



Overcoming The “Middle-Income Trap”: Chile Case Study

Superando la “Trampa del ingreso medio”: El caso de Chile

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Abstract

The following article looks into the concept of the middle-income trap. First it focuses in Latin America as the region is home to several cases of said phenomenon and demonstrates the different struggles various nations go through to overcome it. It also analyses what other regions, like Asia Pacific, have done to deal with middle income. Afterwards it concentrates in Chile to analyze how it has dealt with the middle-income trap. Concludes that while Chile has gone a long way to progress and reach very high levels of income, there are still several aspects in their economy must change in order to fully escape the problems that coincide with the aforementioned phenomenon.

Keywords

Chile, Latin America, Asia Pacific, middle-income trap, economic policies.

Resumen

El presente artículo analiza el concepto de la trampa del ingreso medio. Primero se enfoca en América Latina, ya que la región alberga varios casos de dicho fenómeno, y demuestra las diferentes luchas que atraviesan varias naciones para superarlo. También se analiza la manera en que otras regiones, como Asia Pacífico, han tratado el ingreso medio. Luego, el artículo se enfoca en Chile y analiza el comportamiento de este fenómeno en el país austral, para concluir que si bien Chile ha recorrido un largo camino para progresar y alcanzar niveles altos de ingreso, aún hay varios aspectos que su economía debe cambiar para poder escapar a la problemática que implica la trampa del ingreso medio.

Palabras clave

Chile, América Latina, Asia Pacific, trampa del ingreso medio, políticas económicas

Introduction

The commodity boom that started in the first years of this millennium, made most Latin American economies dependent on commodity exports at high-income levels borders. Promising policies targeted at increasing the overall welfare across the region were possible due to increased government revenues during the boom. As commodity exports started to show a decline and as terms of trade deprived for virtually all nations in Latin America, countries in the region encountered stronger incentives to undertake structural reforms (Loman, 2015).

This article aims at outlining a blueprint for action, abstracting relevant measures for the case of Chile, one out of only two Latin American economies that have been able to overcome the so-called middle-income trap. By critically assessing public policy decisions that the Chilean government has undergone short before, but especially after its return to democracy, it aims at shedding light to the importance of investing in innovation, research and development, in order for a country to sustain economic growth that allows an increased social welfare.

Currently, Latin American countries score poorly in infrastructure, education and competitiveness. Furthermore, evidence shows that the level of technological complexity often related to the investment in research and development sharply declined during the years of the boom (IBID). During that period of time, policymakers comfortably spent money without targeting investment to long-term strategies that would allow for an increase in welfare that could be sustained over time.

Latin America remains being the most unequal region in the world and the reversed trend in growth of income evidences a need for structural reforms. The Chilean experience in overcoming the middle-income trap and its attempts to improve social conditions can prove to be useful for other countries in the region replicating those measures, some of which have been resembled already as it is the case of exports promotion. This article includes an analysis of the weaker points of the Chilean model, backed with recent literature about the topic, the current state of economic indicators, and the valuable input of Christian Fresard, former representative of Chile in the WTO and director of the Latin American division of the Chilean Exports Promotion Agency.

Income levels across the region

The World Bank categorizes countries according to their income levels in 4 different categories: low-income, lower middle-income, upper middle-income and high-income economies. For the current 2018 fiscal year, the categories are defined as summarized in table 1.

Table 1. Income categories

Value (min)	Value (max)	Category
\$-	\$ 1.005	Low-income
\$ 1.006	\$ 3.955	Lower middle-income
\$ 3.956	\$ 12.235	Upper middle-income
\$ 12.236	\$ 99.999	High-income

Source: World Bank Data Help Desk, 2018.

Income levels in Latin America are as diverse as the countries that are part of the region. Measured in terms of gross national income per capita calculated with the World Bank Atlas method (2016), income levels in the region range from USD \$780 – in Haiti (a low-income economy), to USD \$15.230 – in Uruguay (a high-income economy). According to data from the United Nations Economic Commission for Latin America (UNECLA) the region is the world's most unequal one: inequalities are to be found not only within countries, but also between them as evidenced by Table 2 (Bárcena & Byanyima, 2016). Table 2 shows how Latin American countries are classified according to income levels and presents them ordered by population.

Table 2: Classification of Latin American Economies according to income levels

Country	Income Level - GNI per capita, Atlas method (current US\$)	Category
Brazil	\$ 8.840,00	Upper middle-income
Mexico	\$ 9.040,00	Upper middle-income
Colombia	\$ 6.310,00	Upper middle-income
Argentina	\$ 11.970,00	Upper middle-income
Peru	\$ 5.950,00	Upper middle-income
Venezuela*	\$ 11.760,00	Upper middle-income
Chile	\$ 13.540,00	High-income
Ecuador	\$ 5.800,00	Upper middle-income
Guatemala	\$ 3.790,00	Lower middle-income
Cuba*	\$ 6.570,00	Upper middle-income
Haiti	\$ 780,00	Low-income
Bolivia	\$ 3.070,00	Lower middle-income
Dominican Republic	\$ 6.390,00	Upper middle-income
Honduras	\$ 2.150,00	Lower middle-income
Paraguay	\$ 4.060,00	Upper middle-income
Nicaragua	\$ 2.100,00	Lower middle-income
El Salvador	\$ 3.920,00	Lower middle-income
Costa Rica	\$ 10.840,00	Upper middle-income
Panama	\$ 12.140,00	Upper middle-income
Uruguay	\$ 15.230,00	High-income

Table 2: World Bank Open Data, 2018.

It is noticeable that 17 out of 20 economies in the region belong to the categories of lower middle-income and upper-middle income. In short, 85% of Latin American countries are middle-income economies. Haiti is the sole country in Latin America that remains being classified as a low-income economy. The remaining two, Chile and Uruguay, belong to the category high-income. Critics are vocal about the inaccuracy of this kind of classifications in effectively reflecting the economic realities of the countries subject to analysis.

When analyzing the categories, it is important to be aware about the implications of such classifications. The fact that the majority of Latin American countries belong to the category of middle-income economies tells little about the class structures within the countries and the disparities in income distribution that still pose a huge challenge for governments across the region. For that aim, the Gini Index is a more adequate measure. As coined by the Glossary of statistical terms of the Organization for Economic Development and Cooperation (OECD), "the Gini index measures the extent to which the

wealthier economies on capital-intensive products with limited resources available to invest in innovation. That is an economic nightmare.

The challenges of the middle-income trap have been long identified by economists and ways to overcome it include (1) targeting investments to key areas relevant for economic development and (2) building strong institutions. Regarding the (1) aspect, investments should be targeted at education that allows for higher-skilled individuals to join the working-age population, at improving infrastructure and communications, and at increasing research and development (R&D) that fosters innovations. Those were generally included in the strategies pursued by the developmental states of East Asia, leading macroeconomic planning activities. Japan, Singapore, South Korea and Taiwan followed such postulates and were able to overcome the middle-income trap.

Subsidies, export promotions, low-interest and condonable credits directed towards key industries or industries of national importance together with the argument of protecting infant industries were also some of the strategies pursued by East Asian economies. The former president and dictator of South Korea - Park Chun-hee's said, "In order for a country not to fall, it must cultivate its own strength". This is one of his most famous quotes (Shin, 2006). Those measures were directed exactly at doing so. In addition to that and regarding the (2) aspect, those measures were successful thanks to the transparent and strong institutions that directed the resources to key areas enabling and supporting economic development.

Recent literature has proved that Latin America not only lacks such institutions, but that there are no demands for those in the region's society (Doner & Schneider, 2016). Subsidies can prove to increase competitiveness. Nevertheless, without a strong institutional framework that prevents corruption, subsidies are likely to be unfairly distributed, increasing inequalities and not benefiting the economy as a whole.

An example of that is "Agro Ingreso Seguro": a government program that was implemented during the mandate of Álvaro Uribe Vélez in Colombia in order to provide subsidies to farmers that allowed them to improve their productivity to better face the process of internationalization. On September 7th 2009, Cambio magazine denounced that 72.500 million Colombian pesos (around 30 million US dollars at that time) that were originally intended to strengthen the Colombian peasantry had been handed over to 100 traditionally wealthy families in the regions of Magdalena and Valle del Cauca.

The idea of subsidizing agricultural production in order to increase competitiveness in the international level is a widespread protectionist practice to be found even in more developed European and North American countries. Those subsidies did not work in Colombia due to a lack of transparent and strong institutions that foster honesty. Little was done after the scandal in order to start a much needed land reform: one of the structural causes of inequality not only in Colombia but also across the region.

The East Asian developmental states conducted similar macroeconomic policies to those implemented following the Import Substitution Industrialization model (ISI). The model as it stands is a way for developing markets to look into self-sufficiency and not need to depend on developed nations. "It aimed at strengthening the domestic production of those goods that were previously imported. A (...) state-led model of development and thus reflects internal decision-making processes" (Neumann, 2013: 1).

distribution of income among individuals or households within an economy deviates from a perfectly equal distribution” (OECD, 2018).

According to the Gini Index, 0 represents perfect equality while an index of 100 represents perfect inequality. Using estimates from the World Bank, by 2015 the average Gini index in Latin America reached levels over 50, indicating deep inequalities. It is important to say that around 1/3 of the data was missing when the calculation was done but it certainly sheds light to the widespread phenomenon of income inequalities in the region. Having clarified that a country being classified as middle-income has little to nothing to do with the size of its middle class and in spite of being the most unequal region in the world, the middle class in Latin America has experienced tremendous growth during past years.

In various countries in the region, more than 50 million people became members of the middle class in the decade between 2002 and 2012. That number represents an increase of around 50% of the middle class (Ferreira et al., 2012). According to a report published by the World Bank, Latin America’s middle class has hit a record high of historic relevance. One third of Latin American families are now considered to be middle class, pegged with an equivalent reduction in the proportion of the region’s share of the poor (World Bank Group, 2012). The latter implies that Latin Americans are moving up the income ladder, even in the aftermath of the economic and financial crisis of 2008-2009.

The aforementioned facts appear promising for the region and might imply there is a correlation between the increasing size of the middle class and the fact that most of the economies in Latin America managed to make the move from low-income to middle-income. Nevertheless, a correlation is not the same as causation. In fact, 85% of the countries in the region might be heading to an economic “trap” and the increase in the size of their middle classes might be masking the need for deeper economic reforms that tackle economic inequalities from their roots.

The middle-income trap

Of 101 countries that were classified as middle-income economies in the 1960s, only 13 of them managed to trespass the threshold and become high-income economies almost 50 years later (Agénor, Canuto, & Jelenic, 2012). Most of those countries were dynamic Asian economies including South Korea and Singapore. Only two Latin American countries made it to the list: Chile and Uruguay. The rest are stuck in the middle-income category, and some of them even for decades now.

The middle-income trap is a concept widely used by “developmental economists to describe a newly industrializing economy that reaches a mean income threshold usually about USD \$11.000 (...) which begins to compromise the economy’s competitive advantages in low-wage manufacturing” (Shambaugh, 2016). In the region, and as evidenced by Table 2, at least 6 countries are bordering the threshold: Argentina, Panama, Venezuela, Costa Rica, Mexico and Brazil. What follows is a shift in the labor market: a phenomenon tied with the “Lewis Turning Point”. The turning point describes a phenomenon where cheap labor (mostly originating from rural migration to urban centers) begins to exhaust, pushing wages up.

According to Taylor (2017), “many of Latin America’s largest economies are stuck in the so-called middle-income trap”. When wages go up, productivity growth slows down. Countries with middle-income economies cannot compete with low-income economies on labor-intensive products requiring large quantities of unskilled labor. In addition to that, they cannot compete with

Those measures did not work in Latin America due to a clear lack of an appropriate institutional framework. States in the region were setting the wrong priorities, deepening income inequalities and structural poverty. The implementation of the ISI model did not increase competitiveness across the region; it unfairly directed resources to historically privileged groups with strong lobbying capacity and fostered an inefficient allocation of resources together with a widespread corruption. During that time, short-term measures were preferred over long-term reforms that could actively shape the path of overcoming the middle-income trap.

The ISI model was replaced in the region with the so-called Washington Consensus rooted in the ideas of free market and trade liberalization. Latin American economies perceived a shock after opening to international trade, with inefficient industries and poorly allocated factors of production that configured an atmosphere where competitiveness was nowhere to be seen. What those countries did essentially, was “Kicking away the ladder” of economic development. Quoting Chang (2002): “Almost all of today's rich countries used tariff protection and subsidies to develop their industries. Interestingly, Britain and the USA, the two countries that are supposed to have reached the summit of the world economy through their free-market, free-trade policy, are actually the ones that had most aggressively used protection and subsidies.”

Blindly trusting the markets to determine prices is increase dependency of Latin American countries to commodity exports (intensive in low-skilled labor), worsening terms of trade and making them vulnerable to market prices fluctuations. In short: it would make Latin American countries unable to overcome the middle-income trap. Demonizing macroeconomic policies that are protectionist in nature just because of the sake that they are protectionist is not going to help countries increase their competitiveness in industries of national relevance that allow for a cultivation of a country's own strength.

Taylor (2017) connects the arguments of Doner & Schneider (2016) with the reality of large Latin American middle-income economies such as Brazil, Mexico, Colombia and Peru. A lot of different indicators show how far Latin American countries are from taking measures in line with the ways of overcoming the trap.

In summary:

1. Regarding investment in research and development: “Latin American countries have less than ¼ of high-skilled workers in the field of R&D in comparison to high-income Asian countries (...) R&D spending is less than ¼ of their richer peers.”

2. Regarding investment in education: “The share of the labor force that has higher education is less than 60 percent that of the wealthy countries (...) Latin middle-income countries' scores on PISA educational attainment tests are over 1/5 lower than their wealthy peers (...) Informal employment is above 50 percent on average (...) The shadow economy has been growing, rather than shrinking.”

It is not a secret either that investment in infrastructure and connectivity is way behind in Latin America. Taking a glance at the logistics performance index of East Asian economies and comparing them to Latin American ones can easily prove that. Some remarks by the OECD Secretary-General Angel Gurría during the Annual Meeting of the World Economic Forum in Davos during a private session titled Prioritizing Policy for Inclusive Productivity included that the middle-income trap in Latin America “(...) Is traced to the inability of countries to undergo a process of structural change towards innovation and more knowledge-intensive production” (Gurría, 2017).

Paus (2014) distinguishes between two different approaches to the middle-income trap after extensively reviewing literature on the unprecedented challenge of overcoming it. The first approach has a focus on “the lack of structural change, the driving forces behind it and the national and global context in which it unfolds”. The other approach “stresses growth slowdowns irrespective of time and place”. The author favors the structural change approach and concludes that the experience of latecomer countries trying to overcome the middle-income trap such as Chile, Dominican Republic, Jordan, Ireland, and Singapore “suggest that a cohesive productive capabilities-focused development strategy holds out great promise for generating growth-enhancing structural change.” Again, just leaving Latin American economies vulnerable to the (not so) “free market” is not likely allow for a transition from middle-income to high-income.



Chile overcoming middle income: a case of study

Chile has had a unique experience in becoming a high-income country. It currently ranks as the 33rd most competitive country in the world⁴, while Brazil and Argentina rank 80th and 92nd respectively, being the most competitive country in South America and one of the most within the American continent. The realities of this growth are primarily thanks to political reforms that have allowed not only connecting with the global market on an important scale, but also promoting Chilean exports and establishing mechanisms to counter the effects of economic crisis, especially those faced back in 2008. Chile has been able to sustain growth through internal structures.

⁴ This ranking is based off of the World Economic Forum's The Global Competitiveness Report 2017-2018.

“(…) Chile's economy has proved resilient and entered the crisis with a fundamentally strong position. This owes much to its sound policy framework, including an inflation- targeting regime, a flexible exchange rate, and a prudent

budget rule. Large fiscal savings accumulated in past years have been critical to preserving macroeconomic stability and covering financial needs, while the banking system remains well capitalized. The policy response has also played an important role in buffering the impact of the crisis. The government's bank liquidity support and economic stimulus measures have been sizable, well balanced, and coordinated" (Chile, 2017: 117).

This case study analyses how Chile managed to achieve high-income within a context of many middle-income countries yet look to see if they have been able to avoid the infamous "middle income trap" in doing so. It will show that through policy reform a country can be able to aspire to develop at a standard that both benefits their economy and their social structures.

Commodity economy?

One of the first aspects that spark interest into viewing Chile's story is to look at what its GDP is made up of. While the notion of high-income countries is that of being able to diversify their exports to avoid commodity dependence, literature often asserts that the Chilean economy still depends heavily on one commodity as copper. "The country is over dependent on copper exports, which account for 50% of its total exports. According to the Chilean Copper Commission, copper exports declined from USD 43.6 billion in 2011 to USD 26.1 billion in 2016. A further fall in prices would negatively affect government budgets and its planned spending program" (Chile, 2017: page 25). This is very interesting to elaborate into how Chile has managed to become a high-income country.

The Observatory for Economic Complexity ranked in 2016 the most important exports Chile had during that year. They provided the following list: Refined Copper (USD 14.9B); Copper Ore (USD 13.7B); Sulfate Chemical Woodpulp (USD 2.64B); Raw Copper (USD 2.35B); Fish Fillets (USD 2.12B); Refined Petroleum (USD 3.6B); Cars (USD 3.28B); Crude Petroleum (USD 2.45B); Delivery Trucks (USD 1.71B); Broadcasting Equipment (USD 1.56B) (OEC database, 2018).

Christian Fresard is former representative of the Chilean government in the World Trade Organization and Director for Latin America of ProChile (Chile's Export Promotions Agency). In an interview, Fresard defended the fact copper and other natural resources are important in the share of Chilean exports, but there are other very important sectors in the economy such as tourism, which do not depend on the extraction of natural resources. There are also industries based on natural resources, such as the wine sector, but their economic contribution lies in the added value that is given to the product in addition to the sustainable management that is given to the resources.

Taking an isolated glance at exports provides for a wrongful interpretation of the economy's composition: The mistake most scholars do. As of today, the Chilean economy is far from being an economy that is dependent on the extraction of natural resources. GDP composition data by 2016 gathered by the World Development Indicators databank showed that agriculture accounted for 4% of the economy's output, industry for 31%, manufacturing for 12% and services for 64%. Ever since 2005, the structure of economic output has been migrating from industry and manufacturing to services: Chile's strongest economic sector today. The latter goes in line with Fresard's argument and his example of tourism as a pillar of the services share of the GDP.

The OEC lists the major recipients of Chilean exports, which are, in order of importance: China, the USA, Japan, South Korea, and Brazil, all of which are relevant copper markets. There is no doubt that copper is still an important

part not only of exports, but also of the Chilean's government revenue, with at least 20% of it originating in copper exports. Nevertheless, exports do not provide the entire picture of economic composition and performance.

Analyzing exports, it can be contested that Chile is dependent on raw materials. Grouping the Chilean exports in categories, we see that the first sector continues being copper, followed by automobiles, fish fillets and electronics. Copper and copper derivatives have, as explored above, a disproportional share of exports, and that leads people to think that the country's economy is dependent on the sourcing of those commodities: Copper (USD 30.95 B); Automobiles (USD 4.99 B); Petroleum (USD 3.6 B); Wood pulp (USD 2.64 B); Fish (USD 2.12 B); Electronics (USD 1.56 B).

Nevertheless, in the category copper and derivatives, around 50% of exports have added value, with refined copper products topping the category. The fact that copper has a disproportionate share in the country's exports might not be problematic and shows a mature economy where the management of resources is, in line with Fresard's assessment, sustainable. "To the extent that being a high-income country is determined by GNI per capita, it is naturally an economic result. There are many differences between the ways to reach this result". Fresard explained that that is the reason why other variables have been incorporated to try to improve the measurements of economic development and wellness of countries like indicators of happiness of societies. Poverty and inequality remain being a challenge in most high-income countries and developed societies such as the United States.

Comparatively, Chile still is one of the most unequal countries within the OECD rankings, coming up at 0.46 within the GINI score as of 2014 (OECD, 2016) and currently second to last ahead of Mexico. Regionally speaking, Chile is also one of the most unequal countries in South America, just surpassed by Paraguay, Colombia, Brazil and Suriname. So, although income per capita is high, many other elements of Chile prove it still is not too far off from indicators other than income per capita when compared to other regional economies, sharing some characteristics with them.

Reflections on history and policies

Many scholars explain Chile's economic growth as stemming from the adoption of neoliberal economic policies and the opening of its economy. To this, Fresard said that it remains a controversial issue. There are authors who would respond affirmatively, but others point out that the adoption of "Keynesian" policies helped to have a sustained growth. In addition, the political stability that Chile has had after the return to democracy in 1990 has been an important element to support the rapid economic growth.

At least partly, market-friendly government policies used to encourage trade and economic openness granted Chile's success. Some of those policies were implemented towards the end of the Pinochet dictatorship but found its peak after Chile's return to democracy. Political and economic stability, countercyclical fiscal policy, a perceptive government during good times willing to increase spending in bad periods, economic and commercial openness, and investments in infrastructure and education are all factors that played a role in what has been called "Latin America's economic miracle". All of the above has allowed the Chilean government to benefit from the commodities boom of the past two decades while adequately facing international crises.

The first step of Chilean reforms and policies leaned in from opening the country to global trade. The mentality of many Chileans was to be incorporated into the global economy and to learn how to incorporate global trends as local habits. Tariff reductions as well as trading off flat trade rates with the

use of an impeccable commercial diplomacy are examples of that. “Both the reduction in the tariff and the transparency gained from a flat system were fundamental to achieving the competitiveness that the Chilean companies needed to compete worldwide” (Büchi, 2006: 4).

Another early step involved a policy shift influencing the levels of privatization of national- relevant industries in the country:

In fact, important sectors such as electricity generation, distribution and telecommunications were still managed by state companies. After we implemented a massive privatization plan that included more than 50,000 new direct shareholders and several million indirect (through pension funds) shareholders. Private entrepreneurs that carried out important expansion plans managed these companies (Büchi, 2006: 7).

From there on, the country managed to open up and granted evolution of major industries. From here, what truly performed well was the way the government intervened within the economy, subtly protecting key industries, granting them with low interest loans, and boosting their competitiveness with a regionally unparalleled exports promotion agenda. Investments in social welfare paired with the growth of strong institutions led self-control and self-regulation in the development of the economy. The progress of public agencies created to work within different factions of the economy have maintained the momentum to conduct structural reforms and pursue growth:

To achieve permanent results, social and economic reforms must count on an institutional framework that provides stability. The 1980 Constitution strengthened property rights, which were key to guaranteeing a favorable environment for investment and enterprise. Likewise, the Constitution established the autonomy of the Central Bank, which later restricted its own lending operations to the financial sector. This limitation eliminated one of the primary sources of inflation. The Constitution also restricted government spending, which now requires the approval of a law by special quorum (Büchi, 2006: 9).

However, as is has been made clear, policies have opened up to realities that Chile face towards the future. As copper prices have taken a hit, future policies must lean in towards changing this focus in terms of economic development.

Chile's long-term economic outlook rests on its ability to maintain prudent policies to bolster its non-mining sectors. The end of the commodity boom has exposed Chile's continuing dependence on copper exports, particularly to China, as economic activity remains leveraged to shifts in global economic conditions. With copper production likely to grow only modestly in the coming decade, Chile's long-term economic growth necessitates diversification (Chile Country Risk Report, 2018: 23).

This is an important prospect into the future: although current work to establish the value chain onto further integrating with foreign markets has succeeded and helped to expand copper exports, the future economic performance of the country depends on Chile leading to invest in other economic sector and work to potentiate these. This includes investing heavily on the service sector, which base their advancement in how much the country invests in innovation and technological education. “While government efforts to support private investment and reform its education system suggest that Chilean policymakers are committed to forward-looking policy, lack of progress in either area is likely to undermine long-term growth prospects” (Chile Country Risk Report, 2018: page 24). If Chile does not act upon this necessity, they will begin to return into facing the problematic situation the middle-income trap very common in most of the countries in Latin America.



Strong commercial diplomacy

One leading aspect Chile has forged in its post-dictatorship history was its impeccable commercial diplomacy and the reach the government had in creating important trade decisions and agreements all over the world. During the 1990s, Chile had begun to look into projects to expand themselves into a more globalized community, first focusing on creating regional partnerships.

Regarding international economic policy, this implied persisting in opening up and promoting trade agreements, especially with Latin America. Andrés Rebolledo—former Minister of Energy— indicates that this option was not exclusive, since in addition to negotiating with the countries of the region, Chile maintained interest and explored other alliances (DIRECON, 2009: 198).

From here, Chile began an incredible expansion process into developing commercial ties with their regional neighbors. They began with some starting initiatives like creating pacts with Bolivia, Mercosur, and Venezuela in the early 1990s and moved onto signing their first Free Trade Agreement with Canada in 1997. Since then and until 2010, they signed another nine Free Trade Agreements – FTAs, with important international markets like the USA, Mexico, Australia, EFTA and South Korea as well as with regional partners like Colombia and Peru⁵. To this date, the country accounts for 26 different agreements, 15 of them being FTAs. By the year 2010 Chile's economy was already reaping the benefits of these accords.

⁵ For the full list of treaties signed between Chile and the countries they currently hold commercial ties with you can review DIRECON's list at <https://www.direcon.gob.cl/acuerdos-comerciales/> where you can see not only who they signed a deal with but also the full treaty itself.

Sustained economic growth has been possible thanks to the vigor of exports and investments. The country has achieved a broad and diversified insertion in its international economic relations: around 90% of its foreign trade is carried out within the framework of agreements negotiated with different economies of the world (DIRECON, 2009: 204).

Their diplomatic approach to entering commercial relations post dictatorship stands in hand into part of the success to Chile's economic growth, capitalizing on their entrance into foreign markets and being successful in directing their national brand. An important player in all of this has been the General Direction of International Economic Relations (DIRECON as for its Spanish acronym). The public entity, created by the Ministry of Foreign Relations of Chile, manage everything that dictates foreign commercial relations.

DIRECON was created back in 1979 and since then has been the main actor in terms of exercising the government's interests in foreign trade. Through DIRECON, they have created ProChile, another entity that focused on managing the "Chile" national brand while opening commercial possibilities in other countries and gathering relevant information to support exports. They account of having 50 offices across the world and 15 offices regionally to allow for businesses in Chile to look into foreign markets with an edge and assistance by the Chilean government.

ProChile inspired several exports promotion agencies across the region, including Colombia's ProColombia. These entities that work alongside the government's interests have shown that through commercial relations Chile has been able to expand and develop its national economy into entering foreign markets and sustaining growth in doing so, while reducing dependency on commodities, shielding from sharp market fluctuations and improving terms of trade.

Evolving investment in R&D and education

Research and development are key aspects to an evolving economy and Chile's interest in developing its knowledge base has been crucial towards such a development. The fact of the matter is that although Chile's income has sparked interest in its success, remains that in the long term. If Chile does not restructure its investment in innovation, it could soon begin to see signs of falling behind. At first glance, the amount of GDP percentage invested into R&D is very low. Only 0.38% of its GDP was invested in 2015, very low compared to other Latin American countries like Brazil (1.16%), Argentina (0.58%), and Mexico (0.53%)⁶: all middle-income economies. In regards to other OECD nations, Chile ranks as one of the lowest in the group, with the overall average being a staggering 2.5%. This lack of innovation easily shows up in Chile's knowledge base. Through an OECD report in 2018:

Despite the progress of the last decade, Chile still has a limited knowledge base. A growing number of Chileans pursue graduate degrees, but few do so in relevant areas for future competitiveness: 3% of graduates are in information and communication technology (ICT), and only 1% in natural sciences, mathematics and statistics (the lowest share of all OECD countries) (OECD, 2018: 28).

With recent interest during Bachelet's presidency towards offering free education to people across the country, the government has also set up agencies to help develop educational opportunities for their young nationals. Through the National Commission for Scientific and Technological Research or CONICYT, Chile has begun to invest into educational programs from the basic levels of education to more investment into developing masters and

⁶ All of these sets of data are taken directly off of the World Bank database, in particular Research and development expenditure (% of GDP).

PhDs. Yet these programs focused on an educational basis. Educational evolution can lead to a future generation of innovation; however, there are not many systems that allow enterprises or entrepreneurs to evolve and improve current practices.

To promote business innovation, the strategy has proposed the development of dynamics of accumulation of relevant knowledge in strategic sectors (those where the country has comparative advantages, high growth potential and deficit of social capital) in order to generate true clusters of innovation around them. This effort, which forms the basis of the cluster development policy, is essential to generate greater diversification and productive sophistication in the country (together with the development of the ecosystem for innovation) (CNIC, 2010: 38).

What is most surprising about this report is that the recommendations by the CNIC do not reflect any boost of current innovation trends rather the establishment of some. These include mechanisms for loan programs to entrepreneurs, the development of institutions dedicated to bettering the sciences in the country, and support innovation within established companies. This shows that Chile setting up initial programs for innovation, and although are already conscious about them, will take time and effort in doing so. In spite of the latter, there has not been a marked de-acceleration in the Chilean economy unlike in other countries in the region. Long-term public policy focus is the essence of Chile's new economic plan towards developing further current industries and finding where else the country could potentially participate in given its current competitive advantages.

Strengthening of institutions and battling corruption

Another important aspect of Chile's recent success in the region has been by the strength the government and institutions have had in against corruption. Since 2012 Chile has been growing as succeeding in being a more transparent country. Transparency International, an NGO dedicated to measuring the perception and power of corruption across the globe, currently ranks Chile the 24th most transparent country in the world after a 2016 study⁷. This could be linked to the work Chile has put into combating corruption within its political and economic structure.

From these efforts, the country has birthed Chile Transparente, a non-profit organization that looks to create networking systems with industry leaders and national politicians to ensure the development of proper practices while combating corruption. Starting from 1998 all the way to our present time, this organization has worked to develop a systematic evaluation of how Chile can look to combat corruption and reduce the presence of such. In conjunction with Transparency International, Chile Transparente has managed to develop the Transparency in Corporate Reporting (or TRAC) which is a methodology created to evaluate the information that is publicly reported by companies in the country to evaluate the current status of their anti-corruption policies. All of this with the best interest of Chile to lead the charge in safe-proofing its economy from both public sector and private sector corruption dynamics.

While these initial findings look nice on paper, recent development of large corruption scandals in Latin America has also brought attention towards Chile. The reality is that although Chile's fight against corruption has been strong, it still has a way to go. In 2014-2015, several top flight scandals by industry financial juggernauts The Penta Group and chemical developers: Sociedad Química y Minera de Chile S.A. were caught in tax evasion scandals that rocked the nation. Not just that but during Bachelet's presidency her own family under the Caval group were caught in obtaining loans to turn investment into profit fast after obtaining insider information.

⁷ The report ranks Chile as 24 in the globe and 4th in the Americas, behind Canada, the USA, and the Bahamas. The focus on their report is the perception of corruption and sees where in the world political and economic scandals affect the most.

With the image of the president's family involved in corruption scandals, Bachelet had to increase Chile's anti-corruption mechanisms but had been hit hard with social discontent. "The Chilean government's strong institutional response was fueled by the broad public outcry and important political consensus on the severity of the problem" (Casas & Carter, 2017). Not only had she lost approval rating in the process, but also her son had to step down from being involved in high-profile positions.

Although the result of this scandal was the birth of more government mechanisms to combat corruption it still shows that Chile has a way to go. Yet, as Casas and Carter (2017) state: "the integrity challenges that matter and drive people to the keyboard or onto the street in Chile or Uruguay are hardly comparable to those in Venezuela or Honduras." With that in mind although Chile still has aspects to work on, it is in a further position regarding anti-corruption than its regional neighbors. An aspect that still reinforces the success Chile has had in its development.

Has Chile overcome the trap? Not entirely

The success of Chile has been overall well perceived, especially in Latin America with some countries willing to copy-and-paste public policy measures inspired by the success experience of the country. Brazil, Argentina, Colombia, Peru and Ecuador do not account for the economic growth and development Chile has fostered during the last 30 years. However, this is not to say that everything for Chile is in top form. The reality is that Chile did find a way out of the middle-income trap but needs deep reforms in order to battle staggering inequality and other welfare indicators.

One of the starting points is that Chile still lacks evolution in its production methods, basically taking a hit from their lack of innovation as mentioned in a previous section. "As already mentioned, what you export matters and therefore the quality of competitiveness should be taken into account as well. In the case of Chile, it still relies heavily on primary exports, especially of copper. Being more efficient does not equate to being more innovative" (Dingemans, 2016: 656). This also shows based on the loss in complexity of their exports, a valuable asset for any developing country (especially those within the ranking of the OECD):

This means that over the last 40 years, Chile's economic complexity has diminished on average further than that of any other country in Latin America, and therefore its economic success, however impressive, is based on efficiency gains in low-productivity, economically less sophisticated sectors. Despite the fact that Chile possesses, in general, an excellent hard and soft infrastructure with human capital being its Achilles' heel, according to the 2013 Global Competitiveness Report, it has been unable to spur innovation (Dingemans, 2016: 661).

Bearing these aspects, it can be said that Chile is still far from avoiding falling into some of the holes of the middle-income trap it is stated to have left. Although indicators of Chile's GNI per capita reflect those of a high-income country as they are indexed within various indicators. The reality of middle income is not related to the amount you make rather their excellence, or as stated by Agenor (2015) "It is often not the quantity of production inputs (public or private) that matters, but rather their quality". Agenor later goes off into explaining that

Indeed, the fundamental source of multiple equilibria in a middle-income trap is often related to the lack of innovation activity—itsself related to poor quality of human capital, which may prevent a country from escaping a low or moderate-growth equilibrium—rather than, say, low savings, poor nutrition, lack of basic infrastructure, etc., as typically observed in low-income countries (page 11).



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Bearing this in mind you could say that Chile faces a paradoxical situation, one where their income is that of a high-income country but still reflect structural problems that reverse their status within an income trap. Dingemans offers one last view on this situation:

(...) In order to maintain progress in its economic development, it is more than likely that its current strategy is inadequate and that, additionally, conditions are present to expect a probable success in implementing industrial policies, not by introducing a hegemonic state, but by means of an entrepreneurial state that pays attention to legitimizing economic strategies (Dingemans, 2016; 664).

Yet, beyond this reality that Chile has a way to go before truly escaping the trap, especially in terms of innovation, we can still declare this a true success story. The evolution of Chilean policies post-dictatorship, its approach to commercial diplomacy, and its rapid growth show that through policy reforms, the state can play a role in bettering the economic situation of a country to a point where they excel further than even the largest economies in the region like Brazil, Colombia and Argentina. While Chile still finds aspects, it needs to work in. It has done more into pushing further from the middle-income trap than many in the region. Thus prove that beyond the concept of neo-liberalism, what most satisfied Chile's growth was its political pursuit of finding a structural path towards development, which will ultimately feed into future expeditions towards transforming its economy.

Conclusion

Chile has been an inspiration for many to escape the rankings of middle income. They have done it through well-developed institutional policies that reflect open mechanisms in both financial and economic structures. They have created value chains in their exports by reaching out and entering foreign markets through their various agreements signed and ratified by their government. However, what Chile also shows is that high income does not mean escaping the trap that many middle-income countries find themselves in. The debate stands at it being a case of quality over quantity, a focus that what takes developed countries into high ranking positions on how well they perform is not based around how much they export rather what they export and how much of it they do.

As necessary conditions to have a rapid economic growth that can be sustained during long periods of time and even in the face of economic crisis, the Chilean case allows to abstract the following requirements: political stability, sound economic policies, a balanced fiscal policy, a government favoring long-term commitments over short term decisions, and economic openness paired with an impeccable commercial diplomacy. Such an environment is supportive for economic development, allowing traditional industries to move up the value ladder.

Ultimately though it demonstrates that, like all economies, evolution and innovation are the next step towards development. What truly establishes value is not how much wealth comes into a nation and how equally it is distributed rather the real end product a country produces. If Chile wants to further its chances into potentially being the most developed economy in Latin America it must, like China, focus on innovation and development of new industries, with the idea that the only way to sustain growth in the long-run and create social welfare out of it is through having above standard products that are knowledge-intensive and not labor-intensive. If a country like Chile keeps producing basic goods at standard levels as they do today, for as much as they may be considered high-income that situation will be stuck in not increasing exports and look to rewind into an income trap.

A bigger question here is that what economic standard can tell us if an economy is one to model after? After all, high income for Chile only reflects statistical proportions of their trade income but does not reflect the faults in Chile's lack of innovative industries and deviation from focusing on commodities and agricultural exports. The reality is that this country is a proper example for good fiscal and monetary policies functioning in conjunction rather than excelling in exports and product quality. Their use of their agreements to push exports further has only demonstrated that their government has been working effectively, and that although their exports are important had they not been backed up policies to efficiently work them into the market none of Chile's success would have been possible.

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