

Arnold Harberger's Contribution to Development in Chile¹

Cristián Larroulet V.

Full Professor, Universidad del Desarrollo

It would be no exaggeration to say that Arnold Harberger is the citizen who has contributed the most to the teaching, research, and promotion of sound economic policies in Chile over the past 100 years. The same as during the nineteenth century the Venezuelan citizen Andrés Bello played a fundamental role in the establishment in Chile of a culture based on the rule of law and the French citizen Courcelle Seneuil was key to the advancement of the banking industry and the opening to international trade, Harberger will be recognised for his contribution to the construction of an economic strategy that will make it possible for our country –sooner rather than later, I hope– to attain development.

Arnold Harberger was born in the United States in 1924. He completed undergraduate studies at Johns Hopkins University, and he received his PhD from the University of Chicago. He has taught at leading universities in the world, such as Chicago, Harvard, MIT, Princeton, and others, and he culminated his career as Emeritus Professor at the University of California in Los Angeles (UCLA) in 2014. He had already been appointed as Emeritus Professor by the University of Chicago in 1991. He has also taught and done research in countries in Latin America, Africa, Asia, and Europe.

His contribution to the knowledge of economic sciences has been enormous. It is impossible to detail his academic publications, books, and memoranda. Consequently, many have wondered why he hasn't been awarded the Nobel Prize.

I am only going to mention some of his academic contributions. He is outstanding for his contribution to Public Finance through classic works on the incidence of the corporation

¹ This work is an edited version of the speech delivered during Arnold Harberger's investiture as Doctor Honoris Causa by Universidad del Desarrollo on August 23, 2017.

income tax² and the development of methodologies for social investment project evaluation³. In the Industrial Organization area, he is famous for his research concerning the assessment of the social cost of monopolies⁴. He also made a big contribution to the improvement of public policies in the social area, as a result of his methodological approach to “basic needs”⁵ and his studies on welfare economics⁶.

But his contributions also extend to other areas, such as the causes of inflation and the policies to reduce it;⁷ the relevance of international trade for proper allocation of productive resources; exchange rate policy issues⁸; and his reflections on economic growth in his already classic speech as President of the American Economic Association in 1998. In this speech, called “A Vision of the Growth Process”⁹, Harberger draws attention to the relevance of cost reduction for growth and its relationship to Schumpeterian “creative destruction”¹⁰. A direct relationship to our university is found here as he encourages more exhaustive research on corporations and their role in development.

There is no doubt about the excellence of his academic work and, especially, about his remarkable ability to apply this to the real world and to teach it to his students. His emphasis on how relevant it was for universities to teach the discipline of data observation and analysis and to apply their economic rationale to create proposals that are not only sound but also simple to explain and implement reflects his influence as a practical economist¹¹. Not in vain, the IMF, the World Bank, the National Economic Council of the U.S. Government, and a

² Harberger, A. C. (1962). The incidence of the corporation income tax. *Journal of Political Economy*, 70(3), 215-240.

³ Harberger, A. (1985). Reflections on social project evaluation. *The Economic Evaluation of Projects*, 23.

⁴ Harberger, A. C. (1995). Monopoly and resource allocation. In *Essential Readings in Economics* (pp. 77-90). Macmillan Education UK.

⁵ Harberger, A. C. (1978). On the use of distributional weights in social cost-benefit analysis. *Journal of Political Economy*, 86(2, Part 2), S87-S120.

⁶ Harberger, A. C. (1971). Three basic postulates for applied welfare economics: an interpretive essay. *Journal of Economic Literature*, 9(3), 785-797.

⁷ Harberger, A. C. (1978). A primer on inflation. *Journal of Money, Credit and Banking*, 10(4), 505-521.

⁸ Harberger, A. (1986). Economic adjustment and the real exchange rate. In *Economic adjustment and exchange rates in developing countries* (pp. 369-424). University of Chicago Press.

⁹ Harberger, A. C. (1998). A vision of the growth process. *The American Economic Review*, 88(1), 1-32.

¹⁰ Schumpeter, J. A. (2013). *Capitalism, socialism and democracy*. Routledge.

¹¹ Harberger, A. C. (1994). La búsqueda de relevancia en la economía. *Estudios Públicos*, (55-56), 87.

countless number of countries in all the continents have consulted him for advice on policy enhancement. He has been awarded many distinctions by, among others, the American Academy of Arts and Sciences and numerous prestigious universities, such as Cambridge University in the United Kingdom, ITAM in Mexico, and the Pontificia Universidad Católica in Chile.

But there is another facet that I want to highlight today. Countries progress not only as a result of ideas and sciences; they also need “good policies”. As expressed by Professor Harberger at Universidad Católica, one of the lessons learned after forty years studying economic policies is that it is not always the most intelligent policy-makers that are the most successful. Courage, perseverance, firmness, and tenacity are likely to be more important than mere brain power to lead a country to economic success. His recommendations¹² on how to implement successful economic reforms and the leaders’ roles in this process are worth reading.

In relation to the design of “good policies”, I would like to recall Universidad del Desarrollo’s foundational spirit. We were conscious of the fact that, concerning ideas and good policies, the progress already attained by the country in terms of the importance of macroeconomic balance and an open-market economy was crucial. However, we considered that Chile needed to give much more relevance to the role of the entrepreneur as a fundamental factor for development; that person who is characterised by having an idea or adapting an idea to introduce a new good or service through a cost reduction or greater valuation of the satisfaction of a need; that person who, with courage, perseverance, and high performance orientation, makes productivity increases possible. Accordingly, 27 years ago, we decided to bet for UDD’s hallmark: the promotion of entrepreneurship and innovation. Some friends asked “and what is that?” or criticised us stating that “other universities do not teach this, why do you do it?”

¹² Harberger, A. C. (1993). Secrets of success: a handful of heroes. *The American Economic Review*, 83(2), 343-350.

Today, all prestigious universities in the world and in every country have specific programs on this subject. But once again, thanks to our bet and to our persistence, we are the leaders in undergraduate and graduate teaching of entrepreneurship in Latin America, and our Faculty of Economics and Business is at the forefront of academic research in this area. It goes without saying that Professor Harberger also contributed to inspiring us in this endeavour by teaching us the essential role played by entrepreneurs in the creative destruction process leading to growth, thereby enabling our university to make a fundamental contribution to the challenges facing Chile today.

Now I would like to read part of a remarkable document called "*Memorandum sobre la economía chilena*"¹³, sent by Harberger to his colleagues at the University of Chicago in 1956, where he describes the disastrous economic policy in place at the time, addressing the reality in the most important areas. He reflected a pessimistic view, "Inflation can be curbed by means of a truly restrictive Central Bank policy, but this is unlikely to occur." Also, when he refers to the level of State intervention in international trade, he sustains, "The subtlest cause of poor resource allocation is the country's foreign trade policy. Until a few years ago, the exchange rates applied to different products ranged over a proportion of 1 to 6", and he continued "the general protectionist exchange rate system for many local industries and the straightforward prohibition to import certain products are still in place."

There is a completely different situation today! We have had an autonomous Central Bank for 37 years now, with the capacity to overcome the pressure of interest groups and attain an annual 3% inflation rate! We are one of the most emblematic open economies in the world, with a tariff system regulated by law and legal trade agreements with all the main world economies. And we have a free-floating exchange rate system without distortions. Note the big contrast with the description provided by that young economist when writing to his colleagues! I am sure that back then he did not imagine that many of the current accomplishments were driven by his sound advices.

¹³ Harberger, A. (2000). *Memorandum sobre la economía chilena*. *Estudios Públicos*, 77, 399-418.

However, there is something even more important: Arnold Harberger is, by far, the person who has had the greatest influence on the modernisation of our economy through the training of specialised human capital in the area. For a university, having the mission to provide professional training, this sole reason is more than enough to award him a Doctor Honoris Causa honorary degree. This is not only for his role in the Agreement¹⁴ signed between the University of Chicago and the Pontificia Universidad Católica to modernise the teaching of economy, but also for his effort during more than 60 years, collaborating so that Chilean students may pursue studies at prestigious universities in the United States. As Juan Pablo Couyoumdjian and I once wrote¹⁵, Chile is outstanding at a global level for the quality of its economic teams over the last four decades; these are recognised by their academic degrees and the results obtained in terms of wellbeing for Chilean citizens, especially the most deprived ones.

But, are the aforementioned attributes the only considerations based on which our university presents this award? I wouldn't say so. There are three aspects that characterise both Universidad del Desarrollo and Arnold Harberger that I cannot leave without mentioning. The first is at the origin of this academic institution and is part of its name and its hallmarks. Here, I would like to recall our dear first Chancellor, Ernesto Silva Bafalluy. He was his student and one of the best. I am sure that he is happily watching from heaven, with a big smile of satisfaction on his face, how the university that he founded and conducted for 21 years recognises today the contribution of someone who was his teacher and friend.

It is not by chance that our university is called "Universidad del Desarrollo" (Development University), but rather due to its deep commitment to the promotion of opportunities for all Chilean citizens. We were not born either to accept the "economic inferiority" described by

¹⁴ Fontaine, E. (2009). Mi visión. *Universidad del Desarrollo*.

¹⁵ Couyoumdjian, J.P., and Larroulet, C. (2011). La importancia del capital humano y de las instituciones en un proceso de reforma económica: dos programas comparados. In: A. Ibáñez, S. Edwards, C. Garay, R. Lüders, C. Larroulet, and J. Couyoumdjian, ed., *Reformas económicas e instituciones políticas: la experiencia de la misión Klein-Saks en Chile*, 1st ed., Santiago: Universidad del Desarrollo, pp. 241-253.

Encina¹⁶ at the beginning of the twentieth century or to talk about the “frustrated development” referred to by Aníbal Pinto¹⁷ during the second half of the past century. On the contrary, we were born to promote the leaderships, the ideas, and the institutions that bring to life that set of virtues that makes it possible for countries to thrive. Alito Harberger taught them to us in his classes and through his life example.

For all the above, we wish to perpetuate his testimony through this acknowledgement: the award of the Doctor Honoris Causa honorary degree to an intellectual entrepreneur who will undoubtedly continue to enlighten our university duties.

¹⁶ Encina, F. A. (1912). *Nuestra inferioridad económica, sus causas, sus consecuencias* (Vol. 1). University press.

¹⁷ Pinto, A. (1996). *Chile, un caso de desarrollo frustrado*. Editorial Universidad de Santiago.