fund here in the Bank's Executive Dining Room on Monday, July 15 at one o'clock.

The Ambassador and I would be deeply honored if you could attend. Besides, the Ambassador would like to pay you a courtesy call, hopefully the same day, Monday 15, before the lunch.

I would appreciate it very much if you would let me know whether you could receive him that day and if you would be able to attend.

Ambassador Domingo Santamaria is a Civil Engineer who has been closely related to different private enterprises in Chile, and was the first Minister of Economy of President Frei for a period of close to three years. After that he was the Head of the Chilean Delegation to the UNCTAD Meeting in New Delhi.

President has seen

OFFICE MEMORANDUM

TO: Mr. Robert S. McNamara DATE: July 15, 1968

FROM: Roger Chaufournier *Rh*

SUBJECT: Visit of Chilean Ambassador to the United States, Domingo Santa Maria

Mr. Luis Escobar has arranged a luncheon for the new Ambassador, Mr. Domingo Santa Maria, in the Bank subsequent to his meeting with you. I understand that the Ambassador's visit to the Bank is simply to pay you a courtesy call.

Following is some background information on the Ambassador which may be helpful to you.

Mr. Domingo Santa Maria was born in 1920 in Viña del Mar where he also received his secondary education. After his graduation he took up engineering at Santiago's Catholic University. He received his engineering degree with distinction. During his student years, he became one of the leaders of the Catholic students' movement in Chile, which explains his subsequent affiliation with President Frei's Chilean Democratic movement.

From 1944 to 1964, his professional career was in engineering in the private sector. During most of this time, he worked in various firms engaged in construction work of various sorts. During this time, he also held a number of important posts in private sector associations, such as, President of the Chamber of Construction, President of the Steel Institute, Director of the Board of the National Mining Institute, etc.

In 1964, President Frei called him into his Cabinet and appointed him Minister of Economy. During the years 1965 and 1966, we worked very closely with Mr. Santa Maria in setting up a technical assistance program to help in the improvement of the organization and operations of the State Railroads, which at that time fell under the jurisdiction of the Ministry of Economy. Generally, Mr. Santa Maria has always had a keen interest in improving the transport coordination and policies in Chile.

He resigned from the Cabinet in late 1967. Prior to his appointment as Ambassador to the United States, he served as a delegate to various important international conferences. Among others, he was the President of the Chilean Delegation to the UNCTAD conference in New Delhi.

3

OFFICE MEMORANDUM

TO: Mr. Robert S. McNamara

DATE: November 6, 1968

FROM: Gerald Alter *ga*SUBJECT: CHILE - Visit of Chilean Officials

The following Chilean Government officials, who are in Washington for the annual CIAP review, will be visiting your office for the meeting scheduled at 6 p.m. on Thursday, November 7:

Mr. Andres Zaldivar	Minister of Finance
Mr. Carlos Massad	President, Central Bank of Chile
Mr. Sergio Molina	Executive Vice-President, Corporación de Fomento de la Producción
Mr. Carlos Figueroa	Undersecretary of Agriculture
Mr. Edgardo Boenninger	Director of the Budget
Mr. Domingo Santa Maria	Ambassador of Chile, Washington, D.C.

The first three of the officials whose names are listed above are among the small group of top economic policy officials in President Eduardo Frei's Government. Each of them is young, highly intelligent, and has a sophisticated understanding of economic policy issues. They have been the main architects of President Frei's efforts at containing inflation while expanding social programs. Beginning in 1967, these economic stabilization efforts were frustrated mainly by political opposition to the Government's proposed incomes policies.

The Bank's Lending Program and Strategy

Our lending strategy is to concentrate initially on the transportation sector, where we are the largest lender to Chile, and to gradually expand our loans to agriculture and perhaps later to industry. The five-year lending program for Chile totals \$175 million. In the near-term, our strategy is reflected in proposed loans for ports (\$7 million) in FY 1968/69, for highway construction (\$20 million) in FY 1969/70, and perhaps later for railroad improvement and rehabilitation, where we are presently acting as executing agency for a UNDP project in organization and operations.

In agriculture, we plan a second loan for livestock development for 1969/70 (about \$15 million) and a possible loan relating to agrarian reform. (An exploratory mission will visit Chile later this month, as proposed in your letter of September 20, 1968, to the Minister of Agriculture.)

Mr. McNamara

*regard as to how
lean - expectate!*
W. P. ...
November 6, 1968

You might ask the Chileans about their views on the future prospects for successful implementation of agrarian reform, the Government's plans for removing uncertainty about expropriation and gaining support for the program, and about price and incentive policies in general.

We also expect to present a loan for secondary education (\$10-12 million) before the end of FY 1968/69, and a second vocational educational project (\$2-3 million) in FY 1969/70.

We have so far not discussed with the Chileans the five-year lending program in terms of composition, strategy and policy conditions. I would not suggest that you raise or discuss this matter during the meeting since I am planning a separate meeting with the Chileans for this purpose.

Economic Policy Issues

As far as the Chilean economy is concerned, the near-term prospects are distinctly unfavorable. However, the outlook for the period after 1970 is substantially brighter, since Chile's creditworthiness should be substantially improved by the expansion of copper exports and other industrial investments now under way, and because some of the adverse short-term factors should no longer apply (e.g., this year's severe drought and the economic effects of the forthcoming elections).

*ask on how
for copper
refinancing*

There is little doubt that the Government's stabilization efforts, initiated in 1965, have failed in their main objective, primarily because the Government has been unable to resist pressures for higher incomes and further general increases in public expenditures. Another unfavorable factor has been the environment in which the private sector, both in industry and agriculture, has been operating, partially as a result of the Government's credit, incomes and tax policies. On the positive side, the Government has to be given credit for its achievements in the expansion of social services, foremost education, for improving rural conditions, for impressive tax efforts and for skillful management of the balance of payments through adherence to flexible exchange rate policies, sound debt management and controls over domestic credit.

✓
*what is
the*

A 30 percent rate of inflation is expected for 1968 (it was 22 percent in 1967). Given the present Chilean political environment, the Government is not in a position, during the remaining 18 months of the present administration, to reverse the trend of the past two years and to make any significant headway towards renewed stabilization. On the other hand, the situation is not expected to get entirely out of hand, if certain reasonable economic policy efforts are made by the Government in key areas, such as exchange rate policy, external debt management, incomes policy, public expenditures and policies affecting the private sector. Here, the Bank, acting in concert with the U.S. Government, the IMF, and possibly the IDB, may be able to exercise some useful influence in helping to protect the economy against major distortions in the allocation of resources which could result from the continuing inflation. We would also be prepared to go on lending to Chile so

✓

November 6, 1968

long as certain minimum general economic conditions are satisfied and on the condition that progress is made in tackling key problems in the important sectors where we would be making project loans.

Minimum general conditions would be the continuation of a flexible exchange rate policy and continued limitations on short and medium-term external debt, as well as action in the area of fiscal, incomes and monetary policy, which could reasonably be expected to prevent the rate of inflation from rising above 30-40 percent a year, and which would permit an adequate part of public investment (60-70 percent) to be financed out of public savings.

Inquire

You should be aware that in the CIAP meetings during the course of this week, the Chileans have been subject to very extensive questioning and examining on the above-referred issues and policies. However, in order for you to form certain judgments about the country's basic policies and problems, you might wish to question the Chilean visitors about the Government's policies in key areas for 1969, such as containing Government expenditures, wages and salary policies, operating deficits of decentralized agencies, and industrial and agricultural policies to stimulate private sector activity.

Sector Conditions for Lending

Even if the economic policies discussed above are carried out, they can be expected only to avoid further economic deterioration. We therefore plan to apply sector conditions for transportation and agriculture in connection with our forthcoming loans in these sectors. Again, we have not yet discussed this approach with the Chilean Government and we would not suggest that you do so during the meeting since I am planning to inform the Chileans about our position in a separate meeting. Nevertheless, it may be useful for you to raise some questions concerning sectoral policies.

In the transport sector, beginning with the recently-signed loan for \$11.6 million for highway maintenance, we are planning to become more deeply involved in assistance to the Government in its efforts to coordinate transport policies and investments, and to relate our activities on any new loans in that sector to improvements in important parts of the sector as a whole.

Our first target would be the Chilean State Railways whose operating deficits of the equivalent of about \$40-50 million are covered from the Government budget. In this connection, you might ask the Chileans their opinion about the priority measures which they feel should be taken to ensure a progressive decline in the financial losses of the Railways (our preliminary view is that measures must be taken to begin reducing surplus personnel, increasing rates and adopting measures to reduce service on, and eventually eliminating, uneconomic railway lines).

November 6, 1968

We also propose to apply similar sector conditions to future loans in agriculture. I would suggest you ask the Chileans to give their views on the main measures which should be taken in this field to encourage greater agricultural production and hence decrease the severe balance of payments impact of food imports (our view is that continued liberalization of agricultural prices and the removal of the uncertainty in connection with expropriation under agrarian reform are key areas of necessary action). ✓

cc: Messrs. Wiese
Weiner
Lerdau
Zinman o/r

4

OFFICE MEMORANDUM

TO: Mr. Robert S. McNamara

DATE: February 4, 1970

FROM: Gunter K. Wiese

SUBJECT: CHILE - The Forthcoming Meeting with the Minister of Education

1. I understand that you will be meeting with Mr. Maximo Pacheco, Minister of Education (Chile), at 5.30 p.m. on February 6 at the request of the Minister. We understand from the Embassy of Chile that it will be strictly a courtesy call. We have previously sent to you, through Mr. Christoffersen's office, a brief background information pertaining to Mr. Pacheco.

2. Mr. Pacheco is here to participate in negotiations of the proposed loan of \$7.4 million for the Third Education Project, which were resumed on February 4. The following is a summary of developments pertaining to this project.

3. In May 1969, we recommended to the Loan Committee (LC/0/69-65), and the Committee agreed, to invite the Chilean Government to negotiate a loan of \$12.5 million for the aforementioned project. The project consisted of the construction and equipment of seven new comprehensive secondary schools; construction and equipment of three new primary teacher training colleges; extension and equipment of nine existing primary teacher training colleges; construction and equipment of four new agricultural secondary schools; extension and equipment of seven existing agricultural secondary schools; and technical assistance, including fellowships, in each of the above-mentioned fields.

4. After negotiations were substantially completed in June 1969, the Government decided to postpone the construction of the seven comprehensive secondary schools pending a review of the desirability of introducing the comprehensive secondary school system in Chile at this time. It has also decided to delete one new primary teacher training college from the project, since it was felt that the existing colleges plus additional facilities to be provided by the colleges included in the remainder of the project would be adequate to accommodate the projected demand for primary teacher training facilities. The revised project would thus comprise:

- a) construction and equipment of two new primary teacher training colleges;
- b) extension and equipment of nine existing primary teacher training colleges;
- c) construction and equipment of four new agricultural secondary schools;
- d) extension and equipment of seven existing agricultural secondary schools; and
- e) technical assistance, including fellowships, in each of the above-mentioned fields.

President has seen

February 4, 1970

5. The total cost of the revised project is estimated to be about \$14.8 million including the estimated foreign exchange cost of \$3.3 million. The proposed loan of \$7.4 million would finance 50 percent of the total project cost, which would be the same percentage as the one we applied to the original project. Bank financing of this proportion of the project is deemed desirable to permit the Bank to continue a meaningful association with the planning and execution of Chile's education improvement efforts. Confining the Bank's loan to the small foreign exchange component would not be consistent with this objective.

6. For your general background information on Chile, I am also attaching a copy of a Back-to-Office Report of the economic mission which returned from Chile recently. You may wish to glance through it before meeting with the Minister.

Attachment

January 29, 1970

Mr. Maximo Pacheco has been the Minister of Education since July 1968. Prior to this he was the Chilean Ambassador to Russia from early 1965 until June 1968.

Mr. Pacheco is about 40 years old and a lawyer by profession. He holds a law degree from the University of Chile and has done some post-graduate work in law in Italy.

5

OFFICE MEMORANDUM

TO: Memorandum for Record

DATE: February 25, 1971

FROM: Gerald Alter *GA*SUBJECT: Meeting of Mr. McNamara with the Minister of Economy of Chile,
Mr. Pedro Vuscovic

Mr. Vuscovic, Minister of Economy, accompanied by Mr. Alfonso Inostroza, President of the Central Bank and Mr. Orlando Letelier, Chilean Ambassador, called on Mr. McNamara on February 23. Messrs. Knapp and Alter were also present. The Minister described the purposes of his visit which included the presentation before CIAP of his Government's program and discussions with international organizations and foreign financial institutions on the importance which the Government attached to maintaining the good relations which Chile has enjoyed with these institutions. The Minister explained that his purpose was not to discuss specific financial operations, although he was interested in exploring in what manner the various institutions could cooperate with Chile.

Mr. McNamara assured the Minister that the World Bank had absolutely no problem in cooperating with the new Chilean Government. The Bank was not, in any way, constrained by the particular ideology of a country, whether it be socialist, capitalist or mixed. The Bank had much experience in dealing with countries with widely differing ideologies. He cited the example of Yugoslavia, also a socialist country, one of the Bank's larger borrowers. Mr. McNamara went on to explain, however, that the fact that we were not ideologically constrained did not mean that we were easy to deal with. Our standards are high. We insist that capital should be applied economically. We have a responsibility to those who provided our funds to see that such capital is effectively used. We must frequently insist on certain conditions being fulfilled if the Bank is to be able to make a loan. We may have differences on specific points even though we have every interest in cooperating with the new Chilean Government. We would like to see a first operation materialize as soon as possible in order to establish an even better rapport between the Bank and Chile, on which basis we could make even greater progress in the future. It was observed by Mr. Knapp that in many ways it should be easier for the Bank to reach agreement with Chile than with many other member countries. We are very much impressed with the sophisticated thinking of the Chilean leaders, and we should be able to establish a common ground on many issues.

The Minister cited the electric power tariff problem as an illustration of how World Bank conditions for loans may be a source of difficulty. He referred to the fact that the tariff increases required by the Bank may conflict with the price stabilization objectives of the present economic policy. Mr. Knapp emphasized that the Bank's objectives in this field were, we felt, perfectly consistent with the Chilean Government's

President has seen

February 25, 1971

objectives in the field of mobilizing savings and financing investment in the power field with internally generated funds. The discussion was not carried to the point where the possible conflict between Chilean and Bank objectives was clearly identified. Mr. McNamara urged that the staffs should get together in subsequent meetings and see whether the objectives of the Bank and of Chile could not be reconciled in the particular case of power tariffs. If they could not be, he was sure that the Bank could find other projects in Chile where it would be possible to reach an understanding with the Chilean authorities. The Minister gladly accepted this approach.

Mr. McNamara raised the question of the status of the livestock project. Mr. Alter explained that in accordance with the agreement that we had reached with the Chilean authorities a few weeks ago, we were planning to send a mission in March to review the status of the project. Two major questions called for re-examination: the role of the cooperative settlements in the program and the extent of the demand for credit under the new situation prevailing in Chile.

cc: Mr. Knapp
Mr. Evans/Wapenhans
Mr. Weiner
Mr. Avramovic
Mr. Dosik

GAlter:pa.

OFFICE MEMORANDUM

TO: Mr. Robert S. McNamara

DATE: February 23, 1971

FROM: Gerald Alter *gla*SUBJECT: CHILE - Your Meeting with the Minister of Economy

1. You are to meet with the Chilean Minister of Economy, Mr. Pedro Vuscovic, at six this afternoon. The Minister is in Washington to attend the annual CIAP Country Review which began yesterday and is scheduled for completion tomorrow. This is the Minister's (and the new Chilean Government's) first appearance in international financial circles. The new Chilean Ambassador to the United States, Mr. Orlando Letelier, is expected to accompany the Minister to his meeting with you; Mr. Letelier was for many years a high ranking IDB official. It is possible that the Minister may also be accompanied by one or both of the other two principal members of the Chilean delegation to CIAP, Mr. Alfonso Inostroza, President of the Central Bank, and Mr. Kurt Dreckmann, the Executive Vice President of CORFO.

2. Mr. Vuscovic is undoubtedly the key figure in the new Government's economic team. He appears to enjoy the full confidence of President Allende, whom he served for many years as personal economic adviser. Although a Marxist economist, and a committed one, Mr. Vuscovic does not appear dogmatic; as you know from the notes on my recent mission to Chile, we had quite open and frank discussions and were able to discuss both economic policy and operational matters in non-ideological terms. Most of Mr. Vuscovic's career (he is 46 years old) has been spent in academic life and in doing research and writing for the United Nations Economic Commission for Latin America and affiliated organizations headquartered in Santiago. He was most recently Director of the reputable Institute of Economics of the University of Chile. Mr. Vuscovic has no formal political affiliation; when the composition of the new Chilean Cabinet, which is finely balanced between the parties in President Allende's coalition, was announced he was described as an independent. However, many regard Mr. Vuscovic as a de facto communist.

3. As of this writing, I have not been able to ascertain whether Mr. Vuscovic regards his meeting with you as mainly in the nature of a courtesy call, or whether he wishes to discuss operational matters. In the former case, the Minister will probably limit himself to reiterating the new Government's interest in continued collaboration with the Bank and reaffirming the Government's intention of fully observing Chile's international financial commitments. While Mr. Vuscovic and the Government are undoubtedly skeptical about the Bank's willingness and ability to continue lending to Chile, it is interesting to note that at the first CIAP session on Monday he stated explicitly that his Government greatly appreciate the positive attitude displayed by the missions from the international financial agencies which had recently visited Santiago (a Fund mission was there a week prior to our visit). If the Minister does raise operational issues he will probably be primarily concerned with a possible loan to ENDESA, the state-owned electric power enterprise, although he may also allude to the proposed Second Livestock Development Project.

President has seen

ENDESA

4. ENDESA, one of the Bank's oldest borrowers is about to embark on a \$294 million expansion program covering the 1971-76 period. The enterprise's management has indicated that it would like to see the Bank associated with the financing of the entire program but I think we would prefer to lend for a specific high priority component of the program such as the Antuco hydroelectric project (which has an estimated foreign exchange component of \$30 million). The major obstacle to our appraising a project for a possible new loan to ENDESA is the question of the new Government's tariff policy. As you can see from the notes on my conversations in Santiago, Mr. Vuscovic took the position that (1) raising ENDESA's tariffs to a level sufficient to provide an adequate rate of return would be inconsistent with the Government's price control policies and (2) Bank insistence on an understanding on tariffs as a condition for a loan would be an infringement on Chilean sovereignty. After listening to my explanation of the Bank's position, President Allende said he would take the matter under consideration. Mr. Vuscovic informed us this morning that his Government's position has not changed. He continues to emphasize the sovereignty issue.

5. I do not think we have much real room for maneuver on this issue. The tariff covenant agreed upon for the loan to ENDESA (479-CH) now being implemented is a minimal one which states only that ENDESA must earn a "reasonable" rate of return. The accompanying supplemental letter defines this as 10%, the rate of return permitted under Chile's electricity law. Last year, ENDESA actually earned a rate of return of about 9%, which we regard as acceptable, but unless there is a prompt and adequate tariff adjustment this year ENDESA's earnings will fall far short of the level agreed upon. The lack of a satisfactory tariff adjustment would not only preclude us from further consideration of a new loan to ENDESA, but would also raise a serious question about the Government's performance under the present loan, of which some \$26 million still remains to be disbursed. The best hope of resolving this issue now appears to lie in the direction of a selective tariff adjustment, which would involve little or no increases for small residential consumers and perhaps some other "preferred" groups, but would provide ENDESA with adequate overall earnings. The Government is reportedly considering such a tariff increase but appears unlikely to grant one now that would be sufficient. We might wish to consider going ahead to appraise the project on the basis of only a partial tariff adjustment now if the Government is willing to agree to review the matter and make a satisfactory adjustment prior to negotiations.

Livestock

6. A possible Second Livestock Development Project was appraised by a mission which visited Chile last year. The proposed project would continue the livestock program began under our first loan (366-CH); the principal innovation proposed would be the inclusion of financing for up to 100 agrarian reform settlements ("asentamientos") as well as 800 private ranchers. The mission recommended a loan of \$21 million provided agreement could be reached

February 23, 1971

with the Government on a suitable rate of interest and indexing mechanism -- a nine percent real rate of interest was suggested -- and assurances could be obtained as to the maintenance of adequate incentives for livestock producers. In Santiago, the Minister of Economy indicated that he saw no objection in principle to the Bank's position on these issues. The Minister of Agriculture concurred, but stated that the Government wished to consider whether, in view of its plans for greatly accelerating the agrarian reform, it might not wish to request the Bank to consider modifying the project to provide for a greater role for the agrarian reform settlements. We hope to send a small mission from the Agriculture Projects Department to Chile next month to review the current situation in the livestock sector.

cc: Messrs. J. Burke Knapp
Weiner
Evans

CHILE: MEETING NOTES

President Allende

1. President Allende received Messrs. Alter, Avramovic and Dosik, together with Dr. Mey, for about 45 minutes on February 2. Also present were the Minister of Economy, Mr. Pedro Vuskovic, and the Deputy Director of ODEPLAN, Mr. Jose Ibarra.

2. President Allende stated that Chile looked forward to the continued collaboration of the World Bank in its development efforts. He emphasized repeatedly that his Government intended to scrupulously observe Chile's existing international commitments. The President pointed out that he had been democratically elected in accordance with Chile's constitutional procedures and that the establishment of a popular front type of Government in Chile did not represent an abrupt break with the past but rather reflected an element of stability in Chilean politics and society. He recalled that Chile had its first popular front government, in which he was Minister of Health, about 30 years ago, and that this government had many accomplishments to its credit including the creation of CORFO, of many of the present state enterprises and of one of the world's first comprehensive national health services. Over the intervening years the principal parties comprising the popular front had consistently advocated certain basic policies and it should have come as no surprise that his government moved quickly after taking office to implement these policies. In particular, the introduction of the constitutional reform bill that would govern the expropriation of the large copper mining companies was a matter of great urgency since, as the President put it, for Chile copper is a matter of life itself while for the others it is only a matter of a pleasant life. Mr. Alter responded that he personally felt that the most important consideration in the copper situation would be to maintain adequate flexibility on both sides so that a mutually satisfactory solution could be worked out.

3. The President said he understood that a problem had arisen between his Ministers and the Bank as regards the proposed ENDESA loan and asked our views. Mr. Alter explained the Bank's position on the tariff question, stressing the importance of realistic electricity rates from both the overall fiscal point of view and as a means of assuring the availability of sufficient resources to meet the ever growing investment needs of the sector. He emphasized that the Bank's position was based on many years of experience throughout the world and pointed out that many countries had found that "the most expensive kilowatt hour was the one that was not available". Mr. Alter stated he understood the reluctance of the Government to raise tariffs where this appeared inconsistent with its overall economic and social objectives. However, he pointed out that for most industries electricity was only a minor cost element and suggested that it should be possible to work out a tariff increase on a selective basis that would have a minimum impact on low income residential consumers, while still providing ENDESA with the overall earnings it requires.

President has seen

4. The President responded^{by}/expressing interest in Mr. Alter's suggestion of a selective tariff increase. He said he would take the matter under consideration and that the Bank would be advised of his Government's decision. He added that he was fortunate in that in Mr. Vuskovic and his economic team he had advisers of great competence and broad experience.

Richard S. Dosik
February 11, 1971

FORM No. 75
(2-6C)

INTERNATIONAL BANK FOR
RECONSTRUCTION AND DEVELOPMENT

INTERNATIONAL FINANCE
CORPORATION

INTERNATIONAL DEVELOPMENT
ASSOCIATION

ROUTING SLIP		Date February 22, 1971	
NAME		ROOM NO.	
Mr. Robert McNamara		A 1230	
	To Handle		Note and File
	Appropriate Disposition		Note and Return
	Approval		Prepare Reply
	Comment		Per Our Conversation
	Full Report		Recommendation
	Information		Signature
	Initial		Send On
REMARKS			
CHILE - Briefing for your Meeting with <u>the Minister of Economy</u>			
Attached are additional copies of the notes on the meetings with President Allende and the Minister of Economy that I had during my mission to Chile.			
I will send you tomorrow any additional briefing material that may be useful for your meeting with the Minister of Economy.			
From		Gerald Alter <i>GA</i>	

CHILE: MEETING NOTES

Ministers of Economy and Finance

1. Messrs. Dosik and Ahmad met briefly with Mr. Pedro Vuskovic, Minister of Economy, on January 28. On February 2 Messrs. Alter, Dosik and Thiebach met at length with Mr. Vuskovic and with the Minister of Finance, Mr. Zorilla. Dr. Mey was present at the latter meeting. At the first meeting we briefly reviewed with Mr. Vuskovic the status of the new projects in which the Bank had been interested and indicated the nature of the principal project issues. We also explained the importance the Bank attached to obtaining a thorough understanding of the Government's economic policies as the necessary background for future operations. A complete set of the briefing memoranda on Bank operations were left with Mr. Vuskovic. The bulk of the first meeting was taken up with operational matters; the second meeting was largely devoted to discussion of the Government's economic program.

Economic Policies

2. Mr. Alter began the second meeting by expressing appreciation for the opportunity to meet with the two Ministers and obtain a better understanding of the Government's economic objectives and its 1971 program. He stated that the 1971 program, as we understood it, aimed at reducing inflation to zero but that this did not appear consistent with the very large budget deficit and massive increase in the money supply which were also components of the program. The Ministers replied that halting inflation was not, in itself, a major goal of the Government for 1971 and that they could not imagine how the notion of a zero inflation target had gotten about. The Government's principal economic policy objectives in the current year are to bring about a substantial redistribution of income and to reactivate the economy. The wage readjustment for 1971 would average 40% in nominal terms and would result in a real wage increase ranging from 25%, assuming no inflation, to nothing if inflation remains at last year's level. The actual increase in real wages will undoubtedly fall somewhere in between, in the Ministers' view. Large increases in the money supply can take place without an excessive inflationary impact if the Government succeeds in breaking Chile's inflationary psychology which it intends to do by administering the "shock treatment" of an immediate price freeze reinforced by rigid controls. Once the Government feels it has won the essential psychological battle it will follow a more flexible price policy aimed at correcting distortions in the price structure.

3. In response to the Ministers' remarks, Mr. Alter observed that any economy would have great difficulty in absorbing such a sudden sharp change in income distribution as the Government appeared to be seeking in 1971. Mr. Vuskovic responded that he could answer this in general terms by pointing to the fact that the national income was presently distributed 50/50 between wages and other factor remuneration, thus leaving ample room for change. More specifically, the Minister stated that he believed many enterprises could absorb a large real wage increase without substantially raising prices if (1) the Government succeeds in raising demand by 8-10%, (2) interest rates are cut

and (3) other input prices are held down. In other sectors, these conditions will have to be supplemented by more specific measures. For example, to keep food prices down the Government aims at drastically reducing marketing margins, while in other areas, the Government intends to carry out its price policy through such means as agreements fixing prices and profit margins in particular industries (e.g., shoes, clothing) and "production contracts" under which the Government undertakes to buy an industry's output and undertake distribution for its own account (e.g., building materials and other inputs for Government construction programs).

4. As regards the budget, we stated that the projected increases in 1971 revenues and expenditures appeared very large and that we would appreciate additional information so that we could better understand the basis for these projections. We indicated that we would particularly like to know the basis for the E⁰1,500 million of unspecified "economies" projected on the expenditure side and the E⁰1,500 million of income expected from the collection of past due taxes. The Minister of Finance responded by stating that the budgetary revenue projections were based not on zero 1971 inflation but on the assumption of a 25% average price increase this year over the 1970 level and by promising to provide detailed tax-by-tax information on these projections. The projected economies, he stated, would be made in current, not capital, expenditures. Past due taxes would be collected by greatly strengthening tax administration and by permitting the "white washing" of previously undeclared income.

IBRD Operations

5. Mr. Vuskovic stated that Chile wishes to continue working with all the international financial agencies and that it has great interest in continued cooperation with the Bank. The Bank's traditional areas of operation in Chile fit in well with the Government's development plans and continued Bank assistance in livestock development and in the power sector would, in principle, be most welcome. In addition to its interest in our traditional areas of operation, the Government would like at a later date to explore with the Bank the possibilities of new types of operations, particularly in the industrial sector. The Government regards private entrepreneurial ability as a valuable asset, which it wishes to preserve, but feels that, especially in view of the financial weakness of Chilean private enterprise which is now being exposed, this will involve the widespread formation of mixed enterprises with majority Government control. The Government will be able to obtain majority control of many important private enterprise by capitalizing their debts to CORFO, the Banco del Estado, etc. and will seek to put them on a sound financial basis and expand their operations through the injection of new capital.

6. Mr. Vuskovic suggested that the proposed livestock project be discussed in detail with the Minister of Agriculture and other authorities concerned to determine whether the project as originally conceived is still feasible, or whether it would be better to restructure it in view of the Government's plans for accelerating agrarian reform. He indicated that he, personally, did not have any objection, in principle, to the Bank's position

on interest rates or indexing and that he regarded these as essentially "mechanical" problems which could be solved to our mutual satisfaction.

7. As regards the ENDESA tariff problem, Mr. Vuskovic took the position that this cannot be dealt with in isolation but only in the context of the Government's overall economic and financial policies. The avoidance of large tariff increases was important to the Government's stabilization efforts because of the importance of power as an industrial cost and because large tariff increases for residential consumers would be inconsistent with the Government's efforts to project an image of stability and break the inflationary psychology. Furthermore, there was no sound economic reason for seeking to maximize profits in all state enterprises; for example, the Government might wish, for development reasons, to hold electricity rates down in order to reduce industrial costs and stimulate industrial development in general. Moreover, quite apart from the substance of the Government's tariff policies, the Ministers made it clear that they would regard Bank insistence on an understanding on tariffs as a condition for a new ENDESA loan as an unacceptable infringement on Chilean sovereignty.

8. In reply, Mr. Alter explained that the Bank invariably considered an understanding on tariff policy to be an essential component of its power loans and that such understandings were contained in the Bank's existing loans to ENDESA. He discussed the rationale for the Bank's view in terms of both the need to maintain public savings generally and the importance of assuring the availability of adequate financing for investments in the power sector. Mr. Alter pointed out that the longer adjustment was delayed, the more difficult it would be to raise tariffs to a realistic level since, as the Government itself realized (see para. 2 above), inflation was actually likely to continue at a substantial rate this year and there would be a need for corrective adjustments to remove distortions in the price structure. He noted that the tariff covenant in our last loan to ENDESA took the form essentially of a reaffirmation of the Government's intention to carry out Chile's own electricity law. Mr. Vuskovic observed that he regarded the latter law as unwise and that the Government intended to seek its repeal. In closing the discussion on this subject he stated that he and the Finance Minister had given us the Government's position as it presently stood, but that a final decision would have to be taken by the President.

Richard S. Dosik
February 12, 1971

6

MEMORANDUM FOR THE RECORD

August 16, 1971

Messrs. McNamara and Knapp met with former Ambassador of Chile, Sergio Gutierrez Olivos, on June 29. Mr. Knapp informed me that no substantive issues were discussed. It was merely a courtesy visit.

L.E. Christoffersen

OFFICE MEMORANDUM

TO: Mr. Gunter K. Wiese

DATE: August 6, 1971

FROM: Richard S. Dosik

SUBJECT: CHILE - Ambassador Letelier's Meeting with Mr. McNamara

1. For your briefing with respect to the subject meeting, the following are some notes concerning the principal subjects of current interest in Chile.
2. Earthquake. The earthquake which hit Chile on July 8 killed 80-90 people and did an estimated \$250 million in property damage in Valparaiso and the coastal region to the north. Most of the destruction appears to have been suffered by homes but damage to a refinery, ports and other infrastructure was also reported. It is my best guess that the Ambassador is calling on Mr. McNamara to request Bank assistance in financing earthquake reconstruction. This is a matter of great concern to the Allende Government and there are no project or other issues between the Bank and Chile which would appear to warrant the Ambassador's call at this time. The Bank has not heretofore been approached by Chile for earthquake assistance so far as I am aware. The only communication we have received on this subject was a cable addressed to Mr. McNamara from the UNDP which was received in the Bank on July 21; it did no more than forward damage estimates provided by its Resident Representative in Santiago and his request for approval for a UNDP food relief project. Mr. Alter decided no reply to this cable was called for since, while serious indeed, the earthquake did not seem from the information provided to be a national disaster of the magnitude of the recent Peruvian quake, or of the one in Chile in 1960, or to have done the sort of damage for which Bank assistance in reconstruction might be suitable. (As you may recall, IDA Credit 4-CH for a highway project was granted in part to assist Chile in recovering from the 1960 quake.)
3. Copper Nationalization. The constitutional amendment providing for the nationalization of the large copper companies was passed by the Congress and signed by President Allende on July 19 and the process of valuation of the companies' properties for the purposes of compensation is reportedly already underway. Executives of the Kennecott Corporation called on Mr. McNamara on July 28; their principal point seems to have been that the constitutional amendment precluded adequate compensation by providing that it be based on the book value of the mining properties rather than on market value or income earning power. The Legal Department is currently preparing a detailed analysis of the constitutional amendment for the purpose of determining whether it would permit acceptable compensation. We hope ourselves to take a close look at some of the recent settlements of investment disputes in Latin America to see if we can discern any pattern as to what, in practice, constituted an acceptable settlement in these cases.

August 6, 1971

4. Fruit Development Project. This is the only project currently on the "front burner". It would provide approximately \$7 million to cover the foreign exchange cost of a program of loans to farmers and agrarian reform settlements for orchard extension and improvement. An appraisal report is now in preparation and is scheduled for completion in yellow cover later this month. We have advised the Minister of Agriculture of the Bank's decision to proceed with the project and that we hope to be able to invite representatives of Chile for loan negotiations by October-November. In a letter just received, the Minister expressed his satisfaction with the Bank's action on this project, and his willingness to discuss the interest rate question further at negotiations.

5. Livestock. CORFO has agreed with the conclusion of our reappraisal mission that sufficient local currency funds remain from the first loan (366-CH) to finance ranch loans for at least another year, and that consideration of a second Bank loan may therefore be postponed accordingly. Various problems relating to the implementation of the first project --including the future of the Technical Director and the institution of a system of repayment in kind-- seem to have been satisfactorily resolved.

6. Power. We have received the awaited feasibility material on ENDESA's investment program but it is understood on all sides that Bank consideration of another power loan awaits the Government's action on the tariff question. This is, in any case, not holding up implementation of ENDESA's program since work on the Antuco hydroelectric project, the item in the investment program most eligible for Bank financing, is not scheduled to begin until late next year. Our last word from ENDESA was that the Government had definitely decided to grant a tariff adjustment this year and that negotiations for a substantial adjustment were underway. The recent IMF mission reported that it understood that the Government intended to revise all public sector tariffs effective September 1.

7. Education. The problems which have arisen with the implementation of the Third Education Project (Loan 668-CH), and about which Ambassador Letelier contacted Mr. Knapp in June, appear well on the way to final resolution. Good progress was made during the recent visit here of a Chilean mission and a Bank supervision mission has just visited Santiago to examine some of the remaining questions.

OFFICE MEMORANDUM

TO: Memorandum for the Record

FROM: Gerald Alter *GA*

SUBJECT: Meeting of Mr. McNamara with Ambassador Designate
of the U.S. to Chile, Mr. Nathaniel Davis

DATE: September 22, 1971

Mr. Nathaniel Davis, Ambassador Designate of the U.S. to Chile, called on Mr. McNamara on September 13. Mr. Alter was also present. The focus of the discussion was on the problems created by the nationalization of the copper companies. Mr. McNamara explained the Bank's posture vis-a-vis the new Chilean Government. We had made it perfectly clear in our early dealings with the new Government that we were not bound by ideological constraints. We had discussions with the new Government about specific projects and were now working on a small loan for fruit development. The Bank had a well-established policy on expropriation matters, which was known to the Chilean Government. We hoped to be able to proceed with this fruit loan on the assumption that the Chileans were following a proper course in determining compensation for expropriated properties. If these assumptions were not realized - and it is possible to raise many questions concerning the implications of the Constitutional Amendment relating to expropriation - we might have difficulty in establishing our good intentions by consummating this loan.

The Ambassador was interested in finding out whether the Bank had communicated its policy vis-a-vis expropriation to the new Chilean Government, returning to this theme several times. We pointed out that we had not pounded the table with the Chilean Government on this issue, but that we had urged upon President Allende flexible provisions in the Constitutional Amendment during a visit last February and had mentioned the issue with high officials of the Government on other occasions.

cc: Mr. Knapp
Mr. Broches
Mr. Dosik

President has seen

GAAlter:pa



OFFICE MEMORANDUM

TO: Mr. Robert S. McNamara

DATE: October 5, 1971

FROM: J. Burke Knapp

SUBJECT: CHILE - Meeting with Delegation

Please find attached memoranda reporting the conversations which Mr. Alter and I had with the Chilean Delegation during the Annual Meeting. Also attached is a copy of the letter to you left with me by the Governor of the Central Bank, asking for clarification of the World Bank's position vis-a-vis Chile. We shall prepare an answer to this letter after October 14, which as you know may prove to be a significant date in the Chilean process for fixing the compensation price for the copper properties.

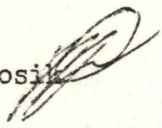
Attachments

cc: Mr. Broches
Mr. Alter

President has seen

OFFICE MEMORANDUM

TO: Files

FROM: Richard S. Dosi 

SUBJECT: CHILE - Mr. Knapp's Meeting with Delegation

DATE: October 4, 1971

1. On Friday afternoon, October 1, Mr. Alfonso Inostroza, President of the Central Bank and Governor of IBRD, called on Mr. Knapp. Mr. Inostroza was accompanied by Mr. Javier Urrutia, the CORFO representative in New York, and by Messrs. Morales and Sierra of the Chilean Delegation. Mr. Alter and the writer were also present.
2. Mr. Inostroza began by stating that his meeting with Mr. Alter on September 28 had left him very much concerned. He had understood Mr. Alter to say that Bank operations in Chile had been suspended pending the satisfactory settlement of the compensation claims of the copper companies. He had no previous idea that Bank policy permitted such action or that it was being applied to Chile in the way he understood.
3. Mr. Knapp replied that he was certain there had been a misunderstanding in Mr. Inostroza's meeting with Mr. Alter. He referred back to Mr. Alter's visit to Santiago earlier this year in which it had been made clear to the Government, and to President Allende, that the Bank had no hesitation about continuing to work with Chile. Since then, while we have not been able to make any progress on a possible loan to ENDESA because of the tariff issue, other operations have been moving ahead normally. We have, in fact, been quite anxious to develop a concrete means of collaborating with Chile and, since learning that the fruit project might be ready for Bank financing in the near future, had given it high priority and done much intensive work. This was the situation as of last Tuesday --i.e., our operations in Chile were moving ahead a d, as Mr. Inostroza knows, we had an economic mission in the field.
4. Mr. Knapp then went on to indicate that events subsequent to last Tuesday had caused a setback. Although we have not yet had time to study the implications of the President's decision on deductions from compensation for "excess profits", it had come as something of a shock to us because it might indicate that the copper companies would receive no settlement. It was not the Bank's policy to insist on the final resolution of an expropriation dispute before lending and we have in fact gone ahead to lend in several recent cases where such disputes existed. However, for the Bank to continue lending in such situations, the possibility of reasonable progress toward a reasonable settlement had to remain open. Up until Tuesday we had felt this was the case in Chile, but the President's decision had introduced a new element into the situation and we would have to come to a decision soon on its implications for the Bank.

President has seen

October 4, 1971

5. Mr. Inostroza seemed to be reassured by Mr. Knapp's remarks. He said he wanted to emphasize that Chile had a real interest in working with the Bank. His Government had already settled claims with several foreign companies, American as well as European, and resolution of the copper case was subject to a long process that had only just begun. It was important that the Bank be willing to hear Chile's point of view and to consider the issue on its merits. If the Bank were to take a position now, by suspending operations, this would be exercising "pressure". Mr. Inostroza then handed Mr. Knapp a letter addressed to Mr. McNamara which he said set down the views he had just discussed with us. He said he would greatly appreciate a written reply stating the Bank's position as Mr. Knapp had outlined it. (A translation of Mr. Inostroza's letter is attached.) He suggested that the Bank communicate with Chile on this matter in the future through Mr. Urrutia, who would be designated an Alternate Governor for this purpose.

6. At the close of the meeting Mr. Inostroza stated that he hoped the economic mission would be able to finish its evaluation as quickly as possible. He also said that the Government intended to present the Bank with specific proposals for using the balances in existing loans for earthquake reconstruction. In addition, we could expect to hear from the Government on the ENDESA tariff question.

cc: Messrs. Alter
Wiese
Avramovic
Ahmad

RSDosik:mts

OFFICE MEMORANDUM

TO: Files

DATE: October 4, 1971

FROM: Richard S. Dosik

SUBJECT: CHILE - Mr. Alter's Meeting with Delegation

1. On Tuesday afternoon, September 28, Mr. Alter met with Messrs. Inostroza and Morales. Also present for the Bank were Messrs. Wiese, Avramovic, Ahmad and the writer.

2. Mr. Alter began by stating that the Bank's technical evaluation of the fruit project was nearing completion but that consideration of a Bank loan would also depend on two non-project factors. The first of these was the findings of the economic mission as regards Chile's economic situation and prospects --i.e., its creditworthiness. The second factor was the Bank's established policy towards disputes between borrowers and foreign investors arising out of expropriations. Under this policy the Bank might have to make a judgment on the reasonableness of any valuation of the copper mines for purposes of compensation that might be made prior to the presentation of the fruit project loan to the Executive Directors.

3. Mr. Inostroza interrupted, in some agitation, to state that he did not understand the connection between the expropriation of the copper mines and the fruit project. The former was a strictly internal Chilean matter which should not concern the Bank at all. He could not see why Chile's use of the resources of a multilateral institution of which it was a member should depend on something that was totally unrelated to the quality of the project being considered for financing. Mr. Alter responded by referring to the history of the Bank's concern with disputes arising between borrowers and foreign investors, beginning with the early postwar disputes over defaulted bonds. He emphasized that under the Bank's policy the benefit of the doubt was given to the borrower in that the existence of a dispute did not mean an automatic interruption of the Bank's operations. Rather, Bank lending usually continued normally so long as the settlement of the dispute with foreign investors was being considered in good faith.

4. Mr. Inostroza continued to indicate that he could not appreciate the basis of the Bank's policy. He particularly could not understand how the Bank could question the outcome of the legal process for determining compensation that had been established in Chile. Mr. Inostroza asked repeatedly if the Bank policy to which Mr. Alter referred had been approved by the Executive Directors and whether he could receive in writing the Board's "decision" on this matter. Mr. Alter stated that the Bank's policy had been established over a long period and the Executive Directors had, in many specific cases, made decisions under this policy. A paper that had recently been distributed to the Board gave the background of the Bank policy and recorded many occasions in which it had been discussed by the Executive Directors. Mr. Alter had already asked Dr. Mey to provide the Chileans with a copy of this paper following his recent discussion of the subject with the Ambassador. Dr. Mey said that he had not received Mr. Alter's request, but that he would see that Mr. Inostroza received the Board document as soon as possible.

October 4, 1971

5. Mr. Alter emphasized that the Bank's operations have not been suspended in any sense. He had only wanted to raise the expropriation issue with Mr. Inostroza at this time to indicate that inadequate compensation could be an obstacle to Bank operations in the future. Mr. Inostroza replied by repeating that Mr. Alter's reference to the compensation of the copper companies being taken into consideration in Bank lending raised an issue that was completely new to him. He had understood that readjustment of electric power tariffs was a condition for Bank lending, but not about this new criterion. He regarded the compensation question as a very dangerous one since it gave a veto over Bank lending to one important member country and thereby called into question the multilateral character of the Bank.

6. Turning to another subject, Mr. Inostroza stated that the Government was preparing to present to the Bank a project for the rapid utilization of the balances in existing loans for earthquake reconstruction purposes. He inquired whether the reprogramming of funds in existing loans would require the approval of the Executive Directors and was told this would probably be the case, since changes in the original projects would be involved. As regards ENDESA, Mr. Inostroza confirmed that the Government does intend to restructure power tariffs but that he could not say exactly when this would be done. He then asked whether, even if ENDESA's tariffs were readjusted, a Bank loan would still be subject to the expropriation policy. Mr. Alter replied that this was so -- i.e., that the Bank's policy on expropriation naturally applied to all of its operations.

cc: Messrs. Alter
Wiese
Avramovic
Ahmad

RSDosik:mts

IBRD LANGUAGE SERVICES DIVISION	
CONTROL No. E-546/72	DATE: October 4, 1971
ORIGINAL LANGUAGE: Spanish (Chile)	
DEPT. South America	TRANSLATOR: RFW:dmc

OCT 8 REC'D

October 1, 1971

Mr. Robert S. McNamara
President
International Bank for Recon-
struction and Development
1818 H Street, N.W.
Washington, D.C.

Dear Mr. President:

On Tuesday, September 28, together with the Temporary Alternate Governor, Mr. Morales, I attended, at the request of Mr. Gerald Alter, a working meeting at which he and other staff members were present.

During this meeting Mr. Alter reviewed the applications which Chile currently has pending with the Bank and stated categorically that processing of these loans was conditional upon the outcome of compensation arrangements for the private United States companies in the large-scale copper mining sector, whose installations were recently nationalized by my country's Government. Mr. Alter based this decision on operating criteria that he said the Bank has adopted in dealing with particular cases it has had to settle.

The opinion expressed by Mr. Alter appears to us to be of the utmost consequence and gravity; it would be tantamount to direct interference with my country's exercise of its sovereignty, since the nationalization of the US copper companies is in accord with the principles of

a constitutional amendment that was passed unanimously by the Chilean Congress. This amendment contains clear and specific provisions on the procedure for determining and paying compensation to these companies.

In view of the foregoing situation, which conflicts with Chile's sovereignty and violates the multilateral character of the Bank, I ask you for an unequivocal statement on the position the World Bank intends to adopt with respect to the loan applications which my country now has pending with it and any it submits in the future.

Very truly yours,

(sgd.) Alfonso Inostroza

Governor of IBRD for Chile

Boards of Governors · 1971 Annual Meetings · Washington, D.C.

INTERNATIONAL BANK FOR RECONSTRUCTION AND DEVELOPMENT
INTERNATIONAL FINANCE CORPORATION INTERNATIONAL DEVELOPMENT ASSOCIATION
INTERNATIONAL MONETARY FUND

Address replies to:

JOINT SECRETARIAT - ANNUAL MEETINGS
IBRD AND AFFILIATES - IMF
19TH AND H STREETS, N.W.
WASHINGTON, D.C. 20431

Cable Address

INTERMEET
WASHINGTONDC

1° de Octubre de 1971

Señor
Robert S. McNamara
Presidente
Banco Internacional de Reconstrucción
y Fomento
1818 H Street, N.W.
Washington D.C.

TRANSLATED
INTO ENGLISH

OCT 4 1971

CONTROL No. E-546/71
I.B.R.D.

Señor Presidente

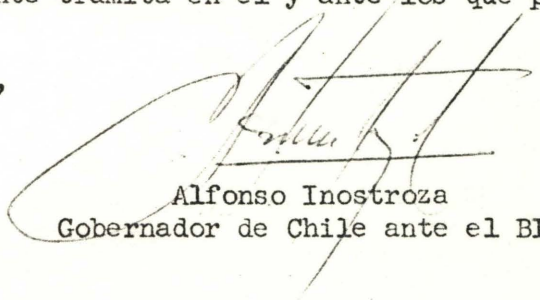
El martes 28 de septiembre último asistí, acompañado del Gobernador Alterno Temporal, señor Morales, a una reunión de trabajo, a requerimiento del señor Gerald Alter, con él y demás miembros del staff.

En esta reunión el señor Alter analizó las operaciones que Chile tiene pendiente con el Banco y expresó, en forma categórica, que las tramitaciones de estos créditos quedaban supeditadas al resultado de las eventuales indemnizaciones a las compañías privadas norteamericanas de la Gran Minería del Cobre, cuyas instalaciones han sido nacionalizadas recientemente por el Gobierno de mi país. El señor Alter fundamentó esta decisión en criterios operativos que, según él, el Banco habría adoptado ante casos particulares que ha debido resolver.

La opinión expresada por el señor Alter nos parece de la mayor trascendencia y gravedad, ya que importaría una intervención directa en el ejercicio de la soberanía de mi país, toda vez que la nacionalización de las empresas norteamericanas de la Gran Minería del Cobre se ajusta a las normas de una reforma constitucional aprobada unánimemente por el Congreso Nacional de Chile. Esta reforma consulta disposiciones claras y precisas sobre el procedimiento a seguir para determinar y pagar la indemnización a estas empresas.

Considerando la situación expuesta, contraria a la soberanía de Chile y atentatoria contra el carácter multilateral de este Banco, solicito de Usted un pronunciamiento definitivo sobre la actitud que el Banco Mundial observará ante los créditos que mi país actualmente tramita en él y ante los que presentará en el futuro.

Saluda a Usted muy atentamente,


Alfonso Inostroza
Gobernador de Chile ante el BIRF