The Shock Doctrine

by

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THE OTHER DOCTOR SHOCK

MILTON FRIEDMAN AND THE SEARCH FOR A LAISSEZ-FAIRE LABORATORY

> **Economic technocrats may be able to structure a tax reform here, a new social security law there, or a modified exchange rate regime somewhere else, but they really never have the luxury of a clean state on which to set up, in full flower as it were, their complete preferred economic policy framework.**
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> —Arnold Harberger, University of Chicago economics professor, 1998[1]

There are few academic environments as heavily mythologized as the University of Chicago's Economics Department in the 1950s, a place intensely conscious of itself not just as a school but as a School of Thought. It was not just training students; it was building and strengthening the Chicago School of economics, the brainchild of a coterie of conservative academics whose ideas represented a revolutionary bulwark against the dominant "statist" thinking of the day. To step through the doors of the Social Science Building, under the sign reading "Science Is Measurement," and into the legendary lunchroom, where students tested their intellectual mettle by daring to challenge their titanic professors, was to seek nothing so prosaic as a degree. It was to enlist in battle. As Gary Becker, the conservative economist and Nobel Prize winner, put it, "We were warriors in combat with most of the rest of the profession."[2]

Like Ewen Cameron's psychiatric department at McGill in the same period, the University of Chicago's Economics Department was in the thrall of an ambitious and charismatic man on a mission to fundamentally revolutionize his profession. That man was Milton Friedman. Though he had many mentors and colleagues who believed just as fiercely as he did in ultra laissez-faire, it was Friedman's energy that gave the school its revolutionary fervor. "People would always ask me, 'Why are you so excited? Are you going out on a date with a beautiful woman?'" recalls Becker. "I said, 'No, I'm going to a class in economics!' Being a student of Milton's was magic indeed."[3]

Friedman's mission, like Cameron's, rested on a dream of reaching back to a state of "natural" health, when all was in balance, before human interferences created distorting patterns. Where Cameron dreamed of returning the human mind to that pristine state, Friedman dreamed of depatterning societies, of returning them to a state of pure capitalism, cleansed of all interruptions—government regulations, trade barriers and entrenched interests. Also like Cameron, Friedman believed that when the economy is highly distorted, the only way to reach that prelapsarian state was to deliberately inflict painful shocks: only "bitter medicine" could clear those distortions and bad patterns out of the way. Cameron used electricity to inflict his shocks; Friedman's tool of choice was policy—the shock treatment approach he urged on bold politicians for countries in distress. Unlike Cameron, however, who was able to instantly apply his pet theories on his unwitting patients, Friedman would need two decades and several twists and turns of history before he too got the chance to put his dreams of radical erasure and creation into action in the real world.

Frank Knight, one of the founders of Chicago School economics, thought professors should "inculcate" in their students the belief that each economic theory is "a sacred feature of the system," not a debatable hypothesis.[4] The core of such sacred Chicago teachings was that the economic forces of supply, demand, inflation and unemployment were like the forces of nature, fixed and unchanging. In the truly free market imagined in Chicago classes and texts, these forces existed in perfect equilibrium, supply communicating with demand the way the moon pulls the tides. If economies suffered from high inflation, it was, according to Friedman's strict theory of monetarism, invariably because misguided policy makers had allowed too much money to enter the system, rather than letting the market find its balance. Just as ecosystems self-regulate, keeping themselves in balance, the market, left to its own devices, would create just the right number of products at precisely the right prices, produced by workers at just the right wages to buy those products—an Eden of plentiful employment, boundless creativity and zero inflation.

According to the Harvard sociologist Daniel Bell, this love of an idealized system is the defining quality of radical free-market economics. Capitalism is envisaged as "a jeweled set of movements" or a "celestial clockwork . . . a work of art, so compelling that one thinks of the celebrated pictures of Apelles who painted a cluster of grapes so realistic that the birds would come and pick at them."[5]

The challenge for Friedman and his colleagues was how to prove that a real-world market could live up to their rapturous imaginings. Friedman always prided himself on approaching economics as a science as hard and rigorous as physics or chemistry. But hard scientists could point to the behavior of the elements to prove their theories. Friedman could not point to any living economy that proved that if all "distortions" were stripped away, what would be left would be a society in perfect health and bounteous, since no country in the world met the criteria for perfect laissez-faire. Unable to test their theories in central banks and ministries of trade, Friedman and his colleagues had to settle for elaborate and ingenious mathematical equations and computer models mapped out in the basement workshops of the social sciences building.

A love of numbers and systems is what had led Friedman to economics. In his autobiography, he says his moment of epiphany came when a high-school geometry teacher wrote the Pythagorean theorem on the blackboard and then, awed by its elegance, quoted from John Keats's "Ode on a Grecian Urn": "'Beauty is truth, truth beauty,'—that is all / Ye know on earth, and all ye need to know."[6] Friedman passed on that same ecstatic love of a beautiful all-encompassing system to generations of economics scholars—along with a search for simplicity, elegance and rigor.

Like all fundamentalist faiths, Chicago School economics is, for its true believers, a closed loop. The starting premise is that the free market is a perfect scientific system, one in which individuals, acting on their own self-interested desires, create the maximum benefits for all. It follows ineluctably that if something is wrong within a free-market economy—high inflation or soaring unemployment—it has to be because the market is not truly free. There must be some interference, some distortion in the system. The Chicago solution is always the same: a stricter and more complete application of the fundamentals.

When Friedman died in 2006, obituary writers struggled to summarize the breadth of his legacy. One settled on this statement: "Milton's mantra of free markets, free prices, consumer choice and economic liberty is responsible for the global prosperity we enjoy today."[7] This is partially true. The nature of that global prosperity—who shares in it, who doesn't, where it came from—are all highly contested, of course. What is irrefutable is the fact that Friedman's free-market rulebook, and his savvy strategies for imposing it, have made some people extremely prosperous, winning for them something approximating complete freedom—to ignore national borders, to avoid regulation and taxation and to amass new wealth.

This knack for thinking highly profitable thoughts appears to have its roots in Friedman's early childhood, when his parents, immigrants from Hungary, bought a garment factory in Rahway, New Jersey. The family apartment was in the same building as the shop floor, which, Friedman wrote, "would be termed a sweatshop today."[8] Those were volatile times for sweatshop owners, with Marxists and anarchists organizing immigrant workers into unions to demand safety regulations and weekends off—and debating the theory of worker ownership at after-shift meetings. As the boss's son, Friedman no doubt heard a very different perspective on these debates. In the end, his father's factory went under, but in lectures and television appearances, Friedman spoke of it often, invoking it as a case study for the benefits of deregulated capitalism—proof that even the worst, least-regulated jobs offer the first rung on the ladder to freedom and prosperity.

A large part of the appeal of Chicago School economics was that, at a time when radical-left ideas about workers' power were gaining ground around the world, it provided a way to defend the interests of owners that was just as radical and was infused with its own claims to idealism. To hear Friedman tell it, his ideas were not about defending the right of factory owners to pay low wages but, rather, all about a quest for the purest possible form of "participatory democracy" because in the free market, "each man can vote, as it were, for the color of tie he wants."[9] Where leftists promised freedom for workers from bosses, citizens from dictatorship, countries from colonialism, Friedman promised "individual freedom," a project that elevated atomized citizens above any collective enterprise and liberated them to express their absolute free will through their consumer choices. "What was particularly exciting were the same qualities that made Marxism so appealing to many other young people at the time," recalled the economist Don Patinkin, who studied at Chicago in the forties—"simplicity together with apparent logical completeness; idealism combined with radicalism."[10] The Marxists had their workers' utopia, and the Chicagoans had their entrepreneurs' utopia, both claiming that if they got their way, perfection and balance would follow.

The question, as always, was how to get to that wondrous place from here. The Marxists were clear: revolution—get rid of the current system, replace it with socialism. For the Chicagoans, the answer was not as straightforward. The United States was already a capitalist country, but as far as they were concerned, just barely. In the U.S., and in all supposedly capitalist economies, the Chicagoans saw interferences everywhere. To make products more affordable, politicians fixed prices; to make workers less exploited, they set minimum wages; to make sure everyone had access to education, they kept it in the hands of the state. These measures often seemed to help people, but Friedman and his colleagues were convinced—and they "proved" it with their models—that they were actually doing untold harm to the equilibrium of the market and the ability of its various signals to communicate with each other. The mission of the Chicago School was thus one of purification—stripping the market of these interruptions so that the free market could sing.

For this reason, Chicagoans did not see Marxism as their true enemy. The real source of the trouble was to be found in the ideas of the Keynesians in the United States, the social democrats in Europe and the developmentalists in what was then called the Third World. These were believers not in a utopia but in a mixed economy, to Chicago eyes an ugly hodgepodge of capitalism for the manufacture and distribution of consumer products, socialism in education, state ownership for essentials like water services, and all kinds of laws designed to temper the extremes of capitalism. Like the religious fundamentalist who has a grudging respect for fundamentalists of other faiths and for avowed atheists but disdains the casual believer, the Chicagoans declared war on these mix-and-match economists. What they wanted was not a revolution exactly but a capitalist Reformation: a return to uncontaminated capitalism.

Much of this purism came from Friedrich Hayek, Friedman's own personal guru, who also taught at the University of Chicago for a stretch in the 1950s. The austere Austrian warned that any government involvement in the economy would lead society down "the road to serfdom" and had to be expunged.[11] According to Arnold Harberger, a longtime professor at Chicago, "the Austrians," as this clique-within-a-clique was called, were so zealous that any state interference was not just wrong, but "evil. . . . It's as if there is a very pretty but highly complex picture out there, which is perfectly harmonious within itself, you see, and if there's a speck where it isn't supposed to be well, that's just awful . . . it is a flaw that mars that beauty."[12]

In 1947, when Friedman first joined with Hayek to form the Mont Pelerin Society, a club of free-market economists named for its location in Switzerland, the idea that business should be left alone to govern the world as it wished was one barely suitable for polite company. Memories of the market crash of 1929 and the Great Depression that followed were still fresh—the life savings destroyed overnight, the suicides, the soup kitchens, the refugees. The scale of this market-created disaster had led to a surging demand for a distinctly hands-on form of government. The Depression did not signal the end of capitalism, but it was, as John Maynard Keynes forecast a few years earlier, "the end of *laissez-faire*"—the end of letting the market regulate itself.[13] The 1930s through to the early 1950s was a time of unabashed *faire*: the can-do ethos of the New Deal gave way to the war effort, with public works programs launched to create much-needed jobs, and new social programs unveiled to prevent growing numbers of people from turning hard left. It was a time when compromise between left and right was not a dirty word but part of what many saw as a noble mission to prevent a world, as Keynes wrote to President Franklin D. Roosevelt in 1933, in which "orthodoxy and revolution" are left "to fight it out."[14] John Kenneth Galbraith, heir to Keynes's mantle in the U.S., described the prime missions of politicians and economists alike as "the avoidance of depression and the prevention of unemployment."[15]

The Second World War lent new urgency to the war against poverty. Nazism had taken root in Germany at a time when the country was in a devastating depression, provoked by the punishing reparations imposed after the First World War and deepened by the 1929 crash. Keynes had warned early on that if the world took a laissez-faire approach to Germany's poverty, the blowback would be ferocious: "Vengeance, I dare predict, will not limp."[16] Those words went unheeded at the time, but when Europe was rebuilt after the Second World War, the Western powers embraced the principle that market economies needed to guarantee enough basic dignity that disillusioned citizens would not go looking once again for a more appealing ideology, whether fascism or Communism. It was this pragmatic imperative that led to the creation of almost everything that we associate today with the bygone days of "decent" capitalism—social security in the U.S., public health care in Canada, welfare in Britain, workers' protections in France and Germany.

A similar, more radical mood was on the rise in the developing world, usually going under the name developmentalism, or Third World nationalism. Developmentalist economists argued that their countries would finally escape the cycle of poverty only if they pursued an inward-oriented industrialization strategy instead of relying on the export of natural resources, whose prices had been on a declining path, to Europe and North America. They advocated regulating or even nationalizing oil, minerals and other key industries so that a healthy share of the proceeds fed a government-led development process.

By the 1950s, the developmentalists, like the Keynesians and social democrats in rich countries, were able to boast a series of impressive success stories. The most advanced laboratory of developmentalism was the southern tip of Latin America, known as the Southern Cone: Chile, Argentina, Uruguay and parts of Brazil. The epicenter was the United Nations' Economic Commission for Latin America, based in Santiago, Chile, and headed by the economist Raúl Prebisch from 1950 to 1963. Prebisch trained teams of economists in developmentalist theory and dispatched them to act as policy advisers for governments across the continent. Nationalist politicians like Argentina's Juan Perón put their ideas into practice with a vengeance, pouring public money into infrastructure projects such as highways and steel plants, giving local businesses generous subsidies to build their new factories, churning out cars and washing machines, and keeping out foreign imports with forbiddingly high tariffs.

During this dizzying period of expansion, the Southern Cone began to look more like Europe and North America than the rest of Latin America or other parts of the Third World. The workers in the new factories formed powerful unions that negotiated middle-class salaries, and their children were sent off to study at newly built public universities. The yawning gap between the region's polo-club elite and its peasant masses began to narrow. By the 1950s, Argentina had the largest middle class on the continent, and next-door Uruguay had a literacy rate of 95 percent and offered free health care for all citizens. Developmentalism was so staggeringly successful for a time that the Southern Cone of Latin America became a potent symbol for poor countries around the world: here was proof that with smart, practical policies, aggressively implemented, the class divide between the First and Third World could actually be closed.

All this success for managed economies—in the Keynesian north and the developmentalist south—made for dark days at the University of Chicago's Economics Department. The Chicagoans' academic archrivals at Harvard, Yale and Oxford were being enlisted by presidents and prime ministers to help tame the beast of the market; almost no one was interested in Friedman's daring ideas about letting it run even more wildly than before. There were, however, a few people left who were keenly interested in Chicago School ideas—and they were a powerful few.

For the heads of U.S. multinational corporations, contending with a distinctly less hospitable developing world and with stronger, more demanding unions at home, the postwar boom years were unsettling times. The economy was growing fast, enormous wealth was being created, but owners and shareholders were forced to redistribute a great deal of that wealth through corporate taxes and workers' salaries. Everyone was doing well, but with a return to the pre–New Deal rules, a few people could have been doing a lot better.

The Keynesian revolution against laissez-faire was costing the corporate sector dearly. Clearly what was needed to regain lost ground was a counterrevolution against Keynesianism, a return to a form of capitalism even less regulated than before the Depression. This wasn't a crusade that Wall Street itself could lead—not in the current climate. If Friedman's close friend Walter Wriston, head of Citibank, had come forward and argued that the minimum wage and corporate taxes should both be abolished, he naturally would have been accused of being a robber baron. And that's where the Chicago School came in. It quickly became clear that when Friedman, a brilliant mathematician and skilled debater, made those same arguments, they took on an entirely different quality. They might be dismissed as wrongheaded but they were imbued with an aura of scientific impartiality. The enormous benefit of having corporate views funneled through academic, or quasi-academic, institutions not only kept the Chicago School flush with donations but, in short order, spawned the global network of right-wing think tanks that would churn out the counterrevolution's foot soldiers worldwide.

It all came back to Friedman's single-minded message: everything went wrong with the New Deal. That's when so many countries "including my own, got off on the wrong track."[17] To get governments back on the right track, Friedman, in his first popular book, *Capitalism and Freedom*, laid out what would become the global free-market rulebook and, in the U.S., would form the economic agenda of the neoconservative movement.

First, governments must remove all rules and regulations standing in the way of the accumulation of profits. Second, they should sell off any assets they own that corporations could be running at a profit. And third, they should dramatically cut back funding of social programs. Within the three-part formula of deregulation, privatization and cutbacks, Friedman had plenty of specifics. Taxes, when they must exist, should be low, and rich and poor should be taxed at the same flat rate. Corporations should be free to sell their products anywhere in the world, and governments should make no effort to protect local industries or local ownership. All prices, including the price of labor, should be determined by the market. There should be no minimum wage. For privatization, Friedman offered up health care, the post office, education, retirement pensions, even national parks. In short, and quite unabashedly, he was calling for the breaking of the New Deal—that uneasy truce between the state, corporations and labor that had prevented popular revolt after the Great Depression. Whatever protections workers had managed to win, whatever services the state now provided to soften the edges of the market, the Chicago School counterrevolution wanted them back.

And it wanted more than that—it wanted to expropriate what workers and governments had built during those decades of frenetic public works. The assets that Friedman urged government to sell were the end products of the years of investment of public money and know-how that had built them and made them valuable. As far as Friedman was concerned, all this shared wealth should be transferred into private hands, on principle.

Though always cloaked in the language of math and science, Friedman's vision coincided precisely with the interests of large multinationals, which by nature hunger for vast new unregulated markets. In the first stage of capitalist expansion, that kind of ravenous growth was provided by colonialism—by "discovering" new territories and grabbing land without paying for it, then extracting riches from the earth without compensating local populations. Friedman's war on the "welfare state" and "big government" held out the promise of a new font of rapid riches—only this time, rather than conquering new territory, the state itself would be the new frontier, its public services and assets auctioned off for far less than they were worth.

The War against Developmentalism

In the United States of the 1950s, access to those kinds of riches was still decades away. Even with a hard-core Republican like Dwight Eisenhower in the White House, there was no chance of a radical right turn like the one the

Chicagoans were suggesting—public services and workers' protections were far too popular, and Eisenhower was looking to the next election. Although he had little appetite for reversing Keynesianism at home, Eisenhower proved eager to take swift and radical action to defeat developmentalism abroad. It was a campaign in which the University of Chicago would eventually play a pivotal role.

When Eisenhower took office in 1953, Iran had a developmentalist leader in Mohammad Mossadegh, who had already nationalized the oil company, and Indonesia was in the hands of the increasingly ambitious Achmed Sukarno, who was talking about linking up all the nationalist governments of the Third World into a superpower on par with the West and the Soviet Bloc. Of particular concern to the State Department was the growing success of nationalist economics in the Southern Cone of Latin America. At a time when large portions of the globe were turning to Stalinism and Maoism, developmentalist proposals for "import substitution" were actually quite centrist. Still, the idea that Latin America deserved its own New Deal had powerful enemies. The continent's feudal landowners had been happy with the old status quo, which supplied them with steep profits and a limitless pool of poor peasants to work in the fields and mines. Now, they were outraged to see their profits being diverted to build up other sectors, their workers demanding land redistribution, and the government keeping the price of their crops artificially low so food could be affordable. American and European corporations doing business in Latin America began to express similar complaints to their governments: their products were being blocked at the borders, their workers were demanding higher wages and, most alarmingly, there was growing talk that everything from foreign-owned mines to banks could be nationalized to finance Latin America's dream of economic independence.

Under pressure from these corporate interests, a movement took hold in American and British foreign policy circles that attempted to pull developmentalist governments into the binary logic of the Cold War. Don't be fooled by the moderate, democratic veneer, these hawks warned: Third World nationalism was the first step on the road to totalitarian Communism and should be nipped in the bud. Two of the chief proponents of this theory were John Foster Dulles, Eisenhower's secretary of state, and his brother Allen Dulles, head of the newly created CIA. Before taking public posts, both had worked at the legendary New York law firm Sullivan & Cromwell, where they represented many of the companies that had the most to lose from developmentalism, among them J. P. Morgan & Company, the International Nickel Company, the Cuban Sugar Cane Corporation and the United Fruit Company.[18] The results of the Dulleses' ascendancy were immediate: in 1953 and 1954, the CIA staged its first two coups d'état, both against Third World governments that identified far more with Keynes than with Stalin.

The first was in 1953, when a CIA plot successfully overthrew Mossadegh in Iran, replacing him with the brutal shah. The next was the 1954 CIA-sponsored coup in Guatemala, done at the direct behest of the United Fruit Company. The corporation, which still had the ear of the Dulles brothers from their Cromwell days, was indignant that President Jacobo Arbenz Guzmán had expropriated some of its unused land (with full compensation) as part of his project to transform Guatemala, as he put it, "from a backward country with a predominantly feudal economy into a modern capitalist state"—apparently an unacceptable goal.[19] Soon enough Arbenz was out, and United Fruit was back in charge.

Eradicating developmentalism in the Southern Cone, where it had taken far deeper root, was a much greater challenge. Figuring out how to achieve that goal was the topic of discussion between two American men as they met in Santiago, Chile, in 1953. One was Albion Patterson, director of the U.S. International Cooperation Administration in Chile—the agency that would later become USAID—and the other was Theodore W. Schultz, chairman of the Department of Economics at the University of Chicago. Patterson had become increasingly concerned about the maddening influence of Raúl Prebisch and Latin America's other "pink" economists. "What we need to do is change the formation of the men, to influence the education, which is very bad," he had stressed to a colleague.[20] This objective coincided with Schultz's own belief that the U.S. government wasn't doing enough to fight the intellectual war with Marxism. "The United States must take stock of its economic programs abroad . . . we want [the poor countries] to work out their economic salvation by relating themselves to us and by using our way of achieving their economic development," he said.[21]

The two men came up with a plan that would eventually turn Santiago, a hotbed of state-centered economics, into its opposite—a laboratory for cutting-edge free-market experiments, giving Milton Friedman what he had longed for: a country in which to test his cherished theories. The original plan was simple: the U.S. government would pay to send Chilean students to study economics at what pretty much everyone recognized was the most rabidly anti-"pink" school in the world—the University of Chicago. Schultz and his colleagues at the university would also be paid to travel to Santiago to conduct research into the Chilean economy and to train students and professors in Chicago School fundamentals.

What set the plan apart from other U.S. training programs that sponsored Latin American students, of which there were many, was its unabashedly ideological character. By selecting Chicago to train Chileans—a school where the professors agitated for the near-complete dismantling of government with single-minded focus—the U.S. State Department was firing a shot across the bow in its war against developmentalism, effectively telling Chileans that the U.S. government had decided what ideas their elite students should and should not learn. This was such blatant U.S. intervention in Latin American affairs that when Albion Patterson approached the dean of the University of Chile, the country's premiere university, and offered him a grant to set up the exchange program, the dean turned him down. He said he would participate only if his faculty had input into who in the U.S. was training his students. Patterson went on to approach the dean of a lesser institution, Chile's Catholic University, a much more conservative school with no economics department. The dean at the Catholic University jumped at the offer, and what became known in Washington and Chicago as "the Chile Project" was born.

"We came here to compete, not to collaborate," said Schultz of the University of Chicago, explaining why the program would be closed to all Chilean students but the few selected.[22] This combative stance was explicit from the start: the goal of the Chile Project was to produce ideological warriors who would win the battle of ideas against Latin America's "pink" economists.

Officially launched in 1956, the project saw one hundred Chilean students pursue advanced degrees at the University of Chicago between 1957 and 1970, their tuition and expenses paid for by U.S. taxpayers and U.S. foundations. In 1965, the program was expanded to include students from across Latin America, with particularly heavy participation from Argentina, Brazil and Mexico. The expansion was funded through a grant from the Ford Foundation and led to the creation of the Center for Latin American Economic Studies at the University of Chicago. Under the program, there were forty to fifty Latin Americans studying graduate-level economics at any given time—roughly one-third of the department's total student population. In comparable programs at Harvard or MIT, there were just four or five Latin Americans. It was a startling achievement: in just a decade, the ultraconservative University of Chicago had become the premier destination for Latin Americans wanting to study economics abroad, a fact that would shape the course of the region's history for decades to come.

Indoctrinating the visitors in Chicago School orthodoxy became a pressing institutional priority. The head of the program, and the man in charge of making the Latin Americans feel welcome, was Arnold Harberger, a safari-suit-wearing economist who spoke fluent Spanish, had married a Chilean and described himself as "a seriously dedicated missionary."[23] When the Chilean students started arriving, Harberger created a special "Chile workshop" where University of Chicago professors presented their highly ideological diagnosis of what was wrong with the South American country—and offered their scientific prescriptions on how to fix it.

"Suddenly, Chile and its economy became a topic of daily conversation in the Department of Economics," recalled André Gunder Frank, who studied under Friedman in the 1950s and went on to become a world-renowned development economist.[24] All of Chile's policies were put under the microscope and found wanting: its strong social safety net, its protections for national industry, its trade barriers, its controls on prices. Students were taught disdain for these attempts to alleviate poverty, and many of them devoted their PhD theses to dissecting the follies of Latin American developmentalism.[25] When Harberger would return from his frequent trips to Santiago in the fifties and sixties, Gunder Frank recalled that he would lambaste Santiago, Chile's health and education systems—the best on the continent—as "absurd attempts to live beyond its underdeveloped means."[26]

Within the Ford Foundation, there were concerns about financing such an overtly ideological program. Some pointed out that the only Latin American speakers invited to address the students in Chicago were alumni of the same program. "Although the quality and impact of this endeavor cannot be denied, its ideological narrowness constituted a serious deficiency," wrote Jeffrey Puryear, a Latin American specialist with Ford, in one of the foundation's internal reviews. "The interests of developing countries are not well-served by exposure to a single point of view."[27] This assessment did not stop Ford from continuing to fund the program.

When the first group of Chileans returned home from Chicago, they were "even more Friedmanite than Friedman himself," in the words of

Mario Zañartu, an economist at Santiago's Catholic University.*[28] Many took up posts as economics professors in the Catholic University Economics Department, rapidly turning it into their own little Chicago School in the middle of Santiago—the same curriculum, the same English-language texts, the same unyielding claim to "pure" and "scientific" knowledge. By 1963, twelve of the department's thirteen full-time faculty members were graduates of the University of Chicago program, and Sergio de Castro, one of the first graduates, was appointed faculty chairman.[29] Now Chilean students didn't need to travel all the way to the U.S.—hundreds could get a Chicago School education without leaving home.

The students who went through the program, whether in Chicago or its franchise operation in Santiago, became known throughout the region as "los Chicago Boys." With more funding from USAID, Chile's Chicago Boys became enthusiastic regional ambassadors for ideas Latin Americans call "neoliberalism," traveling to Argentina and Colombia to set up more University of Chicago franchises in order to "expand this knowledge throughout Latin America, confronting the ideological positions which prevented freedom and perpetuated poverty and backwardness," according to one Chilean graduate.[30]

Juan Gabriel Valdés, Chile's foreign minister in the 1990s, described the process of training hundreds of Chilean economists in Chicago School orthodoxy as "a striking example of an organized transfer of ideology from the United States to a country within its direct sphere of influence . . . the education of these Chileans derived from a specific project designed in the 1950s to influence the development of Chilean economic thinking." He pointed out that "they introduced into Chilean society ideas that were completely new, concepts entirely absent from the 'ideas market.'"[31]

As a form of intellectual imperialism, it was certainly unabashed. There was, however, a problem: it wasn't working. According to a 1957 report from the University of Chicago to its funders at the State Department, "the central purpose of the project" was to train a generation of students "who would become the intellectual leaders in economic affairs in Chile."[32] But the Chicago Boys weren't leading their countries anywhere—in fact, they were being left behind.

In the early sixties, the main economic debate in the Southern Cone was not about laissez-faire capitalism versus developmentalism but about how best to take developmentalism to the next stage. Marxists argued for extensive nationalization and radical land reforms; centrists argued that the key was greater economic cooperation among Latin American countries, with the goal of transforming the region into a powerful trading bloc to rival Europe and North America. At the polls and on the streets, the Southern Cone was surging to the left.

In 1962, Brazil moved decisively in this direction under the presidency of João Goulart, an economic nationalist committed to land redistribution, higher salaries and a daring plan to force foreign multinationals to reinvest a percentage of their profits back into the Brazilian economy rather than spiriting them out of the country and distributing them to shareholders in New York and London. In Argentina, a military government was trying to defeat similar demands by banning the party of Juan Perón from running in elections, but the move had only radicalized a new generation of young Peronists, many of whom were willing to use arms to retake the country.

It was in Chile—the epicenter of the Chicago experiment—that defeat in the battle of ideas was most evident. By Chile's historic 1970 elections, the country had moved so far left that all three major political parties were in favor of nationalizing the country's largest source of revenue: the copper mines then controlled by U.S. mining giants.[33] The Chile Project, in other words, was an expensive bust. As ideological warriors waging a peaceful battle of ideas with their left-wing foes, the Chicago Boys had failed in their mission. Not only was the economic debate continuing to shift leftward, but the Chicago Boys were so marginal that they did not even register on the Chilean electoral spectrum.

It might have ended there, with the Chile Project just a minor historical footnote, but something happened to rescue the Chicago Boys from obscurity: Richard Nixon was elected president of the United States. Nixon "had an imaginative, and on the whole effective, foreign policy," Friedman enthused.[34] And nowhere was it more imaginative than in Chile.

It was Nixon who would give the Chicago Boys and their professors something they had long dreamed of: a chance to prove that their capitalist utopia was more than a theory in a basement workshop—a shot at remaking a country from scratch. Democracy had been inhospitable to the Chicago Boys in Chile; dictatorship would prove an easier fit.

Salvador Allende's Popular Unity government won Chile's 1970 elections on a platform promising to put into government hands large sectors of the economy

* Walter Heller, the famed Kennedy-government economist, once mocked the cultishness of Friedman's followers by dividing them into categories: "Some are Friedmanly, some Friedmanian, some Friedmanesque, some Friedmanic and some Friedmaniacs."

that were being run by foreign and local corporations. Allende was a new breed of Latin American revolutionary: like Che Guevara, he was a doctor, but unlike Che, he looked the part of the tweedy academic, not the romantic guerrilla. He could deliver a stump speech as fiery as any by Fidel Castro, but he was a fierce democrat who believed that socialist change in Chile needed to come through the ballot box, not the barrel of a gun. When Nixon heard that Allende had been elected president, he famously ordered the CIA director, Richard Helms, to "make the economy scream."[35] The election also reverberated throughout the University of Chicago Economics Department. When Allende won, Arnold Harberger happened to be in Chile. He wrote a letter home to his colleagues describing the event as a "tragedy" and informing them that "in rightist circles the idea of a military takeover is also sometimes broached."[36]

Although Allende pledged to negotiate fair terms to compensate companies that were losing property and investments, U.S. multinationals feared that Allende represented the beginning of a Latin America-wide trend, and many were unwilling to accept the prospect of losing what was a growing portion of their bottom line. By 1968, 20 percent of total U.S. foreign investment was tied up in Latin America, and U.S. firms had 5,436 subsidiaries in the region. The profits that these investments were able to produce were staggering. Mining companies had invested $1 billion over the previous fifty years in Chile's copper mining industry—the largest in the world—but they had sent $7.2 billion home.[37]

As soon as Allende won the vote, and before he was even inaugurated, corporate America declared war on his administration. The center of activity was the Washington-based Ad Hoc Committee on Chile, a group that included the major U.S. mining companies with holdings in Chile, as well as the de facto leader of the committee, the International Telephone and Telegraph Company (ITT), which owned 70 percent of Chile's soon-to-be-nationalized phone company. Purina, Bank of America and Pfizer Chemical also sent delegates at various stages.

The committee's single purpose was to force Allende to back off his nationalizations "by confronting him with economic collapse."[38] They had many ideas for how to make Allende feel the pain. According to declassified meeting minutes, the companies planned to block U.S. loans to Chile and "quietly have large U.S. private banks do the same. Confer with foreign banking sources with the same thing in mind. Delay buying from Chile over the next six months. Use U.S. copper stockpile instead of buying from Chile. Bring about a scarcity of U.S. dollars in Chile." And the list goes on.[39]

Allende appointed his close friend Orlando Letelier to be his ambassador to Washington; that gave him the task of negotiating the terms of expropriation with the same corporations plotting to sabotage the Allende government. Letelier, a fun-loving extrovert with a quintessential seventies moustache and a devastating singing voice, was much beloved in diplomatic circles. His son Francisco's fondest memories are of listening to his father play the guitar and belt out folk songs at gatherings of friends in their Washington home.[40] But even with all Letelier's charm and skill, the negotiations never stood a chance of success.

In March 1972, in the midst of Letelier's tense negotiation with ITT, Jack Anderson, a syndicated newspaper columnist, published an explosive series of articles based on documents that showed that the telephone company had secretly plotted with the CIA and the State Department to block Allende from being inaugurated two years earlier. In the face of these allegations, and with Allende still in power, the U.S. Senate, controlled by Democrats, launched an investigation and uncovered a far-reaching conspiracy in which ITT had offered $1 million in bribes to Chilean opposition forces and "sought to engage the CIA in a plan covertly to manipulate the outcome of the Chilean presidential election."[41]

The Senate report, released in June 1973, also found that when the plan failed and Allende took power, ITT moved to a new strategy designed to ensure that he would not "make it through the next six months." Most alarming to the Senate was the relationship between ITT executives and the U.S. government. In testimony and documents, it became clear that ITT was directly involved in shaping U.S. policy toward Chile at the highest level. At one point, a senior ITT executive wrote to National Security Adviser Henry Kissinger and suggested that "without informing President Allende, all U.S. aid funds already committed to Chile should be placed in the 'under review' status." The company also took the liberty of preparing an eighteen-point strategy for the Nixon administration that contained a clear call for a military coup: "Get to reliable sources within the Chilean military," it stated ". . . build up their planned discontent against Allende, thus, bring about necessity of his removal."[42]

When grilled by the Senate committee about his brazen attempts to harness the force of the U.S. government to subvert Chile's constitutional process in order to further ITT's own economic interests, the company's vice president, Ned Gerrity, seemed genuinely confused. "What's wrong with taking care of No. 1?" he asked. The committee offered a response in its report:

"'No. I' should not be allowed an undue role in determining U.S. foreign policy."[43]

Yet despite years of relentless American dirty tricks, of which ITT was only the most scrutinized example, in 1973 Allende was still in power. Eight million dollars in covert spending had failed to weaken his base. In midterm parliamentary elections that year, Allende's party actually gained support beyond the number that had first elected it in 1970. Clearly, the desire for a different economic model had taken deep root in Chile, and support for a socialist alternative was growing. For Allende's opponents, who had been plotting his overthrow since the day the 1970 election results came in, that meant their problems would not be solved by simply getting rid of him—someone else would just come along and replace him. A more radical plan was needed.

Lessons in Regime Change: Brazil and Indonesia

There were two models of "regime change" that Allende's opponents had been studying closely as possible approaches. One was in Brazil, the other in Indonesia. When Brazil's U.S.-backed junta, led by General Humberto Castello Branco, seized power in 1964, the military had a plan not merely to reverse João Goulart's pro-poor programs but to crack Brazil wide open to foreign investment. At first, the Brazilian generals tried to impose the agenda relatively peacefully—there were no obvious shows of brutality, no mass arrests, and though it was later discovered that some "subversives" had been brutally tortured during this period, their numbers were small enough (and Brazil so large) that word of their treatment barely escaped the jails. The junta also made a point of keeping some remnants of democracy in place, including limited press freedoms and freedom of assembly—a so-called gentlemen's coup.

In the late sixties, many citizens decided to use those limited freedoms to express their anger at Brazil's deepening poverty, for which they blamed the junta's pro-business economic program, much of it designed by graduates of the University of Chicago. By 1968 the streets were overrun with antijunta marches, the largest led by students, and the regime was in serious jeopardy. In a desperate bid to hold on to power, the military radically changed tactics: democracy was shut down completely, all civil liberties were crushed, torture became systematic, and, according to Brazil's later-established truth commission, "killings by the state became routine."[44]

Indonesia's 1965 coup followed a very different trajectory. Since the Second World War, the country had been led by President Sukarno, the Hugo Chávez of his day (though minus Chávez's appetite for elections). Sukarno enraged the rich countries by protecting Indonesia's economy, redistributing wealth and throwing out the International Monetary Fund and the World Bank, which he accused of being facades for the interests of Western multinationals. While Sukarno was a nationalist, not a Communist, he worked closely with the Communist Party, which had 3 million active members. The U.S. and British governments were determined to end Sukarno's rule, and declassified documents show that the CIA had received high-level directions to "liquidate President Sukarno, depending upon the situation and available opportunities."[45]

After several false starts, the opportunity came in October 1965, when General Suharto, backed by the CIA, began the process of seizing power and eradicating the left. The CIA had been quietly compiling a list of the country's leading leftists, a document that fell into Suharto's hands, while the Pentagon helped out by supplying extra weapons and field radios so Indonesian forces could communicate in the remotest parts of the archipelago. Suharto then sent out his soldiers to hunt down the four to five thousand leftists on his "shooting lists," as the CIA referred to them; the U.S. embassy received regular reports on their progress.[46] As the information came in, the CIA crossed names off their lists until they were satisfied that the Indonesian left had been annihilated. One of the people involved in the operation was Robert J. Martens, who worked for the U.S. embassy in Jakarta. "It really was a big help to the army," he told the journalist Kathy Kadane twenty-five years later. "They probably killed a lot of people, and I probably have a lot of blood on my hands, but that's not all bad. There's a time when you have to strike hard at a decisive moment."[47]

The shooting lists covered the targeted killing; the more indiscriminate massacres for which Suharto is infamous were, for the most part, delegated to religious students. They were quickly trained by the military and then sent into villages on instructions from the chief of the navy to "sweep" the countryside of Communists. "With relish," wrote one reporter, "they called out their followers, stuck their knives and pistols in their waistbands, swung their clubs over their shoulders, and embarked on the assignment for which they had long been hoping."[48] In just over a month, at least half a million and possibly as many as 1 million people were killed, "massacred by the thousands," according to *Time*.[49] In East Java, "Travelers from those areas tell of small rivers and streams that have been literally clogged with bodies; river transportation has at places been impeded."[50]

The Indonesian experience attracted close attention from the individuals and institutions plotting the overthrow of Salvador Allende in Washington and Santiago. Of interest was not only Suharto's brutality but also the extraordinary role played by a group of Indonesian economists who had been educated at the University of California at Berkeley, known as the Berkeley Mafia. Suharto was effective at getting rid of the left, but it was the Berkeley Mafia who prepared the economic blueprint for the country's future.

The parallels with the Chicago Boys were striking. The Berkeley Mafia had studied in the U.S. as part of a program that began in 1956, funded by the Ford Foundation. They had also returned home to build a faithful copy of a Western-style economics department, theirs at the University of Indonesia's Faculty of Economics. Ford sent American professors to Jakarta to establish the school, just as Chicago profs had gone to help set up the new economics department in Santiago. "Ford felt it was training the guys who would be leading the country when Sukarno got out," John Howard, then director of Ford's International Training and Research Program, bluntly explained.[51]

Ford-funded students became leaders of the campus groups that participated in overthrowing Sukarno, and the Berkeley Mafia worked closely with the military in the lead-up to the coup, developing "contingency plans" should the government suddenly fall.*[52] These young economists had enormous influence over General Suharto, who knew nothing of high finance. According to *Fortune* magazine, the Berkeley Mafia recorded economics lessons on audiotapes for Suharto to listen to at home.[53] When they met in person, "President Suharto did not merely listen, he took notes," one member of the group recalled with pride.[54] Another Berkeley grad described the relationship in this way: we "presented to the Army leadership—the crucial element in the new order—a 'cookbook' of 'recipes' for dealing with Indonesia's serious economic problems. General Suharto as the top Army commander not only accepted the cookbook, but also wanted the authors of the recipes as his economic advisers."[55] Indeed he did. Suharto packed his cabinet with

* Not all the U.S. professors sent under the program were comfortable with this role. "I felt that the University should not be involved in what essentially was becoming a rebellion against the government," said Len Doyle, the Berkeley professor appointed to head Ford's Indonesian economics program. That point of view got Doyle recalled to California and replaced.

members of the Berkeley Mafia, handing them all the key financial posts, including minister of trade and ambassador to Washington.[56]

This economic team, having studied at a less ideological school, were not antistate radicals like the Chicago Boys. They believed the government had a role to play in managing Indonesia's domestic economy and making sure that basics, like rice, were affordable. However, the Berkeley Mafia could not have been more hospitable to foreign investors wanting to mine Indonesia's immense mineral and oil wealth, described by Richard Nixon as "the greatest prize in the Southeast Asian area."*[57] They passed laws allowing foreign companies to own 100 percent of these resources, handed out "tax holidays," and within two years, Indonesia's natural wealth—copper, nickel, hardwood, rubber and oil—was being divided up among the largest mining and energy companies in the world.

For those plotting the overthrow of Allende just as Suharto's program was kicking in, the experiences of Brazil and Indonesia made for a useful study in contrasts. The Brazilians had made little use of the power of shock, waiting years before demonstrating their appetite for brutality. It was a near-fatal error, since it gave their opponents the chance to regroup and for some to form left-wing guerrilla armies. Although the junta managed to clear the streets, the rising opposition forced it to slow its economic plans.

Suharto, on the other hand, had shown that if massive repression was used *preemptively*, the country would go into a kind of shock and resistance could be wiped out before it even took place. His use of terror was so merciless, so far beyond even the worst expectations, that a people who only weeks earlier had been collectively striving to assert their country's independence were now sufficiently terrified that they ceded total control to Suharto and his henchmen. Ralph McGehee, a senior CIA operations manager during the years of the coup, said Indonesia was a "model operation. . . . You can trace back all major, bloody events run from Washington to the way Suharto came to power. The success of that meant that it would be repeated, again and again."[58]

The other crucial lesson from Indonesia had to do with the pre-coup partnership between Suharto and the Berkeley Mafia. Because they were ready to take up top "technocratic" positions in the new government and had already converted Suharto to their worldview, the coup did more than just g

* Interestingly, Arnold Harberger was hired as a consultant to Suharto's finance ministry 1975.

rid of a nationalist threat; it transformed Indonesia into one of the most welcoming environments for foreign multinationals in the world.

As momentum began to build toward Allende's ouster, a chilling warning began appearing in red paint on the walls of Santiago. It said, "Jakarta is coming."

Shortly after Allende was elected, his opponents inside Chile began to imitate the Indonesia approach with eerie precision. The Catholic University, home of the Chicago Boys, became ground zero for the creation of what the CIA called "a coup climate."[59] Many students joined the fascist Patria y Libertad and goose-stepped through the streets in open imitation of Hitler Youth. In September 1971, a year into Allende's mandate, the top business leaders in Chile held an emergency meeting in the seaside city of Viña del Mar to develop a coherent regime-change strategy. According to Orlando Sáenz, president of the National Association of Manufacturers (generously funded by the CIA and many of the same foreign multinationals doing their own plotting in Washington), the gathering decided that "Allende's government was incompatible with freedom in Chile and with the existence of private enterprise, and that the only way to avoid the end was to overthrow the government." The businessmen formed a "war structure," one part of which would liaise with the military; another, according to Sáenz, would "prepare specific alternative programs to government programs that would systematically be passed on to the Armed Forces."[60]

Sáenz recruited several key Chicago Boys to design those alternative programs and set them up in a new office near the Presidential Palace in Santiago.[61] The group, led by the Chicago grad Sergio de Castro and by Sergio Undurraga, his colleague at the Catholic University, began holding weekly secret meetings during which they developed detailed proposals for how to radically remake their country along neoliberal lines.[62] According to the subsequent U.S. Senate investigation, "over 75 percent" of the funding for this "opposition research organization" was coming directly from the CIA.[63]

For a time, the coup planning proceeded on two distinct tracks: the military plotted the extermination of Allende and his supporters while the economists plotted the extermination of their ideas. As momentum built for a violent solution, a dialogue was opened between the two camps, with Roberto Kelly, a businessman associated with the CIA-financed newspaper *El Mercurio*, acting as the go-between. Through Kelly, the Chicago Boys sent a five-page summary of their economic program to the navy admiral in charge. The navy gave the nod, and from then on the Chicago Boys worked frantically to have their program ready by the time of the coup.

Their five-hundred-page bible—a detailed economic program that would guide the junta from its earliest days—came to be known in Chile as "The Brick." According to a later U.S. Senate Committee, "CIA collaborators were involved in preparing an initial overall economic plan which has served as the basis for the Junta's most important economic decisions."[64] Eight of the ten principal authors of "The Brick" had studied economics at the University of Chicago.[65]

Although the overthrow of Allende was universally described as a military coup, Orlando Letelier, Allende's Washington ambassador, saw it as an equal partnership between the army and the economists. "The 'Chicago boys,' as they are known in Chile," Letelier wrote, "convinced the generals that they were prepared to supplement the brutality, which the military possessed, with the intellectual assets it lacked."[66]

Chile's coup, when it finally came, would feature three distinct forms of shock, a recipe that would be duplicated in neighboring countries and would reemerge, three decades later, in Iraq. The shock of the coup itself was immediately followed by two additional forms of shock. One was Milton Friedman's capitalist "shock treatment," a technique in which hundreds of Latin American economists had by now been trained at the University of Chicago and its various franchise institutions. The other was Ewen Cameron's shock, drug and sensory deprivation research, now codified as torture techniques in the *Kubark* manual and disseminated through extensive CIA training programs for Latin American police and military.

These three forms of shock converged on the bodies of Latin Americans and the body politic of the region, creating an unstoppable hurricane of mutually reinforcing destruction and reconstruction, erasure and creation. The shock of the coup prepared the ground for economic shock therapy; the shock of the torture chamber terrorized anyone thinking of standing in the way of the economic shocks. Out of this live laboratory emerged the first Chicago School state, and the first victory in its global counterrevolution.