

Chile

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US SIGNS FREE TRADE PACT WITH CHILE

The United States signed a Free Trade Agreement with Chile on June 6 and said its first such accord with a South American nation was a stamp of approval for Chile and a marker for future regional accords.

The agreement was signed in Miami, a US gateway to Latin America, by US Trade Representative Robert Zoellick and Chilean Minister of Foreign Relations Soledad Alvear. Congresses in both nations are likely to approve the pact this year. Zoellick called Chile, an island of political and economic calm in a troubled region, "an exemplary economic partner". "Chile is the freest, most competitive economy in Latin America and it has set a very high standard", he said.

The agreement, signed after 11 years of planning and negotiations that concluded in December 2002, makes Chile the only country in Latin America apart from Mexico to win Washington's blessing as a preferred trade partner. Zoellick said the US hoped the accord would encourage other nations to reach such agreements and would be a boost for talks on an Americas-wide free trade zone.

Although negotiations on the pact were completed in December, the actual signing was apparently delayed because of a chill in relations over Chilean President Ricardo Lagos' opposition to the US-led war in Iraq.

Lagos said the pact would eventually produce a 40% jump in exports to the US, its biggest export market and foreign investor.

Lagos, a left-leaning free trader who has signed free trade pacts with the European Union, EFTA, and South Korea, said exports to the US would increase during the first three or four years of the pact to US\$ 5 billion a year from the current US\$ 3.6 billion. In a televised message to Chileans, he said the country

would see the full impact three years after the pact went into effect, when 95% of all Chilean exports would enter the United States duty free. Chile's main exports to the US are copper, salmon, wine and grapes.

The US has similar agreements with Canada and Mexico under the NAFTA deal, and with Israel and Jordan. Washington also recently signed a free trade pact with Singapore that is pending Congressional approval. The Bush administration hopes the Chile pact will give momentum to talks on the Free Trade Area of the Americas, which is meant to be completed by 2005 and would encompass all 34 countries in the Americas except for Cuba. At a news conference Zoellick acknowledged the Americas project is far more complex than a bilateral deal but said he had a "cautious optimism" over prospects after a trip last month to Brazil, which is co-chairing talks toward the FTAA.

The Chile accord was welcomed by the Andean Community bloc, which groups Peru, Ecuador, Colombia, Venezuela and Bolivia. Chile was a member until it withdrew in 1976.

Reuters, June 6

REMARKABLE GOVERNANCE INDICATORS IN CHILE

Every two years, the Governance Group of the World Bank Institute (WBI) publishes a research on Governance Indicators, which are defined as the traditions and institutions by which authority in a country is exercised for the common good. This definition of governance is condensed in six dimensions or criteria: 1) Voice & Accountability; 2) Political Stability; 3) Government Effectiveness; 4) Regulatory Quality; 5) Rule of Law, and 6) Control of Corruption.

These indicators cover 199 countries and territories and are based on several hundred

individual variables measuring perceptions of governance, drawn from data sources constructed by 18 different organizations.

As with its 2000 report, the World Bank's 2002 Governance Indicators ratify Chile's status as one of the most transparent countries in the world. Ranked 19th on both editions (in the highest 90.2% percentile in 2000 and 90.7% in 2002, respectively), Chile's "Control of Corruption" indicator is better evaluated than Spain's (21st) and France's (22nd), and similarly as the average of OECD countries.

Chile also maintained the 19th position (90.2%), in the "Regulatory Quality" indicator, above France (29th), Italy (33rd) and the Czech Republic (36th) among others. In the "Rule of Law" indicator Chile took the 26th place with a percentile score of 87.1%. The country is placed just above Hong Kong (27th) and Spain (31st).

Chile's position in the "Government Effectiveness" indicator was 27th (86.6%) in 2002. It outperformed Japan (31st), Italy (39th) and South Korea (41st). At the same time, Chile had an excellent performance in the "Political Stability" indicator, going up from the 35th position in 2000 to the 27th in 2003 (86.9%), better placed than the United States (37th) and the United Kingdom (50th).

However, the biggest improvement of all was in the "Voice & Accountability" indicator, in which Chile leapt spectacularly from the 68th (64.9%) position in 2000 to the 32nd (84.3%) in 2002. It scored above Italy (33rd) and Japan (42nd), among others. According to some analysts, the reason behind this is the rigor of the Chilean press when monitoring the public apparatus. It is important to note that, in every indicator, Chile did better than Latin America's biggest economies: Argentina, Brazil and Mexico.

World Bank (www.worldbank.org), May 8

CHILE MAINTAINS HIGH COMPETITIVENESS LEVELS

Chile's overall high competitiveness levels have been reaffirmed in the 2003 *World Competitiveness Yearbook* published by Swiss-based business school IMD in May.

In this edition, the report divided countries in two categories. The first one is comprised by 30 economies with a population larger than 20 million, such as the United States, Australia, Canada, Malaysia, Germany, Colombia and Brazil. The second is made up of 29 economies with less than 20 million inhabitants, like Finland, Denmark, Iceland, Norway and New Zealand. Chile is the only Latin American country in this last group.

Chile obtained a score of 61.5 (in a scale of 1 to 100) and was placed 16th, above the Czech Republic, Hungary and Slovenia.

Chile was ranked number one among the 29 economies in the following criteria: Image abroad as supportive of business; and Availability of competent senior management. It was ranked second in Absence of price controls; Freedom of foreign investors to acquire domestic companies; and Effective supervision by corporate boards.

The country also made the third position in these items: Integration into regional trade blocs; Absence of legal discrimination against foreign investors; Employers' social security contribution rates, and Absence of government subsidies.

Other relevant criteria include: Quality of air transportation encourages business development (8th); Maintenance & development of infrastructure is adequately planned & financed (9th); Standards of University Education (10th), and IT Skills (11th).

The IMD also pointed out the challenges Chile faces: The modernization of the State and reduction of unemployment are the most important, along with the incorporation of IT for the bettering of production processes and management and the

improvement of the quality of education in order to increase productivity to international levels.

Finally, other criteria in which Chile is still lagging are, among others, Estimated female to male earned income (24th); Employee training as a high priority in companies (27th); treatment plants: Percentage of population served by Waste water treatment plants (27th); and number of inhabitants per physician and per nurse (29th).

IMD (www.imd.ch), May 14

MOP UNVEILS US\$ 1.93 BILLION CONCESSIONS PROGRAM

Chile's Ministry of Public Works (MOP) unveiled the government's 2003-2004 concessions program, consisting of 33 projects worth a total of US\$ 1.93 billion. The projects range from airports to dams, and cover the length of the country. They include 15 initiatives from other national ministries, where the Ministry will act as contractor. The largest project is the US\$ 350 million traffic bridge to link Region X's Chiloé Island with the mainland across the Chacao Canal. Offers for this 30-year-plus concession will be opened in July.

Capital Santiago is due to see several major investments aimed at upgrading and streamlining its public transport systems. Some US\$ 367 million in public-transport infrastructure concessions will be awarded over the period, including four multi-modal transport stations, the El Salto-Kennedy Avenue intermediate beltway, and exclusive bus lanes and other public transport-related facilities under the *Transantiago* program. These schemes are designed to "transform Santiago's public transport system into a world-class capital, with the highest roadway infrastructure standards and technologies", according to Minister Javier Etcheberry. Santiago will also benefit from a US\$ 26 million concession to revamp the areas along the Mapocho River, which snakes through the city.

The regions also feature heavily on the MOP's to-do list. Three regional capitals,

Arica (Region I), La Serena (IV) and Temuco (IX) are in line to receive new or upgraded airports under concessions. The US\$ 9 million concession to expand capacity at Arica's Chacalluta airport is due to be awarded next semester, while new airports are planned for Temuco (US\$ 48 million) and La Serena (US\$ 25 million), with construction starting 2H04. The country's highway concessions program also rolls on, led by a US\$ 65 million highway system for northern Region II, benefiting the cities of Antofagasta, Calama and Mejillones. Offers are due 2H04. Connections with Argentina could get a boost from a concession to rehabilitate a trans-Andean railroad in central Chile. The US\$ 260 million project was analyzed and submitted by Argentine construction firm Tecnicagua, and would connect Mendoza in western Argentina with the town of Los Andes, northeast of Santiago, eventually continuing on to the Pacific port of Valparaíso. The MOP is reviewing the project and, if approved, may call for tenders early 2004.

Ferries loom large in the Ministry's plan to improve transport in the south of the country. A US\$ 20 million system to connect Regions X and XI with four ferry routes among six port terminals will go ahead in 2004, linking the mainland with Chiloé and other islands in the archipelago. Further south in Region XII, the Puerto Natales passenger terminal will be expanded and the Kirke Passage upgraded, at an estimated cost of US\$10 million. Other projects include prison concessions and three major dam projects for the agricultural heartland between Regions V-VIII.

Since 1992 public-private investments under the MOP's concession system have brought in US\$ 5.54 billion, helping build 36 projects including four major highway systems and nine airports, said. The influx of private capital has freed up more government money for other priorities, such as secondary road systems, fishing ports, education and health.

Business News America, May 21

US\$ 400 MILLION IN DAMS, IRRIGATION CONCESSIONS FOR 2003-4

Chile's Ministry of Public Works (MOP) is planning to award some US\$ 400 million in concessions to build three major dams and an irrigation system in the country's central regions over the 2003-4 period, Minister Javier Etcheberry said. The three dams, *Convento Viejo*, *Ancoa* and *Punilla*, have a total price tag of some US\$ 267 million.

Convento Viejo (US\$ 105 million), will be constructed near Chimbarongo in Region VI. A call for tenders is due to be made in June, with offers received 2H04. This dam will irrigate some 19,000 ha and improve irrigation on a further 15,000 ha from Chinbarongo to the Nilahue valley I, also in Region VI, increasing the land's productivity fivefold, according to the Ministry. Construction will include a 32 m-high dam wall and some 300 km of irrigation network.

Ancoa dam carries a US\$ 34 million price tag and will be built in Region VII on the Ancoa River near its confluence with the larger Maule River. It will be used for hydroelectric generation and irrigation. Ancoa will serve 80,000 ha, some of which is already partly irrigated. The concession will be carried out in 1H04. The *Punilla* dam will be built on the Ñuble River in Region VIII. It is designed to more than double irrigation coverage to 66,000 ha and sustain a 90 MW hydroelectric facility. The project has an estimated cost of US\$ 130 million, and will be offered in 1H04.

The MOP is also planning to offer to concession a US\$ 130 million irrigation system for the Aconcagua Valley in the interior of central Chile's Region V. The project consists of building a storage area for underground waters and irrigating 102,000 ha (29,000 ha of new land and upgrading the irrigation of an existing 73,000 ha). The Aconcagua system will go to concession in 2H04. The projects are part of the MOP's US\$ 1.93 billion concession program for 2003-4.

Business News Americas, May 21

CHILE MAY BE POLITICALLY BORING, BUT ITS ECONOMY WORKS

The following is an editorial published by columnist Andrés Oppenheimer, a journalist and expert on Latin American political issues, in the June 8 edition of the Miami Herald:

Here is something you rarely read about: While much of Latin America is lashing out against free trade and US-backed economic reforms these days, Chile is going in the opposite direction, and is doing better than everybody else in reducing poverty. Chile's success story - or its relative success compared to its neighbors - was the talk of the day at the Miami ceremony in which Chile became the first South American country to sign a Free-Trade Agreement with the United States. The deal, once approved by the two congresses, will allow Chile to export 85% of its goods without paying tariffs to the world's biggest market.

At the ceremony, presided over by Chile's Minister of Foreign Relations, Soledad Alvear, and US trade representative Robert Zoellick, some in the audience were commenting - only half jokingly - that Chile is South America's most politically boring country, and at the same time the one that works best. While most of Chile's neighbors are still passionately debating which economic system they want to embrace, Chile has long made up its mind. Governments in Chile come and go - from the right, the center and the left - but they all stay the free-market course.

Basic Consensus: "In Chile, we have been able to generate a basic consensus in society", Alvear said after the ceremony. "There are no serious questions about the wisdom of economic openness". So much so that the Free-Trade Agreement was signed by the Socialist Party government of President Ricardo Lagos. Among the Chilean visitors at the signing was Diego Olivares, the Vice-President of Chile's United Confederation of Workers, the country's biggest labor union.

Chile's ability to avoid the dramatic political shifts that have ruined most of its neighbors has paid off handsomely. Since the 1988 plebiscite that defeated former dictator General Augusto Pinochet, Chile has cut its poverty level - the number of people living on less than US\$ 2 a

day - from 42% of the population to 20%. By comparison, the countries with messianic leaders who blame free market policies or the US for their countries' ills have sparked a cycle of capital flight, greater unemployment and greater poverty.

While Chile's economic growth rates have dropped from 7% average in the mid-1990's to 2.5% over the past three years, it has shown the most consistent growth in the region. Last year, Chile's economy grew by 2.1%, while Argentina's dropped by 10.9%, Venezuela's by 8.9%, and Latin America as a whole fell by 1.2%.

Chile's US\$ 9,417 a year per capita income is among the highest in Latin America, according to United Nations figures.

Against the Tide: In many ways, Chile is swimming against Latin America's tide. It is a country where the role of the state has been shrinking over the years, young people are swinging to the right while their parents stick to the left and political life is increasingly converging to the center. "We're becoming a US-styled democracy", said Eugenio Tironi, a Chilean sociologist who has been an image advisor to Lagos. "Like in the US, we have two political coalitions, an increasingly smaller government and a society that is increasingly individualistic".

Will Chile be an island of economic stability in South America or will it be a model that will be soon followed by its neighbors? we asked Minister. "A model we don't like to be: It creates resentment, it makes us look presumptuous" Alvear said. "But we have been successful in establishing key strategic targets for the country and in maintaining them over time. You cannot reinvent the country every time a new government takes office".

There are many things to be criticized in Chile, including a military that preserves obnoxious economic privileges dating from the Pinochet era, a gap between rich and poor that is still wider than in most developed countries and a press that - while free - could be much more aggressive. But there is little question that while much of the rest of Latin America has made dramatic political swings, Chile has stuck to its economic targets, and has done much more for the poor than the region's self-appointed champions of the poor.

The Miami Herald, June 8

CHILE HAS A CLEAR EXPORT STRATEGY

Minister of Foreign Relations María Soledad Alvear discusses the country's push for Free Trade Agreements and about relations with the US:

Considered the most disciplined free-market economy in Latin America, Chile started opening to foreign competition in the early 1980's and today boasts an average 6% tariff on all imported goods. The country of just 15 million inhabitants has Free Trade Agreements with the European Union, Canada, Mexico, and Korea, and special trade accords with most of Latin America.

When the North American Free Trade Agreement was approved back in 1993, Chile was promised it would be the next country to get a free trade deal with the US. Although President Bill Clinton was unable to win fast-track negotiating power, Chile went ahead with the talks anyway, two years ago. Then the Bush Administration won fast-track authority last August.

The two countries finalized negotiations late last year, around the same time a similar US-Singapore trade deal was wrapped up. Yet Bush signed the Singapore agreement in early May in a White House ceremony and made Chile wait for a June 6 signing-in Miami. Why? Officials in Washington said they were "disappointed" with Chile's failure to support the Iraqi war from its seat at the UN Security Council. Political analysts in Washington and Santiago believe the delay was aimed at making the Chileans aware of how deep that disappointment was.

On May 28, the day after the US finally announced the June 6 signing date, Chilean Minister of Foreign Relations María Soledad Alvear talked with *BusinessWeek* about US-Chile relations and the prospects for free trade. They met in the Foreign Relations palace in downtown Santiago. Alvear, 52, a lawyer, formerly served as Chile's Minister of Justice and as the Minister for Women after Chile returned to democracy in 1990 after 17 years of military rule. Edited excerpts of their conversation follow:

Q: What is the significance of the Chile-US Free Trade Agreement for the Chilean economy?

A: I'm very happy about it. We've negotiated a Free Trade Agreement that's very good for both countries. Chile has a clear export

strategy aimed at developing the economy and in particular aimed at diversifying our exports. We couldn't do that without this agreement. It's a seal of quality for our country as a reliable place to make investments. We have signed agreements with the US, the European Union, South Korea, Latin America, and soon we'll sign with the non-EU nations. This gives us a very interesting horizon.

Q: This is said to be a "third-generation" trade agreement because it covers intellectual property, electronic commerce, services, and government procurement. In that sense, it could be a template for other trade agreements around the world. But some Chileans say the government wanted the agreement so badly it caved in by not insisting on eliminating US anti-dumping rules. Chile also agreed to loosen its restrictions on capital flows even though those restrictions have protected the country from financial volatility in recent years.

A: We were very conscious that we weren't going to manage to eliminate US anti-dumping rules, which are being looked at in multilateral forums like the World Trade Organization. Nevertheless, we agreed to mechanisms for dispute resolution that are quite modern. And with regard to capital controls, we're satisfied with what was achieved.

Q: Some say the Chile-US Free Trade Agreement is a template for the proposed Free Trade Area of the Americas, the 34-nation accord currently under discussion for the hemisphere.

A: This is a FTA negotiated between a small emerging-market country and the most developed economy of the world. If we're capable of reaching such an agreement, that improves the possibility of reaching a larger agreement among 34 countries with different levels of development around the region. Some countries in the region believe that it's perilous for small developing countries to sign commercial agreements with industrial countries, but we are proof that it's not. The negotiation between Chile and the US and the negotiations now under way between the US and Central America will be very interesting and important for the Free Trade Area of the Americas.

Q: Chile already has agreements with all of Latin America except the Caribbean. Why is the Free Trade Area of the Americas important to you if you already have most of the region covered?

A: Because Chile is a small economy, and

we have placed a big emphasis on exports. Having clear rules for all of the countries in the region will be an important stimulus. Chile's decision to open up to the world allowed us to double our gross domestic product in the 1990's -something that had previously taken us 50 years to do. At the same time, we were able to halve the number of Chileans living in poverty. We're very conscious of the fact that this process of market openings mean growth for countries. And if the countries carry out good social policies to lift people out of poverty, even better. That's why it's important that the region enjoy stable, solid democracies. Latin America has lived through very painful periods.

Today we have recovered our democracies, but the problem now is maintaining governability. Many of the problems we see in Latin America today are caused by painful poverty and pent-up demands from society. We believe there's a way out of this situation, and it's important to work together to increase the possibility of development and reduction of poverty.

Q: In just a few months, Chile will mark the 30th anniversary of the bloody military coup that ousted Socialist President Salvador Allende. The military ruled for 17 years, and Chile has been a functioning democracy only since 1990. You've been a Cabinet Minister in all three governments since then. How do you feel the country has changed?

A: If a person had been asleep all these years and woke up today, he would not recognize the country. Of course, the most important thing was the restoration of democracy, freedom, and respect for human rights. Chile was an isolated country, and when it returned to democracy it had to reinsert itself in the world. Today, it's a key member of the most important political forums, including the UN Security Council. If you look at census figures, you'll find that 80% of the young people in college today had parents who didn't attend college. Among the poor, the number of households that own a washing machine has doubled in these 13 years.

The role of women in public life has been remarkable. Chile has a woman serving as Defense Minister. When she and I go to Buenos Aires to meet with our Argentine (male) counterparts, they will see two women, and that reflects in many ways the changes Chile has gone through.

BusinessWeek, June 16

CHILE IN THE EYES OF WALL STREET

The following are excerpts from Wall Street Investment Banks' reports on Chile:

From Credit Suisse First Boston's Emerging Markets Economics, June 26

• Year-to-date, the Chilean economy has been resilient to a series of negative shocks. **Growth has been supported by consumer spending and by the export sector, in an environment of low inflation.** The Central Bank has prudently refrained from tightening monetary policy, and will likely continue to do so until later this year. External imbalances remain small, reflecting below-potential GDP growth, but fiscal accounts may weaken if the government fails to achieve full congressional backing for its recent and controversial tax proposal. This topic will likely continue to dominate the headlines in upcoming weeks and could hurt investor sentiment locally. **In an emerging markets context, however, Chile's fiscal and structural problems are modest, and foreign investors will likely remain unconcerned about them in the foreseeable future.**

• **The Chilean economy is on track to grow by close to 3.5% in real terms in 2003.** The GDP report for the first quarter of the year (real growth of 3.5% year-on-year), though on the low end of original expectations, was acceptable given the series of negative shocks that materialized during the period, including the Iraq war, the spike in oil prices and the local corruption scandals. Available figures for May, like vehicle sales and industrial exports, free from calendar distortions, are already showing signs of a stronger economy. Also, the recovery in April and May in consumer confidence bodes well for future consumption reports. Currently, one of the main risks to our growth forecast is related to potential further downward revisions to our growth estimates for (non-Japan) Asia due to SARS. Fortunately, however, this source of risk has notably lost importance in recent weeks. **We expect growth in Chile to continue to be supported by consumer spending and by the export sector.**

• **Growth is taking place in an environment of low and stable inflation,** which should keep monetary policy on hold until later in the year.

The most recent inflation and real wage data confirm that inflationary pressures are not on the horizon. Annual core inflation, which we view as a better gauge of medium-term inflationary pressures, has remained below 3.0% in eleven of the past twelve months, despite the gradual strengthening of the economy and the distortions caused by rising oil prices. **We expect the Bank to leave monetary policy on hold until late 2003,** based on these factors and on the Central Bank's awareness of the high cost of potentially having to ease shortly after the resumption of a monetary tightening cycle (if inflationary pressures do not materialize and growth disappoints).

• Year-to-May, exports and imports were 9.1% and 13.2% higher than in the same period last year, a significant improvement. Exports of industrial goods have surprised on the upside, rising 17.9% y-o-y in the first five months, more than double the 8.7% growth rate in copper exports. **On the import side, purchases of consumer goods have remained strong (up 13.1% in the first five months), consistent with healthy overall consumer spending.** Meanwhile, weakness in imports of capital goods in the first quarter of 2003 (1.8% growth) was consistent with the (weak) state of fixed investment. In April and May, however, imports of machinery and equipment have accelerated significantly, reaching 22.3% year-on-year growth.

• Fiscal imbalances remain narrow, but uncertainty is growing on some fronts. The Corfo-Inverlink case has not been resolved and could eventually hit the public sector accounts by the equivalent of 0.2% of GDP, if Corfo has to absorb the losses associated with the illegal transfer of close to US\$ 100 million worth of certificates of deposit to Inverlink. Meanwhile, it is still unclear how the government will compensate for rejection in the Senate of the proposed tax hike on alcoholic beverages that was part of the revenue-enhancing tax package submitted to congress by President Lagos in early June. This package seeks to compensate for lower tax collections associated with the recent signing of Free-Trade Agreements and to help finance two specific anti-poverty government

programs. **Fortunately, however, the increase in the VAT rate from 18% to 19% is likely to be ratified in the senate.**

• Finally, progress on the reform agenda has been generally slow; however, no reform initiative is too pressing to affect the country's near-term outlook. Most reforms under analysis seek to improve an already strong institutional system, including: improving the bankruptcy laws; promoting the use of electronic means to reduce red tape; increasing the independence of fiscal tribunals; and, modernizing the customs system. **In June, the government introduced the second round of capital market reform initiatives.** Similar reforms have been successfully implemented in recent years in other Latin countries, like Mexico, particularly those related to corporate governance. Their approval, probably later in the year, should result in more transparent and efficient financial markets.

From Santander Central Hispano's Strictly Macro, June 17

• The proposed tax increases have added noise to the otherwise improved economic sentiment brought by the moderate recovery in economic activity and the signing of the trade agreement with the US. **The logic of the government is straightforward: it needs more resources to finance higher social expenditures, so in order to comply with the 1% structural surplus rule, it needs to increase revenues.** The government should look to adjust fiscal spending before increasing taxes, opposition politicians claim. We have not seen a clear indication from the government of its medium-term plan for fiscal spending and for tax collections, which could quell some of the private sector's uncertainty.

• The government sent Congress a proposal to increase the value-added tax (VAT) by 0.5% immediately and by another 0.5% during March 2004 through 2006. These proposals are intended to reverse fiscal deterioration resulting from the new foreign trade agreements, the social programs of "Plan Auge" (the public health system reform), and "Chile Solidario" (aid for the poorest families in Chile).

CHILE IN THE EYES OF WALL STREET

• Looking forward, we expect that the plan will be approved and that it will not have significant effects in terms of GDP growth for this year and next year. Other projects that are in the government agenda and that could generate some market noise are the electric law, the second part of the capital market reform, the project to modernize the state and some changes in the labor laws. We expect that some of these proposals would be positive for the economy, although we think they would not be enough to produce a turnaround in the still-low economic sentiment of most business sectors.

• **Electriclaw:** The Chilean government, through the Ley Corta (the “Short Law”), is currently discussing making some modifications to the electric utilities sector. These changes relate mostly to the way in which transmission tolls are going to be charged. The Ley Corta was introduced in Congress in May 2002 and was supposed to be approved by May 21, 2003. Owing to some internal differences, the regulator has delayed the deadline but has specified no specific new deadline. It has been extremely difficult for the government to get an internal consensus regarding the way in which transmission tolls should be paid.

• **Capital market reform, Part II:** The government intends to advance in the process of making local financial instruments paperless and the development of an emerging firms stock market. The proposal would also increase the regulatory power of the regulatory agencies and would try to improve the quality of information releases by companies.

• **Modernization of the state:** On January 30, the government agreed and signed with all political parties that have parliamentary representation an agreement for the modernization of the state. The agreement established a vast agenda of 49 legislative and administrative priorities to be developed during 2003. Among the initiatives, we highlight the following: simplification of bureaucratic procedures; a “new deal” in human resource management; strengthening and improving the quality of public managers; government procurement; transparency in the financing of political campaigns; tax benefits for

donations for public purposes; permanent operation of the parliamentary joint budget commission; a process for impeachment of members of Congress; courts for the defense of free competition; and transparency in the administration of resources for Congress.

• **Labor reform:** This is a plan that is intended to increase the flexibility (or adaptability) of the labor market. It deals mainly with the adjustment of working hours, subject to negotiations with labor unions.

From Merrill Lynch's Emerging Markets Debt Monthly, June 6

• **We revise our GDP growth forecast for 2003 to 3.2% from 3%.** However, the fact that GDP growth has been driven by private sector consumption in the context of declining real wages and stable consumer confidence suggests our base case scenario is vulnerable. Investment has been growing below GDP, somewhat surprising in the current phase of the cycle.

• **We estimate that private sector consumption contributed to 100% of the GDP growth of the last three quarters.** While GDP grew 3.2 and 3.5% year-on-year during the fourth quarter of 2002 and first quarter of 2003, respectively, consumption contributed with 3.4 and 3.1 percentage points to economic expansion. Investment has been particularly weak given the current stage of the economic cycle, contributing with only 0.6 and 0.1 percentage points.

• **Consumption as shown by the national accounts has finally caught up with the growth in current household income,** suggesting consumers are turning less conservative. The good news is that the private sector cleaned their balance sheets somewhat, what left them in a better situation to increase leverage. In fact, credit to households has increased by 15% from a year ago, according to the Banks Regulatory Agency.

• **Therefore, for the economic expansion to be maintained or accelerate, the contribution of other sources of demand - investment and net exports- is needed.** On the latter, there is some good news despite lingering doubts about

the ability of net trade to positively contribute to GDP in times of expansion. Exports have been growing at a hefty pace, helped by a weaker peso and stronger copper prices. During the first four months of the year, non-copper exports are up 9.4% year-on-year in average, while copper exports grew 9%. Imports, however are outpacing exports, thus the benefits of net trade on GDP could be minimal. On the investment side, the good news is that imports of capital goods are up 8.2%, while intermediate goods excluding fuels are also up by 9%, suggesting some recovery in investment might be under way.

• **We forecast 2004 growth at 3.6% on average, supported by lax monetary policy and the recovery of the G7 economies.** We believe, however, that the economy should end 2004 with very good momentum, as we expect Q4 2002 to show rates of growth of 6.1% in annualized terms.

• We expect inflation to remain within the Central Bank targeted rates: 2-4%. **While overall CPI broke the ceiling of the band in March, it did so because of the impact of higher oil prices on heating and transportation costs. Core inflation, at 2.8%, remains below the mid point of the Central Bank's inflation band. Wholesale prices continue to outpace CPI, suggesting profitability at the corporate level is being hurt, what, in turn, explains the pressure on real wages low. At the current stage in the cycle, we see no threat to the Central Bank's inflation target policy, thus we expect no change in monetary policy in the short term.**

• **The Free Trade Agreement between Chile and the US will finally see the light.** The US Congress now has 60 days to consider changes to the laws regulating commerce with Chile. The Agreement is a significant step forward for Chile in terms of its relationship with the US, which was somewhat hurt due to the Chilean position at the UN Security Council on Iraq. While the effects will not be felt immediately, the major gains from the Agreement could come if US companies or companies wanting to access the US market move production lines to Chile.

PACKARD BELL SPENDING US\$ 5 MILLION ON FIRST CHILE NOTEBOOKS

International computer maker Packard Bell is spending US\$ 5 million this year to assemble its first line of notebooks in Chile via a joint venture with local partners. The company is preparing for when Chilean notebook prices reach approximately US\$ 1,000, compared to today's US\$ 1,300, and begin to replace traditional PCs on a mass scale, Packard Bell Chile Manager Francisco de Castro said.

Meanwhile Packard Bell is studying the best way to enter the Mexican market, but has ruled out Brazil for now owing to that country's restrictions on imported hardware, de Castro said, adding that the company is looking to boost its sales in the region by 30% this year. Packard Bell is part of Japanese conglomerate NEC Computers International. The Chile subsidiary (www.packardbell.cl) operates as the company's regional headquarters. Packard Bell withdrew from the US in 1999, but remains active in Europe, the Asia Pacific region and Latin America.

Business News Americas, May 20

INAUGURATION OF GE'S INTERNATIONAL TECHNICAL CENTER OF EXCELLENCE IN CHILE

General Electric and Lockheed Martin announced the official opening of GE's new International Technical Center of Excellence, marking a major milestone in the offset fulfillment program with Chile for the acquisition of 10 new Lockheed Martin F-16 Block 50 aircraft.

The center, operated by Adexus, an information and communications technologies integrator, will be GE's hub for the development of highly specialized, world-class technical publications for the international aerospace industry.

"This is an important day for GE, Lockheed Martin and Adexus. It is also a significant milestone for the development of the aeronautical industry in Chile", said Hugo

Silva, GE Regional Executive for Chile, Peru and Bolivia. "This center is the result of extensive research, evaluation and teamwork to make this important project a reality".

This high-technology center is the first outcome of the offset program initiated by the Chilean Government in 2000. The objective of this offset program, led by CORFO (Chilean Economic Development Agency) is to re-enforce industrial and technology development policies by attracting foreign investment and the creation of export-oriented economic activities that compensate defense sector acquisitions.

The Chilean government accepted the GE and Lockheed Martin project recognizing that it would bring high technology and the growth of intellectual capital to the country of Chile. The GE ITCEC represents up to 25% of the total offset obligation.

"This center proves our commitment to the offset program for the F-16 aircraft acquisition", said Larry McQuien, Lockheed Martin's Vice-President for Business Ventures. "Lockheed Martin has an exceptional record of fulfilling our offset obligations. We have completed over US\$ 40 billion in offset programs around the world, and we will continue working with the Chilean Economic Development Agency, CORFO, to execute the offset obligation".

The state-of-the-art aerospace technical publication facility will have many benefits for Chile. Those employed at the center will create a product with a significant export market and a worldwide customer base requiring technical manuals for maintenance work, and ultimately will further development of Chilean intellectual capital.

Although it was officially inaugurated today, the GE ITCEC started operating last year, and about 200 technical service bulletins have already been published and distributed around the world. The bulletins are used by aircraft engine maintenance departments in leading industrial companies.

"The benefits the GE ITCEC will bring to Chile include having a local center associated with the vanguard of aerospace know-how and technology, the creation of new jobs in this field, the development of products aimed at a significant export market, and the strengthening of professional capacity

in the industry", Silva said. "The program has been developed in compliance with all the milestones of the initial planning and the strict standards the GE Aircraft Engines division sets worldwide for the aerospace industry".

After the initiative was accepted within the Lockheed Martin offset program, Adexus was selected to develop the project. In conjunction with GE, Adexus has worked through an "integrated team" concept, creating appropriate planning to satisfy the needs of infrastructure, technological requirements, personnel and training of Chilean professionals who have joined the center.

The second Chilean institution included in the project is the Universidad Técnica Federico Santa María (UTFSM), which signed a cooperation agreement with GE and Adexus. This agreement will support the growth of the GE ITCEC by incorporating in the UTFSM curriculum specific courses related to the aerospace industry.

General Electric (press release), May 19

LAGOS ROLLS OUT PLAN TO ATTACK DIGITAL DIVIDE

Chile's government will train more than 500,000 citizens in the use of new technologies, said President Ricardo Lagos. At a speech at a local school in the suburbs of the capital Santiago, Lagos laid out an adult education program, for citizens of 15 years of age or more, which he explained would be administrated separately from the country's school system. The first group of citizens to receive training -some 100,000- will begin instruction before December of this year, he added. The program, an initiative of the Ministry of Education, received renewed attention from the President, after a government study emerged that more than 70% of Chileans still do not know how to use a computer. "At present only a third of Chileans know how to use word processing or spreadsheet programs, or navigate through cyberspace. As such is the case, the jump that must be made is enormous", Lagos said.

Business News Americas, May 16

BHP BILLITON APPROVES ESCONDIDA NORTE COPPER PROJECT

BHP Billiton and its partners have approved the development of the Escondida Norte copper project in northern Chile, as part of Escondida's operating strategy to maintain copper production capacity in future years. Brad Mills, President and CEO of BHP Billiton Base Metals said that the Escondida Norte open pit would be located 5 km from the existing Escondida mining operations. Escondida Norte will mine a satellite ore body that will be able to provide higher-grade copper ore to the two existing Escondida concentrators, which will also continue to receive ore from the Escondida mine.

"Due to the proximity of the Norte open pit to the Escondida operations, we can develop this property in a manner that maximizes the synergies with the existing Escondida infrastructure. Norte will provide the necessary feed to maintain capacity at Escondida above 1.2 million tons per annum of copper in concentrate and cathode through the end of 2008", Mills said.

Ore grades at the existing Escondida mine are forecast to continue to decline over the next several years. Norte will enable Escondida to maintain existing capacity. The development of the Norte open pit will increase production flexibility and reduce operational risks associated with a single mine source, as well as further reduce the cost of production from an already low base. First copper production from the Norte open pit is scheduled for the fourth quarter of CY2005.

Development costs are estimated at US\$ 400 million (BHP Billiton share US\$ 230 million). These costs include installation of a primary crusher, construction of an overland conveyor, maintenance and operating support facilities, some new mining equipment, the transition of a portion of the current Escondida mobile equipment fleet to the Norte open pit and waste pre-stripping of the new pit. Escondida Norte's combined proved and probable ore reserves are estimated at 526 million tons of sulphide ore at an average copper grade of 1.42% and a cut-off grade of 0.7%, giving an ore reserve life of approximately 17 years.

BHP Billiton (press release), June 16

STARBUCKS ANNOUNCES EXPANSION INTO CHILE MARKS ENTRY TO SOUTH AMERICA

Starbucks Coffee International, a wholly owned subsidiary of Starbucks Coffee Company announced that it has signed a joint venture agreement with Grain Red S.A., to open stores throughout Chile. The new joint venture, Sur-Andino Cafe S.A., plans to open the first Starbucks retail store in the capital city of Santiago during the second half of this year.

Chile marks the first South American market for Starbucks following its successful entry into Latin America with store openings in Puerto Rico and Mexico in September of last year. "Starbucks is proud to have found an outstanding associate, Grain Red, who not only has expertise in the local marketplace, but also shares our business principles and people values", said Julio Gutiérrez, President of Latin America, Starbucks Coffee International.

"Our entry into Chile represents an important milestone for Starbucks expansion into Latin America. We plan to grow our business in Chile by earning the trust and respect of our customers, one cup at a time". In addition to Chile, Mexico and Puerto Rico, Starbucks is actively exploring opportunities in Argentina, Brazil, Central America, Colombia and Venezuela.

"We share the enthusiasm of our Starbucks partners in bringing to Chile the warmth of Starbucks unique and special coffee experience", said Domingo Castaño, Chairman, Grain Red. "Chile's excellent economic and social climate offers great opportunities for Starbucks. Its increasingly cosmopolitan and educated consumers will value the very special relationships that the Starbucks Experience can offer, inspiring great coffee moments in our stores, and becoming an integral partner in the local community".

Business Wire, May 14

INTEL, CODELCO TO CREATE IT LAB FOR MINING SECTOR

US-based microchip manufacturing giant Intel and Chile's state owned Copper miner

Codelco signed a letter of intent to cooperate on e-business initiatives, including the creation in Chile of an IT solutions center for the mining sector, IT Manager at Codelco, Didier de Saint Pierre told *BNamericas*. The executive said the project will be operated by Intel Capital, the investment division at the chipmaker, and will have the characteristics of a joint venture between the two parties.

The lab will focus on the development of specific IT solutions for the mine production process, with possible applications including solutions for the planning of production and administration of reserves. Local software makers are participating in the project also. "We have spoken with them, and they have shown to be very enthusiastic about the project, especially the joint venture model", he said. Over the long term the project aims to commercialize solutions developed locally for export to other countries in Latin America. Chile's Economic Development Agency, Corfo, has shown an interest in the project, as it also sees Chile as being a base for exports of mining applications to the rest of the region. According to de Saint Pierre, the goal for end of this year is to define the total cost of the project, and launch it at the beginning of 2004. Codelco is the world's largest copper mining company, with copper production of 1.52Mt for 2002.

Business News Americas, June 10

BUSINESS SEMINAR IN DUBLIN

We invite you to participate at a business seminar entitled "Chile- A Springboard into New Markets: Opportunities in the IT & Services Sector", which will feature a keynote speech by H.E. President Ricardo Lagos. The event will take place on Friday, July 11, at the Merrion Hall in Strand Road, Dublin.

The seminar is being organized by Enterprise Ireland in association with Prochile. It will also feature a presentation with an update of the Chilean economy by Minister of Finance, Nicolás Eyzaguirre.

If you wish to attend this seminar, please contact: Mr Alan Buckley at Enterprise Ireland (alan.buckley@enterprise-ireland.com)

CHILE KICKS OFF THE GLOBAL CARBON MARKET

Chile, along with the World Bank and the group of six governments and the 17 companies that make up the Prototype Carbon Fund (PCF), announced a landmark event in the fight against climate change. The Chacabuco run-of-river hydropower project, high in the Chilean Andes is delivering more than electricity: The project is putting Chile into the history books with the first ever, verified greenhouse gas emission (GHG) reductions in the developing world, intended for the Clean Development Mechanism (CDM) of the Kyoto Protocol.

The CDM will allow industrialized countries and companies with greenhouse gas reduction commitments, to purchase some of their required reductions, in developing countries. Chacabuco opens a new era of possibilities for Chile and other developing countries, in which reductions in greenhouse gases are exchanged for development dollars. The project demonstrates the potential and value of the CDM as a powerful development tool for Latin America.

“By selling emission reductions to developed countries, Chile is entering fully the international market of environmental cleansing. That will enable the national private sector to access resources to improve their technologies and introduce clean technologies”, said Gianni López, Executive Director, of Chile’s CONAMA, the National Commission for Environment. “Throughout the world, there is growing demand for these type of emission reductions. This opens great possibilities for Chile, a country with low risk rating for investments, compared with other similar nations. Chacabuco is the first success story”.

Latin America has already demonstrated their attractiveness to the newly emerging carbon market. Thirty percent of the Prototype Carbon Fund’s 2003 portfolio is located in the region. The driving force is the Kyoto Protocol, which commits industrialized countries to reduce their carbon emissions by 5% below 1990 levels in the period from 2008 to 2012. Companies can supplement their commitments at home by purchasing lower

cost emissions in developing world countries. As a result, projects in developing countries will get a new source of financing for sustainable development in the energy, industrial and waste management sectors, land rehabilitation, and clean technologies. Industrialized countries can meet part of their Kyoto obligation, while the threat of climate change is reduced at lower overall cost.

Six governments and 17 companies teamed up with the World Bank in 2000, and contributed US\$ 180 million to create the PCF. It has so far purchased or plans to buy about US\$ 110 million of greenhouse gas emission reductions from 26 projects in developing countries. “It is amazing to see how this result has been obtained by continuing and converging efforts of people all around the world, from Japanese companies to European governments and World Bank Staff, and so many people here in Chile and Latin America”, said Jean Claude Steffens, Chairman of the Participants’ Committee of the PCF.

The prototype fund is showing that emission reductions can be cost-effectively created, verified and certified via investment projects, despite the business risks. In Chacabuco’s case, the 26-megawatt, run-of-the-river plant near Los Andes is scheduled to deliver one million tons of carbon dioxide emission reduction credits to the PCF participants, and the power company, Hidroeléctrica Guardia Vieja is forecast to receive US\$ 3.5 million in return. The current independent verification by the German company TUV has documented that 112 thousand tons of carbon emission reductions can be sold to the PCF from Chacabuco’s first year of operation. In parallel to the PCF, the Japanese corporation Mitsubishi has committed to purchase 100 thousand tons of carbon dioxide emission reductions from Chacabuco.

“The World Bank is catalyzing a market in which private capital can flow from OECD countries to developing countries for clean technologies and for development that is sustainable”, said Axel van Trotsenburg, World Bank Country Director for Chile. “The work of the PCF and the real life example of Chacabuco shows how the Bank can help make markets work for global public goods through private capital. This not just a win-win situation, it is a

triple win, for the private sector, for the environment, and for the people of Chile. This project is proof it can happen”.

Five years after it started, the global carbon finance market-providing credits for reductions in greenhouse gas emissions- is approaching the half-billion dollar level in cumulative trade value. It is expected that the JI/CDM carbon market will exceed one billion dollars a year by 2008. Yet right now most developing countries are missing out on the benefits of carbon finance dollars. The Bank’s responsibility is to make sure that an equitable share of this money, much of it private sector, ends up in the hands of the poorest, in the poorest areas of developing countries.

World Bank (press release), June 17

EFE LAUNCHES TENDER PROCESSES

Chile’s state-owned rail company EFE has launched the tender processes for four contracts that fall under its 2003-2005 investment plan, with bidding rules available June 26 through July 3 (www.efe.cl). The contracts are for the supply and installation of rail crossing protection barriers for the Alameda-Chillán and San Rosendo-Talcahuano (Region VIII) stretches; the supply of tracks and track laying equipment for the Talagante-Barrancas stretch; rehabilitation of 114 km of the Temuco-Mariquina (Region IX) line; and rehabilitation of 295 km of the Chillán-Temuco line.

In April, credit rating agencies Fitch Ratings and Humphreys gave their AAA classification to a planned US\$ 91 million bond issue by EFE due to a government guarantee of the issue. Almost half that amount will go to projects left over from EFE’s 2000-2002 investment plan, as well as its 2003-2005 investment plan. The remainder will help finance Region V metro company Merval’s US\$ 300 million, Stage 4 expansion project. EFE president Luis Ajenjo said earlier this year that at least US\$ 150 million will be invested in 2003-2004, as part of the 2003-2005 plan. Extending service to southern Region X’s principal cities (regional capital Puerto Montt, Valdivia and Osorno) is the plan’s main focus.

Business News Americas, June 26

ESSBIO OPENS LOS ANGELES WASTEWATER PLANT

Chile's Region VIII water utility Essbio has opened a US\$ 17 million wastewater plant built by France's Ondeo Degremont that will benefit 140,000 residents in the city of Los Angeles. According to Eduardo Verdugo, General Manager of Thames Water Latinoamerica (Essbio's parent), some US\$ 200 million will be spent in the region in the next four years. He highlighted the fact that wastewater treatment coverage has increased to 76% from 6% in 2000, and that the goal is to increase treatment to 95% by 2006.

In February, the utility began operations at its US\$ 45 million Bío-Bío wastewater treatment plant at port city Talcahuano, also built by Ondeo Degremont. Essbio posted some US\$ 21.6 million net profit in 2002, up 140% from the previous year and sales increased 68%. The positive results were due to a rates adjustment and increased wastewater treatment revenues. Essbio serves 1.56 million residents with 99.3% drinking water coverage and 86.8% sewerage coverage.

Business News Americas, June 2

THE RITZ-CARLTON, SANTIAGO: FIRST SOUTH AMERICAN LOCATION FOR LUXURY HOTEL COMPANY

The 205-room Ritz-Carlton, Santiago, opened on June 4. Located in Chile's capital city, this first Ritz-Carlton in South America offers corporate and leisure travelers a prime

fashionable address on Apoquindo Avenue in the area known as Las Condes, adjacent to the "Mayor's House".

"We have been looking for the perfect opportunity for Ritz-Carlton to enter the South American market, especially with the growth of customers from the region to our hotels in the Caribbean and now in Miami", said Simon Cooper, President and Chief Operating Officer, The Ritz-Carlton Hotel Company, L.L.C. "Santiago offers the perfect location to enter a cosmopolitan destination while providing convenient access to many recreational and cultural attractions in and around the city".

Designed in classic European style, the 15-story boutique hotel, with a brick exterior and terraced plantings, follows in the elegant tradition of many Ritz-Carlton hotels around the world. The main lobby features a two-story rotunda, with floor to ceiling windows overlooking the plaza. Throughout the interior, flooring of imported marble, inlaid with Mediterranean black/gold/cream inlay, and walls of light mahogany distinguish the décor. A fireplace, lobby and wine bar -featuring the finest Chilean vintages- create a welcoming atmosphere for arriving guests. A Mediterranean restaurant, decorated in Chilean blue lapis center table stone, will serve three meals daily and includes a terrace for outdoor dining.

Guestrooms and suites at The Ritz-Carlton, Santiago will feature floral designs in warm shades of blues, reds and greens. Plush fabrics of silk and brocade, and custom-made South American furnishings, will blend with modern in-room conveniences, including high-speed Internet access. Club level rooms, on floors 9-11, offer guests an extra level of comfort and

privacy. Accessible only by elevator key, these rooms feature upgraded amenities. The Club lounge includes food and beverage presentations throughout the day, and the services of a multi-lingual concierge staff.

For meetings and special events, The Ritz-Carlton, Santiago provides a 3,500-square-foot ballroom with 13-foot ceilings, divisible into three sections. Two large meeting rooms provide ample pre-function space. At the top of the rotunda, five additional rooms are available for smaller groups. The rooftop of The Ritz-Carlton, Santiago features a glass-enclosed fitness center and spa. Windows overlook panoramic views of the city and the nearby, snow-capped Andes Mountains.

The Ritz-Carlton Hotel (press release), June 4

EXECUTIVE SALARIES AMONG THE MOST COMPETITIVE IN LATIN AMERICA

Managerial salaries in Chile are among the most competitive in Latin America, according to the latest annual research published by *AméricaEconomía* magazine.

The study covers monthly salaries, including bonuses, in Argentina, Bolivia, Brazil, Chile, Colombia, Ecuador, Paraguay, Peru, Uruguay & Venezuela. On the other hand, the study focused on the following managerial positions: General Manager, Finance, Information, Production, Marketing and Human Resources.

Surveyed companies were divided according to sales, ranging from US\$ 199 million (first group), and US\$ 200 to US\$ 500 million (second group).

EXECUTIVE SALARIES IN LATIN AMERICA

(US\$ monthly, firms with annual sales of US\$ 50- US\$ 199 million)

	Argentina	Brazil	Chile	Colombia	Ecuador	Mexico	Peru	Uruguay	Venezuela
General Manager	7,020	15,568	7,519	5,802	12,188	21,742	10,040	4,440	5,314
Marketing Manager	4,187	6,762	5,084	5,881	3,874	13,416	5,188	-	5,473
Finance Manager	5,050	7,953	4,724	6,183	3,014	13,953	4,559	2,337	6,218
Production Manager	4,515	7,449	4,606	8,111	3,897	13,036	4,447	-	5,905
Information Manager	2,934	7,707	4,079	5,741	2,661	8,971	4,375	-	4,205
Human Resources Manager	3,828	5,829	4,777	6,863	2,619	12,499	4,253	2,016	3,935

EXECUTIVE SALARIES IN LATIN AMERICA

(US\$ monthly, firms with annual sales of US\$ 200- US\$ 500 million)

	Argentina	Brazil	Chile	Colombia	Ecuador	Mexico	Peru	Uruguay	Venezuela
General Manager	13,123	18,354	9,882	5,545	21,439	24,897	10,822	4,027	7,936
Marketing Manager	4,574	7,463	6,880	5,597	7,921	18,309	5,400	2,080	6,383
Finance Manager	5,747	9,316	6,523	5,963	7,057	21,005	4,750	2,326	9,884
Production Manager	5,135	7,935	4,856	6,444	7,357	14,244	-	2,228	10,129
Information Manager	3,368	7,884	5,053	-	7,188	16,539	5,729	1,451	7,470
Human Resources Manager	4,542	7,071	5,132	7,530	5,779	18,519	4,579	1,638	5,329

WASTEWATER COVERAGE AT 42.3%, DRINKING WATER QUALITY IMPROVED IN 2002

Chile's wastewater coverage stood at 42.3% in 2002, compared to 39.4% the previous year, the country's waterworks regulator, the SISS, said. The SISS also reported that there are a total of 141 treatment plants in the country, up from 115 systems operating in 2001. During 2002, the SISS carried out a series of tests on all operating national waste treatment plants and determined that plants are operating at 95% capacity. In regard to technology, the regulator added that treatment systems have gone from stabilization lagoons in 1998 to aerated lagoons at present in order to increase treatment capacity and efficiency.

Chile's drinking water quality improved in 2002 in regard to bacteriological, disinfection, physical and chemical requirements, the country's waterworks regulator, the SISS, also said in a statement. Compliance percentage increases per requirement were: bacteriological to 99.9% from 99.7%, disinfection to 100% from 99.8%, physical (for example, opacity) to 98.4% from 97.6% and chemical to 98.9% from 98.8%. The information corresponds to the 19 water utilities that serve 99% of clients in the country's 13 regions.

Business News Americas, May 27

COSTANERA NORTE HIGHWAY PREPARES US\$ 240 MILLION BOND ISSUE

Highway concessionaire *Costanera Norte*, which is building an expressway in Chile's capital Santiago, plans to launch a bond issue of close to US\$ 240 million next semester, according to concessionaire CEO Diego Sabino. Guarantee contracts with Ambac Assurance Corporation and the Inter-American Development Bank, entities that will back the bond issue, should be inked in July, Sabino said. The proceeds from the bond issue would go towards *Costanera Norte's* 30 km expressway (known as the *Costanera*

Norte) that will link Santiago's northeast with the city's west, and is slated to be finished by end-2004. Works are 35% complete.

The project also includes a 4.75 km, US\$14 million extension to connect the expressway with highway Ruta 68 that connects Santiago with Region V port city Valparaíso and neighboring coastal city Viña del Mar. Italy's Impregilo and Chilean companies Tecsa and Fe Grande make up the *Costanera Norte* consortium, which won the 30-year concession in 1999.

Business News Americas, May 28

CHILE LEADS E-READINESS IN LATIN AMERICA

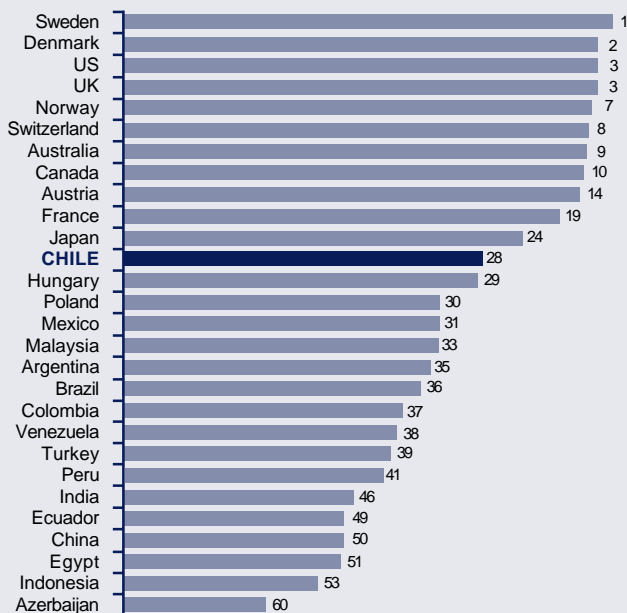
Three years after the dotcom meltdown of 2000, the Internet revolution continues to push forward. In this context, Chile is the most e-ready country in Latin America, according to the Economist Intelligence Unit 2003 e-readiness rankings. Since 2000, the study covers 60 of the world's largest economies and aims to provide a benchmark for countries to compare and assess their e-business environment. "E-readiness" is defined as the extent to which a market is conducive to Internet-based opportunities.

For that purpose, the EIU measures nearly 100 quantitative and qualitative criteria, which are organized into six distinct categories: Connectivity, Business Environment, Consumer & Business, Legal & Policy adoption, Social & Cultural, and Supporting e-services. Although Chile has gone through an economic slowdown, the country emerged as the highest-ranked Latin American nation when it comes to e-readiness, with a 6.3 overall score (in a scale from 1 to 10) reflected in the 28th position in the 2003 edition.

Chile obtained a score of 7.9 in the Business Environment factor, defined by the EIU as the general business climate. In the Legal & Policy adoption criteria (global legal framework and specific laws governing Internet use), the country reached 7.7 points. In Supporting e-services, defined as intermediaries and ancillary services to sustain e-commerce, Chile scored 7.0 while in the Social & Cultural factor (literacy and basic education) the country totaled 6.8 points.

Chile also obtained 5.6 points in the Consumer Business factor (prevalence of e-business practices), and 4.5 in Connectivity, defined as the access that individuals and businesses have to basic fixed and mobile telephony services, personal computers and the Internet.

EIU E-READINESS RANKINGS, 2003



Economist Intelligence Unit (www.eiu.org), May 2003

SPECIAL REPORT: SECOND CAPITAL MARKETS REFORM

MINISTRY OF FINANCE
LAUNCHES SECOND CAPITAL
MARKETS REFORM

Over the past few years, Chile has taken significant steps to improve capital markets regulation. In 2000, a law on tender share offers -known locally as the OPAs law- was passed, addressing the issue of the rights of minority shareholders in listed companies. This was followed in 2001 by a reform of capital markets that sought to increase domestic savings, foster the development of the country's financial markets and, in a bid to reduce firms' costs, increase competition in these markets.

However, a key challenge remained: to improve access to finance for start-up projects developed by innovative entrepreneurs. These projects, which are both the primary expression of private entrepreneurship and the engine of future economic growth, are at the core of the initiative announced on June 23, which aims to ensure that no viable project fail because of lack of finance.

This second capital markets reform, which will soon be presented to Congress, comprises six main elements:

1. DEVELOPMENT OF A
VENTURE CAPITAL INDUSTRY

1.1 Guarantees for Venture Capital Investment Funds: In order to encourage institutional investors to participate in the development of a local venture capital industry, the government's Economic Development Agency (CORFO), in conjunction with the Inter-American Development Bank's Multilateral Investment Fund (MIF), will provide guarantees for debt issued by investment funds. Under this scheme, investment funds will be able to leverage up to twice their capital while their capital and debt will be packaged and offered to investors in such a way that the maximum loss they can incur is capped at one third of the total amount invested. In order to access

these guarantees, investment fund administrators will have to apply for classification.

1.1. Tax Incentives:

a) Capital Gains Tax: Capital gains are generally at their highest during the early stage of a successful project's development and, in order to increase the supply of entrepreneurs with good ideas and solid projects, the proposed reform includes a temporary exemption from capital gains tax. This exemption, which will be subject to some minimum requirements, will be capped at approximately US\$ 240,000.

b) Tax-exempt Earnings: Profits arising from tax-exempt income, distributed to an investment fund's shareholders, will also be exempt from taxation. This measure will eliminate a tax distortion that has discouraged the use of funds as an investment vehicle and favored direct investment in the underlying assets.

2. REDUCTIONS IN
TRANSACTION COSTS

2.1. New Type of Company: The proposed reform will create a new type of company -Limited Liability Corporation- with a dynamic and flexible structure, adapted to the needs of the venture capital industry.

2.2. Assets as Collateral: In a bid to reduce financing costs and to improve market information, the reform includes a new law on the use of assets as collateral, introducing greater flexibility and creating a national register of assets used for this purpose. Experience in Chile shows that small and mid-sized companies depend heavily on the use of collateral and guarantees in order to access financing at competitive costs.

3. IMPROVED CORPORATE
GOVERNANCE STANDARDS

In response to a recent World Bank Report

on Corporate Governance in Chile, the reform seeks to bring Chilean legislation on corporate governance into line with OECD standards. As a result, it includes improvements to existing regulation in areas such as disclosure of information, voting rights, transactions between related parties, insider trading and supervision.

4. IMPROVEMENTS IN SUPERVISION
AND ENFORCEMENT

4.1. Operating Standards: Following the recent collapse of the local Inverlink financial group, a committee was set up to draw lessons from this episode. It proposed a number of initiatives that include Improved control of operational risks and increased levels of transparency in the securities industry; measures to encourage the electronic (rather than physical) issue and trading of high-value securities; higher minimum capital requirements for financial intermediaries; and, increased self-regulation by stock exchanges.

4.2. Entry Requirements: Because financial markets depend on trust and the reputation of their players, instability in one or more institutions can have serious effects on the rest of the economy and this risk is more acute when the products, offered by these institutions, carry a State guarantee. As a result, entry into this market should be subject to strict solvency and competence requirements. In this context, the proposed reform broadens the criteria that will be taken into account by the regulatory authorities, when considering applications for licenses to operate banks, life insurance companies and pension funds (AFPs). In addition, it will increase regulatory powers vis-à-vis changes of control and major stock transactions.

4.3. Crisis Management: One of the most important lessons learned from the Inverlink collapse is that it is imperative to act quickly and effectively to avoid contagion arising from a specific situation of insolvency. As a result, under the proposed reform, a company will no longer be able to obtain a

SPECIAL REPORT: SECOND CAPITAL MARKETS REFORM

stay-of-action on a suspension, ordered by the Securities and Exchange Commission (SVS), simply by filing an appeal to the courts, but will have to obtain a ruling on the appeal. In addition, the reform proposes a mechanism for the intervention of AFPs, as well as measures to speed up the existing mechanism for intervening life insurance companies.

4.4. Coordinated supervision: In order to exercise the appropriate preventive supervision, regulators must have adequate access to information about supervised entities and their main shareholders. To this end, the reform will explicitly authorize the sharing of information by the different regulators, involved in supervising financial markets. In addition, the reform proposes increased solvency requirements for the main shareholders in AFPs and life insurance companies, and will increase the powers of the Banks and Financial Institutions Regulatory Agency (SBIF) to monitor the

activities of bank subsidiaries.

4.5. Coordination between regulatory and supervisory authorities: The role of three coordinating committees -the Superintendents' Committee, the Capital Markets Committee and the Financial Stability Committee- will be strengthened. The latter body has the task of coordinating institutions in order to prevent, detect and resolve situations that represent a threat to the stability of the financial system.

5. IMPROVED VOLUNTARY SAVINGS MECHANISMS

The reform includes mechanisms to complement existing voluntary pension-savings alternatives and will open the way to collective schemes, to which both employers and employees will be able to contribute. Employers' contributions will be considered as an expense that can be deducted from taxable income.

6. UPDATING LEGAL TEXTS

A number of changes are proposed in order to bring legal texts into line with current practice in capital markets.

In summary, the proposed changes are expected to facilitate the development of the venture capital industry, reduce transaction costs, improve the management of corporations, strengthen supervisory mechanisms and facilitate the development of alternative voluntary savings mechanisms. The proposed bill will modernize the Chilean capital market, bringing standards up to current international levels, increasing transparency, competition and the reaction capacity of its agents. The proposed improvements should allow us to build a healthier, credible and solid capital market, further developing one of the fundamental pillars of economic growth.

This second Capital Markets Reform will modify 14 legal texts and the main changes are set out below:

SECOND CAPITAL MARKETS REFORM Summary of Measures

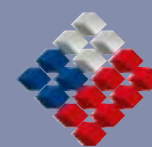
Law	Main Proposed Modifications
1. Income Tax Law (DL 824, 1974)	<ul style="list-style-type: none"> Exemption from capital gains tax for venture capital companies Exemption from capital gains tax on transactions between funds managed by the same administration company Transfer of tax benefits from underlying assets to shareholders in venture capital funds
2. Stamp Tax Law (DL 3,475, 1980)	<ul style="list-style-type: none"> When the value of a securitized bond is higher than that of the underlying assets, only the difference will be liable for taxation In the case of overseas bank loans, the debtor will be responsible for paying withholding tax
3. General Banking Law (DFL 3, 1997)	<ul style="list-style-type: none"> Banks will be allowed to invest the reserve requirement on sight deposits in Central Bank or Treasury securities of any term Banks will be obliged to have a "Customer Defender" The term "sociedades financieras" will be eliminated Formal channels for sharing information among Regulatory Agencies will be created The powers of the SBIF to reject an application for a bank license will be increased The powers of the SBIF to request information from bank subsidiaries will be strengthened
4. Insurance Companies Law (DFL 251, 1931)	<ul style="list-style-type: none"> The arbitration powers of SVS will be increased Insurance companies will be allowed to issue policies in nominal currency Legislation will be adapted in line with Chile's Free Trade Agreements with the US and the EU The SVS will be empowered to request information from a company's controlling shareholders in order to measure their solvency The SVS will be empowered, with the consent of other Regulatory Agencies, to forbid the purchase of stakes of 10% or more in a company The SVS will be empowered to restrict operations between related parties Insurance companies will be required to have a "Customer Defender" Insurance companies will be able to use a larger part of their reserves to provide loans and for other investments that are authorized by the SVS. In addition, new limits will be established for these and other investments

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Summary of Measures**

5. AFP Law (DL 3,500, 1980)	<ul style="list-style-type: none"> • The percentage of securities to be held by an out-house custody service will rise to 100%, up from 90% • AFPs will be allowed to acquire bonds issued by investment funds (this modification is related to the CORFO-MIF program) • AFPs will have to pay value-added tax on voluntary savings schemes, bringing them into line with other institutions offering these schemes • Regulation of voluntary savings mechanisms will be adapted to make them more flexible and competitive • The electronic issue of pension bonds (corresponding to contributions to the old State system) will be permitted • The Pension Funds Administrators' Regulatory Agency (SAFP) will be empowered to request information from a company's controlling shareholders in order to measure their solvency. The SAFP will be empowered, with the consent of other Regulatory Agencies, to forbid the purchase of stakes of 10% or more in a company. The SAFP will be empowered to restrict transactions between related parties and, in the case of a crisis, to appoint provisional management in a pension fund administrator
6. Securities Markets Law (Law 18,045)	<ul style="list-style-type: none"> • Stockbrokers will no longer have to be shareholders in a stock exchange • Controls on insider trading will be tightened and the period for filing claims for damages will be extended to four years, up from one year • Third parties, other than the issuer, will be allowed to register foreign securities • The institution of "guarantor" will be created for syndicated bank loans. A bank will take on this role, accepting guarantees on behalf of both existing and future creditors • Brokers will be obliged to open a special account with the Central Securities Custody Service, if the owners of securities so wish in order to be informed as to the use of their assets. In addition, the conditions that a broker must fulfil, and sanctions for offenses, will be increased
7. Corporations Law (Law 18,046)	<ul style="list-style-type: none"> • A new type of company - the Limited Liability Corporation - will be created to facilitate the formation of small companies and reduce start-up costs • Proxy voting mechanisms will be established in order to facilitate the exercise of minority shareholders' rights • Companies will be allowed to send information to shareholders electronically • Subscribed shares, which have not been paid, will not carry voting rights • The definition of transactions between related companies will be further clarified
8. Investment Funds Law (Law 18,815)	<ul style="list-style-type: none"> • Regulation on dividend and leverage policies will be made more flexible • Investment funds will be allowed to outsource portfolio management • Existing regulation will be adapted to foster the development of investment funds as a vehicle for venture capital
9. Securities and Exchange Commission Law (DL 3,538)	<ul style="list-style-type: none"> • The supervisory powers of the SVS will be strengthened
10. Securities Deposit and Custody Law (Law 18,876)	<ul style="list-style-type: none"> • Custody services will be required to provide information about transactions of securities on the request of their owners • Custody services will be allowed to provide complementary services • Regulation of the electronic issue of commercial paper, and its custody, will be improved • The SVS will be empowered to request information about the charges of custody service and how these are fixed
11. Mutual Funds Law (DL 1,328)	<ul style="list-style-type: none"> • Investment limits per issuer will be increased, and eliminated in the case of index funds • Mutual funds will be allowed to outsource portfolio management • The SVS will be empowered to define procedures in the case of differences in credit ratings. • Tax rules and the regulation of mutual funds' dividend policies will be improved • Mutual funds will be allowed to open checking accounts
12. Housing Funds Law (Law 19,281)	<ul style="list-style-type: none"> • Regulations for House Purchase Saving Funds (AFV), dealing with guarantees, the requirements for directors and capital requirements, will be brought into line with those for mutual, investment and other funds
13. Civil Code and Bankruptcy Law (Law 18,175)	<ul style="list-style-type: none"> • The existence of an order of preference among creditors, presently classified as non-preferred, will be recognized • Derivative contracts, established under a framework agreement, will have to be liquidated when bankruptcy is declared, allowing a firm's liabilities and assets to be automatically corrected
14. A new law of the use of assets as collateral; national register of assets used as collateral	<ul style="list-style-type: none"> • New and comprehensive legislation will be introduced governing the use of non-fixed assets as collateral • The use of stocks, securities and contracts as collateral will be permitted • A national register of assets used as collateral will be created.

Between January and April of 2003, materialized Foreign Direct Investment reached US\$ 441 million, as compared to US\$ 650 million for the same months of 2002. The Foreign Investment Statute (D.L. 600) channeled 62.2% of the inflows. The main recipient sectors were

Electricity, Gas & Water (47.2%), Services (17.8%), Transport & Communications (14.5%), and Mining (13.1%). During those months, materialized FDI came mainly from the US (41.3%), International Organizations (21.9%), Spain (15.6%) and Canada (11.8%).



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FOREIGN DIRECT INVESTMENT REPORT / January - April 2003 (in nominal US\$ million)

Instrument / Period	1992	1993	1994	1995	1996	1997	1998	1999	2000	2001	Jan-Apr 2002	Jan-Apr 2003	Growth rate
Foreign Investment Statute (1)													
-Capital Contributions	894.3	1,544.6	1,802.1	3,948.6	3,825.5	4,382.8	8,606.9	2,541.3	4,320.2	2,243.0	425.1	274.1	-35.5%
-Associated Credits	839.8	976.7	1,238.5	873.3	1,404.3	1,589.9	478.7	436.0	527.5	1,079.1	96.5	0.6	-99.4%
Materialized Investment F.I.S. (D.L. 600)	998.9	1,734.1	2,521.3	3,040.6	4,821.9	5,229.8	5,972.7	9,085.6	2,977.3	4,847.7	3,322.1	521.6	274.7
Chapter XIV (2)													
-Capital Contributions	204.2	410.2	409.5	441.6	920.6	539.3	688.8	735.6	775.2	446.3	128.4	166.7	29.8%
Total F.D.I. Capital Contributions (F.I.S. + Chapter XIV)	1,098.5	1,954.8	2,211.6	4,390.2	4,746.1	4,922.1	9,295.7	3,276.9	5,095.4	2,689.3	553.5	440.8	-20.4%
Total F.D.I. Materialized (Materialized F.I.S. + Chapter XIV)	1,938.3	2,931.5	3,450.1	5,263.5	6,150.4	6,512.0	9,774.4	3,712.9	5,622.9	3,768.4	650.0	441.4	-32.1%
Capital Remittances													
-Foreign Investment Statute (1)	173.2	49.4	392.6	303.4	354.9	119.9	233.9	462.7	674.4	1,708.8	31.1	27.1	-12.9%
-Chapter XIV (2)	0.9	10.1	3.5	30.2	20.6	323.9	47.8	78.7	289.4	32.4	11.8	10.9	-7.6%

(1) Source: Foreign Investment Committee - Chile. Provisional figures as of April 30, 2003.

(2) Source: Central Bank of Chile. Provisional figures as of April 30, 2003.

FOREIGN INVESTMENT UNDER THE FOREIGN INVESTMENT STATUTE (D.L. 600) BY SECTOR 1974 - 2003* (in nominal US\$ million)

SECTOR/PERIOD	MATERIALIZED INVESTMENT									
	74-95	1996	1997	1998	1999	2000	2001	2002*	2003*	Total
Agriculture and Livestock	163	16	14	12	21	22	10	2	0	260
Construction	303	26	114	280	216	29	165	138	10	1,281
Electricity, Gas & Water	93	406	1,395	495	4,560	860	908	490	129	9,336
Fishing and Aquaculture	129	21	12	9	1	94	5	0	2	273
Forestry	133	20	29	37	19	4	1	1	1	245
Industry	2,731	917	593	530	779	191	754	209	8	6,712
Mining	8,558	999	1,705	2,393	1,221	242	1,024	1,935	36	18,113
Services	2,686	1,958	1,197	2,006	1,910	665	700	212	49	11,383
Transport and Communications	906	459	171	211	359	870	1,281	335	40	4,632
TOTAL	15,702	4,822	5,230	5,973	9,086	2,977	4,848	3,322	275	52,235

Note: Materialized investments include amounts authorized each year and in all forms accepted under the Foreign Investment Statute.

Source: Foreign Investment Committee - Chile. *Provisional figures as of April 30, 2003.

MATERIALIZED FOREIGN INVESTMENT UNDER THE FOREIGN INVESTMENT STATUTE (D.L. 600) BY REGION OF ORIGIN 1974 - 2003* (in nominal US\$ million)

REGION	VALUE (in US\$ million)	SHARE
North America	23,575	45.1%
European Union	19,320	37.0%
other European countries	933	1.8%
Pacific Asia and Oceania	3,934	7.5%
other Asian countries	10	0.0%
Central America & the Caribbean	1,578	3.0%
Africa	1,405	2.7%
South America	1,168	2.2%
International Organizations	312	0.6%
TOTAL	52,235	100.0%

Source: Foreign Investment Committee - Chile
*Provisional figures as of April 30, 2003.