

## The Americas



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Chile

## Progress and its discontents

SANTIAGO

**A popular student rebellion shows that, as Chileans become better off, they want the government to guarantee a fairer society. Politicians are struggling to respond**

**I**N A ritual marking the start of the academic year, last month the streets of Santiago were full of students dressed in colourful combinations of rags and body paint politely, seeking donations from passers-by in the late-summer sunshine. Many of their predecessors had spent their summer holidays swotting, having devoted last year to occupying classrooms and taking to the streets in their tens and hundreds of thousands, in sometimes violent demonstrations to demand free and better higher education. This mass popular protest, and the huge public sympathy it aroused, took the centre-right government of Sebastian Piñera by surprise, leaving it floundering.

The habit of protest seems to be catching on. Thousands of residents of Aysén, a remote region in Patagonia, have blocked roads to demand cheaper petrol and in protest over a new fishing law. Similar regional protests have occurred in Calama, a mining area in the northern desert, and (last year) in Punta Arenas.

Such protests have been commonplace for years in Peru, a poorer and more diverse country. But Chile? In the two decades since General Augusto Pinochet's dictatorship gave way to democracy, Chile has stood out in Latin America for its rapid growth, social progress, political stability

and relatively robust institutions. Now Chile's political leaders are wondering if they are seeing a popular rebellion against "the model", as some call the free-market policies bequeathed by Pinochet and left largely intact by his successors.

Two years ago Mr Piñera, a billionaire businessman, led the centre-right Alliance to power after two decades of rule by the centre-left Concertacion coalition. When his government organised a successful rescue of 33 trapped miners in October 2010, his approval rating soared to 63%, says Adimark, a pollster. Thanks mostly to the students, it is now just 29%.

Part of the problem is that Mr Piñera has proved to be an inept politician—a view not confined to the opposition. The government was slow to respond to the student protests. The president zigzagged between talking tough and giving in, undercutting his ministers in the process. The latest casualty was the energy minister, who resigned over the mishandling of the Aysén protest. The public dislikes Mr Piñera's arrogance. "He has convinced Chileans that he's very intelligent, but he hasn't convinced them he has a heart," says Arturo Fontaine of the Centre for Public Studies (CEP), a liberal think-tank.

But the public is equally dismissive of the Concertacion. At just 21%, its approval

rating is even lower than the governing Alliance (24%), according to Adimark. Rather, the emblematic figure of Chile's year of discontent is Camila Vallejo, a 23-year-old Communist student leader. Having been an irrelevance on the margin of Chile's two-party system, the Communist Party enjoys "more influence than at any time in the past 20 years," says Guillermo Teillier, its president.

What makes this collapse of public confidence in the system odder is that in many ways Chile continues to thrive. The economy is growing by 6% a year, and with virtually full employment, wages are rising equally fast. The government has done a reasonable job of reconstruction after a severe earthquake two years ago.

### Less poor, still unequal

In opinion polls the students' demands enjoy the support of 70% of respondents, even if their sometimes disorderly methods attract the disapproval of a narrow majority. The student movement has struck a chord in a society that is increasingly middle-class but remains highly unequal. Only 5% lived below the poverty line in 2009, down from 45% in the mid-1980s. But the distribution of income in Chile is the most unequal in the OECD, a group of 31 mainly rich countries that it joined in 2010. Taxes and government transfers do little to reduce inequality (see chart 1 on next page). The education system has locked in social inequality rather than breaking it down.

Chile has made a big effort to increase access to education, partly by allowing private entities to run schools and universities. Politicians from both main coalitions repeat the numbers with pride: ••

- over 1.1m young people now study in universities or technical colleges, up from just 200,000 in 1990. That amounts to around 45% of 18-24 year olds. Over 70% of these students are the first generation in their families to go on to higher education. All in, Chile spends around 7% of GDP on education-above the OECD average, though its population is younger. But more than a third of the spending is private. Many Chileans find they are paying a lot for an uncertain return.

All universities, both private and public, rely on student tuition fees, which account for 80% of spending on higher education, according to Carlos Peña, the rector of Diego Portales University. Fees range from \$700-1,000 a month at the top universities, down to around \$70 a month for a two-year vocational course at DUOC, a non-profit technical college linked to the Catholic University

But fees at most universities cluster at the upper end, irrespective of quality. And on average, they have been rising by 3-4% a year in real terms in the past 15 years, notes Harald Beyer, an academic who in January became Mr Piñera's third ("and I hope last") education minister. To make matters worse, the average university course lasts six years and four months, compared with an OECD average of four years and four months, according to Mr Beyer.

Although around 60% of students get grants or government-backed loans, these cover only 70-80% of fees. Loans at "traditional" universities-a group of 25 public and private non-profit institutions-carry an interest rate of just 2% a year. But the interest rate on state-guaranteed bank loans to students at newer private universities, introduced in 2006, was fixed at 5.8%. Many poorer families find that they can achieve their dream of educating their children only by taking on large debts.

Many students arrive with the idea that they will derive the same advantages that universities offered when they catered for only a small minority. That is no longer true. As the number of educated Chileans rises, the premium they command in the labour market falls. (This is why income inequality in Chile has been falling a bit.) Employers give more weight to degrees from the top universities. In addition, drop-out rates are high. Those who drop out have accumulated debts but will be little better off than if they had gone straight into the labour market after school, according to a CEP paper by Sergio Urzúa, an economist at the University of Maryland. Mr Urzúa estimates that 39% of those who do graduate will find that their salaries do not compensate for the cost of their courses. As Andres Velasco, a former finance minister, puts it, "the combination of lower-than-expected income and higher-than-expected debt is explosive."

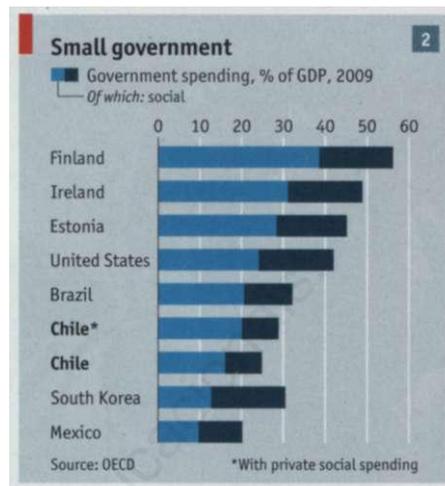
Poorer students are more likely to drop out, and less likely to get into the poshest university courses. That is because they go to worse schools. Thus at DUOC, where three-quarters of students come from the poorest three-fifths of society, about 35% drop out, either for economic reasons or because they find the courses too hard, according to Jaime Alcalde, the rector. "Students arrive without being able to do basic arithmetic or with weak language skills," he says. About a quarter of each course at DUOC involves remedial classes in maths, language and English.

DUOC has a good reputation for achieving upward mobility: within six months, nine out of ten graduates are working in their area of specialisation, for salaries ranging from \$1,150 to \$2,450 a month, says Mr Alcalde. That may be why few of its students joined the protests.

But many other institutions offer much worse value. "In Chile there are good universities for the rich and bad universities for the poor," complains Camilo Ballesteros, president of the students' union at the University of Santiago last year and now the Communist candidate for mayor in one of the capital's student districts. He wants "free high-quality universities for all". The student movement also wants the national government to take over municipal schools and to abolish for-profit state-subsidised schools. Universities are barred by law from making profits, but some find loopholes, such as when their owners set up property companies that charge high rents for their campuses.

#### Fair, not free

"We're not going to yield to demagogic demands," says Andres Chadwick, who is Mr Piñera's cabinet secretary (and first cousin). "Free education doesn't seem fair to us, because those in higher education still tend to be the better-off."



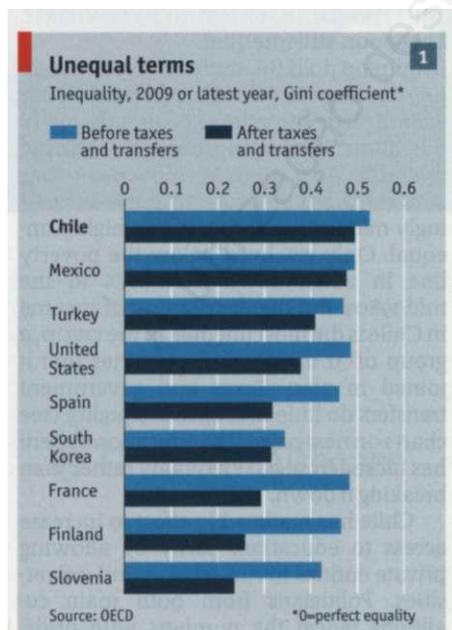
Instead, the government wants to make higher education cheaper and better, in several ways. It has sent a bill to Congress to equalise the interest rate on all student loans at 2% a year. That this has not been swiftly approved suggests that the traditional universities are quietly lobbying against it. Another bill would set up a regulator whose job would be to enforce the law barring universities making profits. The government has also announced a modest rise in state-funded student grants, and it is mulling a law to reform university governance.

Some in the opposition want to see a cap on fees. But that risks hurting quality. Mr Urzúa argues that the biggest problem is the lack of information students have when choosing their course about the cost and the likely economic return.

But most of the government's efforts are directed at improving schools. Mr Beyer points out that, by the time they are ten years old, pupils' performance already varies sharply with household income. That is partly because less than half of Chilean children receive any preschool education. But it is also because the poor go to worse schools.

Pinochet left a voucher system in which the government runs no schools itself, but instead pays a fixed fee per pupil. But while private schools ask parents for top-up fees, most municipal schools do not. The Concertacion government of Michelle Bachelet (2006-10) raised the voucher to \$100 per pupil each month, and added an extra \$50 for poorer children. But Mr Velasco, who was Ms Bachelet's finance minister, says the voucher needs to double if poorer children are not to lose out.

Perhaps the most pressing need in Chile's schools is a radical shake-up of the teaching profession. Because teachers are mediocre, even the poshest private schools in Santiago are no better than an average state school in London or New York. Mr Piñera's government has made a start: a 2010 law gave head teachers more power to hire and fire. Missing is a grand bargain



• in which higher salaries would attract brighter graduates into better teacher-training programmes and then make them accountable to parents for their schools' performance.

Mr Beyer points to a poll showing support for free higher education falling from 80% to 45% over the past year as evidence that the government is starting to win the argument. But it may be losing the wider propaganda war. Roberto Méndez of Adimark says that, for the first time in 30 years, "trust in the liberal economic model has weakened", from 60% to 40%. That may be because the student movement has crystallised a widespread feeling that the economy, politics and the media are all rigged in favour of a small elite.

### Collusion and cartels

Partly because Chile is a fairly small, remote country, its economy is riddled with oligopolies. For example, just three chains of pharmacies control 90% of the market. In January, the competition authority found that they had colluded to push up the price of more than 200 medicines by around half. The authority has also fined bus companies for collusion. It is now investigating an alleged chicken cartel. Retailers get away with usurious interest rates on store cards. This came to light last year when La Polar, a retail chain, was found to be fraudulently covering up loan losses by jacking up interest rates without telling customers. Several senior politicians from both main coalitions are shareholders in for-profit universities—sorry, property companies-in covert defiance of the law. The private health insurers and pension funds that Chileans are required by law to use also extract large profits.

The tax system similarly favours the better-off, though it has also proved effective at promoting private savings and investment. Corporate income is taxed at 18.5%; shareholders receiving dividends can set this against their personal income tax. Since the top rate of personal income tax is 40%, high earners shield their income by creating shell companies. The government is planning a tax reform that would raise the corporate income tax to 20%, while cutting tax rates on personal incomes and for small businesses, as well as cutting a stamp tax on credit. The reform will raise around \$700m (or 0.3% of GDP), to be spent on education, says Felipe Larraín, the finance minister.

Is this enough? Unlike some other left-of-centre governments in Latin America, the Concertación was a model of fiscal responsibility. It raised social spending, but entrenched a fiscal rule that requires the government to balance its books over the economic cycle and to save windfall profits when the price of copper—Chile's main export—is high, as it is now. Alejandro Foxley, finance minister in the first Concerta-

ción government, says that the state needs to raise an extra 2.3% of GDP in taxes to satisfy the public demand for better education, infrastructure and institutions (see chart 2 on previous page).

Mr Larraín disagrees. He says that Chile's total tax take of 23% of GDP is about right for a country of its income level once spending on social security, which is privatised, is taken into account. But the governing Alliance is divided. Pointing to the sense of neglect in far-flung regions such as Aysén, Lawrence Golborne, the minister of public works and a likely presidential candidate in 2013, says that public spending on infrastructure needs to double from its current level of 1% of GDP. The Independent Democratic Union (UDI), the larger and more conservative member of Mr Piñera's coalition, has long favoured a small state. But it now has a populist wing that wants to cut taxes while also doling out additional subsidies.

The debate about public spending will dominate the 2013 presidential election. But even more important are reforms to promote competition and raise productivity. Without them, growth may slow and Chile will remain overly dependent on copper. Reforms often stall in Congress because the vested interests they hurt are often big political donors, points out Eduardo Engel, an economist at Yale and the University of Chile. It took a decade to overcome lobbying from incumbents and approve a law allowing consumers to keep their phone numbers if they switched telecoms providers, for example.



Camila Vallejo leads the revolution

Indeed, the most unpopular oligopoly in Chile may be the two-party system that has given the country stability. It is propped up by an electoral system of two-member constituencies, devised by Pinochet as one of several measures to ensure that the right, then a minority, would maintain a veto over change. Its critics say that this has had the effect of turning political office into a sinecure, which in turn risks creating a gerontocracy. The president has offered to reform the electoral system if there is consensus about an alternative, but ministers acknowledge that the Congress, in which the government lacks an overall majority, has no appetite to change the rules under which it was elected.

It is almost a truism that the student movement marks a generational change in Chile. The student leaders were born as their parents were voting in the plebiscite that ended Pinochet's rule. They do not share their parents' fears. They have grown up in a society used to material progress. They have bypassed Chile's generally conservative media with their own means of communication. Fernando García, a political scientist at Diego Portales, points out that Chile has the fourth-highest usage of Twitter per person in the world, with almost 30% of the population tweeting. Eight out of ten Chileans under 30 are on Facebook and there are more cellphones than people, "so the cost of mobilisation is zero," says Francisco Díaz, a former adviser to Ms Bachelet.

Fatigue may yet diminish the intensity of the protests later this year, but student leaders now talk of a broader movement drawing in regional protests. Some political analysts worry that the current crop of relatively pragmatic student leaders will be replaced by yet more radical ones.

Many believe that Ms Vallejo (who declined requests for an interview) has a bright political future. But that may be despite her affiliation with the Communist Party, not because of it. Mr Teillier says his party and its allies command no more than 10% of the vote. He sees the possibility of a single opposition platform for municipal elections in October. Indeed, in the short term the student movement may have even greater impact on the Concertación than it has on the government. After its leaders were jeered when they tried to join the protest marches, the Concertación sheepishly adopted the movement's main demands. It risks being pulled farther to the left than the country as a whole.

Mr Peña, the rector of Diego Portales, says that popular support for the student movement is "not really a radical rebellion against the market economy". Rather, it is the consequence of a "gigantic revolution of expectations". It is also a sign that Chilean society has changed faster than its elites and its political system. The politicians have been warned.