

THEODORE H. MORAN

# Multinational Corporations and the Politics of Dependence

*Copper in Chile*



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Multinational Corporations  
and the Politics of Dependence

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Multinational Corporations  
and the Politics of Dependence

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COPPER IN CHILE

Theodore H. Moran

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To my family



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## Preface and Acknowledgments

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**T**his book is the work of a skeptic trying to use training in the fields of political science and economics to carry out a study of the political economy of foreign investment. I have found that in fact there are tools in both of these disciplines to do a respectable job. If I had recognized this sooner, and got on with the job, as some of my friends ably suggested, I would have made faster and more effective progress. The fact that the overwhelming bulk of work in these fields is of such low quality is due to laziness, complacency, and lack of imagination on the part of the practitioners more than to the unavailability of useful tools.

A comment should be made about the methodology and tone of this study. Chilean political leaders, scholars, *técnicos* were required to make awesome decisions directly affecting the destiny of their country in a way only rarely equalled elsewhere—often under conditions of great stress, great uncertainty, and great popular pressure. The methodology of this study is based on the retrospective reconstruction of the accuracy, adequacy, and wisdom of those decisions. It benefits from the ease of academic reflection, from the exactitude of hindsight, and from the beginnings of a comparative perspective. The purpose of such second-guessing is not to pass judgment in a supercilious fashion on various episodes in the history of copper in Chile, but rather to extract lessons and suggest analytical tools for a political economy of foreign investment that can be used for other industries in other countries in the service of both scholarly analysis and policy formation.

I have benefited from the extensive and intimate help of persons in most of the Chilean political parties and interest groups studied here, in the North American copper com-

### *Preface and Acknowledgments*

panies, and in the United States government. Many of them still hold positions of responsibility and should not be mentioned by name. They will greet this work with varying degrees of enthusiasm.

Special mention should be made of the encouragement I received from Nancy and Martin Zimmerman, Clinton Bourdon, and Susan and Paul Drake. They will welcome this book if only because they will no longer have to hear me talk about it. To the extent that I followed editorial suggestions of my brother David, readers have grounds to rejoice.

I have had valuable commentaries and incisive critiques from Sam Huntington, Joe Nye, Hendrick Houthakker, Richard Caves, and Raymond Mikesell. And I have received help from the Foreign Area Fellowship Program, the Harvard Center for International Affairs, Vanderbilt University, and the Brookings Institution.

To Harlan Parker, Charles Ackerman, Nadav Safran, Barrington Moore, and Raymond Vernon I owe much of my intellectual inspiration. They might acknowledge it with some reluctance.

Finally, to my wife JoAnn I must give thanks for real sacrifices in her own professional calling. Why I and little Robbie should pursue our careers at the expense of her work in medieval history can only be ascribed to ill-concealed sexism.

The merits of this study come largely from the help of my friends and advisors. The faults, as they have frequently reminded me, are entirely my own.

T.H.M

*Cambridge, Massachusetts*  
*Nashville, Tennessee*  
*Washington, D.C.*  
*December 1973*

Multinational Corporations  
and the Politics of Dependence





## CHAPTER I

### Introduction

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In 1912, looking back over the history of nitrates and forward toward the future of copper, the celebrated Chilean writer and historian Francisco Encina regarded with despair the process which he called the “denationalization” of those industries that exploited the country’s basic natural resources.<sup>1</sup> He was distressed by the spectacle of the nation’s vital industries falling more and more completely into the hands of foreigners, whether British or North American—and he lamented a course of development in which Chileans were content to play essentially a secondary and supportive role to foreigners who were taking over the most important centers of economic growth.

Encina’s term was *denacionalización*, and he longed for Chileans bold enough to recapture the sources of their own natural wealth and recover control over their own destiny. In the quarter of a century following the Second World War, the new term to describe Chile’s plight became *dependencia*. And, at last, there were men bold enough to answer Encina’s call and talented enough to be capable of taking over and running the industries.

Between 1945 and 1970 the Chileans closed in on the foreign-dominated copper industry in their country, successfully surrounded it, and proceeded to take it over. During that period they developed the skills necessary to mine copper, smelt it, refine it, and by the early 1970’s they possessed the capacity to carry out all the operations of production on a large scale on their own.

The early formula for recovering control over the national destiny was, logically, the opposite of *denacionaliza-*

<sup>1</sup> Francisco A. Encina, *Nuestra inferioridad económica, sus causas y sus consecuencias* (Santiago: Imprenta Universitaria, 1912).

## Introduction

ción—namely, *nacionalización*, or putting authority for basic decisions in Chilean hands—although the early Chilean writers would never have entertained the thought of state ownership as part of the notion.<sup>2</sup> The more recent formula for recovering control over the national destiny has been, with equal logic, the opposite of *dependencia*—that is, *independencia*, or *autonomía*. In the early 1970's Chile in fact nationalized the copper industry. The reassertion of sovereignty over the exploitation of natural resources is, in all likelihood, one of the few undertakings with support deep enough to survive, in one form or another, even the most intense domestic conflict.

### I

This is an analytical history of the formation of copper policy in Chile from World War II through the end of the Allende regime in 1973. It is the history of the interaction of two systems—a system of multinational copper companies operating under unstable conditions of imperfect competition, and a system of domestic interest groups in Chile trying to respond to rising demands for national development and national welfare—both struggling to take advantage of each other and reduce each other to manageable proportions.

The Chileans characterized their side of this interaction as the struggle against *dependencia*.

What the idea of *dependencia* gained in popularity after the Second World War, however, it unfortunately lost in precision—in academic as well as political discussion. From the debates on copper policy, this study will abstract three definite objectives that were associated with the movement against *dependencia*: first, the objective of asserting Chilean sovereignty over its own economic and political life; second, the objective of forcing or enticing the foreign cor-

<sup>2</sup> *Ibid.*; Julio Kaulen, *Las empresas mineras extranjeras en Chile y la economía nacional* (Santiago: 1916); Machiavello Varas, *El problema de la industria del cobre* (Santiago: 1923).

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porations to make more of a contribution to Chilean goals of growth and welfare; third, the objective of freeing Chile from having to contribute "captive production" to a vertically integrated corporate system that did not serve Chilean interests.

I shall argue that the first two meanings of *dependencia* embodied legitimate concerns toward which Chilean administrations, despite costly setbacks, made cumulative progress. The third meaning of *dependencia*, however, was based upon an inadequate analysis of international oligopoly behavior and did not acknowledge the limits within which any oligopolistic producer must pursue his individual interests. Pursuit of this objective may put Chile (as well as other nationalistic "independents") in a weak position outside the international copper oligopoly, rather than secure for the country a strong position of interdependence within the international industry.

The quarter-century struggle against *dependencia*, then, which has been necessary to mobilize national skills and gain national confidence in bringing the copper sector more and more under national control, could finish by substituting one kind of international dependence for another—perhaps worse.

## II

The introduction of foreign corporations into the center of national life represents a complex challenge to the interests and to the sovereignty of the host country.

Natural resource companies, such as Anaconda and Kennecott, are large, oligopolistic, vertically integrated. They have substantial discretion in formulating investment policy, pricing policy, marketing policy. A tight hold on the combination of capital, technology, and experience that are necessary to find ore-bodies, bring them on-line, and process and market the output gives them the power to exclude competition. They make their policy decisions according to a global strategy based on their own internal needs—not

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purely in response to market forces (as an atomistic company in a situation of perfect competition would), nor purely in response to the environment created by the host country (as a domestic company would).

At the same time the potential contribution of such corporations to host countries is very great. The economic impact that Anaconda and Kennecott had on Chilean society was enormous. The total value of copper production by these two companies alone accounted for 7% to nearly 20% of Chilean Gross Domestic Product. Tax revenues from copper financed from 10% to 40% of government expenditures. Copper exports ranged from 30% to 80% of all hard currency earnings. No domestic decision about the rate of economic development, the strength of the balance of payments, the level of aggregate employment, the breadth of social welfare programs could be made without a careful calculation, from outside, of how the foreign copper companies might be going to exercise their discretionary power.

This produced an ambivalence about conflict and cooperation, an edge of hostility beneath the game of mutual accommodation. On the one hand, responsible Chilean statesmen wanted to please the foreign companies and obtain as many benefits for their country as possible by cooperative methods. On the other hand, responsible Chilean statesmen felt a mandate to bring the foreigners more and more under national control, force them to serve domestic goals, make them responsive to the society over which they exercised so much power.

The idea of *dependencia* grew out of this ambivalence. Its most fundamental meaning came from a sense that basic decisions about the pace and direction of national development were being dictated by North American corporate officials, unaccountable to any Chilean body politic, according to the internal logistical needs of the vertically integrated companies that those officials served—or, occasionally, according to the foreign policy preferences of their government. No matter how appreciative of the contribu-

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tions of the foreign copper companies, Chileans of diverse political and economic views nursed a simple mistrust of concentrations of power, mistrust of alien self-appointed and self-perpetuating economic organizations whose private, secret, and often mystifying decisions affected the welfare and prosperity of the entire national community. The struggle against *dependencia* sprang from the desire to “restore” sovereignty and independence over the course of national development.

The result was a fight for control over a society’s destiny beside which the populist movements in the United States to regulate the banks, the railroads, and the “trusts” dwindle in magnitude and in difficulty.

All of *Fortune*’s 500 largest US corporations combined do not play nearly the role in the economy of the United States or pay more than a fraction of the percentage of US taxes that Anaconda and Kennecott alone supplied in Chile. All the ranches in Texas, the banks in New York, the aerospace industry in the Northwest are not as responsible, economically, for the fate of their respective states as the copper industry is for Chile. The Rockefellers and the Morgans with all their affiliates at their height were minor operators in comparison to the position that Anaconda and Kennecott occupied for half a century in Chile. Yet if any of these groups were controlled and operated by foreigners according to obscure strategies linking them to headquarters and affiliates outside the United States, it is unlikely that the fear of international dependence and the sense of political frustration would be as comparatively muted and cautious as the Chilean reaction.

The tension about “foreign control” had a strong hold on many Chilean groups even when the foreign presence was considered clearly indispensable for the copper industry. Once the foreign presence was not considered absolutely necessary, the movement toward national control was very rapid—despite warnings that such a policy would have substantial real costs. As Chilean competence in carrying out

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operations at the production stage increased, the political appeal of national take-over became irresistible. Chilean leaders could not refuse the opportunity to "recover" control over the country's basic natural wealth and "restore" sovereignty over the course of national development.

### III

Alongside the challenge to Chilean sovereignty, *dependencia* incorporated a feeling that the powerful foreign companies were not performing dynamically enough to satisfy the needs of national development. This interpretation of *dependencia* stimulated cycles of pulling, pushing, and shoving to encourage or oblige the foreign corporations to commit more of their resources to Chile and share the rewards more generously. With varying degrees of success, these cycles produced a movement to overcome the fundamental disparities of power between the copper companies and successive domestic administrations, and to use ever greater bargaining strength in the service of Chilean goals. In this sense, the struggle against *dependencia* took a course that reflected a fundamental evolution in the balance of power between the international investors and the host country.

In natural resource oligopolies where the largest barriers to entry exist at the production stage—petroleum, copper, and natural gas are the most important—the balance of power between foreign investors and domestic governments begins very much tilted in favor of the foreign producers and tips inevitably away from them toward the host governments. Foreign investors in the typical copper project, for example, must make a large lump-sum investment under conditions of great risk and uncertainty with little possibility of testing or adjusting incrementally. They will not invest unless they have the promise of substantial returns.

When the initial concession is negotiated, the host country is able to evaluate the location and value of prospective mineral deposits even less adequately than the foreign in-

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vestors. Since the foreign companies enjoy near-monopoly control over the techniques and resources needed to bring a major mine on-line, the host country has little choice but to accept terms weighted heavily in favor of the foreign investors.

But once one or more foreign enterprises commit themselves and invest, and once the mines are successful, the bargaining strengths change abruptly. Uncertainty is reduced, and the old doubts are forgotten. The host government gazes out at a profitable operation, carrying off resources the country was sure it had all along, in which a large part of the revenue is flowing away to foreigners. The price paid to the foreign investor seems, in retrospect, too high, and the government in power (or its opponents) point out that the country is being cheated. The foreign company, on the other hand, has sunk its capital and won its bet, and has an attractive mine that it will now continue to operate up to some point even though its share of the revenues may be reduced. Empirically, few large natural resource concessions in underdeveloped countries remain long unchanged. The terms of the original agreement are tightened in favor of the host country.

During the process of loosening conditions to attract new investments and tightening conditions after they have proved successful, the host country gradually moves up a learning curve of negotiating skills and of direct operating skills for the industry. Historically, most Third World countries began to watch the growth of new resource industries with very little domestic capability to monitor industry behavior, very little knowledge of terms of concessions in other countries, and very few skills in negotiating sophisticated agreements. Once the industry was established, the government had an incentive to build a skilled bureaucracy, bring in foreign consultants, demand hiring of nationals in supervisory positions, and require participation of its representatives in the arrangement of international marketing and finance. As the host country invaded those areas that



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were once the exclusive province of the foreigner, it could play the game of mutual accommodation in a tighter and tighter fashion. As the country gained direct operating skills, the cost of replacing the foreigner was lowered.

With agonizing slowness, Chile accumulated both negotiating and operating expertise as part of the drive against a dependent relationship with the North American copper companies in the post-World War II era. Despite clear instances in which particular domestic groups moved against the trend to serve their own private interests, the broad movement to push the copper sector by various means (some successful and some counterproductive) to provide the resources for sustained national development gained momentum. Despite widely advanced hypotheses to the contrary, as the foreign copper companies expanded operations in Chile over time they did not gain power, or influence, or allies on the domestic scene. Rather, their power became attenuated, their position became more precarious, their alliances proved most fragile.

Nowadays the direction of the shift in bargaining strength in natural resource industries is clear. At the end of the Second World War and through the 1950's, it was not. Rather, sanctity of contract (together with the paraphernalia of 99-year concessions and 20-year government guarantees of "inviolability") served the function of attempting to cement the relationship between foreign investor and host government on the initial favorable terms to the foreigner. But in a situation where rapidly diminishing uncertainty meant that *ceteris* did not long remain *paribus*, sanctity of contract could not have much operational meaning. Sanctity was steadily "violated" by "undependable Latins" no less than by "untrustworthy Arabs" and other "firebrand nationalists" in a process that reflected frustration about the original terms and shifts in relative bargaining power.

In retrospect this process can be observed to have taken place in various natural resource industries whose output was vital to the functioning of industrial societies and

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whose largest barriers to entry were located at the production stage—such as in copper or oil. In the petroleum industry the shift in the balance of power toward the host governments began to become clear, after some painful experiences, by the early 1960's. In the copper industry, the consciousness of this shift came more slowly. Chile, no less than Venezuela or Iran, had to suffer the emotional, political, and ideological turmoil required to push history in the direction that now seems both logical and inevitable.

## IV

The use of the word "dependence" to characterize some of the key problems of Chilean development grew out of the domestic desire to reassert sovereign control over the economic and political life of the nation. It was also a reaction against the disparities of power that had historically conditioned relations between the foreign copper companies and the host country. The result was a determination to bring the foreign investors under tighter scrutiny as the country's bargaining position improved and to use the country's power to get more from the copper sector for Chile.

But there was a third dimension to *dependencia*. The rationale for moving in on the copper industry and finally taking it over did not originate entirely in concerns about the division of returns or the loss of sovereignty. Rather, Chileans elaborated the idea of *dependencia* even as their country gained experience in tough bargaining with the foreigners and got higher relative as well as absolute returns from the copper industry. This third aspect of the attack on *dependencia* grew out of the Chilean experience of frustration about corporate pricing and marketing behavior, and became a fundamental critique of corporate strategy and corporate integration.

*Dependencia*, in this dimension, was a sense that the country contributed "captive production" to an integrated system that by nature rendered the struggle for national development extraordinarily difficult while accentuating by

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a large factor the share of costs and risks in the international system that had to be borne by Chile.

From this premise the conclusion emerged that if *dependencia* meant being a "captive" part of the integrated corporate system, *independencia* required being free of that system or even destroying it. A war on the system of private corporate integration became war on the idea of integration *per se*. The mind slipped easily from identification of the problem to prescription of the solution—from dependence to independence, from *dependencia* to *independencia*.

The result would be not only *autonomía*, or more sovereign control over decisions affecting national growth and welfare, but also a chance to achieve at last the full returns as an independent producer from the rich natural resources in Chile. National control of the copper industry would mean that the country would at last break the chains of "captive production" in a larger integrated system, that the country would at last be free to use the full force of its market power to serve its own national interests.

## V

This is an analysis of the domestic politics of economic nationalism that have produced the idea of *dependencia* and mobilized the broad reaction against it in Chile since the end of the Second World War. It is also an analysis of the alternative futures for economic nationalism in Chile as the country now faces the semi-integrated world industry as a major independent producer.

This study will not only ask how the idea of *dependencia* gained support and test whether that idea has provided an adequate interpretation of Chile's past. It will also analyze to what extent the reaction against *dependencia* can provide an adequate guide to Chilean strategy in the future as the international industry reacts to protect itself against the threats of economic nationalism.

This study will argue that the idea of *dependencia*, often left vague or purposefully endowed with a variety of mean-

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ings as it grew out of the Chilean experience, served better to inspire Chileans to close in on the copper companies when the country was in a position of strength, served better to build up domestic competence for exercising the rights of sovereignty in bringing the foreign corporations under national control, than it did to enlighten them about oligopoly strategy in the international industry.

There are dangers as well as opportunities as Chile now fashions its own policy as a large national producer. The country can come to occupy a strong position within the international oligopoly or a very weak position outside it. Unfortunately, there are indications that the heritage of economic nationalism in Chile has not well prepared the country to recognize the opportunities and separate them from the dangers.

There can be no doubt of the poignancy of the feelings about *dependencia* or of the strength of the desire for *independencia* or *autonomía* on the part of many Chileans as long as control of the copper remained in foreign hands. It is less clear, however, whether important Chilean groups of various political and economic ideologies have yet analyzed these concepts with sufficient care to understand the limits within which they can exercise their hard-won liberty or autonomy.

The successful end to their struggle against "dependence" can only come through recognizing the boundaries of their "independence." Whether or not this will be possible within the continuing dynamics of Chilean politics is difficult to predict. If the pressures and ideas used to mobilize opposition against the foreign companies continue to dictate national strategy vis-à-vis the semi-integrated global industry, the outlook cannot be favorable.

## VI

The importance of the Chilean struggle goes beyond the fortunes of any particular ideology or particular regime in one country. It demands study by any producing country

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that wants to use an endowment of natural resources to serve the national welfare in a world where resource industries are integrated from mine or well to consumer by multinational corporations. It requires study by any consuming country that wants access to raw materials in a world where more and more of those materials must come from the hands of sovereign economic nationalists.

The Chilean experience occupies a position of global significance in a world of nations growing increasingly interdependent and increasingly autonomous at the same time.

This work tries to combine the case study of the Chilean copper industry with broader issues of theory and policy in three areas.

First, there is an analysis of the question of what constitutes international "dependence" in a global natural resource oligopoly. Chapters 2, 7, and 8 examine the evolution of structure and strategy in the international copper industry to show what Chile's position has been within the larger corporate-controlled industry in the past, and to identify what are the strengths and weaknesses of the country's position as an independent producer facing the future. They contrast these findings with evolving Chilean perceptions about the dynamics of the global oligopoly. Thus, they provide the setting for the case study of policy formation in Chile. More generally, however, they aim to elucidate the relationship between "dependence" and "interdependence" for any natural resource-producing country trying to shape an effective strategy in the international economy.

Second, there is an analysis of the reaction of domestic groups in the host country to the challenge posed by international "dependence". Chapters 3, 4, 5, and 6 penetrate beneath the abstraction called the "host country" to examine the behavior of Chilean political parties and interest groups at each of the major renegotiations of relations with the foreign copper companies in the post-World War II period. These chapters test and reject hypotheses about "reactionary alliances", "neo-imperialism", and the "consolida-

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tion of underdevelopment”—as well as hypotheses about “good investment climate” and “good corporate citizenship”—before placing the Chilean experience within the context of an alternative model of the evolution of the balance of power in natural resource concession agreements in developing countries.<sup>3</sup> Building on top of this dynamic model, Chapter 6 offers the beginnings of a general theory of foreign investor–host country relations and shows how such a theory would explain the course of economic nationalism among natural resource producers in the Third World.

Third, there is an attempt at broad policy proposals, for both producing and consuming countries. From an analysis of Chilean strategy to pursue its goals as an “independent” national copper producer, Chapter 7 delineates the margins within which any economic nationalist must fashion its policy as an oligopolist to serve its own national interest. Then, Chapter 8 tries to suggest ways in which the major consuming countries can encourage the restructuring of multinational corporate relations to preserve many of the benefits and reduce some of the costs inherent in international resource development.

<sup>3</sup> In the course of fitting this alternative model of the evolution of the balance of power between foreign investors and host countries together with the Chilean experience, Chapter 6 offers its own definition of “exploitation” and “complicity in exploitation” that can be clearly identified, and its effects measured, at various crucial points in Chilean history.

## CHAPTER 2

### Structure and Strategy in the International Copper Industry

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The success of any oligopolistic industry—whether generating private corporate profits, or generating funds for public welfare and national development—comes from exacting an economic rent from final consumers. Such rent is a higher-than-“normal” return that results from the restriction of competition.<sup>1</sup> And the restriction of competition, in turn, is a function of three factors: barriers to the entry of newcomers into the industry; availability of substitutes that can be used in place of what the industry produces; and ability of the members of the oligopoly to coordinate pricing and investment policy (formally or informally) among themselves.

To generate a flow of high earnings, a raw materials producer—whether private company or state agency—must ensure that he can profit from the restriction of competition at some stage that he controls and can pass the commodity at “high” prices continuously on downstream.

In fashioning a strategy to achieve this, the producer must make important but necessarily uncertain judgments about the potential entry of new producers to share his high profit rate, about the potential substitution of alternative products for his, and about what fellow members of the oligopoly will do in response to his choice of moves. In addition, he must try to calculate how best to protect himself from meeting concerted monopoly or oligopoly power at some stage that he does not control downstream from his operations, and how to avoid making his own behavior

<sup>1</sup> The higher-than-“normal” return also of course includes a “Ricardian” or scarcity rent, resulting from the particular characteristics of the Chilean mines that render them superior to the properties of the other members of the oligopoly.