Codelco: back to the People

Codelco, the state copper mining company, has a controversial history in Chile. The company was born out of an outright expropriation of foreign mining companies that gradually took place between 1966 and 1971, with minimal compensation paid to its owners. Later on, newly implemented market reforms would not consider returning its assets to their previous owners. The company was to remain in state hands, so much so as to even ratify this goal in the Constitution itself. Privatization proposals have risen from time to time but ideological opposition and, no less important, some past questionable privatization experiences, have plotted against it. What one could try to do then is to transform Codelco into a dividend paying firm to every living Chilean, after paying a specific 40% tax rate on its net revenues and keeping 10% of them for investment purposes. In so doing, money would start going back directly to the People, without intermediaries, and no constitutional restriction would be violated.

Codelco has been producing copper at levels close to 1.6 million tons per year since 1999. The country as a whole increased its production to 5.4 million tons in 2009 from 4.4 million tons a decade ago. To wit, in 1990, Codelco and Chile produced around 1.2 and 1.6 million tons of copper, respectively; in 2009, they each represented 9% and 30% of an 18 million ton world copper production. In terms of expansion possibilities, Codelco is presumed to have 17% of world copper reserves, much higher than its actual production. And last but not least, Codelco generated to the state coffers around US$ 31 billion from 2004 to 2008, equivalent to approximately one fifth of central government expenditures in the same period. Average prices, in 2008 US$, were near US$ 2.78 per pound in that five year period, whereas its cumulative figure since 1950 was US$ 2.03 per pound[1]. As for the copper market itself, it is less concentrated than the oil market, but not far from its cartelization nature practices.

The state mining company certainly looks as a sluggish and a “cash cow” firm. But one has to remember that because its capability has not been “efficiently” exploited, copper prices have most probably been higher than they would have been. Under the imperfect market scenario copper works, the frailty signaling from a potentially much bigger firm such as Codelco has pervaded the market. Furthermore, this higher price effect has been clearly captured through the income and royalty taxes collected over the other copper producing firms existing in Chile. In other words, we have been witnessing perhaps an unintended result, but one not to be minimized. Inefficiency rarely pays; this one is an exception.

The whole idea about reallocating Codelco´s dividends is to empower Chilean citizens, not the Chilean state. Given that its population amounts to 17 million people, each one would have received in the above period a total dividend close to US$ 900 – the monthly Chilean average wage is close to US$ 700 -. For those under 18 years, an account would be opened in their name until they reach this age. The remaining half of resources would have been used for investment purposes and tax payments, finally solving in the process the anomalous 10% charge for military expenditures as a function of copper sales.

[1] Sources: Codelco, Cochilco and DIPRES

The above proposition would also avoid selling the company or a fraction of it to third parties under imperfect capital markets, keeping that way the upside in the copper price and many times unknown but valuable mining properties. Moreover, new and bigger investments could be financed the same way Iraq is now doing so with its oil resources, offering to pay a fixed fee under an open bidding process for producing a pound of copper while retaining for Codelco the ups and downs of copper price variations[2].

Chilean central government and municipalities spend today over 20% of GDP, even considering that infrastructure and pension funds are collected aside. They already have enough resources. Over saving copper related revenues under sovereign funds does not make sense, much more so when this underdeveloped country is being pushed, contrary to its needs, to transform itself into a net creditor. People know better what they need. They just crave for the opportunity to manage those resources and 34 million eyes will be a much more involved “corporate board” than the present “budgetary” one which has been shown to be incapable, time and again, to confront powerful entrenched interests.

This might be a challenging proposal for the new government but it could finally work, for the real benefit of all Chileans. The present status quo does not. It does not suffice to improve managerial and board practices without a direct economic interest; the power and sway that could be created via an annual dividend for 17 million souls is a much better tool. And in the improbable case a sale of Codelco could be well structured and politically sanctioned, its proceeds should be received by Chileans, not the Chilean state. That confusion has hurt a lot this company and its real owners.

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[2] The same procedure could be applied over world scarce lithium resources existing in Chile.