

Widely considered to be the leading spokesman for Chicago School economics, Arnold "Al" Harberger is best known for his leadership of the Chicago Boys, a group of economists who were instrumental in implementing free-market reforms to the Chilean economy in the early '70s, under Gen. Pinochet.

Harberger provides the reader with an insider's view on the Chicago School—its atmosphere, its influence in the world of economics, and its impact on the Chilean economy.

Latin America's Ill-Fated Import-Substitution Policy

INTERVIEWER: What was the general thrust of Juan Perón's foreign economic policy in Argentina?

AL HARBERGER: Well, it was very much an inward-looking policy, and that was a policy of so-called import substitution that became the flagship story of Latin America for the whole postwar period, heading into the '60s and '70s. Now, the origins of that were probably the Depression, and even more so [World War II]. The Depression spoiled the purchasing power of the Latin American countries, which were mainly primary exporters, and the war interrupted supplies from [abroad], so the plausibility of "Let's do it on our own" seemed so wonderful, you know, and Raul Prebisch was a distinguished Argentine economist, and he became the captain of the ship, so to speak, intellectually, and Argentina, Chile, Uruguay, Mexico, Brazil all went down that import-substitution line. There were times when import tariffs were 200 and 300, even 400 percent. The amount of hothouse industries that were being protected behind these barriers was unimaginable. Most of the protected items would cost there, measured in dollars, one and a half, two, two and a half times what they did in American markets.

INTERVIEWER: Is this the kind of policy that was implemented because he was an ultra-nationalist, designed to make the country strong?

AL HARBERGER: Exactly. He came to power during the war, if I remember correctly, and so he was there right at the birth, so to speak, of this feeling of this need, you see, and [he was] preaching self-sufficiency at a time when you hardly had any alternative. It made a certain

amount of sense and led to a lot of popularity, not only of [Perón] but of other politicians around Latin America, but it was very bad economics.

INTERVIEWER: Why was it such bad economics?

AL HARBERGER: Well, let's say at the time a market economy would have worked the same way. It would have worked to have an exchange rate, a price of the dollar which was sufficiently high to automatically and efficiently protect a lot of domestic industry, but what happened was that the chick was barely out of the egg when the war ended, you see, so this whole enormous hen that came out in the end grew in a period when it was absolutely counterproductive from the standpoint of those economies.

INTERVIEWER: Why were those counterproductive?

AL HARBERGER: Counterproductive because it's kind of easy to think... If you think about 10 pesos per dollar as the exchange rate, you produce something for export, you make a dollar and you get 10 pesos for it. What these guys were doing was, while they were paying only 10 pesos for a guy who makes a dollar, they were giving the guy who substitutes for a dollar 20, 25, 30 pesos, and that distortion is the real cost of excessive protection, which was the rule in Latin America during this period.

Dependencia Theory

INTERVIEWER: What was dependencia?

AL HARBERGER: Well, there was a kind of dependencia theory, which was very much left wing in its origins. There were some European intellectuals who fed into it, and the idea was that these poor, developing countries were so dependent on world marketplace, they were just being exploited by the center. [Raul] Prebisch talked about the center versus the periphery, which is another version of dependencia. But I think that there may be some vague notion, an element of truth behind this idea in the sense that markets are impersonal. I use the analogy of an elephant going through the jungle, and you're a poor mouse. Now the elephant is not going to go after you. He is not against you; he couldn't care less about you. He's just marching through this jungle, and if you get under his feet, wow to you! That is really the way

the market works and the way the market works for landlords when nobody rents their properties, for wheat farmers, when the price of wheat takes a tumble. I've often said to the dependency theorists that our wheat farmers in North and South Dakota are more dependent on the price of wheat than any Latin American country is on the price of any international product. Why? Because North and South Dakota are more concentrated in the production of wheat than the Latin countries are in the production of any single product.

INTERVIEWER: So just a last question about that. Isn't there a kind of paradox there, that a right-wing, deeply Catholic colonel or general could have quite a lot in common with the revolutionaries Che Guevara and Fidel Castro as far as the outside world goes?

AL HARBERGER: In some sense, populism has no political color. You have left-wing populists, communist populists, right-wing populists. Look at Buchanan in the United States; he's a right-wing populist....

INTERVIEWER: And where would Che Guevara and his countrymen be?

AL HARBERGER: He would be at the very extreme, at the left extreme of the spectrum, you know.

Prebisch's Influence on Economics, and on Teaching It

INTERVIEWER: ... What was ECLA? And tell us more about Raul Prebisch.

AL HARBERGER: Well, ECLA—I think they called it Economic Commission for Latin America, ECLA, and now it is ECLAC, which is Economic Commission for Latin America and the Caribbean—this was a place in Santiago in the early, mid-50s. I don't know exactly when it started, but ECLA's first director was Raul Prebisch, who is kind of the intellectual author of the import-substitution approach to economic development, and certainly in those early days ECLA's research staff and group of economists in general could be thought of as an army helping to implement these ideas in Latin America, helping people to go toward import substitution, higher protection.... Now today ECLAC still exists, and I certainly feel that ECLAC is a very different institution today from what ECLA was in the '50s and '60s, and ECLAC is now populated by economists who are of the modern line of thinking and who would applaud

the reforms that have taken place in Chile and Argentina and Mexico and other Latin American countries.

INTERVIEWER: Just give us an idea of how universal throughout Latin America the ideas of Prebisch and dependencia [theory were].

AL HARBERGER: Well, there are two lines here. One is the universities, and I wouldn't be surprised if even today, if you were to count all the places where economics courses are taught in Latin America, that you'll get much more dependencia-style teaching than good economics-style teaching. But the people who go to those universities don't get good jobs as economists. That is to say that it's a losing cause in that there's nothing much to do with that kind of ideological training, and I think it is getting less and less and less and less as time goes on.

What has happened is that the number of centers in Latin America which are really centers of extremely good economics training has multiplied from one, two, three, four, to maybe 20, 30, 40 at least, and these are people who are sent to our graduate schools and whose students come out in our graduate schools, competing with anybody from any part of the world.

The Emergence of the Chicago School in Chile

INTERVIEWER: Now, throughout the '50s, a lot of students were coming up from Latin America. Just tell me the story of how and why a lot of Latin American students were coming to Chicago.

AL HARBERGER: Oh, my! Well, that story began with Theodore W. Schultz, who was a very great economist, won the Nobel Prize, was president of the American Association and so on, and he, in the early '50s, was interested in economic growth and in the role, in particular, of technical assistance in bringing it about. And he had a major project entitled Technical Assistance to Latin America in which he had students—or not students, collaborators—working in the main capitals of Latin America. On a visit to Santiago, he had dinner with the then-AID [Agency for International Development] director, Albion Patterson—it wasn't called AID then, but it was the foreign aid program of the United States—and when Patterson heard Schultz

talk, he said, "This is the kind of idea that Chile needs," so to speak. And so Patterson got the idea of a university-to-university link between a Chilean university and the University of Chicago and tried to interest both the University of Chile and the Catholic University of Chile, which were the only two important universities at that time in Chile, and the Catholic University was very eager in accepting this, and we ended up having this relationship which lasted eight years altogether.... But what that thing started was another story really. I mean, we trained under that program itself around 30 Chileans, many who became later ministers and Central Bank presidents and things like that. But that set in motion a whole tradition of Chilean students coming to Chicago, so after the program stopped, they kept coming under other financial hospices—our own program, our AID, put some money into that kind of thing Meantime, we had a similar program started by the same Albion Patterson in Argentina. He shifted to Argentina and was a director there, and we started a program in Argentina, which lasted from '62 to '67, and once again, we trained about 30 under the program, and afterwards we had a continuing flow of Argentines, and by this time Mexicans, Brazilians, and so on were mingling in so that Chicago, in its heyday, had 40 to 50 Latin American graduate students out of a total stock of, say, 150 to 180, so they made up a very important part of the program. ... Now Latin American students can get in almost anywhere because they have shown how good they are, but in those days, they were viewed with such suspicion that it was lucky if you could find three or four at Harvard at any one time or five or six in MIT, when you could find 40 or 50 in Chicago. That is what gave Chicago such importance in the Latin American scene. In a sense I would say it's partly the result of our admissions policy, because we were ready to admit people and allow them to fail. We wanted to see them compete and thrive, but we were prepared to have a fallout along the way, whereas the more comfortable line that most American universities take is they admit only graduate students that are practically ready to guarantee the Ph.D. from day one, and I think that is a mistake.

INTERVIEWER: You yourself talk about 300 Latin American students and you had I think you said about 25 ministers. How many [of these students] did you teach, and how prominent have they become?

AL HARBERGER: Well, it's so hard to say. We had coming through Chicago you can figure probably 300, 400 altogether over this long span of time, and I was involved in some sense ... with the great bulk of them. I sort of took the Latin operation under my wing, and I had most

of them in my classes, and many of them did their thesis work under me or with my help, and I am really very proud that now the number of ministers is now more than 25 and still moving up, you know, and the number of Central Bank presidents is more than a dozen and still moving up, and there are so many nice things. I like to mention that at one point in time, I had these former students—two Central Bank presidents in South America, one in Chile and one in Argentina, and they were both nearing the end of their terms, and they were both then replaced by a successor, each of whom was another former student, this kind of thing, and happily, these people have been extremely responsible public servants. I think that they had, at great personal sacrifice, [worn] themselves out, so to speak, in order to implement the economic reform and bring about these major changes that we've seen in these economies, and not only the ones at the top, but I feel that the man in the street does not appreciate enough the amount of sacrifice that serious economists and other public servants do when they're engaged in these battles to change some reality that has at least outlived its usefulness. The struggles are enormous, and the strain on the individuals is tremendous, the amount of time that they devote—70, 80 hours a week, and this for years on end. They really deserve the appreciation at least of their fellow citizens.

Back to Basics: What Does the Chicago School Stand For?

INTERVIEWER: People talk about a distinctive Chicago School [of economic thought]. What does Chicago School stand for?

AL HARBERGER: Well, there are kind of two versions of this. One version is, people use the Chicago School to represent an ideology. I think that this has a certain ring truth, but basically, Chicago was not an ideological place. Milton Friedman taught for many years at Chicago, but he didn't teach *Free to Choose* [by Friedman and his wife, Rose]; he taught *A Monetary History of the United States* [also by Friedman, and Anna Jacobson Schwartz]. And the rest of us, in our classes, were not teaching ideology, or what I call the Austrian side of economics, economics as a religion, but rather economics as a science, so our vision—certainly my own vision, which I believe is shared by nearly all or all of my colleagues at Chicago—is that the forces of the market are just that: They are forces; they are like the wind and the tides; they are things that if you want to try to ignore them, you ignore them at your peril, and if you understand that they are there, working their way, if you find a way of

ordering your life that is compatible with these forces, indeed which harnesses these forces to the benefit of your society, that's the way to go.

INTERVIEWER: What was the intellectual atmosphere like in Chicago? People have told me that there's a lot of [brusqueness in the discussions], and constant [arguments].

AL HARBERGER: Well, I think the brusqueness may have had to do with the personality of our workshop system, where when somebody made a mistake, so to speak, or seemed to be making a mistake, there was no sense of tact or diplomacy to kind of paper over this. And this still carries with many of us to this day. If you're sitting in a seminar room and somebody up there is saying something which, if imbibed by your students who are sitting in that same room, it's going to lead them astray, it's up to you to call that guy right now and not later, and that I think is the sort of spirit that prevailed in the Chicago workshop system. There wasn't that much fighting in the lunches. They were pretty cordial. (laughs)

INTERVIEWER: Now, a couple of days from now, we're going to be filming at the Quadrangle Club in Chicago.

AL HARBERGER: Oh, wonderful!

INTERVIEWER: Can you just give us a sense of the atmosphere of that place, those lunches as you remember them? What will be talked about?

AL HARBERGER: Oh, goodness knows what would be talked about. My own recollection is the following: that for many, many years, we had a couple of round tables down in a lower-floor place which was the bar in the eveningtime, but this was set up as a kind of a buffet lunch kind of thing, and economists would just walk in whenever they got there and take a seat at one of these tables. One would fill up, and then they'd spill over and start another table and so on, and the economics conversation would go on and on. What was the biggest, most impressive thing about that was that actually the business school had more economists in it than the economics department, and this was a place where we had really daily interaction between the business school economists and the department economists, and that really operated, I think, to strengthen both institutions.

The Austrian School

INTERVIEWER: To me, you put it quite well. [You said] the Chicago School was in a sense very aware of the real world. Characterize it. What do you think of when you hear the phrase, the "Austrian School"? You said it's almost like a religion?

AL HARBERGER: Well, the Austrian School has its origins in philosophy at the very least. ... The notion of natural law comes in there, and the idea that derived from the first principles of proper human behavior and of natural human behavior, you can derive all the principles of market economics. That is the way that the Austrians approach this. Now, many people out there in the world don't really realize the great distinctions that exist between philosophy and mathematics on one side, which are fundamentally intellectual—they take place in your head—and science on the other. The notions of science are, you're attempting to understand and explain reality, and so your theories are supposed to give rise to hypotheses that can confront reality to see how well they can explain or be refuted by reality. It's this branch that really characterized Chicago all these years and distinguished it from the Austrian School.

INTERVIEWER: So let me get this right: It's almost like the Austrian [School of thought is] almost like ... a scientific hypothesis?

AL HARBERGER: Right.

INTERVIEWER: Does that mean that when Hayek was in Chicago, he was a bit like a fish out of water?

AL HARBERGER: Oh, I don't know. I mean, Hayek was always a friend of many around Chicago, but he didn't mingle with the department, and in his way of teaching ... [he] ventured farther from economics into philosophy and politics and other things than most of the others that I knew and knew of, and so when he was teaching in the Committee on Social Thought, located one floor above us, he was really more linked with philosophy and political science than he was with economics.

INTERVIEWER: You said the Austrian School was more like a religion.

AL HARBERGER: Well, I'll tell you that if a person like myself is giving a long, two-hour seminar, and there are a bunch of faithful Austrians in the audience and I happen to deviate from something that derives from these first principles, maybe just giving a side remark doesn't matter, but they will come and pounce on me after this. They'd say, "How could you dare do such a thing? How could you support evil?," or...

INTERVIEWER: Socialism.

AL HARBERGER: I beg your pardon?

INTERVIEWER: Socialism.

AL HARBERGER: Or socialism. (laughs) ... It's as if there is a very pretty but highly complex picture out there, which is perfectly harmonious within itself, you see, and if there's a speck where it isn't supposed to be, well, that's just awful for the Austrians. Well, us guys who live looking at the real world, which is always a mess, you see, and nothing ever fits perfectly, so for us, it's kind of a different world.

INTERVIEWER: ... But in what way is it like a religion?

AL HARBERGER: Well, the notion in the sense that this picture is derived from the first principles of natural law, the nature of man ... and then you just follow logically, logically, logically, like Aristotle, down to this very complex vision of reality, which has its own internal architecture and beauty, you see, and it is a flaw that mars that beauty that these guys always react against.

The Allende Years

INTERVIEWER: Tell me a bit about Chile.... Allende gets elected....

AL HARBERGER: Well, Allende was a person who had run for president a few times before, and he was a politician of the Socialist Party, and he ran as the candidate of a left-wing coalition. Many people were surprised at the degree to which his policies, once in power, were policies that might have been explainable if he'd had a 65 percent majority, but they did not fit at all,

with a 38 percent vote of his faith for being just a little bit more numerous than the next guy's.... What happened during that time was a huge move toward socialization of the economy. There were many actual expropriations of enterprises, including the major mines, but in addition to that, there was a thing that they call intervention, which is a little bit like what we have as receivership for a bankrupt firm [where] the court appoints a person to run the firm and it isn't the owner. Well, in the Allende system, you could do that on any firm, whether it was bankrupt or not. (laughs) And by the time the Allende period was halfway through, about 90 to 95 percent of the main Chilean industrial sector had been either nationalized or intervened.

INTERVIEWER: ... And what was happening to the huge inflation?

AL HARBERGER: All the things got way out of hand. I don't know how things would have been if the Allende government had had decent economic advice, but they did kind of silly things. They put controls on all the prices while mounting a monetary policy that led to enormous inflationary forces. There was a point in time when there were 13, I believe, official exchange rates to the dollar. The cheapest dollar was 25 escudos, and the most expensive official dollar was 1,300 escudos, but the black market was like 1,800 at that time. You see, it was just a crazy world. The black-market prices of goods, which are usually quoted about a 20 percent premium or a 10 percent premium over the official price, they never talked that way, six times the official price, seven times, 10 times, five times. That's how it worked, and so the market was just out of function, you see. It was not working at all.

INTERVIEWER: So one other question: The CIA intervened, particularly with the [strikes]... Would you say that the economy was sabotaged by the U.S.?

AL HARBERGER: The U.S. was on that side, [and] I don't think there can be any doubt that the majority of Chileans were on that side at that moment in time. ... The Christian Democratic Party, which is now a member of the opposition coalition, was very strong on the side, favoring the military coup at the time the military coup took place.

"The Brick" and Pinochet

INTERVIEWER: What was *El Ladrillo*?

AL HARBERGER: *El Ladrillo*—this is an interesting thing. *El Ladrillo* means "The Brick," and in the 1970 elections, the candidate of the left was Salvador Allende, and the Christian Democratic candidate was Radomiro Tomic. Radomiro Tomic came from the left wing of the Christian Democratic Party and was by I think almost everybody's agreement, even at the time, not really the best candidate for them to put forward, but Eduardo Frei had made a deal that he would be the candidate in 1964 and then Radomiro would be the candidate in 1970, and Don Eduardo did not want to go back on his word, [so] Radomiro was the candidate. Well, it was possible that had a more ... right-wing member of the Christian Democrats been the candidate that there wouldn't have been a third right-wing candidate, but with Tomic being a candidate, there was a late candidacy of Jorge Alessandri, and he had been president before. He couldn't succeed himself but could run for a later term. That's what happened, and as this late candidacy got started, they needed an economic platform, and a bunch of young economists, most of whom, not all, from Chicago, got together and put together a very interesting reformist platform, forward-looking, very modern. And this was developed and sent to Alessandri. But the old politicians of the party, maybe Alessandri himself, it was too radical for them, too free market, too nontraditional, so they deviated quickly from this recommended policy. But this small group stayed together through the Alessandri years, and they used to meet I think every Tuesday for lunch, something like that, and they would write papers, and they would keep kind of a running document in typescript which said how they would reform this economy, how this economy has to be reformed, what is to be done to get out of the swamp that they were putting themselves in. So at the moment when the military coup took place, the only people who had a serious blueprint of how to get out of this were this group known as the Chicago Boys, even though all did not come from Chicago, and the little bible of the group was *El Ladrillo*, which has since been reprinted by the Center for Public Studies in Santiago.

INTERVIEWER: Why was [it called "The Brick"]?

AL HARBERGER: Oh, goodness knows. It was kind of thick and heavy. (laughs) No deeper reason than that.

INTERVIEWER: So what happened to *El Ladrillo*? What about Pinochet's policy...?

AL HARBERGER: Well, the story was this. When the military took over the government, every ministry but one was occupied by a military person and their "technopols," including the Chicago Boys. Many of them were at lower levels, like undersecretary, but not in the top level. In these lower levels, these guys managed to get rid of the price controls almost totally, to greatly liberalize trade, to unify this crazy exchange rate. Many good things happened in that period, but one thing that certainly didn't happen was the control of inflation. Now here you have to go back to the intervention and nationalization of so many industries.

The people who ran them—I call them commissars (laughs)—these commissars, sometimes they'd come in and they'd double wages the first day to make themselves popular with the work groups, and the prices were under price control. How can they ever make money? Do you know what I mean? So what do they do? They lost money in a hemorrhage. And how did they get their deficits covered? Well, they knew some other guy who was the interventor of a bank, and they'd lean on him to get the money, so that's how that worked.

Well, then the military came, and the commissars went away, and the colonels came. Well, they inherited exactly the same ongoing industries, and they were not businessmen, and they continued with these same deficits, and instead of leaning on a commissar, they leaned on another colonel who had been the interventor of a bank, and so, after a year, year and a half of military government, you still had 20 percent per month built-in inflation that wouldn't go away until something structurally changed.

Somewhere around that time, around May of 1975, the military caved in and said, "Look, we can't run this show," and so they backed away, and all the major posts now went to technopols, and Jorge Cauas, who was a Columbia graduate, was the first super minister. He was in a couple of years superseded by Sergio de Castro, who was one of the Chicago Boys and the leader of the Chicago Boys, and that's the period when the takeoff of the Chilean economy really began and major reforms were made.

Milton Friedman in Chile

INTERVIEWER: Tell me about that time Milton Friedman made his famous visit to Chile?

AL HARBERGER: Oh, Milton Friedman's visit took place in March, I believe, of 1975, and his judgment about the economy was not in any sense unique. I mean, it was what any good economist, looking at the Chilean economy at that time and seeing that kind of a mess, would say. But I think that Milton's presence probably helped to maybe stiffen the spine of people who were trying to insist on better economic policies. Maybe his remarks convinced some people that would otherwise not be convinced that this kind of change was needed.

INTERVIEWER: You make it sound like a fairly obvious change, yet I think the term "shock therapy" came into use as the result of the change that the Chileans made.

AL HARBERGER: Well, I have my doubts about [that]. There definitely was a fiscal shock; that is to say what was clear was that these deficits were leading to printing up a huge amount of money, and as long as that continued the inflation was going to continue, and you weren't going to get out of it. So one went from fiscal imbalance to fiscal balance within a year or so, but the overall picture of the economy, the inflation went down like from 400 percent one year to 300 percent the next to 200 percent the next. By then it was like 400 percent in 1974-'75, and it got down under 100 percent, I think for the first time, by '78 or '79, and it got down to 10 percent only in '81. ... [There also] was a recession of the economy in 1975, which was the product of three factors: the fiscal shock, a world recession and a very low price. If you spread the blame among those three factors, I think that's fair.

INTERVIEWER: Of course Milton Friedman especially then became a kind of a kind of hated figure, didn't he? There were demonstrations...

AL HARBERGER: Well, not abroad. (laughs) Let us say when he came back to the United States and when he went to Europe, [there were] things like that, yes.

INTERVIEWER: Why do you think people [hated] him?

AL HARBERGER: Well, it's a hard story there. The left wing of the world loved Allende. Allende was the first socialist elected in a Latin American country as I remember, that actually took office anyway, and he was the darling more of the European left than the American left, but we always in the United States had what we call radical student groups like SDS [Students for

a Democratic Society] who took their cues from the European left, so these are the people for whom Milton Friedman then became a figure of hate. They organized demonstrations against him wherever he went, and this went on for a period of years, and I see nothing that he did to deserve that. (laughs) And he [faced it] with such courage and such strength of character, I marvel to this day at the way he took that.

INTERVIEWER: But going back to those demonstrators, still [there's a sort of] question on Milton Friedman, because of this association. I'm not saying that it's right or wrong, but just why do you think their people are so horrified?

AL HARBERGER: Well, as I say, I think that the whole response picture to Chile has to be linked to somebody loving Allende and somebody being terribly disappointed when Allende was put out of office. Now I think if you look at human rights violations or political violations, you will find them in any Asian country almost at that time, in multiples of whatever was happening in Chile and in Latin America. You would find many other countries in which the same sort of thing was happening and was not getting that treatment, so my question, and the reason for my answer in connection with Allende, is... Allende is what distinguishes the Chilean case from all these others. I mean, Milton Friedman went to Chile for one week. You can take the top 100 economists in the country of that time, and probably 85 of them had been working seriously in places like Korea, Taiwan, Pakistan, Bolivia, Paraguay—you name it—and were not getting any demonstrations.

INTERVIEWER: One of the points Friedman was making was that these kind of free-market policies ultimately lead to a freer political system. In other words, was he sort of suggesting that the free-market policies would ultimately undermine Pinochet's [regime]?

AL HARBERGER: Oh, I think he always said that. He said that that you cannot have a repressive government for long within a genuinely free economic system and that the freedom is going to have to pass over to the political side, and that of course, is exactly what did happen in Chile. The evolution took quite a number of years to make, but it happened, and in that sense, Chile is an example of a peaceful transition from [authoritarianism] to a civilian democratic government.

Chile and Regulation

INTERVIEWER: [Chile's peaceful transition from authoritarianism to democracy was] possibly because of free democratic policy, you'd say?

AL HARBERGER: Well, it's hard to say that, but the political transition was built into a constitution which was submitted in, I believe, 1980 or '81; I think it was '80. According to this constitution, it guaranteed another eight or nine years for Pinochet, and that was one of the things that many people objected to. At the same time, I don't think it is true that the majority of Chileans were against that constitution. The constitution was a return from a more arbitrary, unconstrained, or—I don't know how to put it—not institutionalized governmental setup to one where the new constitution had been drafted by a very distinguished commission of former presidents and former Supreme Court justices and stuff like that.

INTERVIEWER: You spent some time in Chile. In my view... Well, I'm asking you if it's true or not [that the majority of Chileans were in support of the constitution]....

AL HARBERGER: Well, I don't know. Some people might mention Hong Kong, and there have been other places, you know, in varying degrees, but I think what happened was that Chile I think is the first place where coming out of a big collectivist mess, a coherent set of actions were taken that derived from a vision of how the economy works and what is the role of the state in the economy and so on [and] that was successfully implemented and with, I would say, great success.

The Chilean Miracle

INTERVIEWER: You talked earlier on about the Miracle of Chile?

AL HARBERGER: Yes. Well, I think that there are two elements here. One is that all of Latin America, or nearly all, was beset by the so-called debt crisis of the 1980s. This started with the oil boom, oil price boom of 1979-'80, when oil got to \$40 a barrel, and these petrol dollars, people call them, these petrol dollars went to all the oil-producing countries. And the sheikhdoms, in particular Saudi Arabia, those guys, they didn't know what to do with this money, so they dumped it in the international banks, so here were the international banks with billions of dollars and nowhere to earn interest on it. They discovered Latin America,

which had been moving in this free-market direction, and Latin America became their darling. Bankers were coming down, occupying all the hotel rooms in Santiago, Buenos Aires, Rio, and so on and shoving this money down the throats, almost, of the Latin American private sector [and] in some cases of government. The Chilean government didn't borrow much, but the private sector was the one where Chile's step got big. Well, then, all of a sudden, as the country was getting used to an inflow of capital... In Chile's case, 8.15 percent of GDP flowed in in the one year, 1981, and that dropped by a full 10 points by 1982, and that swing—it didn't even go to an outflow; it went from a big inflow to a small inflow—was enough to throw the economy into a huge recession, and all these countries were in this huge recession. The Chilean one was maybe deeper than the others for reasons of it having a large amount of debt to begin with and of again, this problem coinciding with a copper bust, but anyway, Chile led the continent in climbing out of this recession. It was the only debt-crisis country that got back to the pre- crisis levels of GDP before the end of the decade of the '80s, so for most of the countries, it was the full decade that they called the "lost decade"; in Chile, it was the better part of it that was lost. But they were the first to come out. They came out growing at 5, 6 percent per year, and long after, you see, you can say, well, when you're in a recovery period, you're recovering lost ground, [and] it's reasonable to think you'll do that fast, but after you've recovered the lost ground and you're going on, if you continue on the same or even increasing trajectory, that's even more of a miracle. And that is all part of the Chilean picture.

The other part is that the last half of this episode, from 1990 onwards, it was in totally opposite governmental hands, that the Chileans, Chile's free elections put the so-called Concertación [coalition party] in power in 1990, and since then, it has been the Concertación that has governed Chile. We are now in the third [Concertación] presidency. We had [Patricio] Aylwin; we had [Eduardo] Frei; and now we have [Ricardo] Lagos in Chile, all of them people who come from the opposition to the military government, yet the economic policies have remained basically the same, have been, I think, in some degrees, well, certainly carried forward, and in places where there were still things to be done, there had been steps taken in that direction, some people would say maybe not fast enough, but nonetheless enough to say that the big issues of economic policy are not partisan issues in Chile anymore. It is an open economy with low tariffs, without price controls, with plenty of reliance on the market, with

building financial connections with the rest of the world. All this is matter of consensus in Chile, and I still find it a marvel to behold.

The Barbers of Chile: Price Stabilization and Hyperinflation

INTERVIEWER: You spoke of a lovely image, the barbers listening to the radio. Why don't you tell that story now?

AL HARBERGER: Well, we're talking here about what stabilization can be like in a country that has really huge inflation. Many people know that when you're trying to calm down an ordinary inflation, it's hard on the people, and it usually produces unemployment and recession and lots of complaints. There's some silver lining in the inflationary cloud, however, when the inflation gets really, really bad, because when it gets up to 20, 30, 40, 50 percent per month, nobody is thinking in pesos. The barber sets the price of the haircut in dollars—\$3 a haircut—and then when a client comes in, and he says, "How much do I owe you for the haircut?," the barber listens to the radio and finds out the current quote of the dollar, and he translates from his \$3 haircut into pesos what he has to be paid for the haircut.

Well, in Bolivia, before the stabilization, in Argentina, before its great stabilization 1990, in Brazil before its great stabilization later yet, this is the way people were going. They were thinking in dollars; the prices were fixed in dollars. And then, all of a sudden, the exchange rate stabilizes, and guess what? The price level in pesos stabilizes automatically, and that rapid decompression, so to speak, of the inflationary spiral, that is something that is unique to these periods of some call it almost hyperinflation.