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# A Two-Level Game Analysis: Chile under Allende and Its Position within the International Financial System amid the Cold War

Análise de um jogo de dois níveis: a posição do Chile de Allende no Sistema Financeiro Internacional no plano de fundo da Guerra Fria

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**Abstract:** The Chilean experience under Salvador Allende (1970–1973) against the backdrop of a brief period of détente in the Cold War became a model case of the multilateral potential of international financial institutions—particularly the International Monetary Fund (IMF)—and of the contradictions inherent in their relationship with developing countries. The Popular Unity administration played a "two-level game" in its stance toward the International Financial System and its institutions, aided partly by the geopolitical context and partly by Allende's efforts to pursue a financial diplomacy that was both technically grounded and aligned with national interests.

**Keywords:** Chile; Financial Governance; Cold War; International Financial System.
**JEL Classification:** F51

**Resumo:** Entre 1970-1973, no plano de fundo de um breve período de détente na Guerra Fria, o governo de Salvador Allende foi um caso-modelo do potencial multilateral das instituições financeiras internacionais—sobretudo do FMI—e um exemplo daquelas contradições implicadas no relacionamento entre essas instituições e os governos de países em desenvolvimento. A administração da Unidade Popular conduziu um 'jogo de dois níveis' na sua posição diante do Sistema Financeiro Internacional e suas instituições, auxiliado em parte pelo cenário geopolítico e em parte pelos esforços de Allende por uma diplomacia financeira ao mesmo tempo técnica e comprometida com os interesses nacionais.

**Palavras-chave:** Chile; Governança Financeira; Guerra Fria; Sistema Financeiro Internacional.
**Classificação JEL:** F51

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## 1. Introduction

On September 4, 1970, Salvador Allende, candidate of the Socialist Party, won the Chilean presidential election over Jorge Alessandri by a narrow margin of just 1.34%, setting the country on a constitutional path toward socialism. Against the backdrop of a brief period of détente in the Cold War, yet still facing persistent U.S. hostility toward any potential socialist advances in South America—where Washington sought to contain Soviet influence through governments aligned with its own strategic designs—and despite the U.S. "campaign of fear" against Allende, in which at least 500,000 dollars were invested[2], the governing coalition of Popular Unity (UP – *Unidad Popular*) rose to power in Chile.

Only a year later, in August 1971, President Richard Nixon suspended the convertibility of the U.S. dollar into gold, effectively ending the Bretton Woods Agreement. For over two decades, that system had ensured a degree of stability for the International Financial System (IFS) and exchange rates in a context characterized by low and cautious capital mobility, the adoption of financial regulatory policies, and, above all, the pursuit of privileged positions by the United States—which had made its strong currency the international unit of reference in global geopolitics.

Given the expansion of U.S. public spending and the newly inaugurated "financial deregulation" of the IFS, the role of international financial institutions, particularly the International Monetary Fund (IMF), entered a phase of natural uncertainty and required a redefinition of their activities. The IMF reoriented itself toward a consultative role, with IMF technocrats sent on diagnostic and advisory missions in economically vulnerable countries—frequently primary-exporting and heavily indebted economies with weak institutional frameworks and an urgent need for international loans.

The political and economic situation of Latin American countries in the 1970s was precisely the kind of environment that fit the scope of the IMF's technical efforts, since

> The World Bank, in particular, and the regional development banks, have since the 1960's dazzled third world leaders with irrefutably logical arguments on borrowing through promising development aid programmes. Leaders of Third World countries, including Latin America, were therefore convinced by this ideology of credit-based development. In essence, foreign debts were incurred with the hope that such would aid their economic development. (Aremu, 2018, p. 76)

[2] According to an official report by the U.S. Central Intelligence Agency (CIA), a secret budget had been authorized by the American government to prevent Allende's election and subsequently undermine his administration: "On June 18, 1970, [U.S.] Ambassador Edward Korry submitted a two-phase proposal to the State Department and the CIA for review. The first phase involved increased support for the anti-Allende campaign. The second was a contingency plan of $500,000 to influence the congressional vote in the event of a runoff between the first- and second-place candidates" (U.S. Government Staff Report, 1975, author's translation).

Loans granted by the United States and by commercial banks to Latin American countries increased dramatically from the 1970s onward, following the oil shocks and the "secret agreement" between the Nixon administration and Saudi Arabia, which established that oil could only be traded in dollars. Torn between internal economic contradictions and their inability to meet financial obligations—given the already overwhelming volume of development loans—Latin American nations faced growing political resistance to the expanding influence of international financial institutions and their economic-assistance programs, especially those offered conditionally by the IMF. As Kedar (2015, p. 721, author's translation) notes,

> Latin American states strove to avoid conditional IMF loans and instead signed politically less controversial agreements with other creditors such as the Inter-American Development Bank (IDB), the Export-Import Bank, and commercial banks, thereby reducing the Fund's involvement in the region.

Confronted with the prospect of losing their conditional influence over the Southern Cone and other Latin American economies—and faced with the added challenge of a socialist party's victory despite U.S. efforts to prevent it—the agents of international financial governance, particularly the IMF and the World Bank, whose objectives were closely aligned with core U.S. interests, recognized the need to expand their scope of action and engage pragmatically with Chile's new government.

Against the backdrop of the Cold War and the perceived threat of Soviet expansion, Allende's Chile occupied a position within the IFS that can be described as a "two-level game." Domestically, the UP administration had to strive to maintain its democratizing and socializing plans for a centralized government while simultaneously remaining in good standing with its international creditors—for which IMF support was essential. From the standpoint of international financial institutions and U.S. interests in containing the socialist tide in Latin America, relations with Chile needed to encourage the restoration of their political and economic influence over the government's administrative decisions in order to safeguard the country from a "Soviet fate."

## 2. Allende's Chile: A Brief Economic Profile

Until the Great Depression, Chile's economic structure was favorable to international trade, with few restrictions or tariffs on the free exchange of imported goods. Beginning in the 1930s, however, the government launched an import-substitution industrialization program, following the trend of other Latin American countries undergoing late development. The peak of this developmentalist model, which sought to diversify Chile's export portfolio, occurred during Allende's presidency between 1970 and 1973.

Nevertheless, the crown jewel of the Chilean economy—and its most profitable export— was to be found in the extractive sector: copper[3]. According to a case study by Conway (2001), Chile accounted for 25% of total world copper production in 1966. By 1970, at least 87% of Chilean exports to the U.S. market consisted of copper ore, refined copper, and iron ore, representing a significant source of U.S. dollar revenue in the country's trade balance (Conway, 2001).

Allende's government inherited from its predecessor a "high level of international reserves," and "significant momentum had been achieved in the growth of exports beyond copper." The offset, however, was Chile's external debt. The liabilities accumulated in previous years had reached 21 million dollars in Special Drawing Rights (SDRs) with the IMF—and, throughout 1971, the sharp decline in copper prices, which represented a loss of 140 million U.S. dollars in Chilean exports (World Bank, 1980).

In a historical reconstruction of Chile's economy between 1960 and 2017, Saraiva and Caputo (2018, p. 2) identify a balance-of-payments crisis in 1962 and, in 1973, the onset of a hyperinflationary scenario. This period in the country's economic history involved growing interactions and negotiations between Allende's government and international financial institutions—most notably agreements with the IMF and the renegotiation of external debt with the Paris Club—as well as U.S.-imposed restrictions on the Chilean economy and a rapid increase in the fiscal debt of the UP government as part of its centralized development plan based on public spending.

The IMF's presence—through technical and financial assistance and as an influence within the international community via formal and informal missions to Chile—was fundamental in facilitating agreements between Allende and other agents of International Financial Governance. Although the Chilean government adopted a cautious stance toward financial assistance from international institutions, particularly in avoiding the administrative conditions attached to agreements that ran counter to the nature of its administration, the Fund played an essential role in renegotiating Chile's debt and in creating a stabilization plan for the national currency.

The relationship between Allende's Chile and international institutions—and the country's position within the dynamics of the IFS, particularly regarding its economic leverage—was, however, severely undermined and weakened by the interplay of interests within Cold War international politics. Despite its limited and developing economy, and its lack of significant political influence in international governance, Chile stood on the opposite side of the hegemonic power in its governmental choices. The United States, determined to curb the advance and growth of socialist governments in Latin America, sought to use its vast influence over international financial mechanisms to undermine the governability of the UP administration. Responsibility therefore lay with the international institutions—although under pressure from Washington—to decide whether their

[3] In the first quarter of 2024, exports of "copper concentrate" yielded Chile a surplus of 1.096 billion U.S. dollars, according to the Foreign Trade Indicators Report of the Central Bank of Chile.

relationship with the Chileans would remain pragmatic or align with the ideological objectives of the North.

## 3. Chile and the International Financial System: In the Crosshairs of U.S. Influence

One of the most consequential and politically sensitive economic measures proposed by Allende's administration was the nationalization of industrial assets, which primarily included the highly profitable copper extraction and refining activities that were central to Chile's economic interests. According to a World Bank report[4],

> The immediate economic objectives of the Allende government, which took office in November 1970, were to reactivate the economy, early progress toward the establishment of direct state control over those sectors whose resources and functions were considered essential for fulfillment of the Government's development plan, an increase of the wage share of national income, acceleration of the agrarian reform set in motion by [Eduardo] Frei, and to reduction of the rate of inflation.

Within the context of the Cold War, the adoption of this set of nationalizing and centralizing administrative measures represented, for the United States, a clear warning sign of a substantial loss of its sphere of influence in the Southern Cone. The pressure exerted by the U.S. government on the Chilean economy began as a strategy to withdraw its investments from Chilean territory, as indicated in a U.S. government report[5]:

> Following the September 4 elections, the United States government adopted a policy of economic pressure directed against Chile [...]. Specifically, the State Department was directed by the 40 Committee to contact American businesses having interests in Chile to see if they could be induced to take *actions in accord with the American government's policy of economic pressure on Chile*.

The report also mentions a case assessment conducted by the CIA in 1971, which indicated that Chile was not, at least in the short term, vulnerable to direct sanctions—whether monetary, investment-related, or commercial—imposed by the United States. Such sanctions, the document continues, "while it would hurt Chile eventually, was seen to carry one possible short-run benefit-it would have given Chile a justification for renouncing nearly a billion dollars of debt to the United States[6]." Therefore:

[4] Excerpt from the World Bank case study: Chile: An Economy in Transition (1980, p. 62).

[5] Excerpt from the official report of the U.S. Government Operations Committee: Covert Action in Chile: 1963–1973 (1975, p. 13, emphasis added).

[6] Covert Action in Chile: 1963–1973, 1975, p. 33.

> The policy of economic pressure—articulated in NSDM 93[7] of November 1970—was to be implemented through several means. *All new bilateral foreign assistance was to be stopped* [...]. *The United States would use its predominant position in international financial institutions to dry up the flow of new multilateral credit or other financial assistance* (idem, p. 33).

According to NSDM 93, U.S. external conduct would involve "vigorous efforts" to ensure that Latin American governments understood Washington's opposition to the establishment of a communist regime in Chile, as well as to encourage other regional governments to adopt a similar stance and to coordinate joint countermeasures with Brazil and Argentina. Regarding specific actions to be taken within the realm of International Financial Governance, which was the main focus of the sanction regime, the document prescribed[8]:

> a. exclude, to the extent possible, further financing assistance or guarantees for U.S. private investment in Chile, including those related to the Investment Guarantee Program or the operations of the Export-Import Bank;
> b. determine the extent to which existing guarantees and financing arrangements can be terminated or reduced;
> c. **bring maximum feasible influence to bear in international financial institutions to limit credit or other financing assistance to Chile** (in this connection, efforts should be made to coordinate with and gain maximum support for this policy from other friendly nations, particularly those in Latin America, with the objective of lessening unilateral U.S. exposure); and
> d. assure that U.S. private business interests having investments or operations in Chile are made aware of the concern with which the U.S. Government views the Government of Chile and the restrictive nature of the policies which the U.S. Government intends to follow.

Thus, the International Financial System and its institutions became weapons in the U.S. policy of intimidation. As the CIA report shows, U.S. bilateral aid to Chile fell from 35 million U.S. dollars in 1969 to 1.5 million in 1971 (as shown in the table below), while the credit provided by the U.S. Export-Import Bank—amounting to 234 million U.S. dollars in 1967—was reduced to zero by 1971.

**Figure 1: U.S. and International Institutions' External Assistance to Chile—Total Loans and Grants (in millions of U.S. dollars)**

[7] The document refers to National Security Decision Memorandum 93, prepared by the U.S. National Security Council on November 9, 1970, to outline the American foreign-policy strategy toward Chile. The memorandum sought to enable the government to "limit [Chile's] ability to implement policies contrary to U.S. interests in the hemisphere."

[8] Excerpt from National Security Decision Memorandum 93 (1970, p. 2, emphasis added).

| Fiscal year | 1953–61 | 1962 | 1963 | 1964 | 1965 | 1966 | 1967 | 1968 | 1969 | 1970 | 1971 | 1972 | 1973 | 1974 |
|---|---|---|---|---|---|---|---|---|---|---|---|---|---|---|
| Total U.S. economic aid | 339.7 | 169.8 | 85.3 | 127.1 | 130.4 | 111.9 | 260.4 | 97.1 | 80.8 | 29.6 | 8.6 | 7.4 | 3.8 | 9.8 |
| U.S. AID | 76.4 | 142.7 | 41.3 | 78.9 | 99.5 | 93.2 | 15.5 | 57.9 | 35.4 | 18.0 | 1.5 | 1.0 | .8 | 5.3 |
| U.S. Food for Peace | 94.2 | 6.6 | 22.0 | 26.9 | 14.2 | 14.4 | 7.9 | 23.0 | 15.0 | 7.2 | 6.3 | 5.9 | 2.5 | 3.2 |
| U.S. Export-Import Bank | 169.0 | .8 | 16.2 | 15.3 | 8.2 | .1 | 234.6 | 14.2 | 28.7 | 3.3 | | 1.6 | 3.1 | [1] 98.1 |
| Total U.S. Military aid | 41.8 | 17.8 | 30.6 | 9.0 | 9.9 | 10.1 | 4.1 | 7.8 | 11.8 | .8 | 5.7 | 12.3 | 15.0 | 15.9 |
| Total U.S. economic and military aid | 381.5 | 187.6 | 115.9 | 136.1 | 140.3 | 122.0 | 264.5 | 104.9 | 91.8 | 30.4 | 14.3 | [2] 21.3 | [2] 21.9 | [2] 123.8 |
| Total international organizations [3] | 135.4 | 18.7 | 31.2 | 41.4 | 12.4 | 72.0 | 93.8 | 19.4 | 49.0 | 76.4 | 15.4 | [2] 8.2 | 9.4 | 111.2 |
| IBRD (World Bank) | 95.2 | | | 22.6 | 4.4 | 2.7 | 60.0 | | 11.6 | 19.3 | | | | 13.5 |
| Inter-American Development Bank (IDB) | 5.7 | 15.1 | 24.4 | 16.6 | 4.9 | 62.2 | 31.0 | 16.5 | 31.9 | 45.6 | 12.0 | 2.1 | 5.2 | 97.3 |

[1] Includes Ex-Im: 57.0 and other: 41.1.
[2] Total per chart plus Export-Import Bank.
[3] U.S. contributions to I.O.'s included above; therefore U.S. aid and international aid should not be added together.

Source: U.S. Overseas Loans and Grants, Obligations and Loan Authorizations, July 1, 1945 to June 30, 1971, pp. 40, 179; and July 1, 1945 to June 30, 1974, pp. 39, 175. Prepared by Statistics and Reports Division, Office of Financial Management, Agency for International Development.

Source: Covert Action in Chile: 1963- 1973, 1975, p. 34.

The United States also exercised its veto power in decisions regarding loans granted by the IDB, reducing its aid to Chile by 44 million U.S. dollars. During the Allende administration, total assistance from the IDB amounted to only 2 million U.S. dollars. The World Bank—an institution primarily financed by the United States and anchored in the dollar regime—did not approve any new loans to Chile throughout the 1970–1973 period.

The IMF, on the other hand, followed the opposite trend, granting Chile 90 million U.S. dollars in assistance to address its external debt difficulties. What might explain this behavior, given the determination with which the U.S. government sought to restrict international financial aid to the country? And what internal contradictions are implied in this movement, considering the conflicting interests of Allende's government, whose economic objectives diverged from those traditionally prescribed by the Fund's technical staff?

## 4. Chile vs. the International Monetary Fund: Bucking the IFS Trend

As previously discussed, Allende's position within International Financial Governance was constrained from the outside by the geopolitical influence of the United States and the dominance of the dollar over the IFS. Although his government was staffed with technocrats, pragmatic strategists, and intellectuals with experience in mainstream economic policy—often trained in Anglo-Saxon institutions—Allende's "financial diplomacy" was bound by the anti-imperialist and nationalist character of his administration, which sought to distance itself from the financial and economic control exerted by international institutions such as the IMF.

The UP government program made this stance explicit from the outset (p. 6), expressing its view on the control exercised by U.S. imperialism over Chile's national economy through monetary and financial instruments, and particularly through the agency of institutions created under the aegis of the dollar:

> U.S. monopolies, with the complicity of bourgeois governments, have seized almost all of our copper, iron, and nitrate. They control foreign trade and dictate economic policy through the International Monetary Fund and other organizations.

Dancing to the rhythm of the IFS—as a Third World and predominantly primary-exporting country—meant adopting hegemonic interests, bringing them closer, and integrating them into the government's own agenda. This was the central dilemma of Chile's two-level game. Domestically, the UP coalition needed to secure its government program on democratic and nationalizing grounds, focused less on the rapid expansion of reserves and national income than on their fair distribution—that is, less concerned with dollar tutelage and financial diplomacy than with ensuring the conditions for a swift and assertive transition toward state socialism[9]. To create the fundamental conditions for implementing its program and exercising effective governance, however, Allende was compelled to consider the external environment and take into account the international conditions for financing.

The historical trajectory of Chile—like that of other late-developing nations of the Global South—has been marked by a persistent tendency toward external indebtedness and reliance on financial assistance to accelerate the development of key sectors of the economy. These factors, combined with the structural vulnerabilities of its trade balance—highly sensitive to commodity price fluctuations, as in the case of copper—pushed the country toward conditional international agreements. As Kedar (2015, p. 722, author's translation) notes, "since 1950, the IMF had played an influential role in Chile's economy, granting it loans that paved the way for complementary credits from other lenders."

The table below illustrates the flow of SDRs allocated to Chile during the 1950s and 1960s, with a gap between April 1969 and January 1975 marking the period between the UP government and its successor:

[9]According to Caputo and Saravia (2019, p. 11), the Allende government assumed that in 1970 "there was substantial underutilized capital capacity in the manufacturing sector. The fiscal deficit, as a percentage of GDP, rose from 0.5 percent in 1970 to 7.3 percent in 1971. In this context, it was expected that an increase in aggregate demand could be accommodated without generating inflationary pressures in the short run. As a result, in 1971 an aggressive expansionary fiscal policy was implemented. The fiscal deficit, as a percentage of GDP, rose from 0.5 percent in 1970 to 7.3 percent in 1971 [...]". The government therefore implemented an expansionary fiscal policy to increase wages and boost consumption.

**Figure 2: History of IMF Loan Agreements with Chile (in thousands of SDRs)**

| Facility | Date of Arrangement | Expiration Date 4/ | Amount Agreed | Amount Drawn | Amount Outstanding |
|---|---|---|---|---|---|
| Short-Term Liquidity Line | May 20, 2022 | May 19, 2023 | 2,529,000 | 0 | 0 |
| Flexible Credit Line | May 29, 2020 | May 19, 2022 | 17,443,000 | 0 | 0 |
| Standby Arrangement | Nov 08, 1989 | Nov 07, 1990 | 64,000 | 64,000 | 0 |
| Extended Fund Facility | Aug 15, 1985 | Aug 15, 1989 | 825,000 | 806,250 | 0 |
| Standby Arrangement | Jan 10, 1983 | Jan 09, 1985 | 500,000 | 500,000 | 0 |
| Standby Arrangement | Mar 19, 1975 | Mar 18, 1976 | 79,000 | 20,000 | 0 |
| Standby Arrangement | Jan 30, 1974 | Jan 29, 1975 | 79,000 | 79,000 | 0 |
| Standby Arrangement | Apr 19, 1969 | Apr 18, 1970 | 40,000 | 20,000 | 0 |
| Standby Arrangement | Mar 01, 1968 | Feb 28, 1969 | 46,000 | 46,000 | 0 |
| Standby Arrangement | Mar 01, 1966 | Feb 28, 1967 | 40,000 | 40,000 | 0 |
| Standby Arrangement | Jan 06, 1965 | Jan 05, 1966 | 36,000 | 36,000 | 0 |
| Standby Arrangement | Feb 14, 1964 | Jan 05, 1965 | 25,000 | 20,000 | 0 |
| Standby Arrangement | Jan 15, 1963 | Jan 14, 1964 | 40,000 | 40,000 | 0 |
| Standby Arrangement | Feb 16, 1961 | Feb 15, 1962 | 75,000 | 60,000 | 0 |
| Standby Arrangement | Apr 01, 1959 | Dec 31, 1959 | 8,100 | 700 | 0 |
| Standby Arrangement | Apr 01, 1958 | Mar 31, 1959 | 10,000 | 4,400 | 0 |
| Standby Arrangement | Apr 01, 1956 | Mar 31, 1958 | 35,000 | 25,000 | 0 |
| | | Total | 21,874,100 | 1,761,350 | 0 |

Source: International Monetary Fund.

In addition to SDRs—financial assets backed by the U.S. dollar—the most significant IMF loans granted to Chile took the form of Stand-By Arrangements (SBAs)[10] which, according to the institution's Factsheet (IMF, 2016, p. 1, emphasis added), once activated, entail "adjustments in economic policy as recommended by the IMF": "The commitments undertaken by the country, encompassing specific conditionality, are described in the country's letter of intent (which generally includes a memorandum of economic and financial policies)." Access to SBAs also involves the adoption of quantitative targets as performance criteria, including "*targets for international reserves* and *for the state's deficit or indebtedness*, in line with the program's objectives," as well

[10] According to the IMF's Factsheet (2016, p. 1), "the SBA framework allows the Fund to respond flexibly to member countries' external financing needs and to support policies designed to help them overcome crisis and return to a sustainable growth path." SBAs are "the most widely used credit instrument for emerging market and advanced economies," and "any member country facing external financing needs can benefit from Stand-By Arrangements, subject to the Fund's policies."


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as structural performance measures “considered critical for achieving the program’s goals” and “assessed in a holistic manner.”

> Unlike ordinary loans, the drawings under a stand-by arrangement were not disbursed in a single installment, but in tranches, with the loan being “on stand-by” between them. Progress from one tranche to another, or the right to continue drawing, was conditional on the borrower’s ability to meet the Fund’s requirements. (Kedar, 2015, p. 723, author’s translation)

Over the previous decades, SBAs had become the IMF’s standard policy instrument toward Latin American countries, having been employed as

> dominant lending mechanism for developing nations. Countries such as Argentina, Bolivia, Brazil, Chile, Peru, and Uruguay frequently adopted them to support stabilization plans designed, among other purposes, to resolve balance-of-payments problems and contain inflation. (Kedar, 2015, p. 724)

Moreover, they constituted a technical channel through which instruments of international financial governance imposed the U.S. economic agenda, aligning domestic economic policies with the principles of the dollar-based IFS.

During the previous decade, Chile had undergone three episodes of external-debt restructuring, “implemented through International Monetary Fund programs in 1961 and in 1963 to 1965” (Caputo; Saravia, 2019, p. 10). By 1969, however, the country’s external debt had already reached 22% of GDP. As Caputo and Saravia (2019, pp. 6-8) explain:

> “The persistent inflation in the 1960s was, as in the previous periods of Chilean history, closely related to fiscal deficits and wage indexation. [...] During the 1960s, the fiscal authority mainly had access to foreign debt, which increased from 10 percent of GDP in 1960 to 22 percent in 1969.”

By 1970, Allende had inherited an external debt amounting to 3.1 billion U.S. dollars (Kofas, 2002 *apud* Kedar, 2015), illustrating Chile’s deep dependence on international financial assistance. Between 1971 and 1973, in order to sustain its expansionary fiscal policy and growing public deficit—particularly in view of the shutdown of manufacturing activities during the 1972 national strike and the deterioration of foreign trade—the UP government was forced to consume much of its international reserves to finance the fiscal deficit. Allende, however, was not willing to contract further international loans. In 1971, his government declared

> a default, which is reported to have happened in 1972, according to Reinhart and Rogoff (2009). This moratorium implied no more external financing for Chile. In this context, in the absence of enough funding, both domestic and foreign, to cover both the fiscal deficit and the interest rate payments on the debt, the government had to rely on seigniorage as a source of funding. (Caputo; Saravia, p. 9)

## 4.1. A Two-Level Game

In 1969, as the end of the presidential term approached, an IMF mission was sent to Chile to assess the status of its bilateral relations and was informed of the government's intention not to renew the active SBA, which was set to expire in April of the following year. According to the then president of the Central Bank of Chile, Carlos Massad, this decision had been made in light of the improvement in the country's balance of payments (Kedar, 2015)—although, as the U.S. government later indicated, that improvement would deteriorate the following year, as shown in the table below.

**Figure 3: Chile: Balance of Payments Trend (in millions of U.S. dollars)**

| | *1969* | *1970* | *1971 Estimated* | *1972 Projected* |
|---|---|---|---|---|
| Exports (f.o.b.) | 1,174 | 1,129 | 1,000 | 900 |
| Of which: | | | | |
| Copper | (926) | (863) | (710) | (680)[a] |
| Imports (c.i.f.) | -928 | -1,021 | -1,150 | -1,325 |
| Trade balance | 246 | 108 | -150 | -425 |
| Investment income | -234 | -185 | -80 | -40[b] |
| Other services | -23 | -35 | -20 | -20 |
| **Balance on current account** | **-11** | **-112** | **-250** | **-485** |
| Direct investment | 108 | 163 | 20 | 0 |
| Long-term capital | 108 | 76 | 0 | 150 |
| Drawings | 278 | 237 | 200 | 190[c] |
| Amortization | -170 | -161 | -200 | -40[d] |
| Short-term capital (including errors and omissions) | 9 | -57 | -91 | 69[e] |
| **Balance on capital account** | **225** | **182** | **-71** | **219** |
| **Total balance of payments** | **214** | **70** | **-321** | **-266** |
| SDR allocation | 0 | 21 | 17 | 17 |
| Changes in net foreign reserves (a minus sign indicates a decrease) | 214 | 91 | -304 | -249 |
| *Total net foreign reserves (end of year)* | *252* | *343* | *39* | *-210* |
| Financing of reserve changes | | | | |

Source: CIA*: Nacional Security Decision Memorandum 93*, Washington, 1970, p. 14.

A new mission was dispatched to the country in March 1970, on the eve of the agreement's expiration, to evaluate "Chile's economic performance" under the SBA and to observe the presidential race. Although Allende's victory was not anticipated—both the IMF and the U.S. government had pessimistic projections regarding his performance—the elections proved highly competitive, and the UP coalition ultimately emerged victorious.

Relations between the Fund and the Chilean government subsequently underwent an adjustment of expectations. Although Allende's administration was socialist and nationalist in nature, it was also conceived in pragmatic and strategic terms. The individual chosen by Allende to replace Carlos Massad as president of the Central Bank of Chile was Alfonso Inostroza—a "Chicago Boy" who already knew members of the IMF technical staff and had previously undergone a period of training at the institution. Inostroza was a technocrat strategically positioned to lead the relationship between the Chilean Central Bank and the IMF, while Carlos Massad, after being removed from office, went on to work with the Fund itself. The interactions that followed were therefore mediated through a two-level political framework.

One of the first incidents to raise concern within the U.S. government regarding Chile–IMF relations involved the situation in which proposed changes to Chile's exchange rate system—maintained within a fixed band until 1971—conflicted with the Fund's preference for a flexible exchange rate policy. And, "although IMF members were not authorized to alter their exchange rate systems unilaterally, Chile was about to do so" (Kedar, 2015, p. 730, author's translation).

This tension stemmed from a subtle internal maneuver between the IMF and Allende's administration. Del Canto, who represented the Fund's interests and was the one to receive Massad's memorandum concerning the proposed changes, chose not to share it with the institution's Executive Board. Kedar (2015, p. 730, author's translation) attributes this decision to Del Canto's cautious anticipation that "eventually, Washington would request that the U.S. Executive Director at the Fund block contacts with Chile." The U.S. State Department exerted strong influence over the IMF Executive Board, within which the American representative was expected to oppose Chilean initiatives aggressively.

The proposed changes were nevertheless implemented, and their functioning was later assessed by a new IMF mission to Chile in January 1971. The Fund's report was positive, describing the measures as "harmless," including their goal of curbing capital flight. Allende's minor policy adjustments—so long as they indeed remained minor—passed unnoticed by the Fund, whose relationship with Chile became increasingly productive as the government, astutely, appeared open to dialogue and receptive to the institution's influence. Within the broader context of the Cold War and political tensions in Latin America, Chile's partial openness and willingness to engage with a neutral financial institution were interpreted as positive signs of détente, even if Washington remained far from satisfied.

Chile's domestic political motivations ultimately defined the boundaries of its two-level game with the IMF. Even during the January 1971 mission, the UP government remained unwilling to contract any SBA with the Fund—a position driven by political and anti-imperialist principles rather than by technical considerations. As Kedar (2015) observes, despite the deterioration in copper prices—largely influenced by the U.S. decision to sell large volumes of its reserves on the international market precisely to undermine Chilean exports—and its evident negative effect on the country's trade balance, Allende's administration intended to request only ordinary IMF loans, those granted without conditionality. The government reaffirmed its commitment to the constitutional road to socialism, which implied, in Kedar's words, "profound changes in the control of the means of production and in the distribution of income" (2015, p. 732, author's translation).

## 4.2. Renegotiating Chile's Debt: Allende under IMF Tutelage

According to a World Bank report[11], at the beginning of 1970 and by the end of Frei’s administration in Chile,

> Some improvements had been accomplished in trade and monetary policies, education, agriculture, public housing, and other socioeconomic areas; and an agreement had been concluded with the copper companies for the Chileanization of the mines that promised large new investments in that sector. The balance of payments was strong, and international reserves were, for that period, at record levels. On the other hand, *the fiscal situation was deteriorating, inflation was again accelerating despite slackening production and rising unemployment, private saving and investment remained low*, and to many it appeared that the social programs launched by the Christian Democrats had lost their momentum.

One year later, under Allende’s administration, despite visible improvements in employment and real wages, the deterioration of the economic situation described above seemed to have deepened. The fiscal deficit—driven by massive public spending (which rose by more than 66% in nominal terms during 1971)—reached alarming levels, accompanied by a sharp reversal in the balance of payments. The drop in exports, combined with rising imports, turned a surplus of 95 million U.S. dollars into a deficit of 90 million.

Moreover, as the World Bank report[12] continues, the situation of international assistance to the country had also undergone a dramatic reversal.

> Gross disbursements on medium- and long-term public loans fell from US$397 million in 1970 to US$190 million in 1971. Suppliers’ credits, bilateral assistance, and private bank lending all dropped sharply. Deducting payments for amortization and interest, the shift was from a net resource inflow of US$156 million to a net outflow of US$52 million.

Thus, “despite the nonpayment of $80 million in debt service due during the last two months of the year, Chile's loss of net reserves during 1971 totaled US$300 million, or three-fourths of its holdings at the beginning of the year[13].” By November 1971, the Popular Unity (UP) government announced the suspension of external debt payments and began negotiating with its main creditors—a moment when the IMF’s influence and guidance within the political sphere of the International Financial System became more crucial than ever. According to Kedar (2015, p. 737, author’s translation),

> The Chileans understood that without substantial IMF support, their chances of reaching an agreement with European creditors were nil. The WHD, in turn, could not afford to miss the opportunity to act as a mediator between creditors and a Latin American debtor. Ironically, Allende’s Chile and the IMF were mutually dependent.

Although risky, the proposition that there was a relationship of “mutual dependence” between the Fund and the Chilean government proves reasonable when

[11]Excerpt from the World Bank case study: Chile: An Economy in Transition (1980, p. 59).

[12]World Bank. Chile: An Economy in Transition. 1980, p. 72.

[13] World Bank. Chile: An Economy in Transition. 1980, p. 72-73.

placed in the broader context of the IFS at the time. Throughout this period—particularly among South American countries—the Fund faced growing criticism of its conditional practices and intense political-economic debates about the structural causes of chronic balance-of-payments crises and market constraints. The retreat of Global South countries and their growing distrust of the institution coincided with the efforts of ECLAC economists and dependency theorists, which, in turn, made the presence of the Soviet Union appear even more threatening in Western eyes. Meanwhile, for Chile, the IMF's influence guaranteed the credibility of the government's intentions before its external creditors and extended beyond politics. The Fund was also needed to alleviate some of Allende's budgetary pressure in light of the large fiscal and trade deficits faced by his administration.

In November 1971, Chile requested the IMF's technical assistance to conduct its debt renegotiation and the availability of a compensatory loan to offset the immediate losses caused by falling international copper prices, the request

> reflected not only the strength of the cooperation between the IMF and Allende's Chile but also demonstrated that even states not aligned ideologically, politically, or economically with Washington could make use of the Fund as an institution serving their own needs. (Kedar, 2015, p. 737, author's translation)

In December, the IMF Executive Board granted Chile—classified as a member state affected by "circumstances beyond its control"—a budget of 39.5 million U.S. dollars through the Compensatory Financing Facility for Export Fluctuations program. This decision was diametrically opposed—the other side of the same coin—to the U.S. strategy of economic destabilization aimed at depressing the price of Chile's main export commodity. It simultaneously allowed Chile to maintain its standing as an IMF member and enabled the institution to be perceived within the sphere of International Financial Governance as pragmatic and neutral—ultimately, as an organization serving the international financial community.

The renegotiation of Chile's external debt centered on the negotiations with the Paris Club, an informal group of creditors whose purpose since 1956 has been "to find coordinated and sustainable solutions to payment difficulties experienced by debtor countries," in the organization's own words, with the IMF serving as an observer member. One of the conditions for the Paris Club to consider Chile's debt renegotiation was that the IMF grant the country a SBA—an unfeasible condition for both political and economic reasons. Politically, the UP government had already refused to accept conditional loans. Economically, given the country's extreme situation, Chile would have qualified only for the most restrictive type of SBA, which it was unwilling to accept.

Kedar (2015, p. 739, author's translation) analyzes this impasse:

> Obviously, there was no room to expect that an Executive Board strongly influenced by Washington would grant an SBA to the Allende administration. In fact, there was a wide gap between the willingness of the Executive Board and that of the Western Hemisphere Department to grant, or even consider, an SBA for Allende's Chile. The Executive Board

viewed the SBA as a clear seal of approval that it was unwilling to confer upon Allende's government.

An alternative to the Paris Club's requirement was found through a strategically evasive approach. The IMF drafted a statement establishing a set of basic supervisory conditions: targets for Chile's balance of payments, a limit on the country's medium-term external borrowing, and measures to prevent potential trade arrears. This statement was attached to a document submitted to the Paris Club, which, in April 1972, ultimately decided to waive the requirement of a SBA in order to consider Chile's request. The creditors' willingness to proceed with the renegotiation even led the United States to accept the agreement—reluctantly, and only because the Nixon administration recognized the need to align expectations with the other members of the group.

As a result, Allende's government secured a record-level renegotiation among Latin American countries, covering approximately 70% of its total debt. Although Chile's economic situation continued to deteriorate the following year—when a new negotiation with the Paris Club became necessary to establish a stricter stabilization program—the advances obtained during the first two years of the UP administration, under the supervision of the IMF, despite their ideological contradictions, were significant for the political context of the Cold War and for the Fund's image within International Financial Governance. The relationship between Allende's Chile and the IMF moved against the tide of the prevailing political agenda and demonstrated the possibility—however cautious—of neutrality within the processes of the IFS.

## 5. Final Considerations

The frequency of technical exchanges and the close political relationship established between Salvador Allende's administration and the IMF staff—the leading financial institution in the post-World War II international arena and a representative of an IFS guided by the U.S. agenda—demonstrate that, despite its socialist and counter-hegemonic alignment, Chile's position within international financial dynamics was not condemned to isolation. Rather, it was defined by a combination of pragmatism and partial conformity to the system's demands.

This outcome stemmed partly from the geopolitical context of the Cold War and from the growing hostility of Latin American governments toward the conditionalities imposed by international financing (that is, by external indebtedness), which pressured the behavior of international financial institutions—especially the IMF—and partly from the efforts of Allende and his administration to pursue a two-level financial and technical diplomacy. This diplomacy combined technocrats capable of engaging in dialogue with international institutions and a political commitment to defending national economic interests.

Even in the face of the United States' restrictive policy—designed to undermine Chile's export potential and Allende's domestic governability, as well as to use its influence and veto power against the country in international councils—Chile succeeded in negotiating favorable terms with its creditors. More importantly, it managed to gain the sympathy of the IMF staff and benefit from their influence in the negotiation process. According to Kedar (2015, p. 738, author's translation), this was more than mere pragmatism: "Above all, it reflected the determination of Del Canto's team to prevent Chile's withdrawal from the Fund, and Allende's intention to avoid isolation and to make use of all available assistance."

The UP administration—prematurely interrupted and forced to confront internal and external challenges to its economic expansion, such as rising public debt, hyperinflation, falling commodity prices, and a growing external debt—was, nonetheless, a model case of the multilateral potential of international financial institutions. It also exemplified the contradictions inherent in the relationship between these institutions and the governments of developing countries, which remain vulnerable to the dynamics of a capital-liberal financial system and to the erratic movements of low value-added, primarily export-oriented trade balances. Ultimately, Allende's Chile demonstrated the importance of playing a two-level game within International Financial Governance.

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