

Ministerio de Hacienda



CHILE MACRO OUTLOOK AND POLICY PRIORITIES AND PROSPECTS

IMF Spring Meeting, 2022
April 20, 2022

Mario Marcel C. | Minister of Finance

Outline

1

Macroeconomic outlook

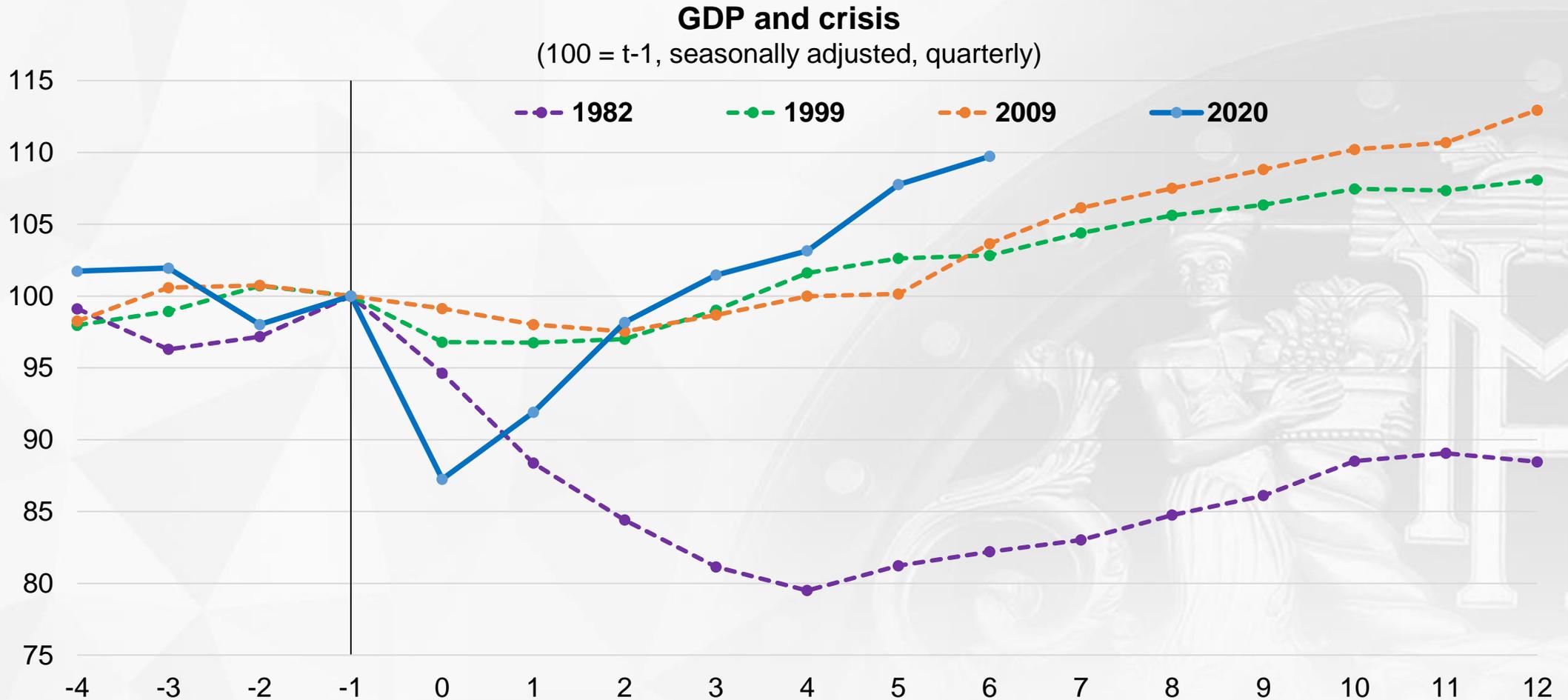
2

Fiscal situation

3

Policy priorities and prospects

Chile recovered rapidly from the Covid-19 crisis, being the shortest crisis in the last 40 years

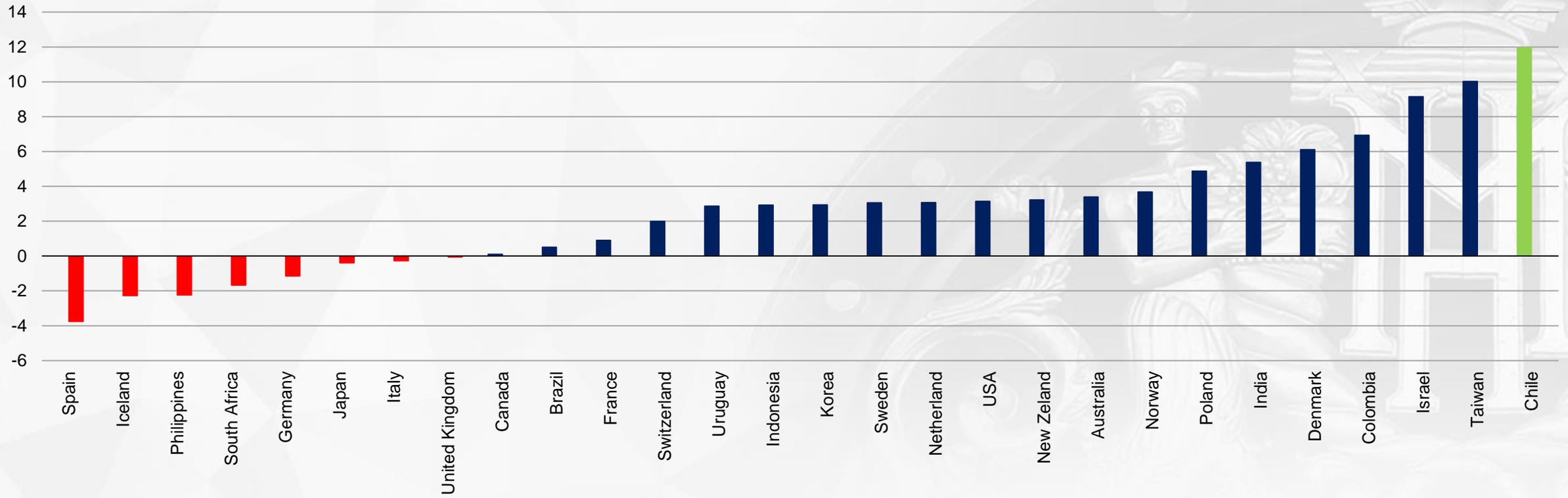


Note: T=0 in periods 1981.Q4, 1998.Q4, 2008.Q4, 2020.Q2 Official seasonally adjusted spliced series for all periods except 1982-83. For that period, the series contained in the volume “Economic and Social Indicators 1960-1988” was seasonally adjusted. **Source:** Central Bank of Chile

... exhibiting the strongest' s global recovery in 2020+2022

Cumulative Economic Growth 4T2019-4T2021 (change, %)

■ Above pre-pandemic level ■ Below pre-pandemic level

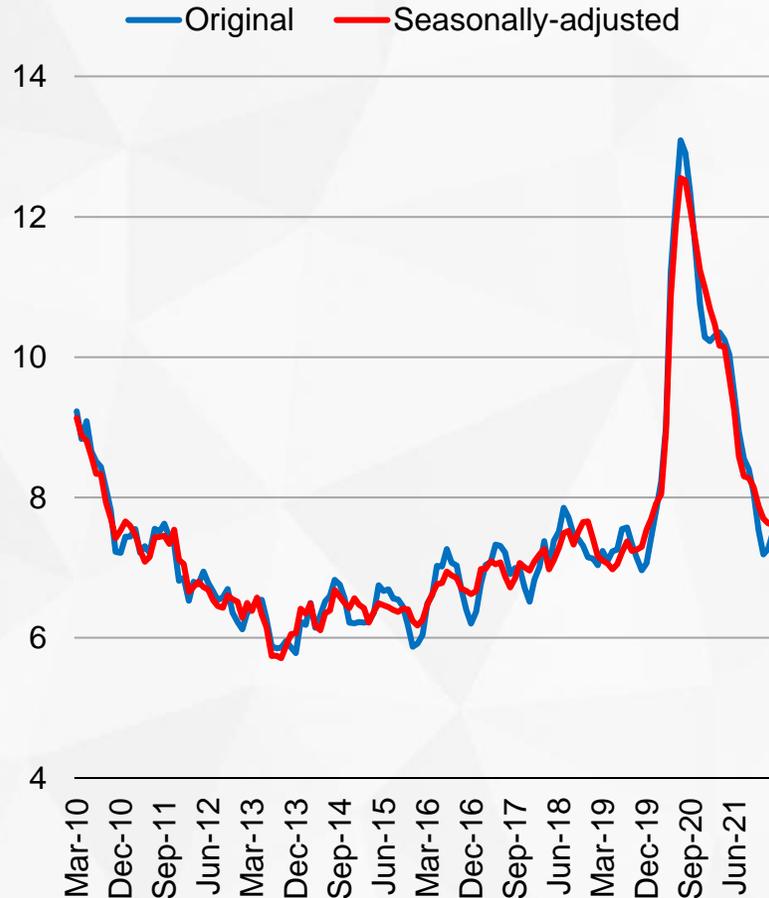


Note: GDP seasonally adjusted

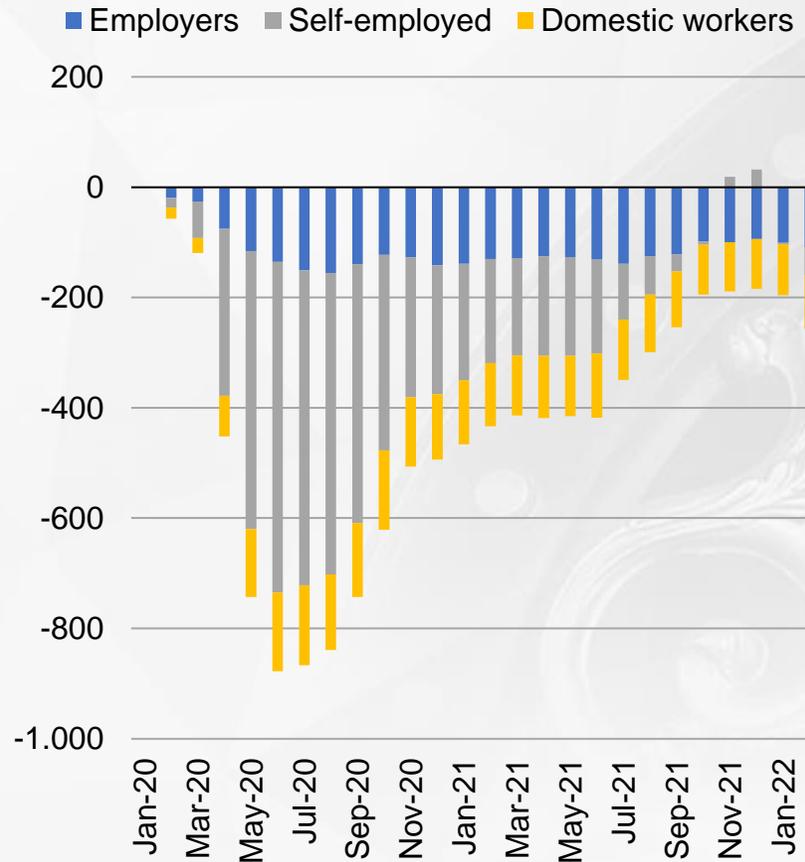
Source: Bloomberg.

The labor market is recovering too, with some gaps still to close

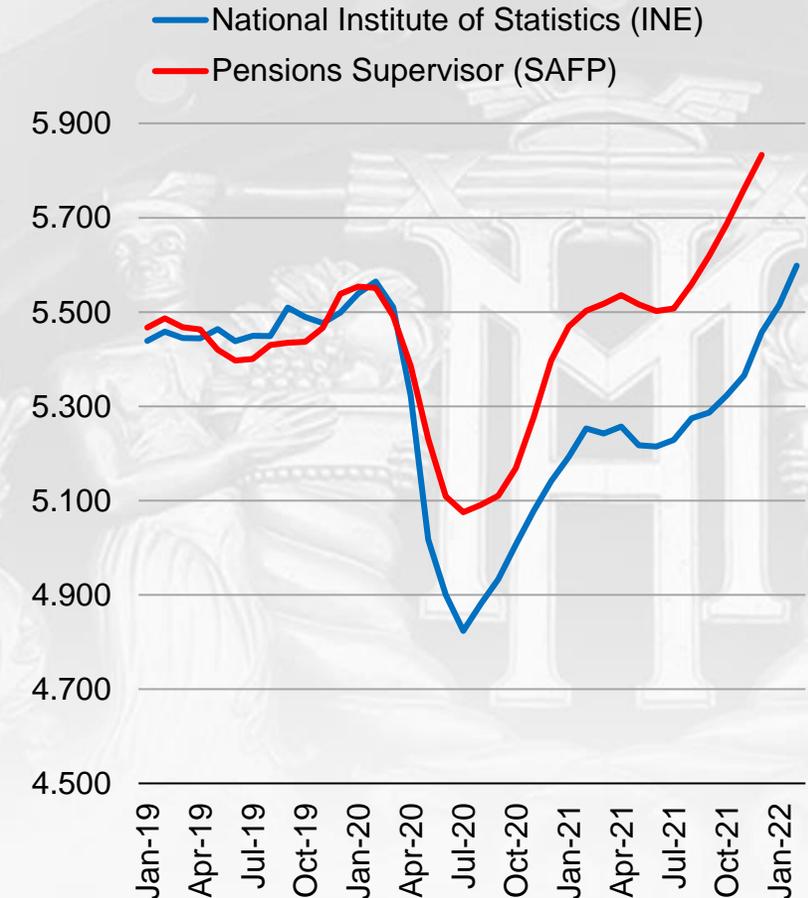
Unemployment rate (%)



Employment recovery by categories (Accumulated variation since jan-20, thousands)



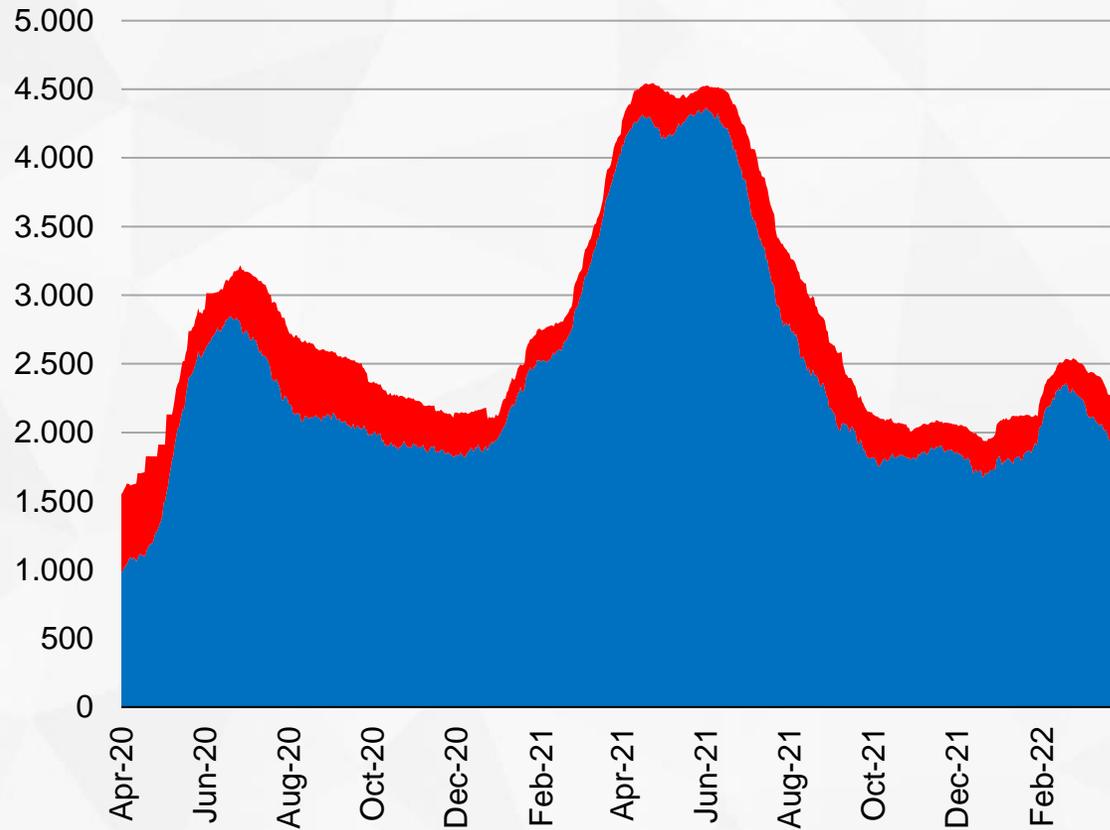
Pension system contributors (thousands, MA3m)



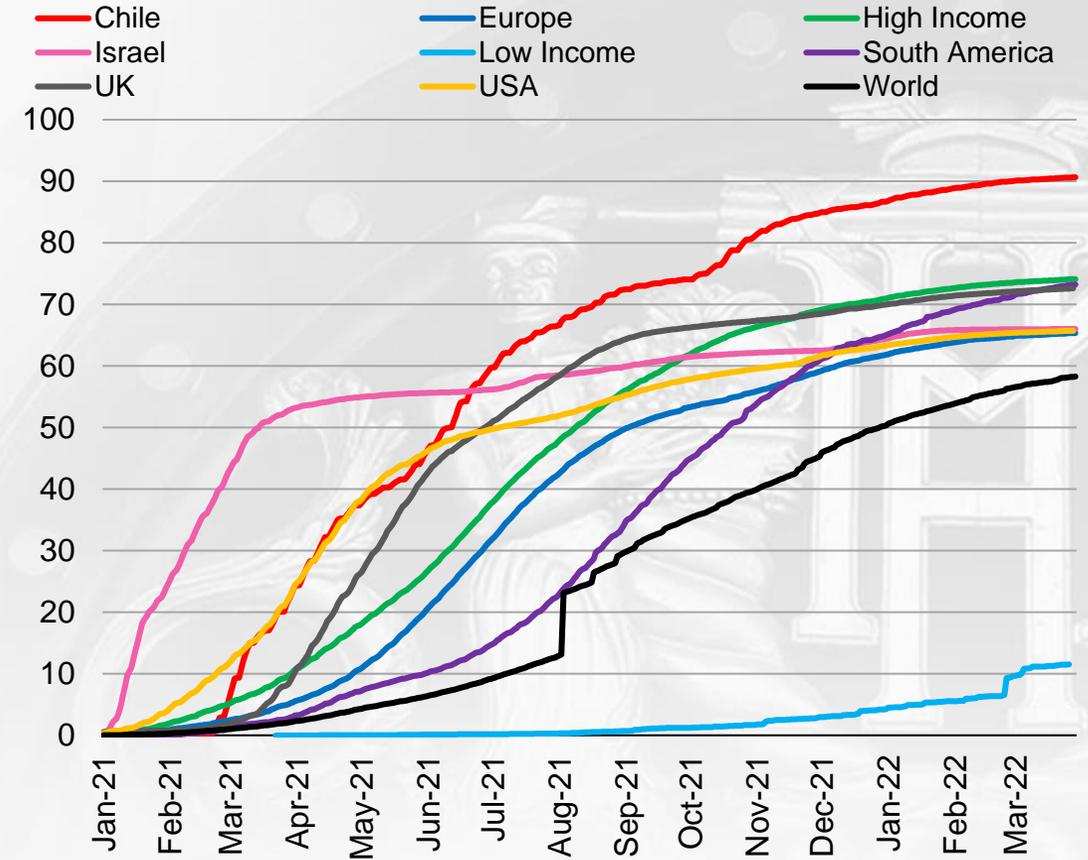
The health policy response to the Pandemic has contributed to a faster recovery of the economy

Chile: ICU availability
(N° of beds)

■ Occupied ■ Available



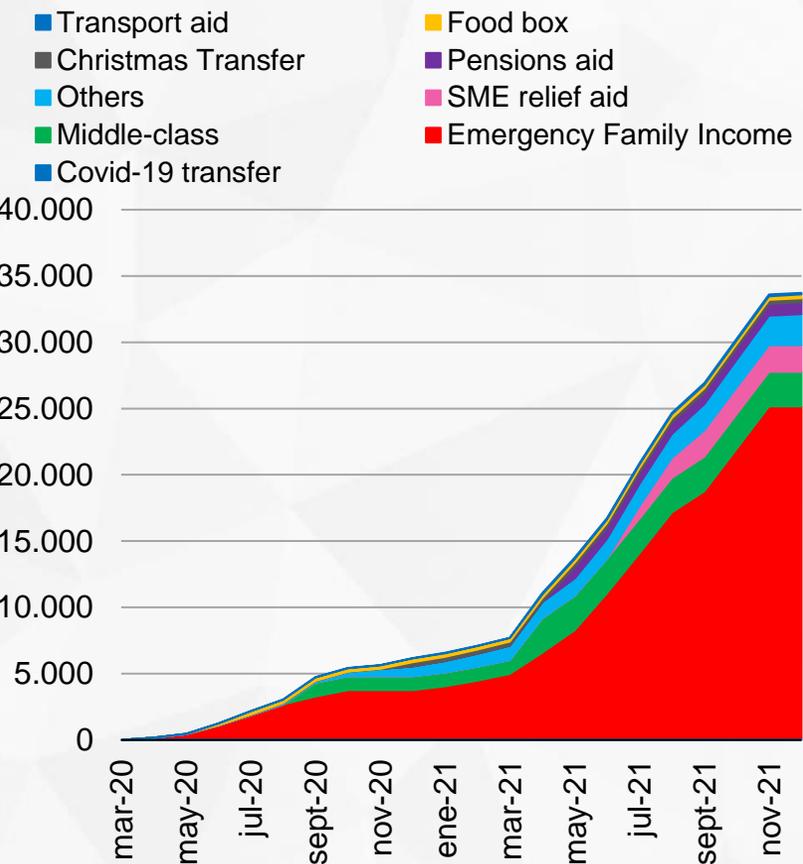
World: vaccine rollout
(% population, fully vaccinated)



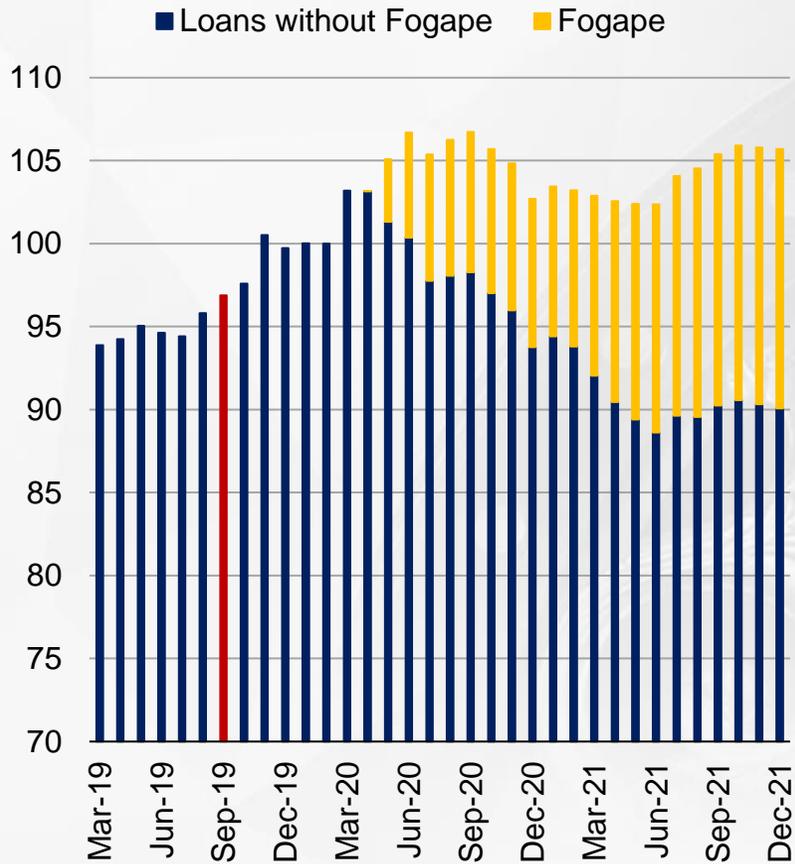
Source: Ministry of Health and Our world in data.

Fiscal transfers, accommodative monetary policy and credit helped households and firms across the pandemic

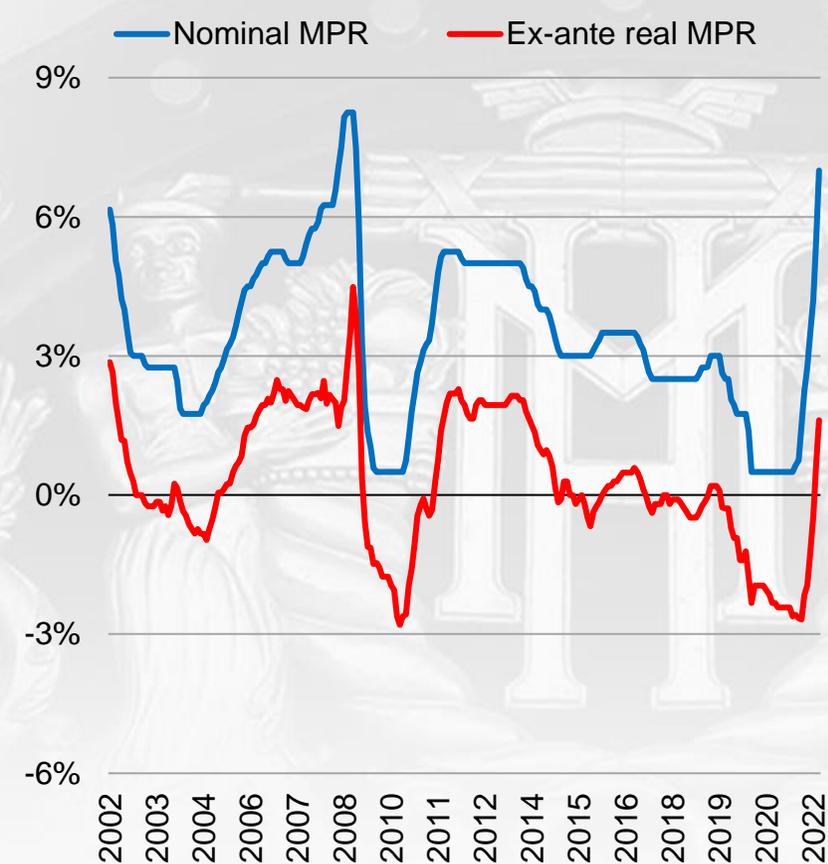
Covid-19 Fiscal Measures (US \$ million)



Real commercial loans balance (Index 100=feb 2020)



Monetary Policy Rate (*) (%)

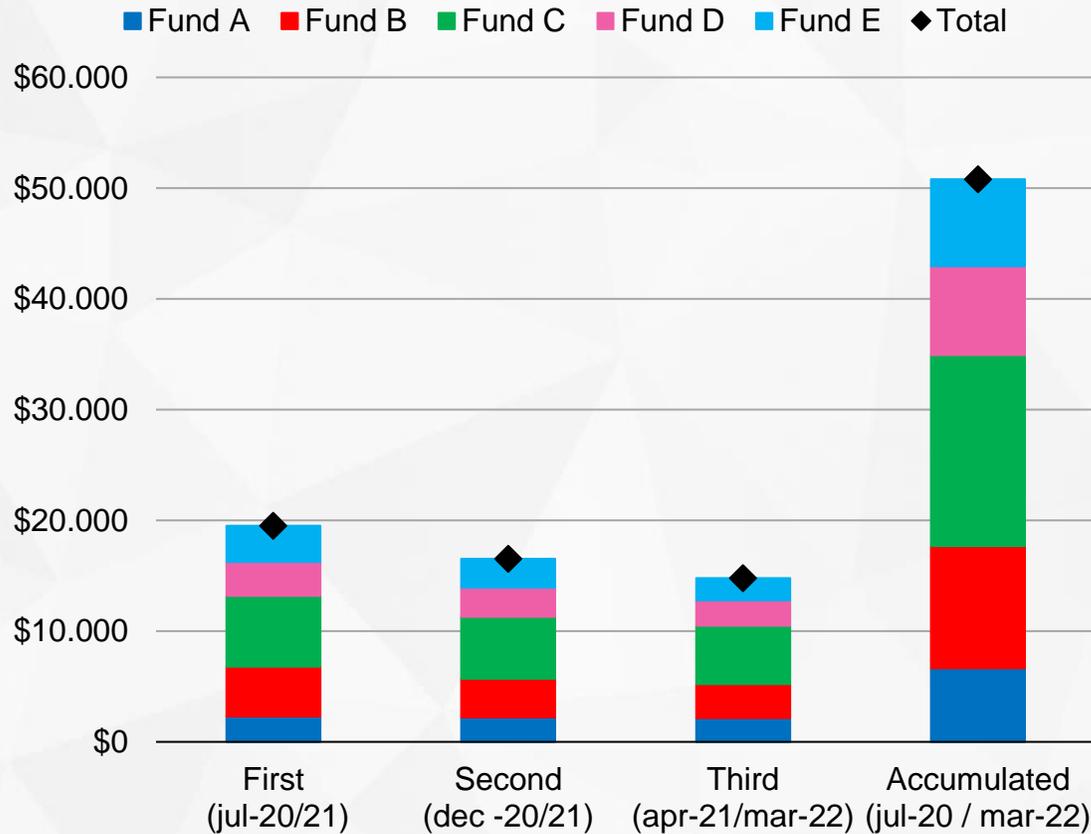


Note: (*) The nominal MPR series shows the average of the month. For March 2022, the nominal MPR is the rate decided in the last Central Bank monetary policy meeting on March 29 (7.00%). Ex-ante measure considers 11-months-ahead inflation expectations from the Economic Expectations Survey (EES).

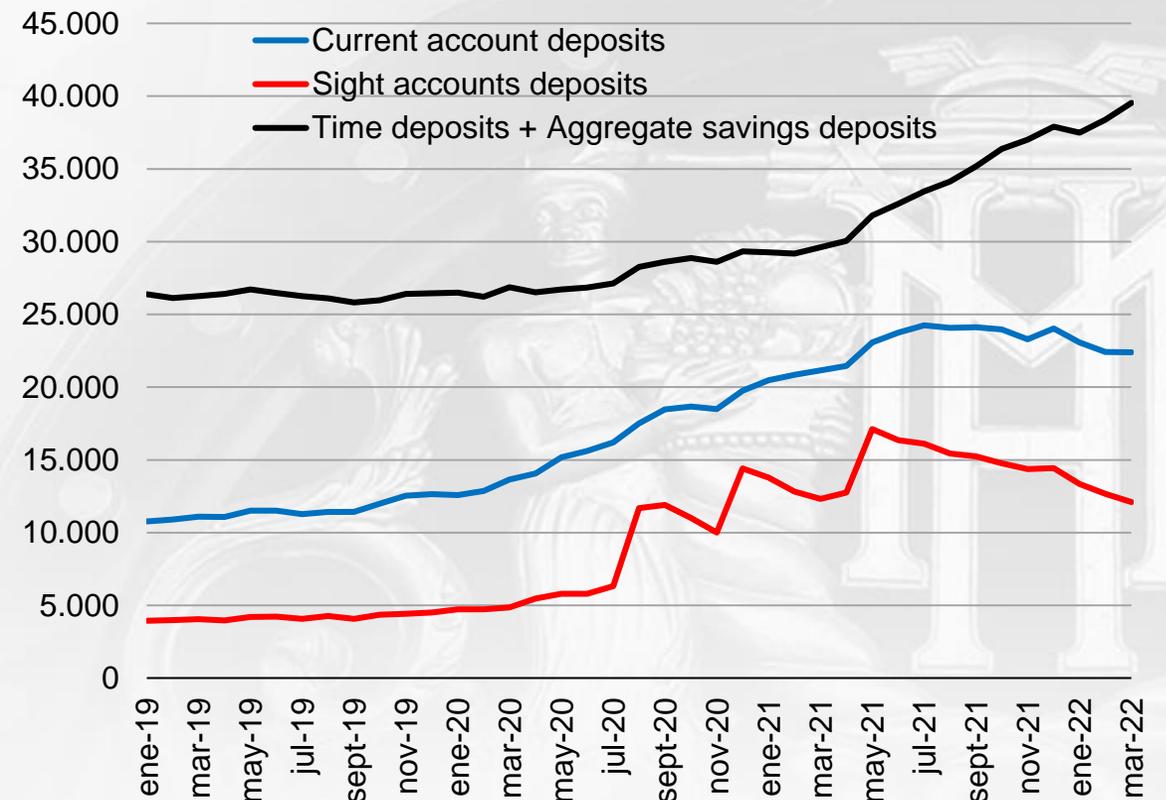
Source: Central Bank of Chile and Ministry of Finance.

Pension funds withdrawals also added liquidity

Pensión funds withdrawals (*)
(US\$, millions)



People's current account, sight accounts and time deposits plus aggregate savings deposits (*)
(balances in USD, millions)

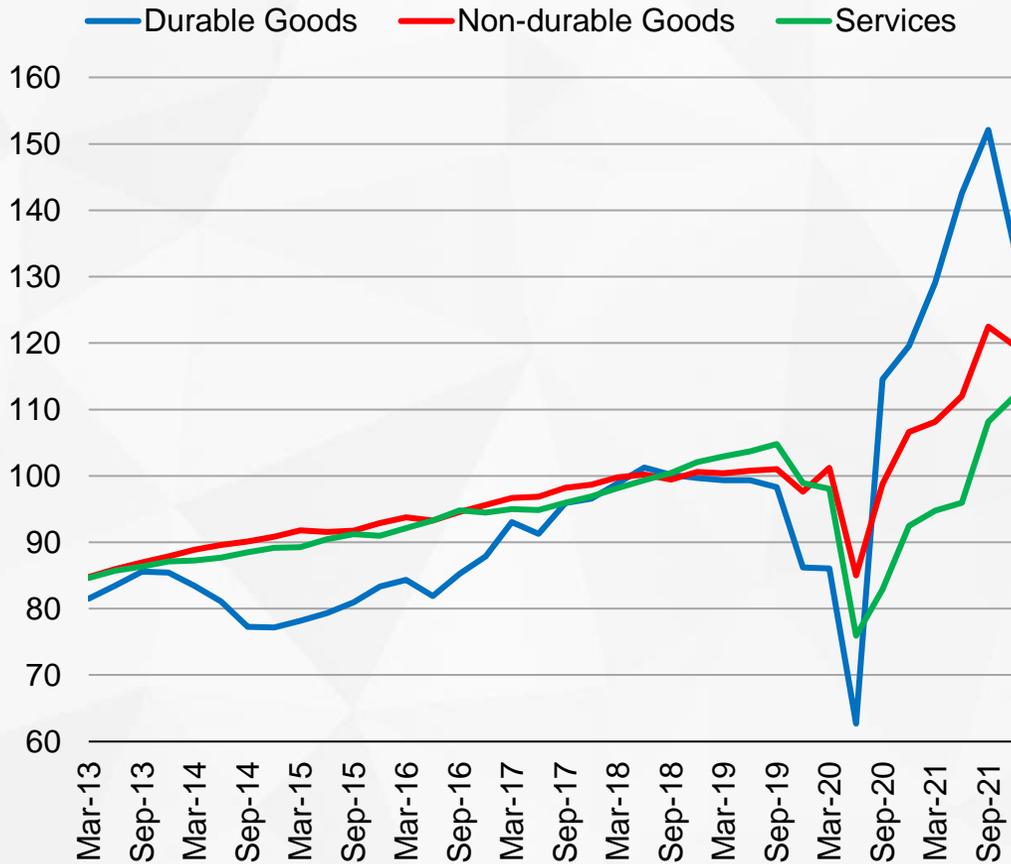


Note: Series in USD are calculated using an exchange rate of \$800 per dolar.

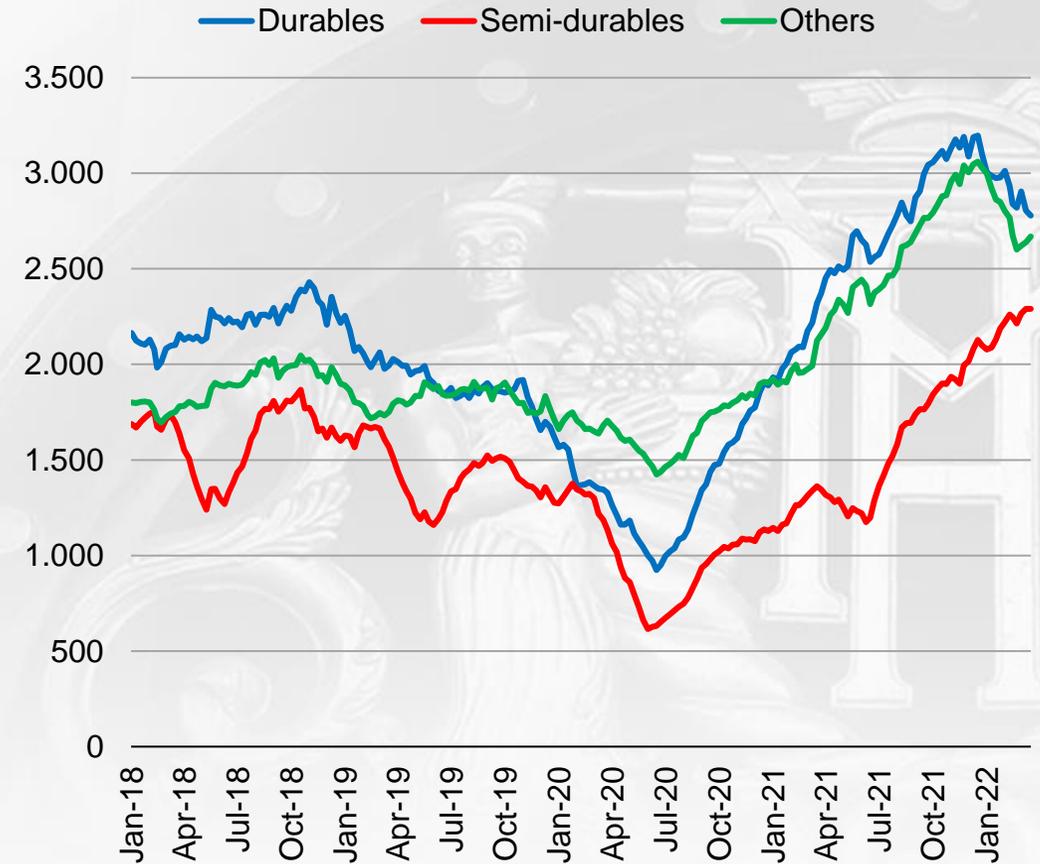
Source: Central Bank of Chile and Chilean Pensions Supervisor (SAFP).

These policies boosted private consumption beyond sustainable levels

Private consumption
(2018=100, seasonally-adjusted series)



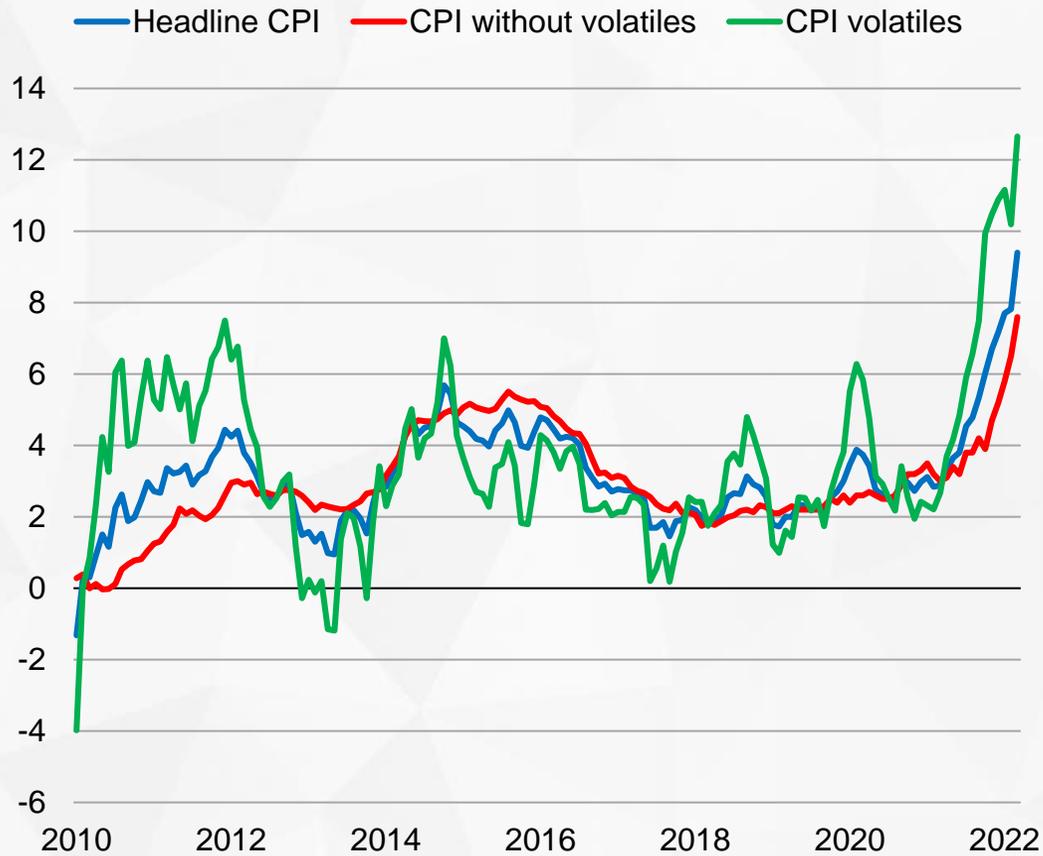
Consumer goods imports
(US\$ million, MA3m)



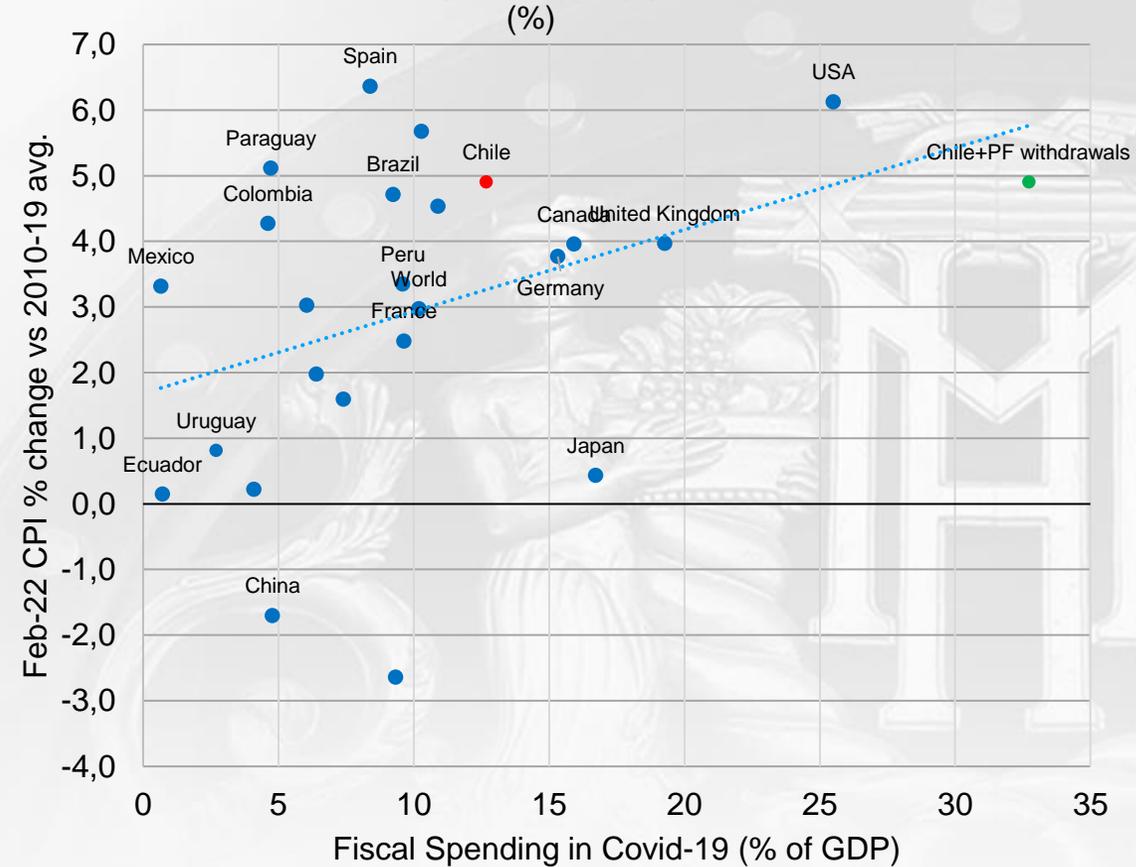
Source: Central Bank of Chile.

Pushing inflation up alongside supply-side constraints

Inflation
(annual change, %)



Excessive' inflation vs COVID-19 fiscal-related expenditure(1)
(%)

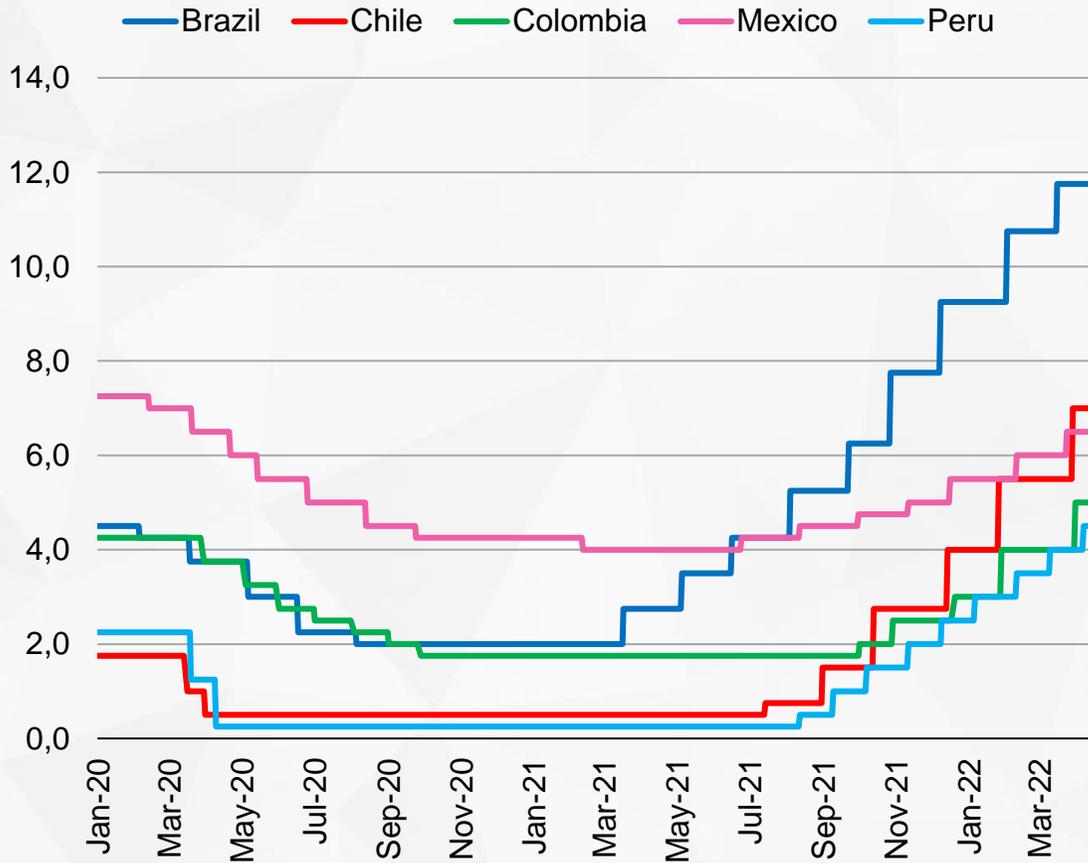


Note: (1) Fiscal above-the-line measures that governments have announced or taken in selected economies in response to the COVID-19 pandemic as of September 27th, 2021. (2) EES: Economic Expectations Survey and FTS: Financial Traders Survey.

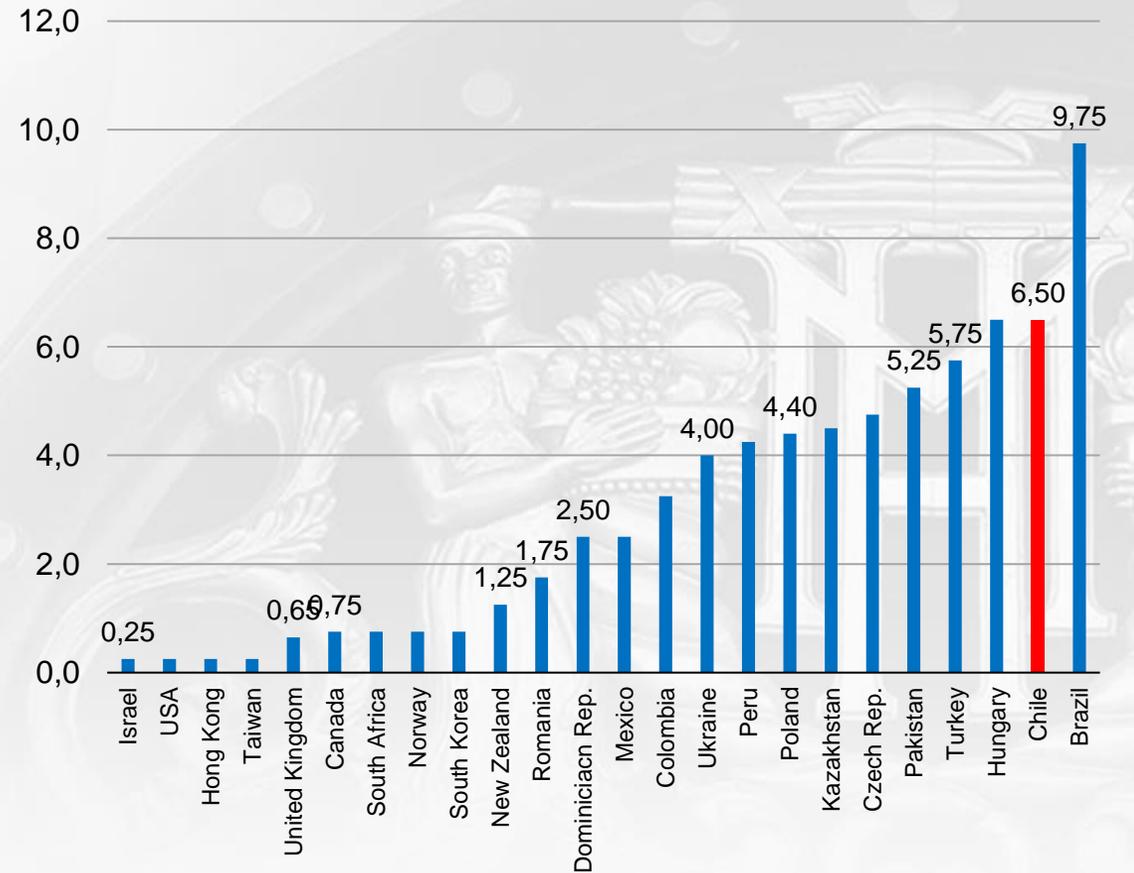
Source: Central Bank of Chile, Bloomberg and IMF.

Monetary policy anticipated inflationary pressures and began to react by mid-2021, entering contractionary territory by the end of last year

Monetary Policy Rate (%)

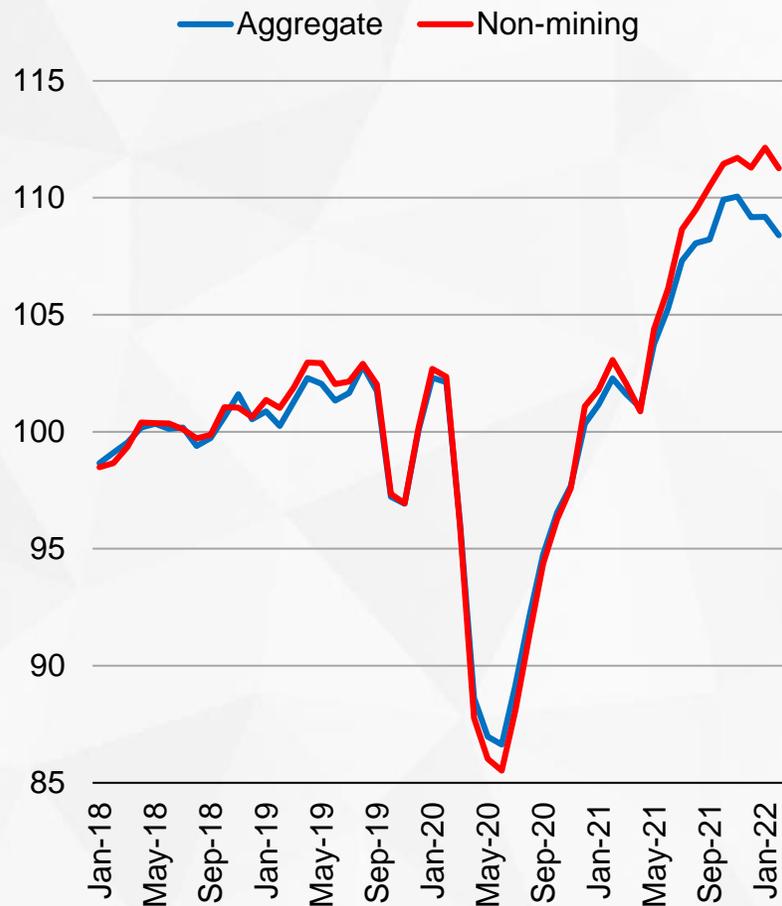


Change in MPR since the lowest value in 2020 (%)

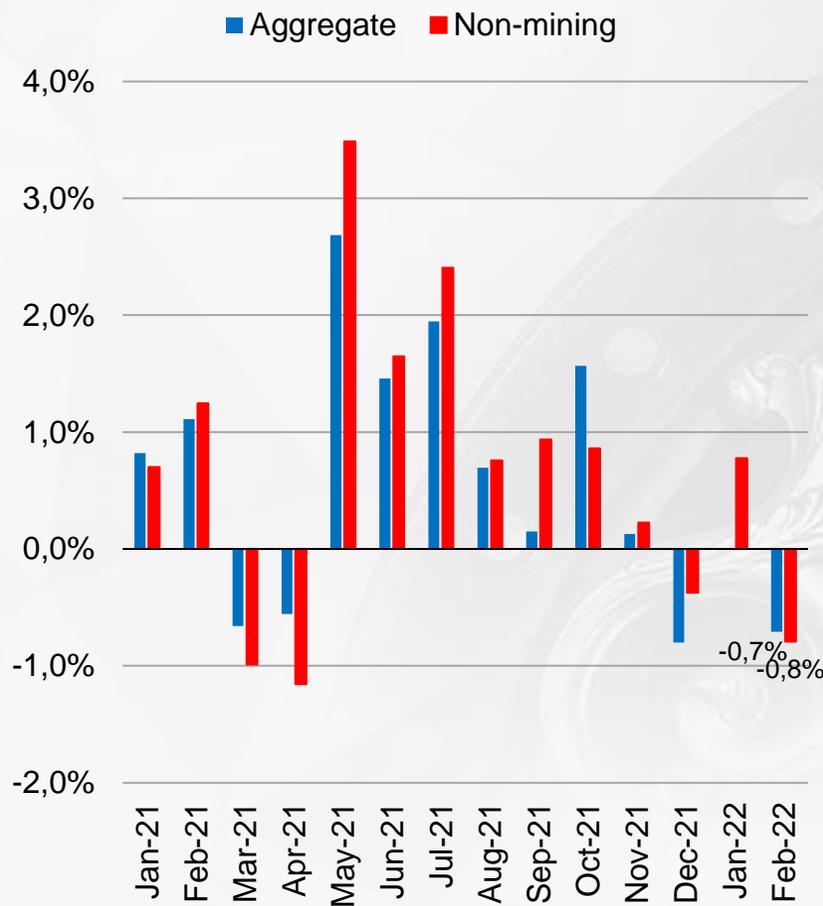


Stabilization efforts are already working. The economy reached its peak by 2021III and different sectors are showing signs of a slowdown, particularly those connected to private consumption

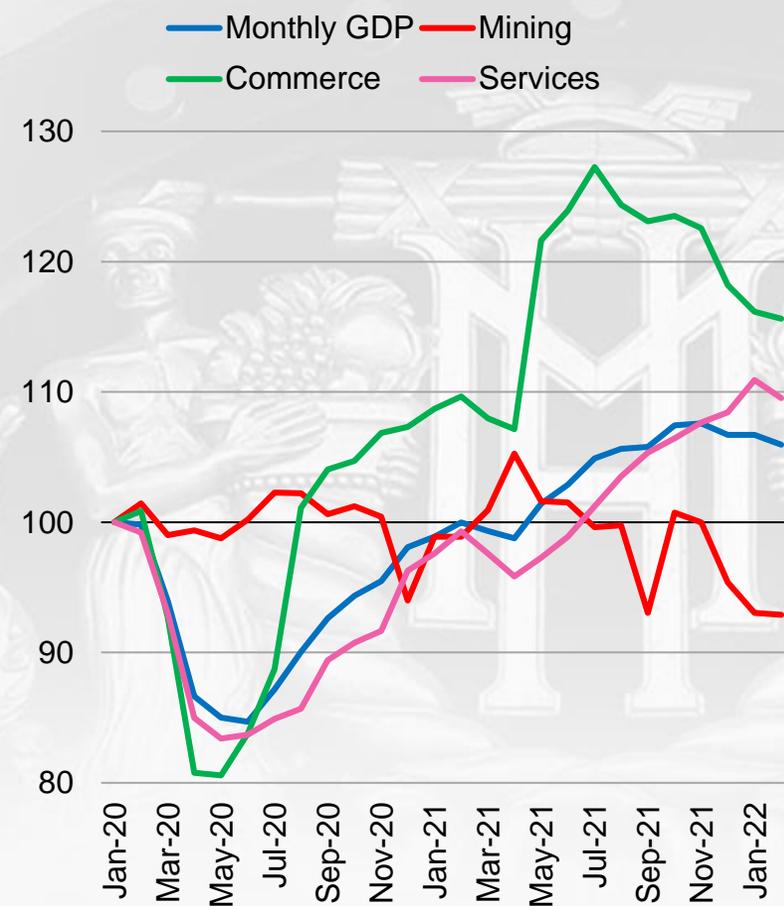
Monthly aggregate and non-mining GDP
(2018 = 100, seasonally-adjusted series)



Monthly aggregate and non-mining GDP
(% change m/m, seasonally-adjusted series)



Seasonally-adjusted monthly GDP
(Jan-20 = 100)



The positive momentum of GFCF's M&E component contrasts with bleaker outlook for construction

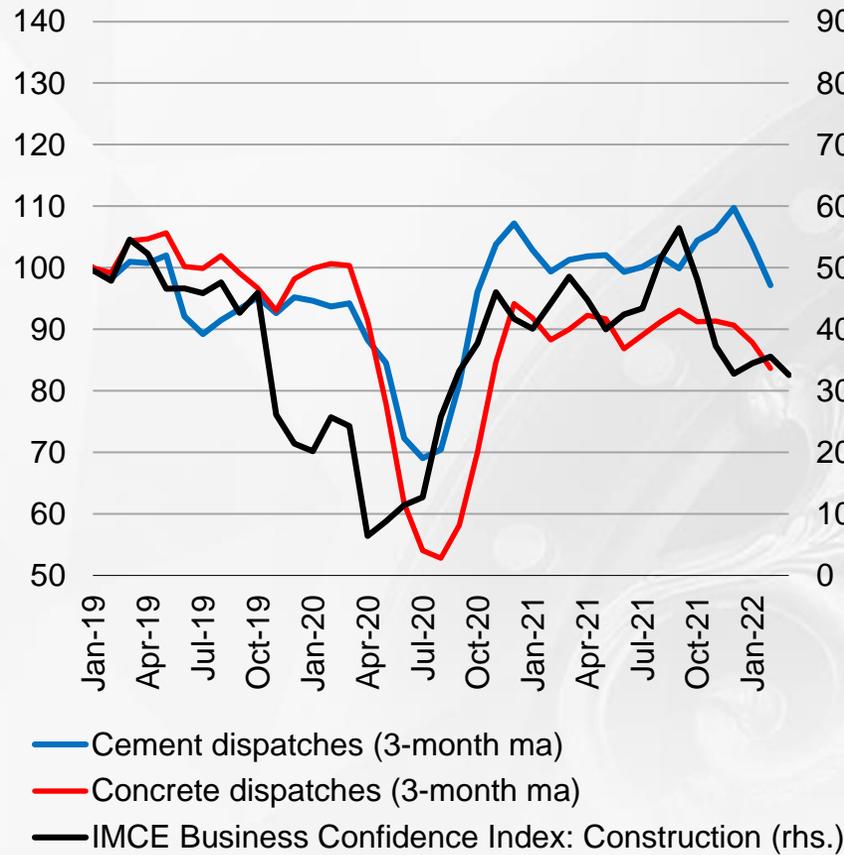
Capital goods imports

(US\$ millions, 3 months moving average)



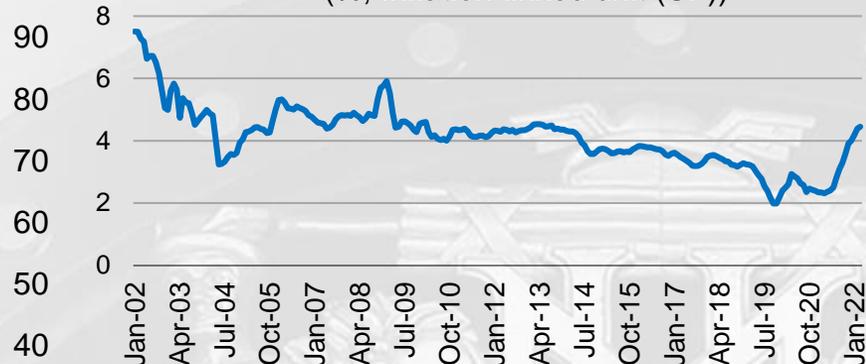
Construction Indicators

(Index Jan.19=100 and diffusion index)



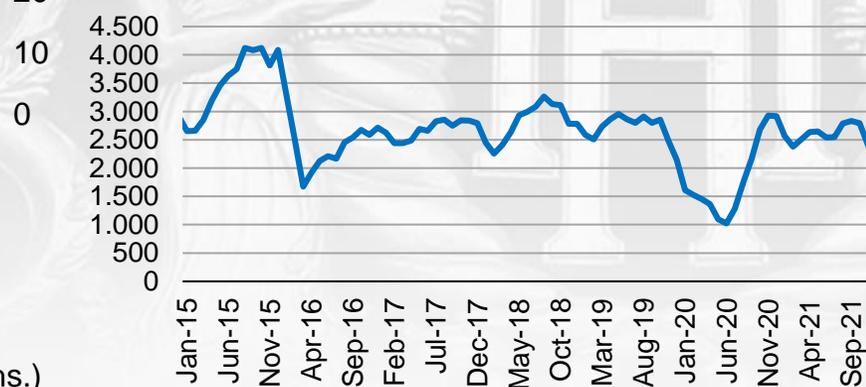
Interest rate on loans

(%, Inflation-linked unit (UF))



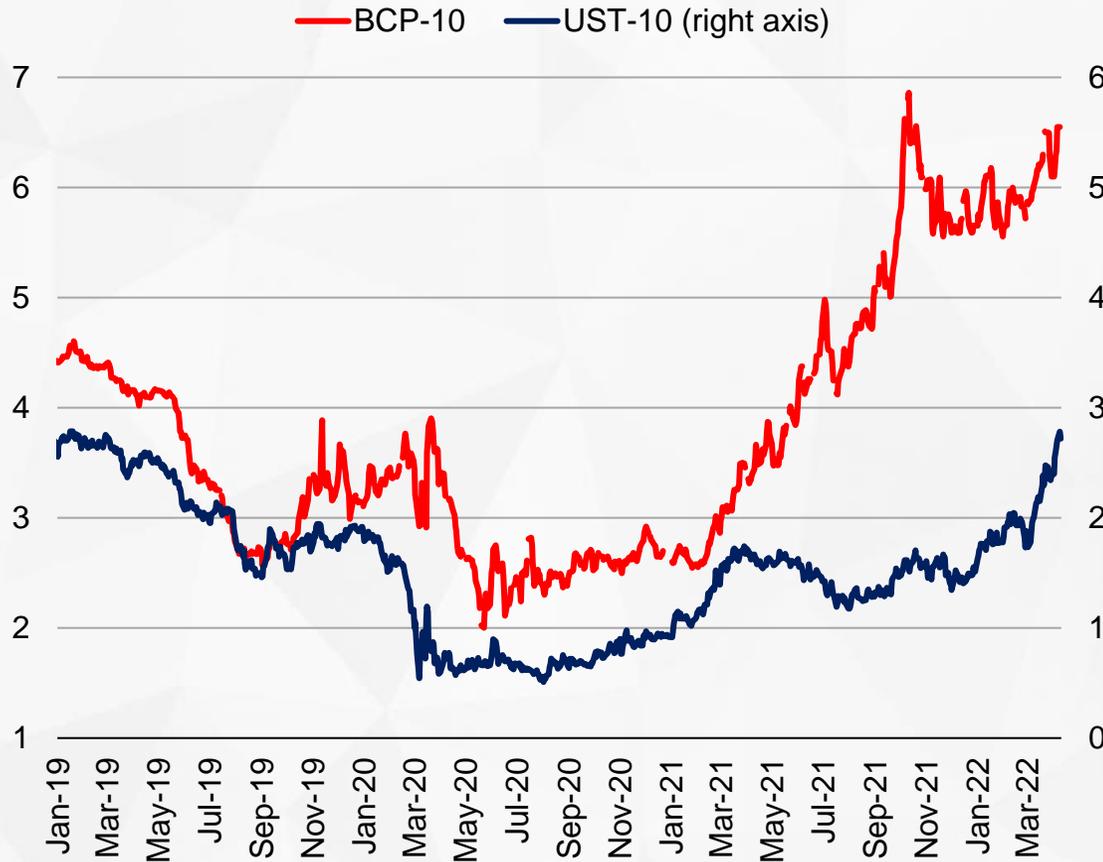
Sale of new homes, Santiago

(#, 3 months moving average)

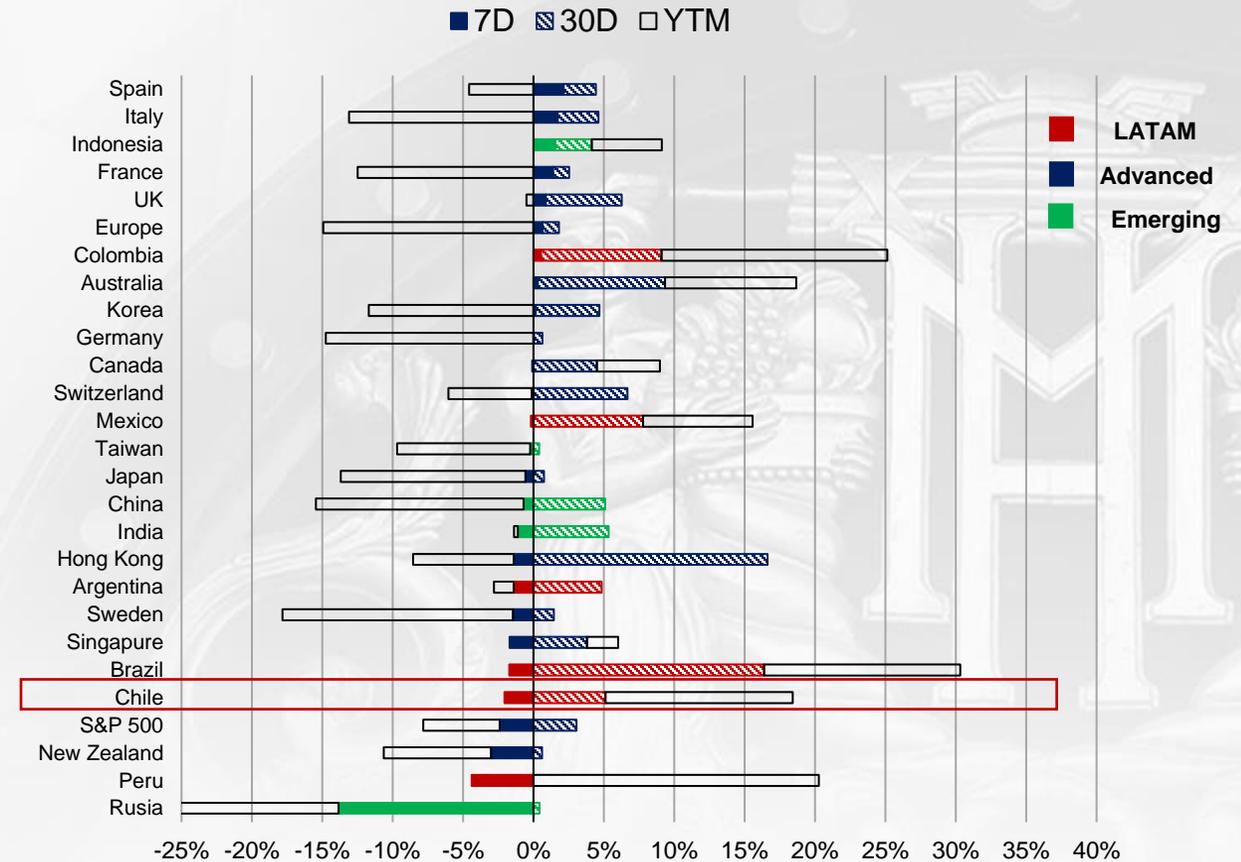


Since late-2021, financial prices started to normalize after a phase of very high uncertainty

10-year yields (%)

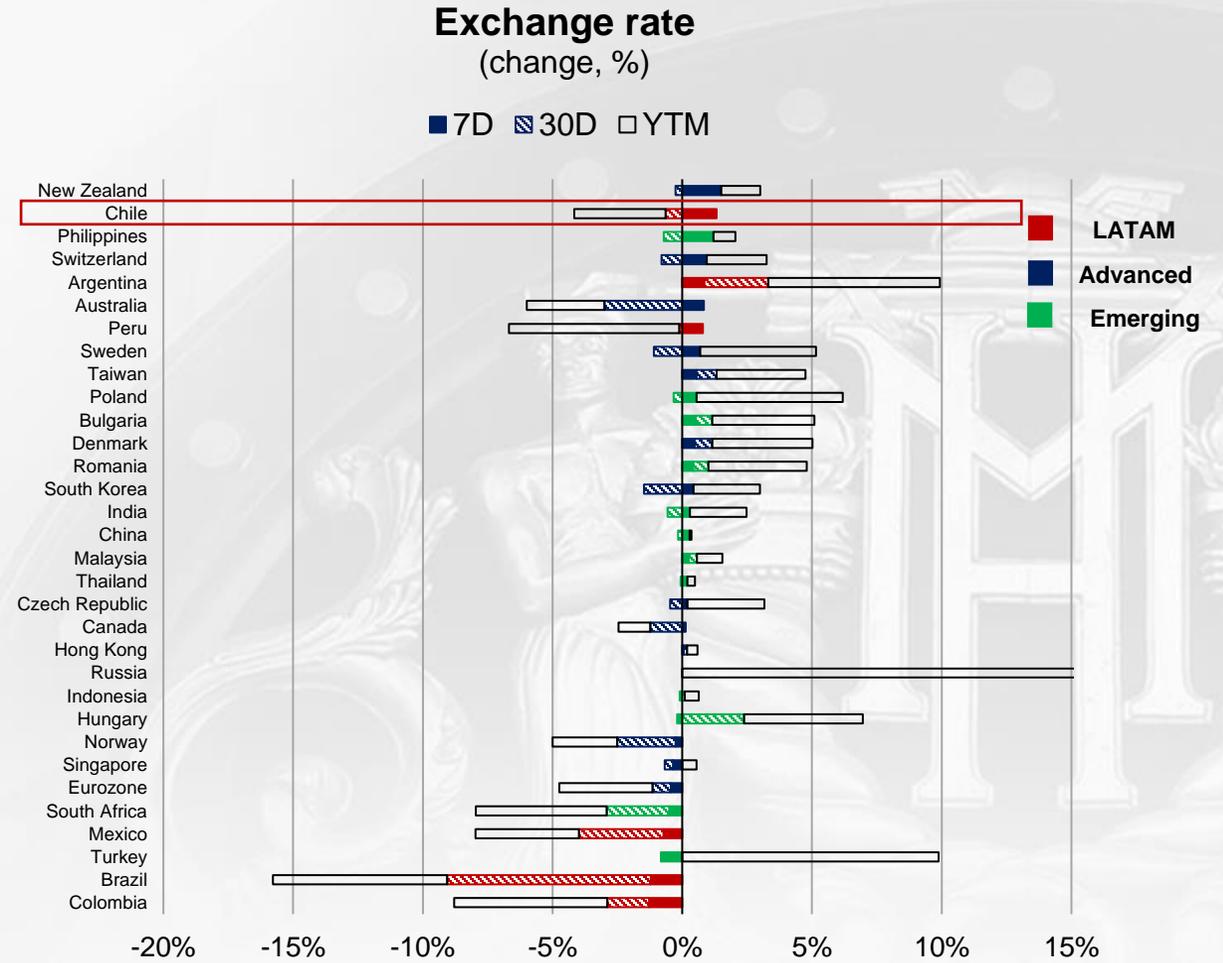
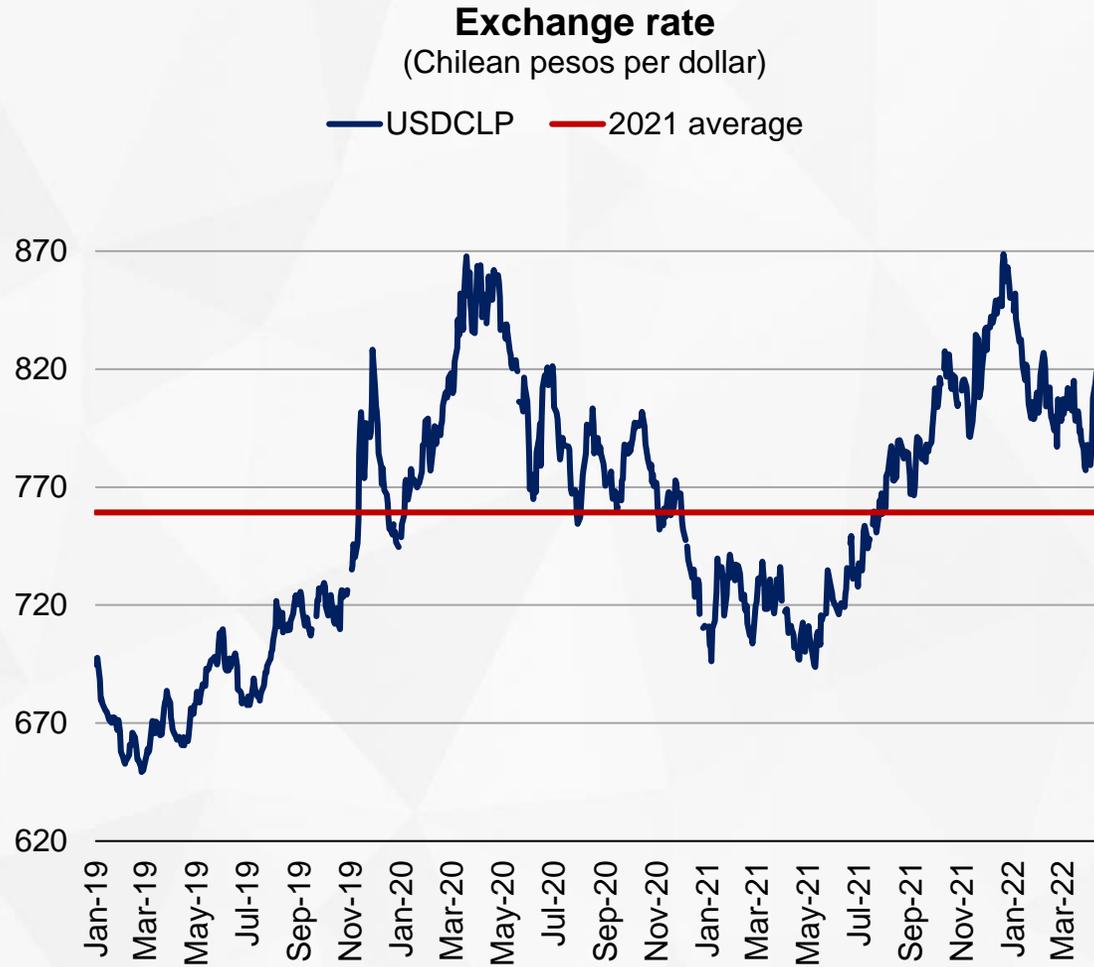


Stock exchange indicators in USD (% change)

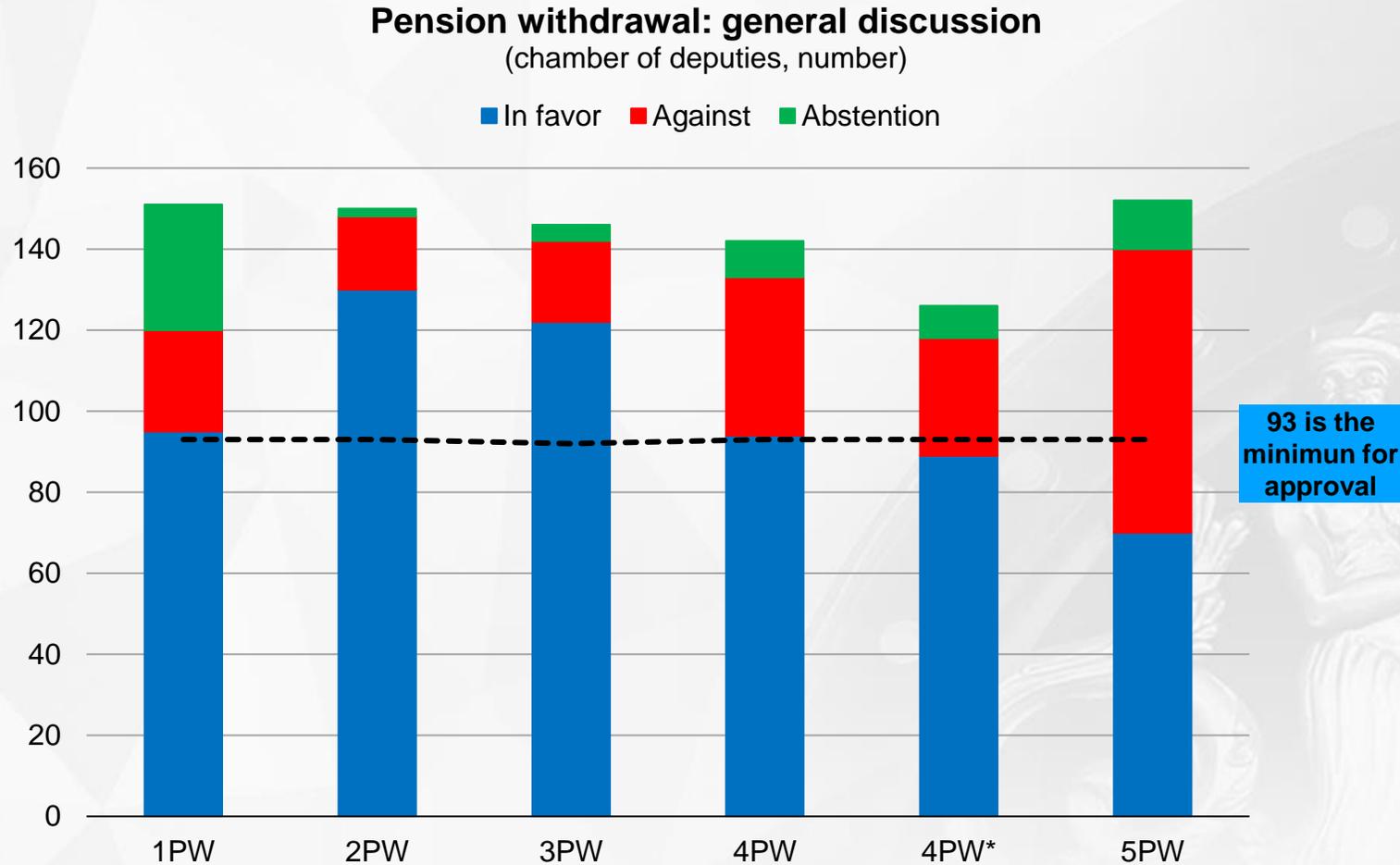


Source: Bloomberg and Central Bank of Chile.

The Chilean peso has also strengthened over the year



Different pension funds withdrawals were discussed since 2020. The last one is the first to be rejected by a significant number of deputies.

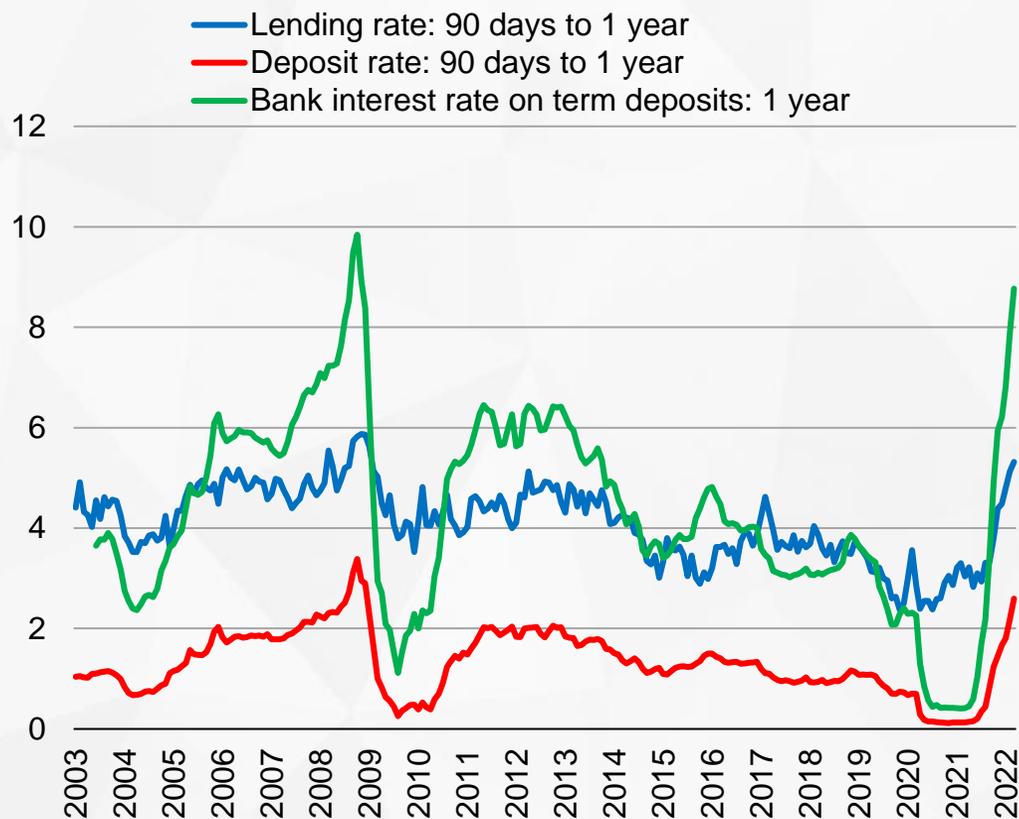


* The 4th withdrawal was rejected by the Senate so the Chamber of Deputies had to vote again after a Mix Chamber proposal.

Short-term rates reflect the transmission from the withdrawal of the monetary impulse. The CB considers that “future increases in the MPR would be smaller than those of recent quarters”

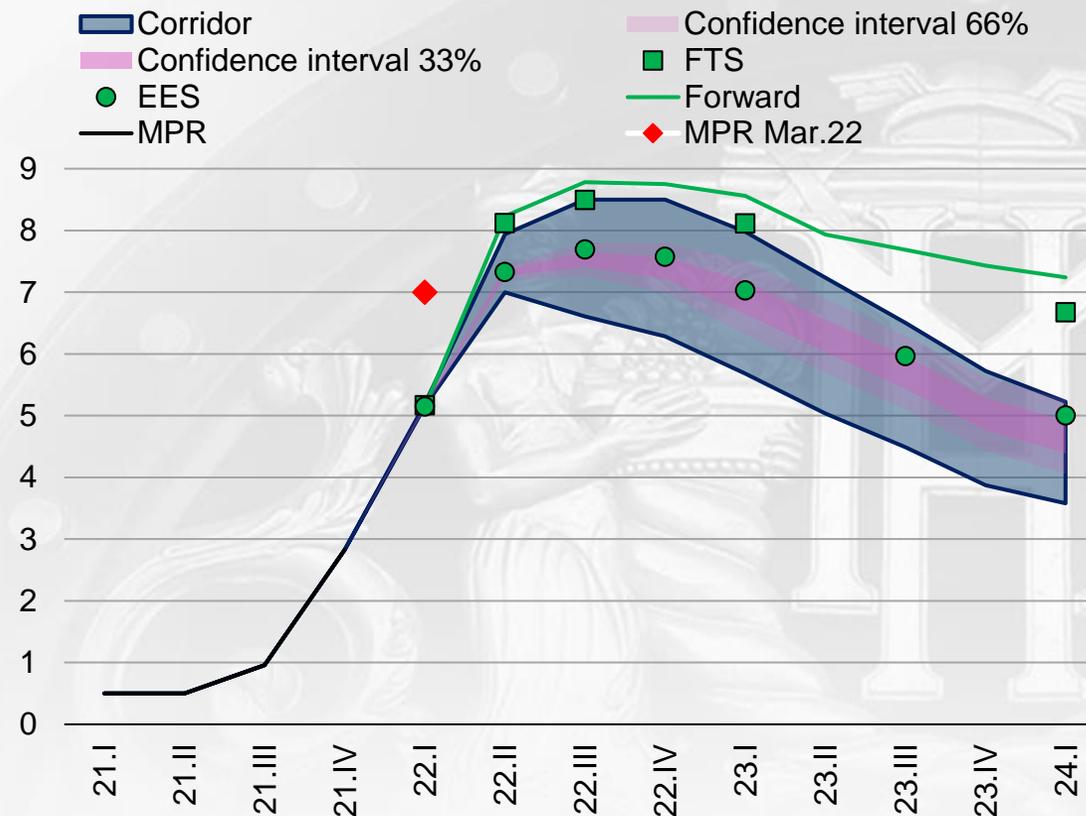
Lending and deposit rates

(%, monthly data)



Central Bank of Chile: MPR Corridor

(quarterly average, %)



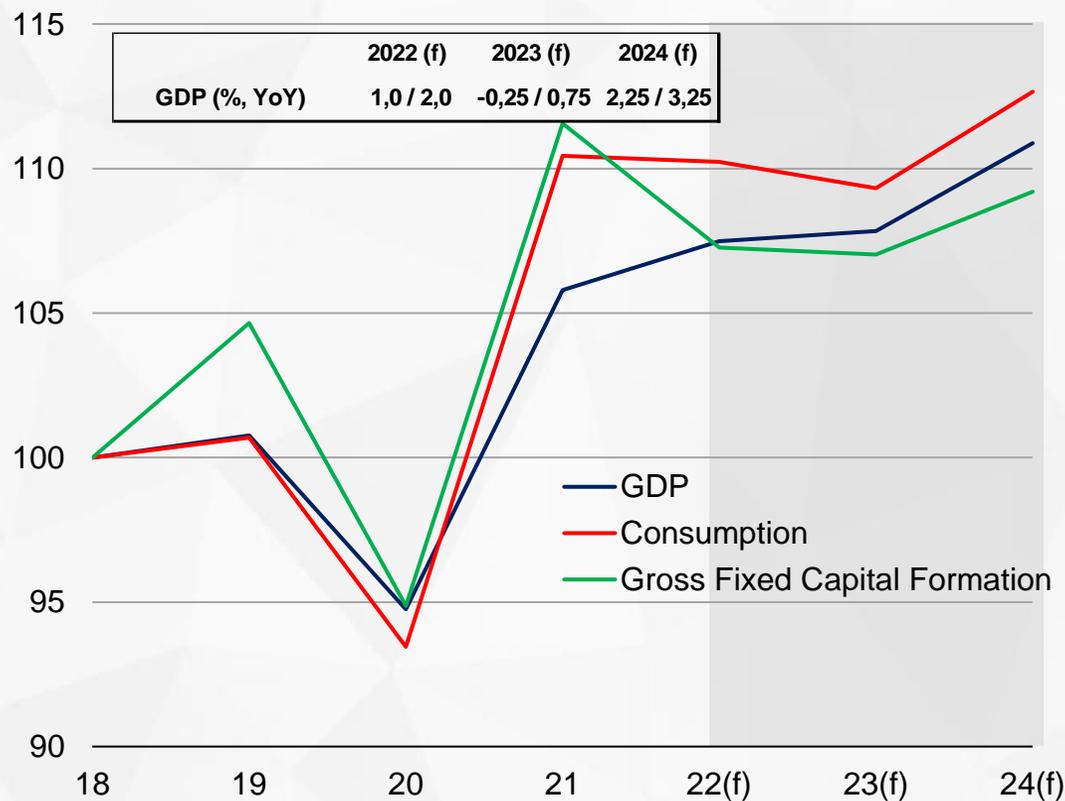
Note: The corridor is built by following the methodology presented in boxes V.1 of March 2020 Monetary Policy Report and V.3 of March 2022 Monetary Policy Report. Includes March EES, FTS pre-policy-meeting of March and the average smoothed forward curve of quarter to 23 March. This is calculated by extracting the implicit MPR considering the forward curve on the interest rate swap curve up to 2 years, discounting the fixed rates at every maturity at the simple accrual of the ICP. For the current quarter the surveys and the forwards consider the average daily effective and are completed with the respective sources.

Source: Central Bank of Chile.

Central Bank foresees economy expansion at rates below its potential in 2022 and 2023, with contractions in private consumption and investment. Inflation will begin to converge to the target in the late-2022

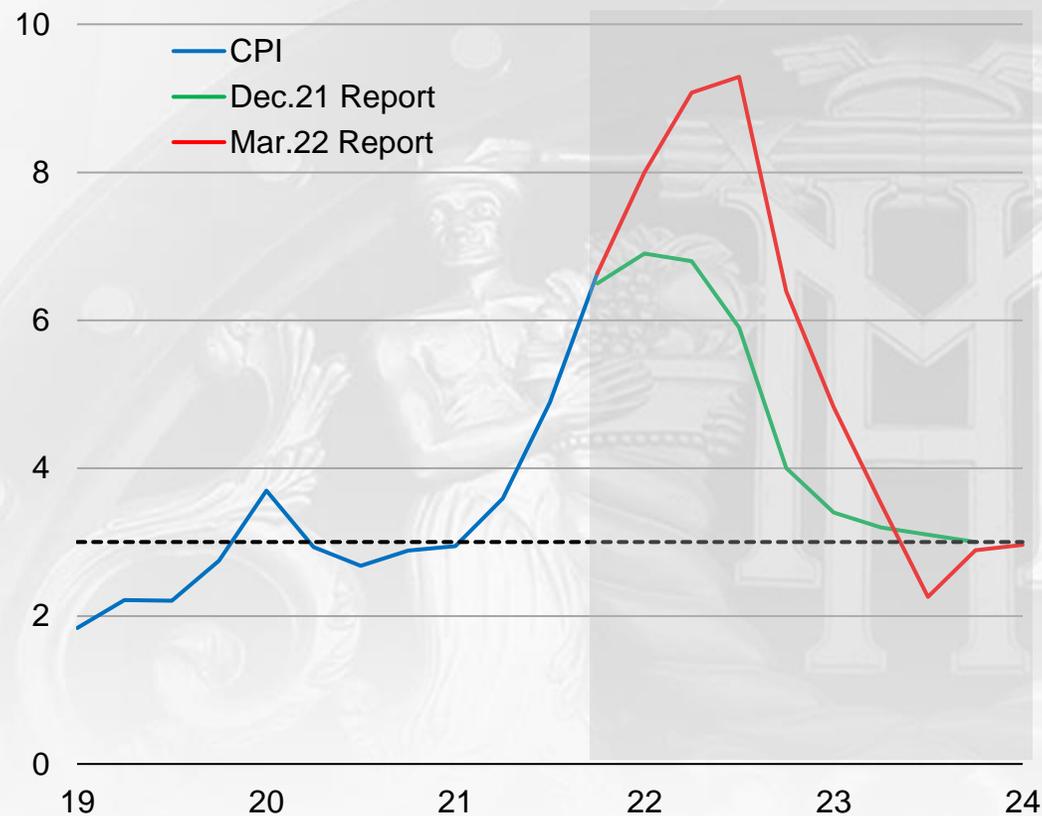
GDP, Consumption and Gross Fixed Capital Formation

(Index 2018=100)



Central Bank Inflation Forecast (*)

(% change YoY)

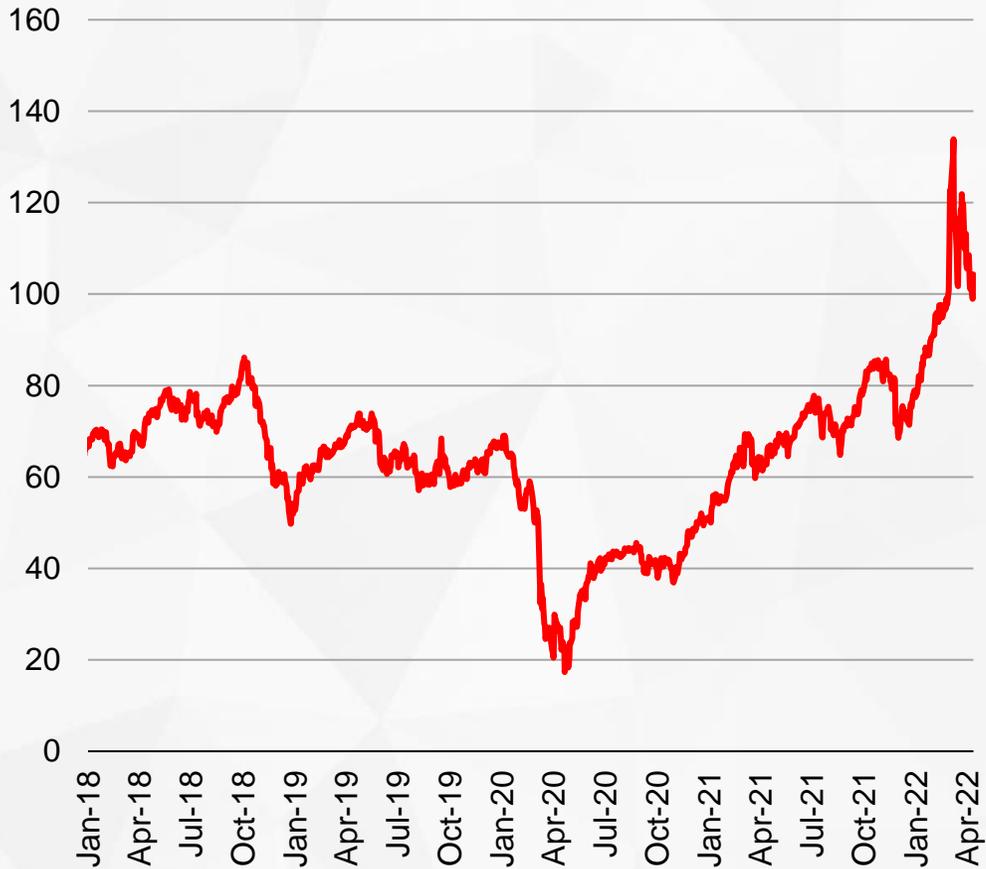


Note: Gray area, as from the first quarter of 2022, shows forecast.

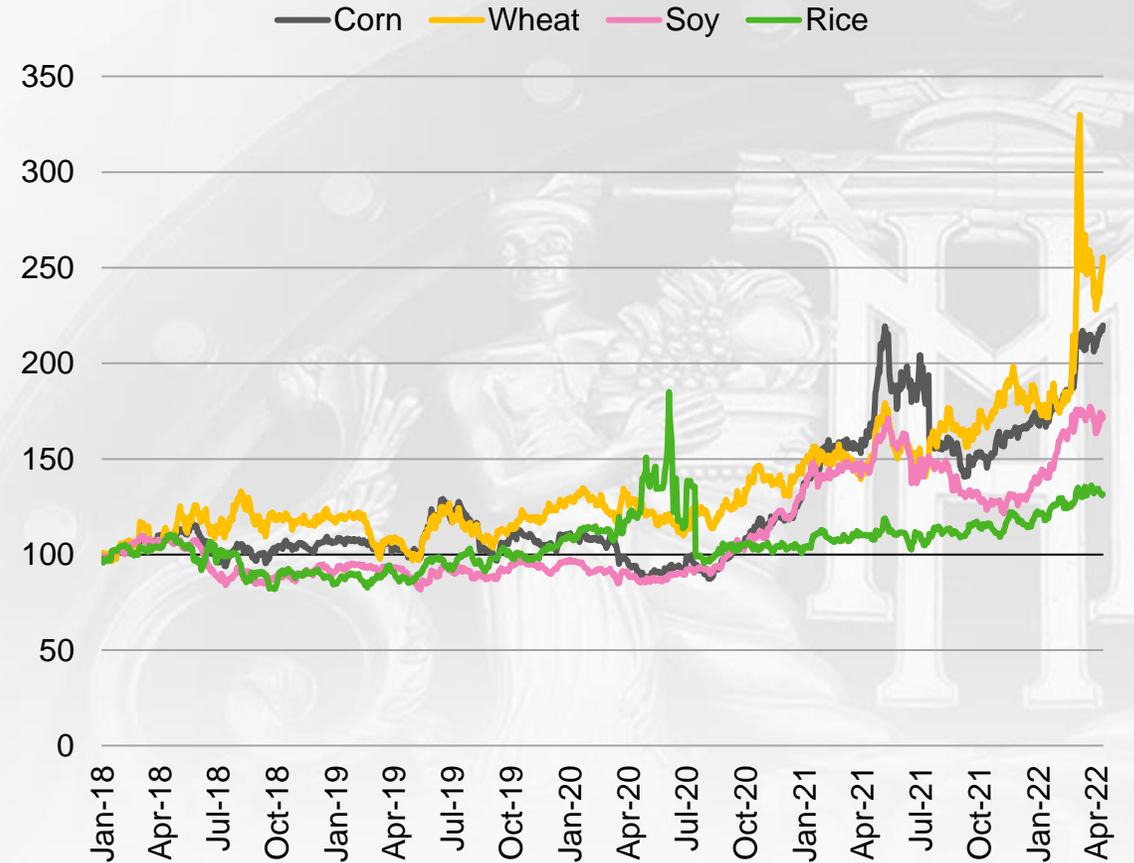
Source : Central Bank of Chile.

The Russian invasion of Ukraine is having an impact mostly through commodity prices, particularly oil and agricultural products

Oil price
(Brent, US\$/barrel)



Commodities prices
(Index, Jan-18=100)

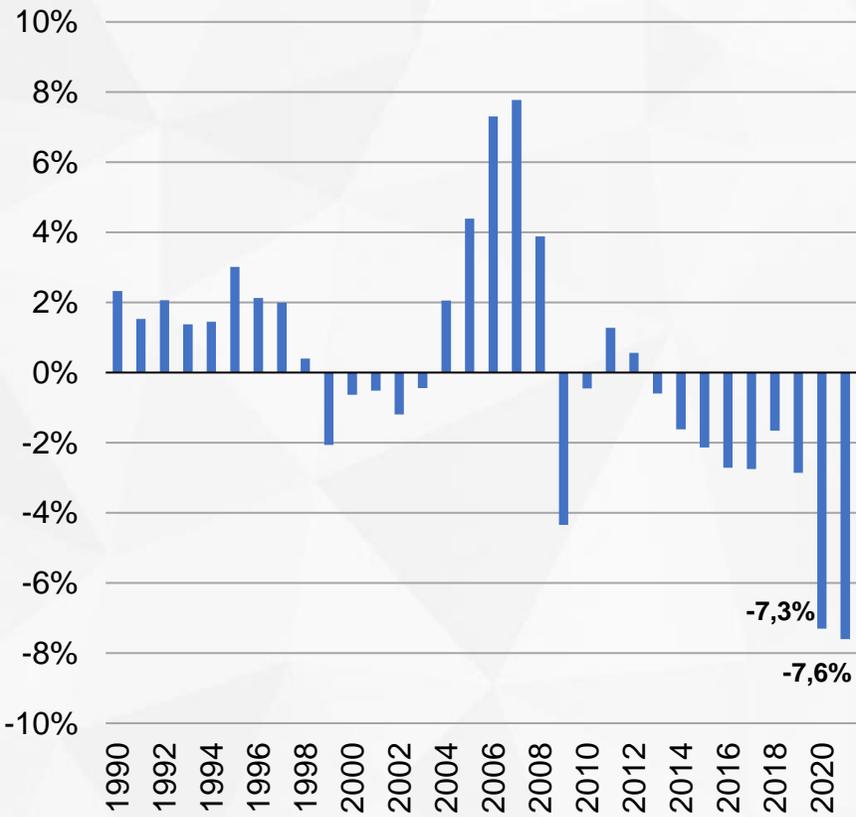


Fiscal situation and prospects

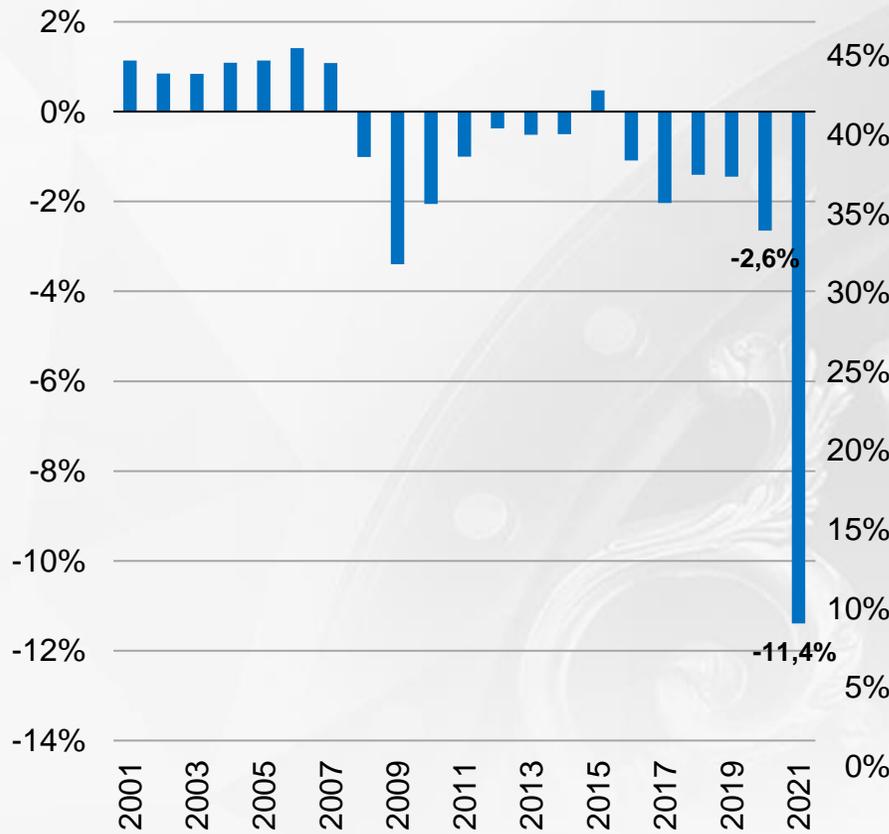


Public finances deteriorated during the crises. Fiscal impulse was stronger in 2021 than in 2020

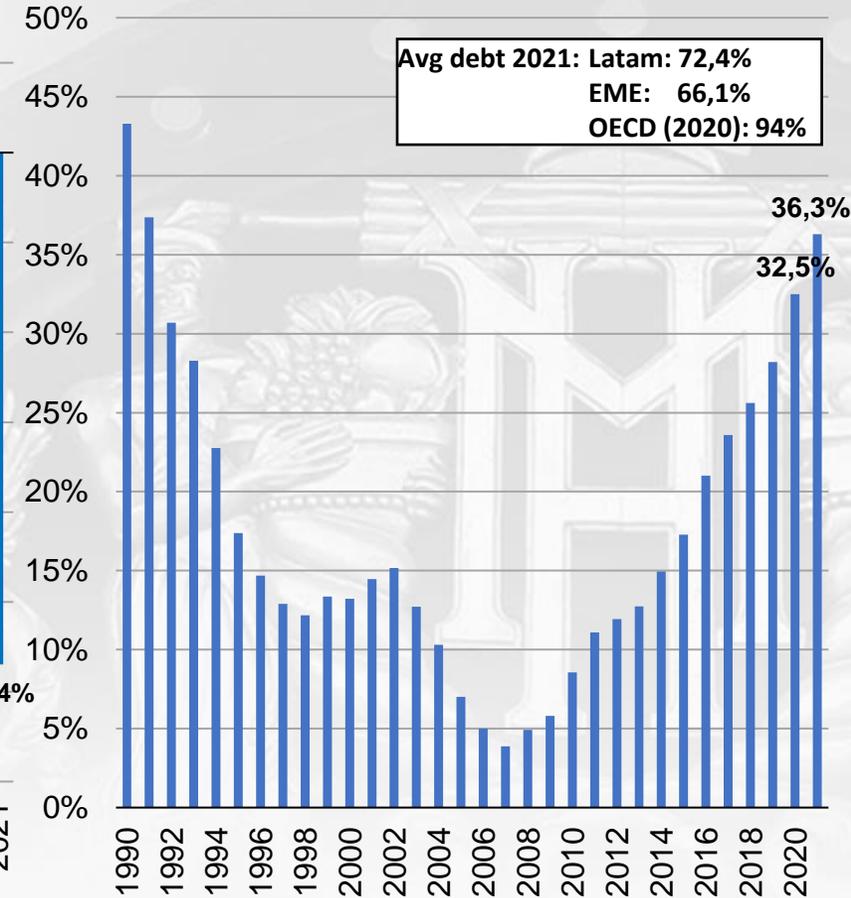
Central Government Overall Balance (% GDP)



Central Government Structural Balance (% GDP)



Central Government Gross Debt (% GDP)

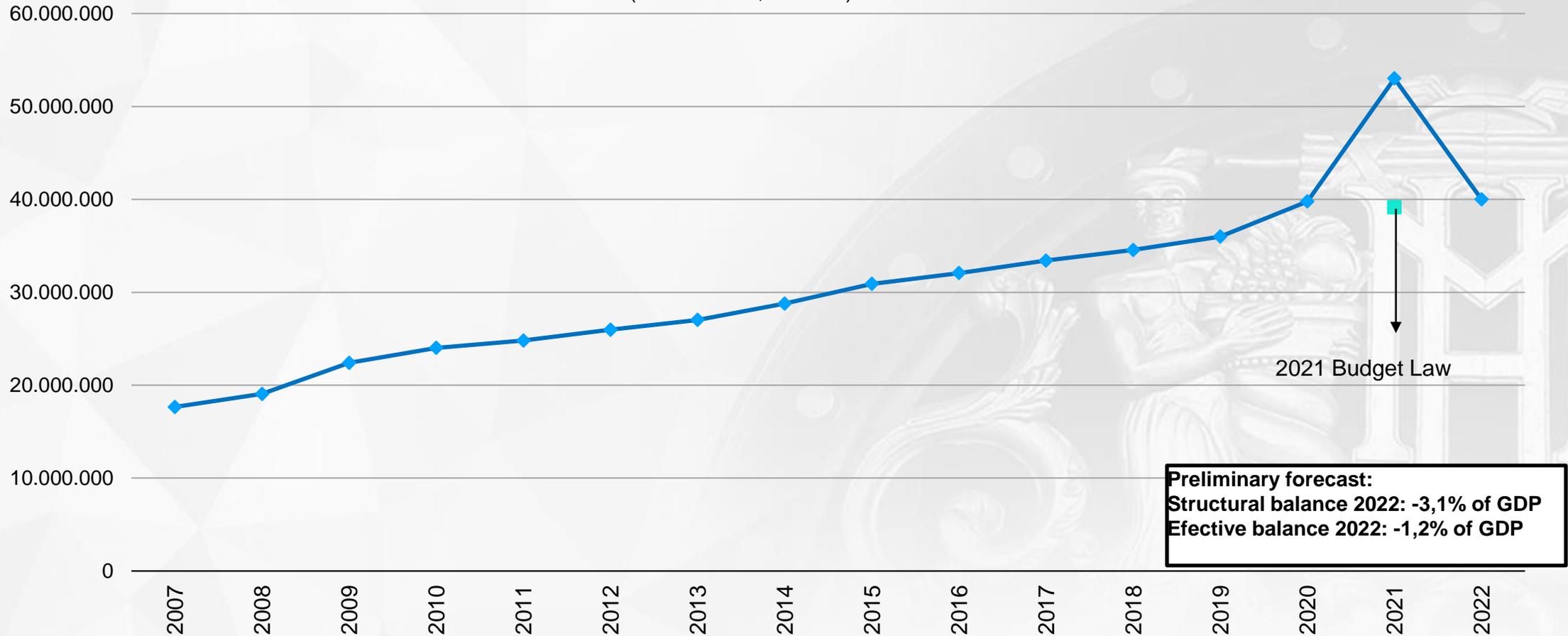


Note: 2021 data is preliminary.

Source: Budget Office (Dipres).

In 2022 fiscal spending will drop by more than 20% in real terms. The 2022 public expenditure level will stand slightly above the 2021 approved Budget Law

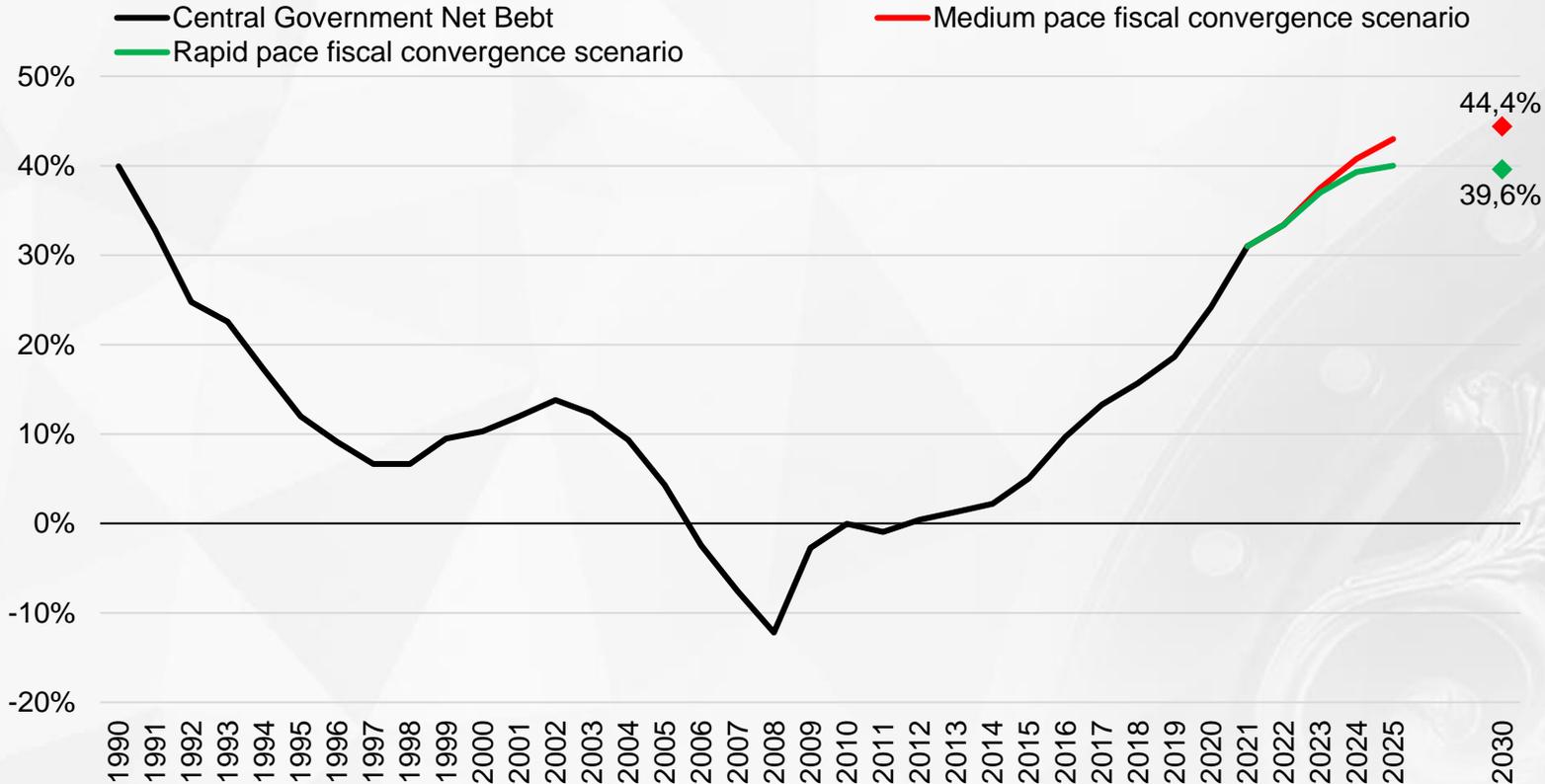
Central Government Expenditure (in 2009 CLP, millions)



Note: 2021 data is preliminary. 2022 shows forecasts.
Source: Budget Office (Dipres).

Going forward, fiscal policy will converge to sustainable debt levels in the course of the current administration

Central Government Net Debt and Forecasts (*)
(% GDP)



Fiscal goals will be established to allow debt convergence.

The announcement will be made on May 3rd.

Note: Net debt is calculated as Central Government Gross Debt, less Total Treasury assets. Fiscal convergence scenarios are made considering Autonomous Fiscal Council forecasts showed in their report: "Informe del Consejo Fiscal Autónomo sobre el Ejercicio de sus Funciones y Atribuciones", published in September 2021. For 2021, net debt corresponds to the effective data. For forecasts between 2022-2026, the data are spliced data using the difference, as a percentage of GDP, of the CFA projections for each year. The forecasts shown in this graph consider a structural balance starting point of -3,9% in 2022, in line with the 2022 Budget Law. The medium pace fiscal convergence scenario refers to a structural balance reduction of 0,5 p.p. of GDP per year, starting in 2023, and the rapid pace fiscal convergence scenario refers to a reduction of 1,0 p.p. of GDP per year.

Source: Budget Office (Dipres) and Chile's Autonomous Fiscal Council (CFA).

During its term, the Boric government aims to implement:

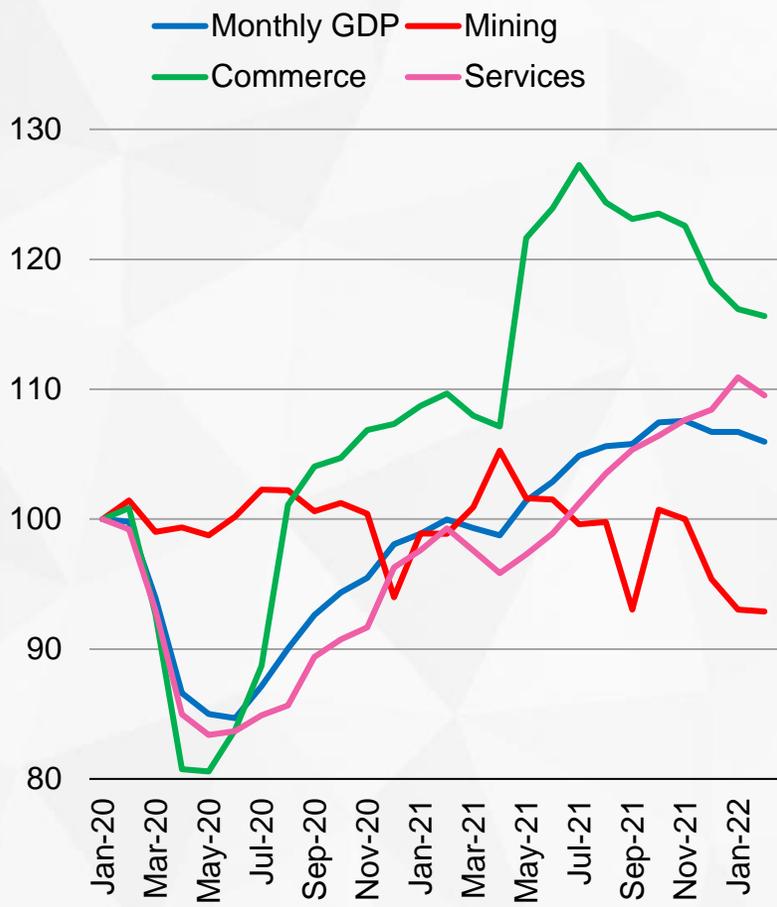
- Inclusive recovery plan
- Tax reform
- Pension reform
- In addition, it will face emerging challenges:
 - Stability and financial inclusion
 - Productivity and Green transition

The reform agenda

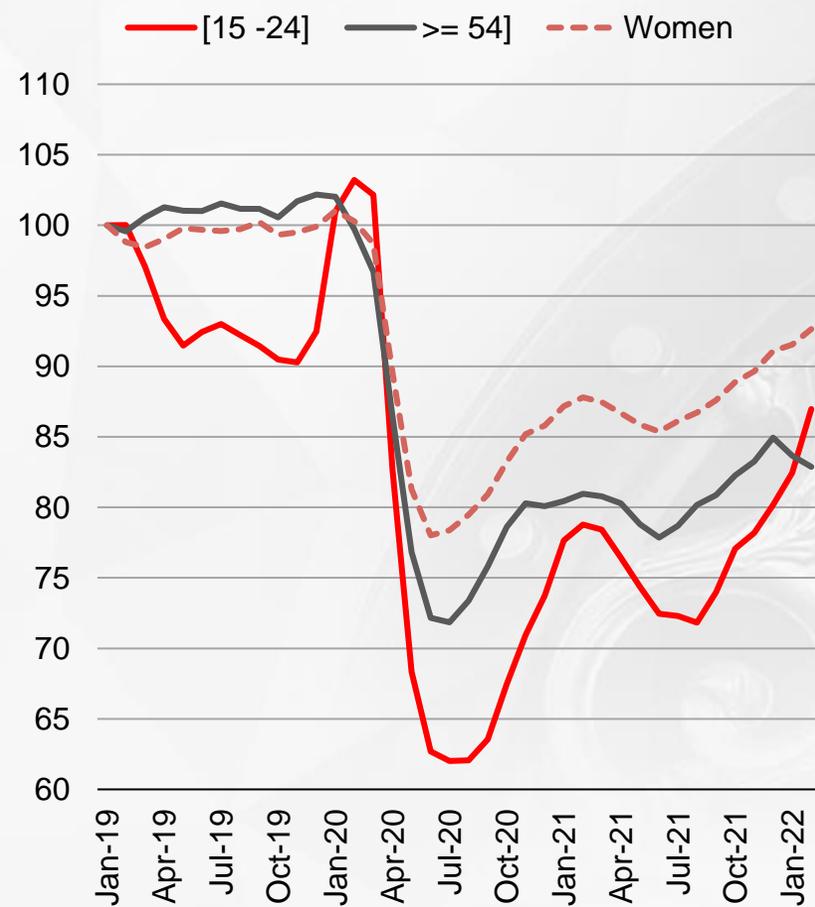


Government efforts will aim at addressing lags and scars left by the crisis. All within the fiscal envelope committed for 2022

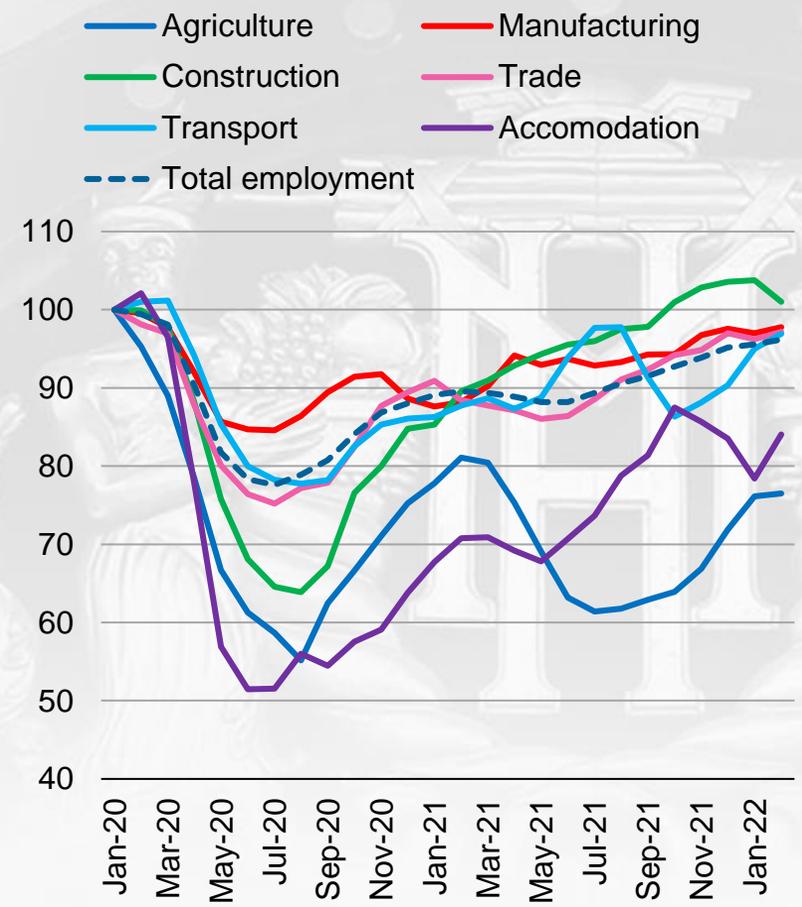
Seasonally-adjusted monthly GDP
(Jan-20 = 100)



Participation rate by groups
(100 = Jan-19)



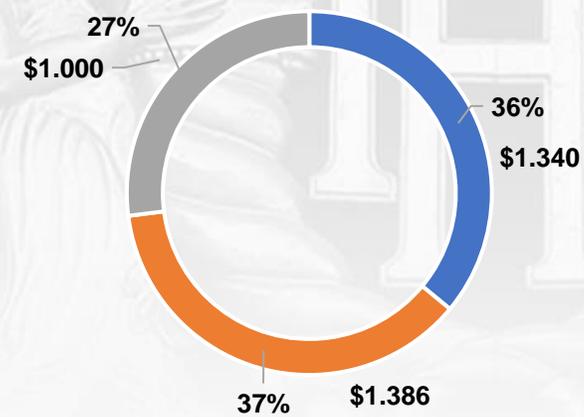
Employment by economic activity
(100 = Jan-20)



The Inclusive Recovery Plan was presented recently



**Expenditure of Inclusive Recovery Plan
(%, US\$ millions)**

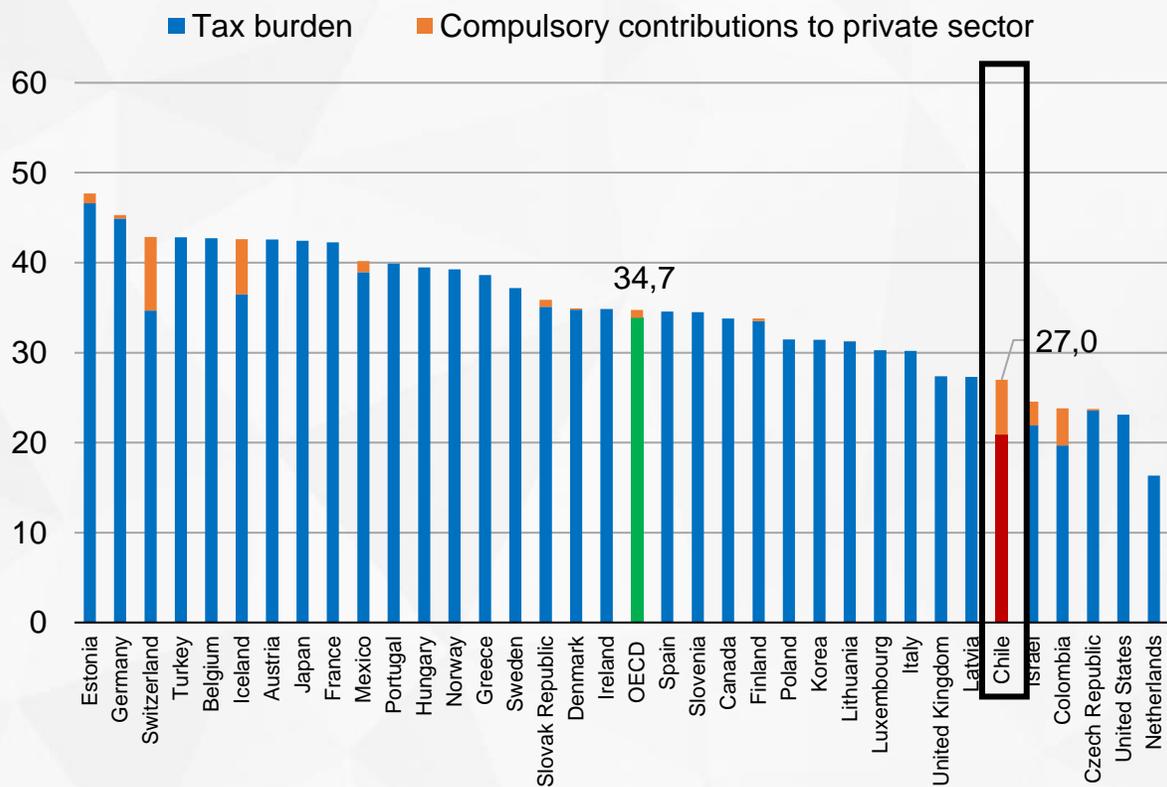


- Direct transfers for families
- Job creation and support for lagged sectors
- SMEs support

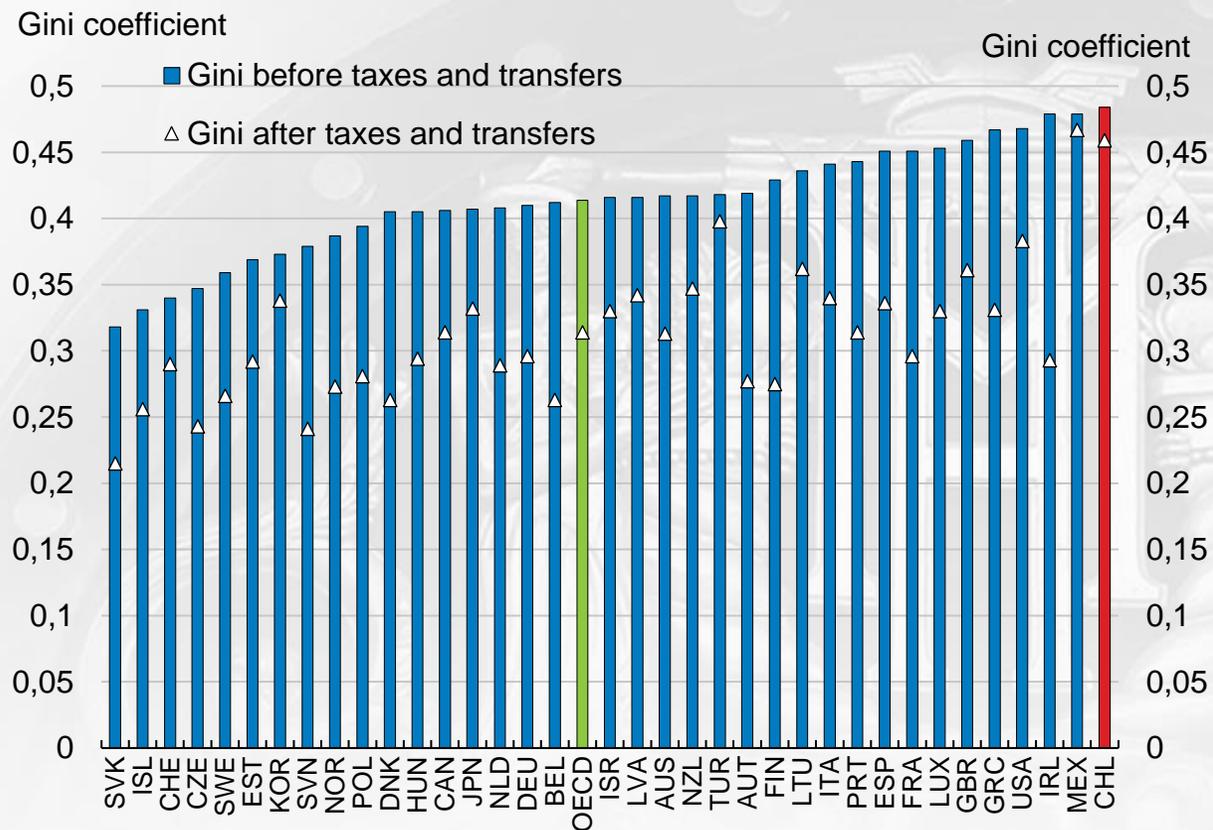
Main pillars	Measures
1. Recovering wage earners jobs	<ul style="list-style-type: none"> Extension of the subsidy of protection of labor Extension of EFI linked with job creation Increase on minimum wages Strengthening of childcare program
2. Public Investment	<ul style="list-style-type: none"> Infrastructure fund for local governments Reforestation Native Forests 32% increase in public investment
3. Support for not recovered population segments	<ul style="list-style-type: none"> Increase on food scholarships Direct transfer for cultural workers Expansion of the support and care network More resources in Day Centers for Elderly.
4. Boosting SMEs	<ul style="list-style-type: none"> Support for small mining Increase on coverage of development and innovation programs More resources for small agriculture business Less conditions for state guaranteed loans Loans for SMEs
5. Rising living costs	<ul style="list-style-type: none"> Stabilization of public transport prices Stabilization of prices of fuels and oil Fair price of gas
6. Economic and social protection mechanisms	<ul style="list-style-type: none"> Automatic EFI on emergency Enhanced benefits of jobless insurance

The tax burden is relatively low and the tax system does not contribute to improve inequality

Tax burden adjusted by compulsory contributions to private sector
(% of GDP)



Income inequality: pre and post-tax and government transfers
(Working population, 2018 or latest year available)

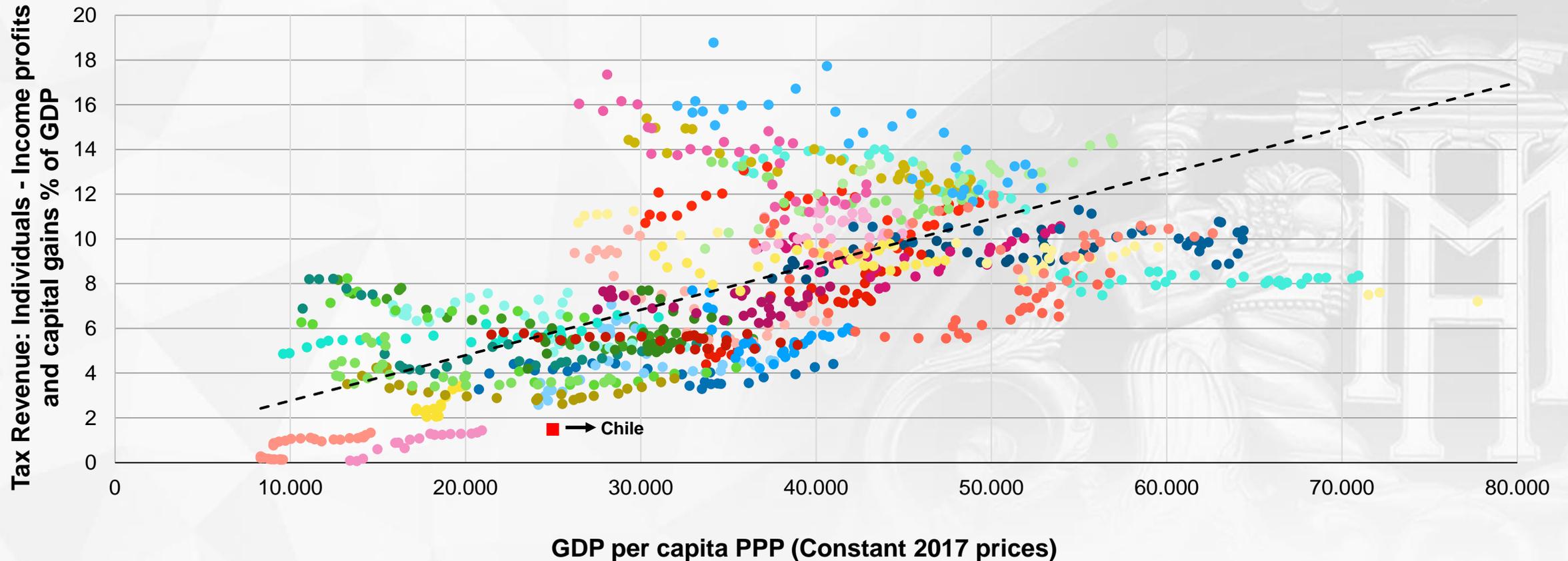


Note: green column stand for the OECD average and the red column for Chile.

Source: OECD, IMF.

Taxes: Chile's tax collection on individuals is below all OECD countries according GDP per capita

Tax revenue Individuals and GDP per capita- OECD countries

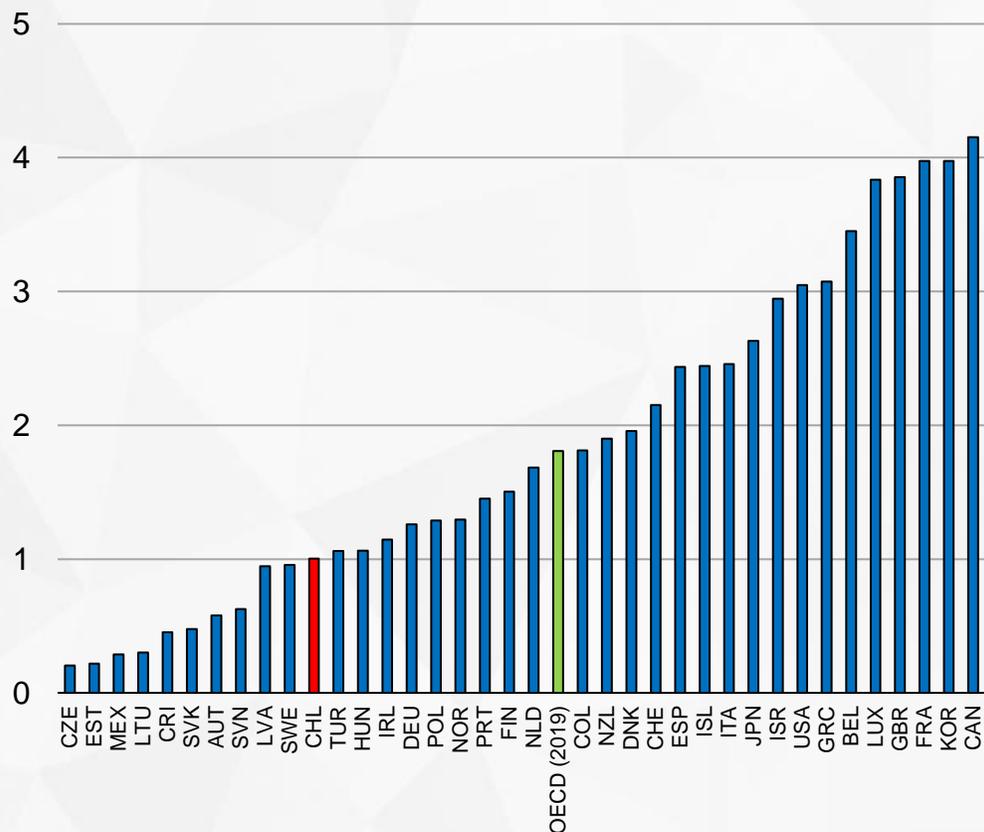


Note: each color accounts for a different OECD country in all years available data. Red mark accounts for latest Chile available data.

Source: OECD, World Bank.

Taxes: Chile's tax collection stands well-below other OECD economies in different categories

Tax revenue from property tax
(% GDP, 2020)



Carbon Tax: International Comparison
(IMF, 2019)

	Year introduced	US\$/ton CO2
Chile	2017	5
Colombia	2017	5
Denmark	1992	26
Finland	1990	65
France	2014	50
Ireland	2010	22
Japan	2012	3
Mexico	2014	1 a 3
Norway	1991	59
Portugal	2015	14
South Africa	2019	10
Sweden	1991	127
Switzerland	2008	96

Note: green column stand for the OECD average and the red column for Chile.

Source: OECD, IMF.

2) Tax Reform

Objective: Increasing government revenue to promote a sustainable development, satisfy social and economic demands and boosting green growth.



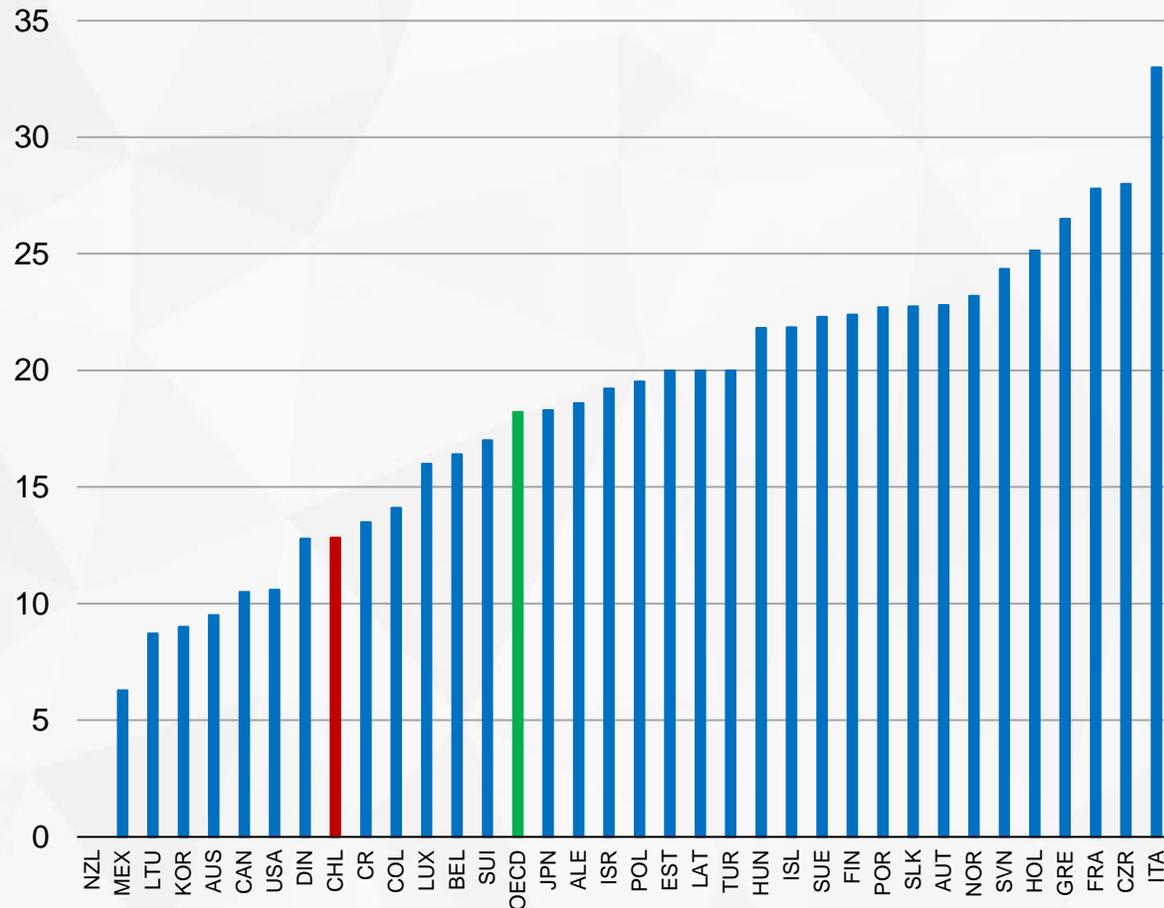
Ongoing: Instrument design

April: Social dialogues with business associations, academics, civil society organizations, social organizations, etc.

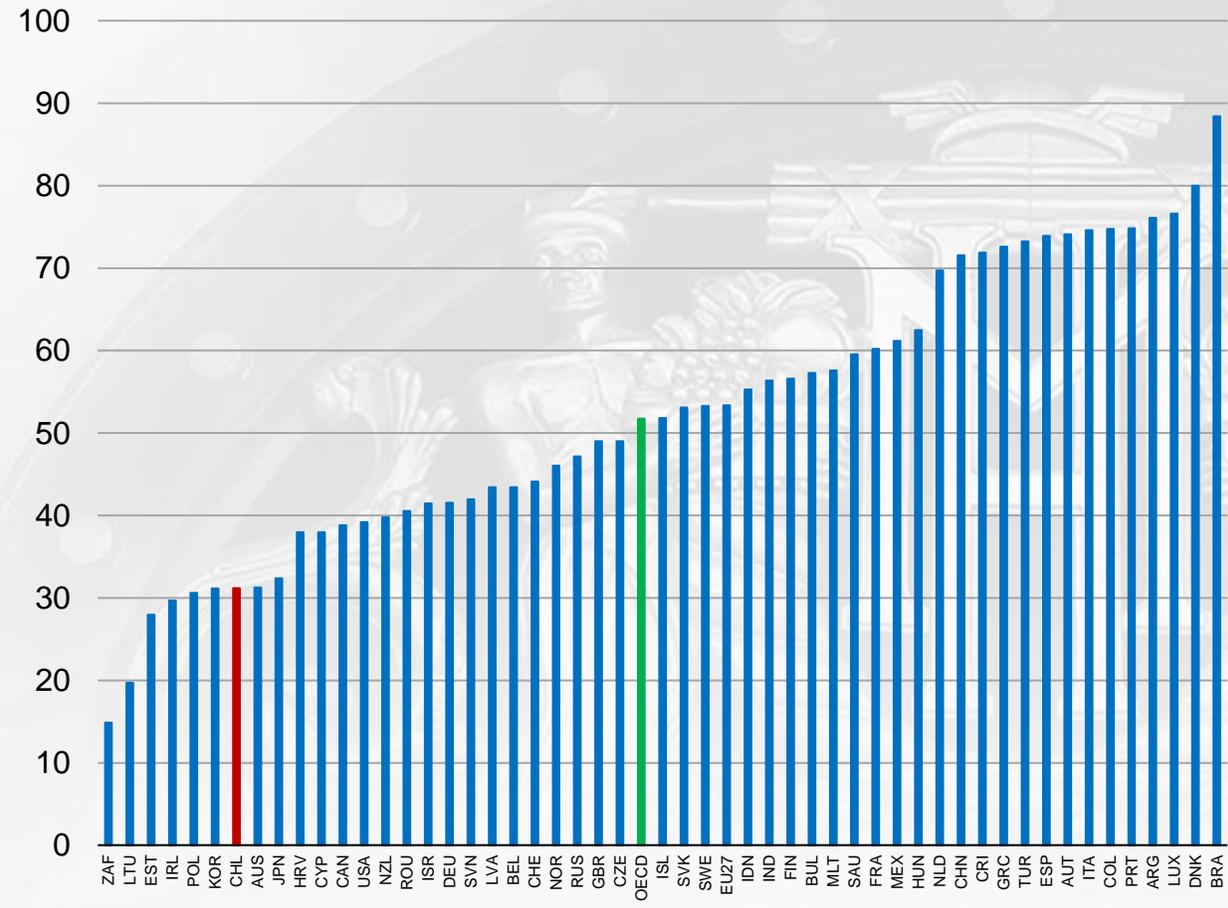
June: Bill is introduced

Effective contributions towards the pensions system are low, limiting a higher replacement rate

Effective contribution to the pensions system
(% gross income, 2020)



Gross replacement rate
(at retirement age, 2020)



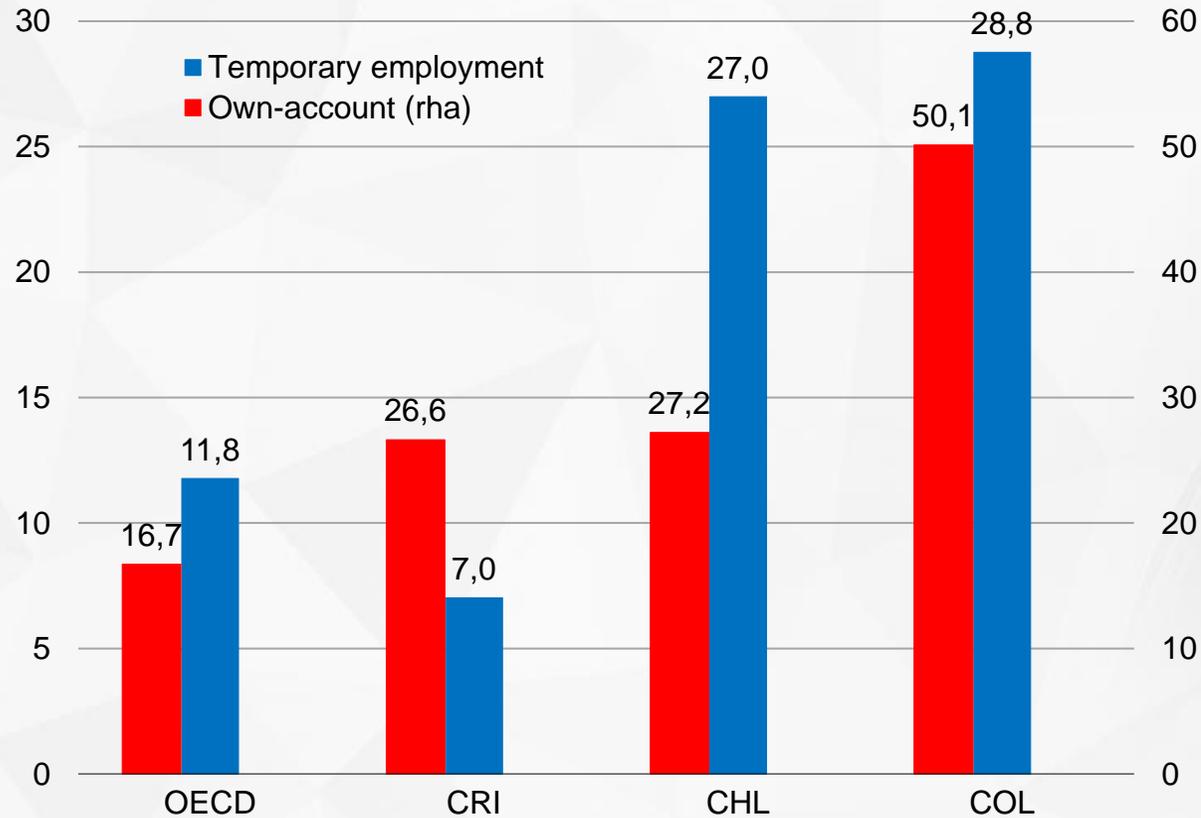
Note: Green column stands for the OECD average and the red column for Chile. In Chile, figures includes the disability insurance and fees paid to AFPs.

Source: OECD, IMF.

The contributions' density is considerably low for women. Also, Chile has a high share of low-quality job positions.

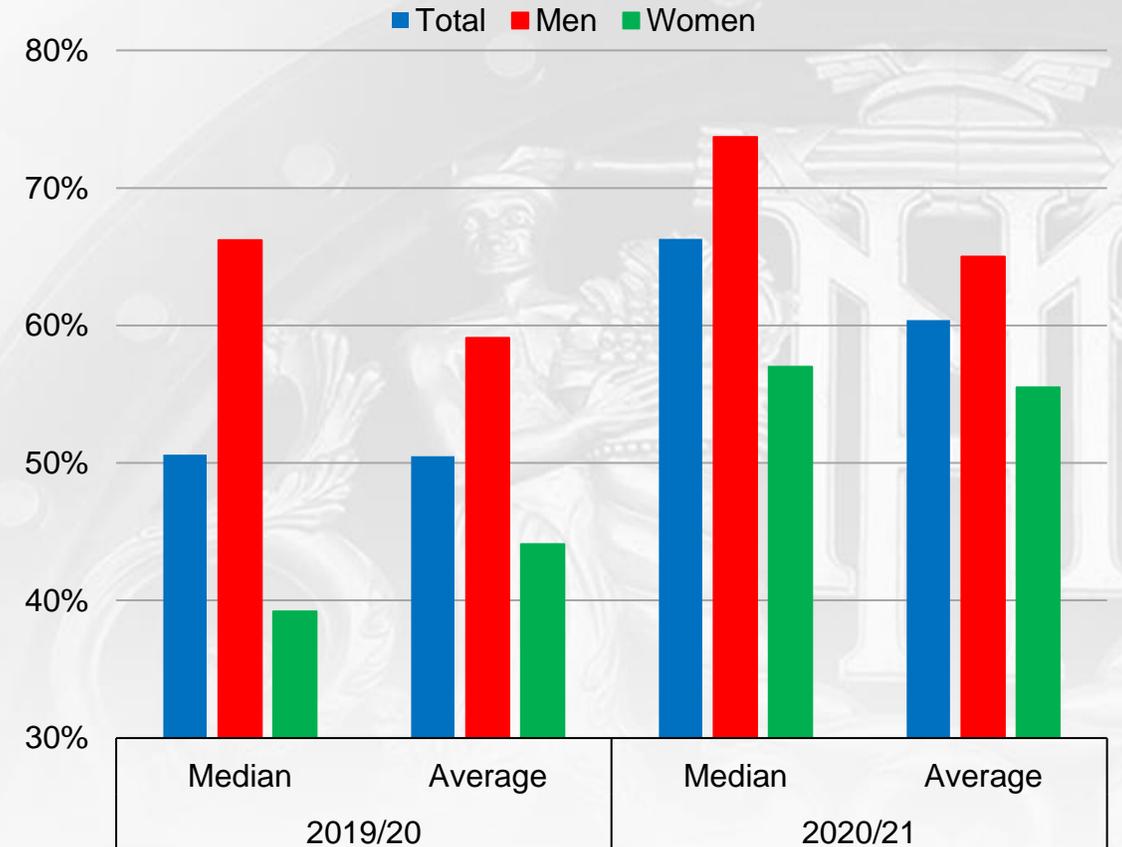
Employment sources

(% of instable workers in total employment, 2019)



Chile's contribution density

(# months contributed over # months affiliated to the system)



3) Pension Reform

Voluntary
Pillar

Social Insurance

Capitalization

Guaranteed individual pension

- What is the purpose of pension systems?
 1. To prevent poverty in old age.
 2. To generate a certain continuity of income in the face of various contingencies, including old age.
 3. Be able to cover all the major contingencies that people may face throughout their lives.
- Need systems that are sustainable in terms of their financial structure. We cannot depend on a single mechanism.
 - Individual capitalization: we cannot secure that we prevent poverty in old age.
 - Pay-as-you-go system: unsustainable financial imbalances as their population ages.
- Need to combine elements, different building blocks to address these three challenges.
 1. Fiscal support to ensure the prevention of poverty in old age.
 2. Capitalization to ensure accumulation over time, which makes feasible a high rate of replacement
 3. A solidarity component to secure that different contingencies are appropriately covered.

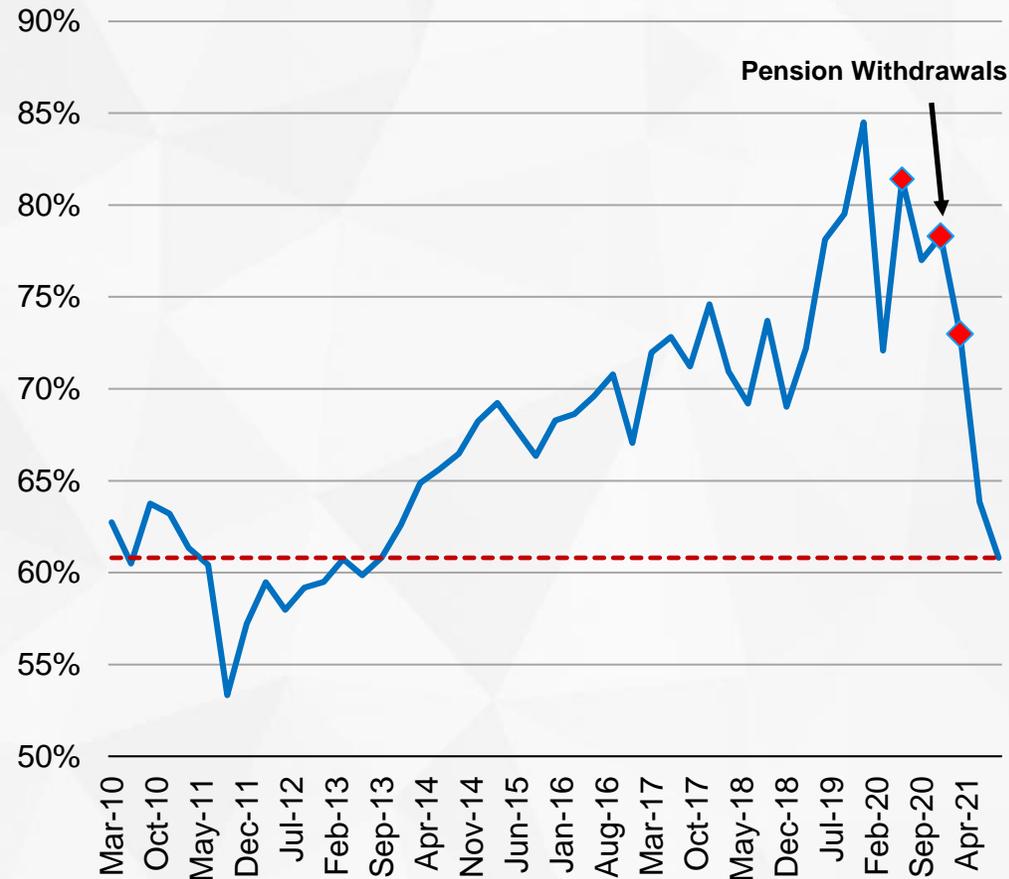
Presenting a proposal by 3Q2022.

Emerging challenges



It is necessary to recover the liquidity and financial depth of the domestic capital market.

Total Assets of Pension System
(% GDP)



Projects and initiatives that will promote further progress towards deeper, more stable, and inclusive capital markets

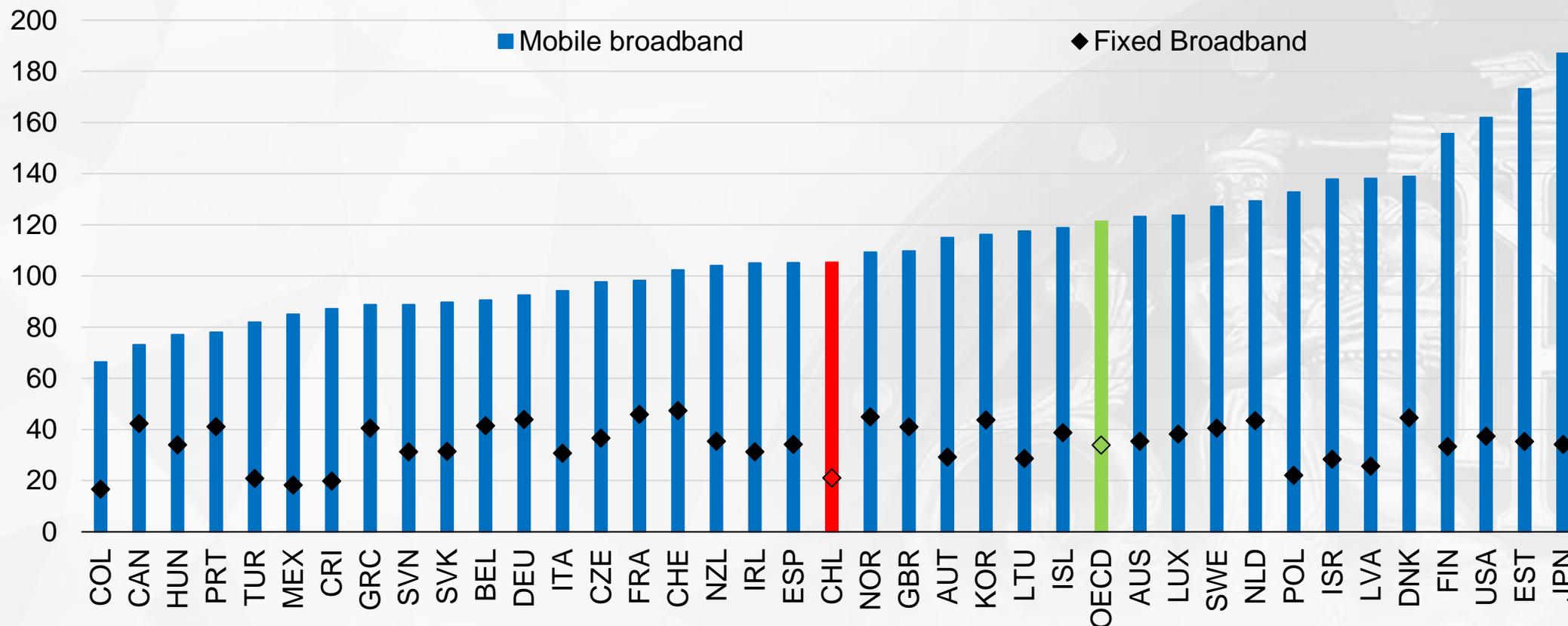
- Financial Innovation Bill. (Fintech)
- Internationalization of the CLP (simplified RUT).
- Resilience of the financial system and its infrastructure. (allow the Central Bank to grant liquidity to non-bank financial players)
- Legislative initiative that establishes a risk-based supervision system for insurance companies.
- Initiative that creates a consolidated debt registry.
- A bill that regulates the protection and treatment of personal data and creates the Agency for the Protection of Personal Data.

Note: green lines represents the mandatory savings PF withdrawals dates (10%)

Source: Chile's Pensions Supervisor (SAFP) and Financial Market Commission (CMF).

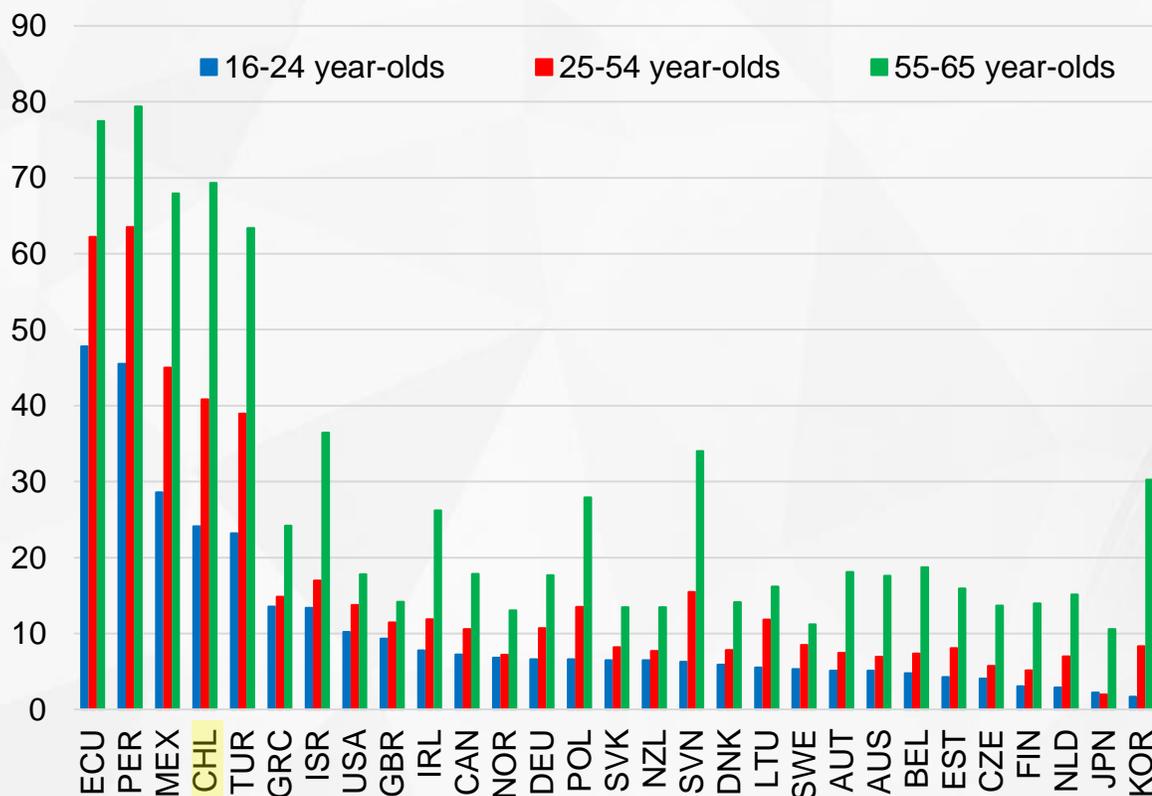
Improve productivity: There're some gaps to close in terms of digital transformation. Chile lags other countries in fixed broadband subscriptions.

Broadband subscriptions
(Subscriptions per 100 inhabitants, June 2021)

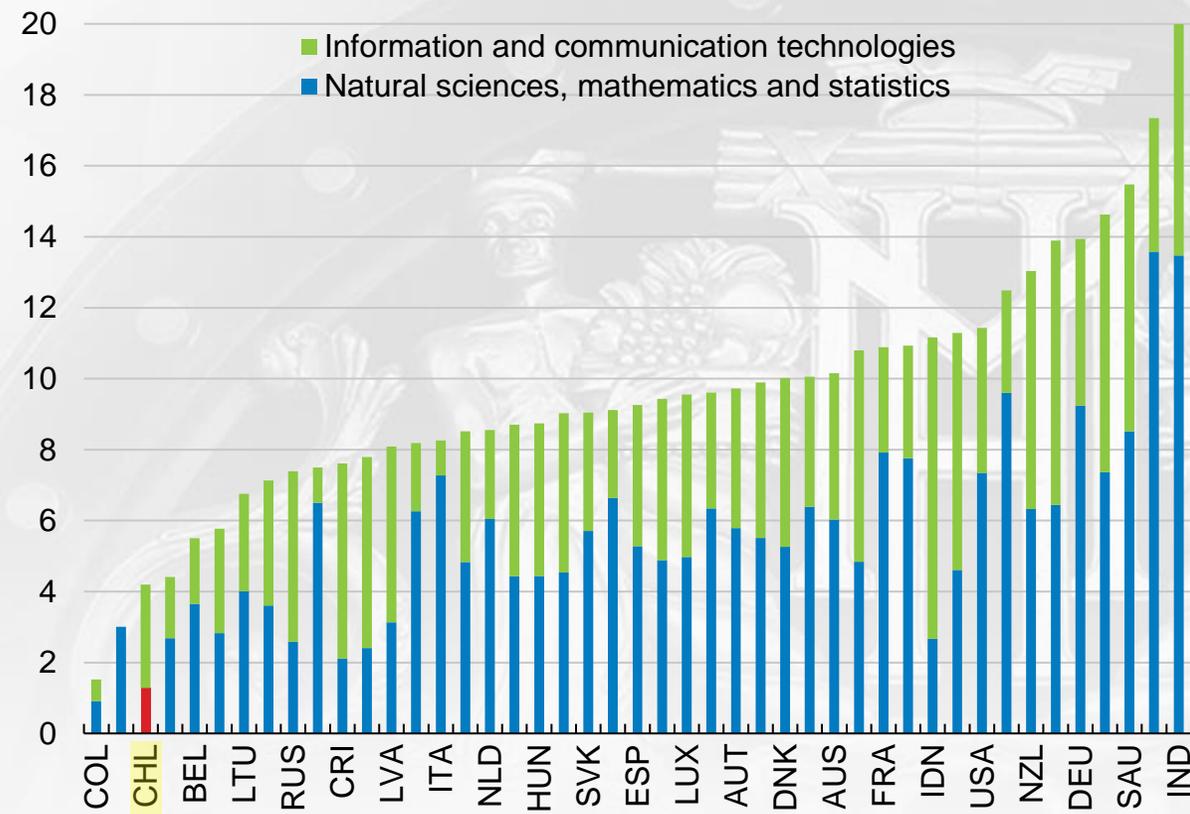


There's room for improvement in digital areas' skills and ICT tertiary-educated workers

Share of youth, prime age adults and older people lacking basic skills in digital areas (*)
(%)



Tertiary graduates by field: IT and STEM
(% of all graduates, 2017 or latest year available)

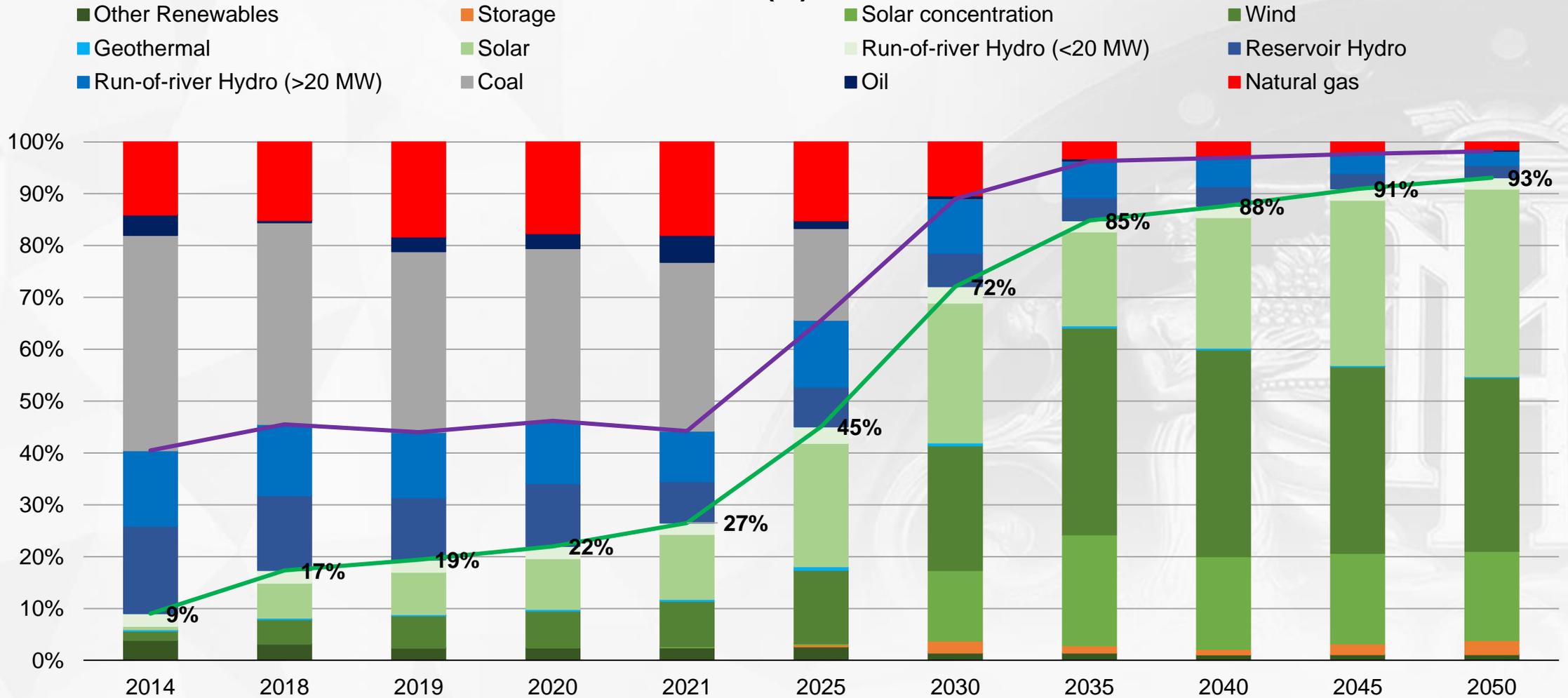


Note: (*) Chile, Greece, Israel, Lithuania, New Zealand, Slovenia and Turkey: Year of reference 2015. Ecuador, Mexico, Peru and United States: Year of reference 2017. All other countries: Year of reference 2012. Data for Belgium refer only to Flanders and data for the United Kingdom refer to England and Northern Ireland jointly.

Source: OECD.

Green Transition: Transitions to low carbon electricity systems

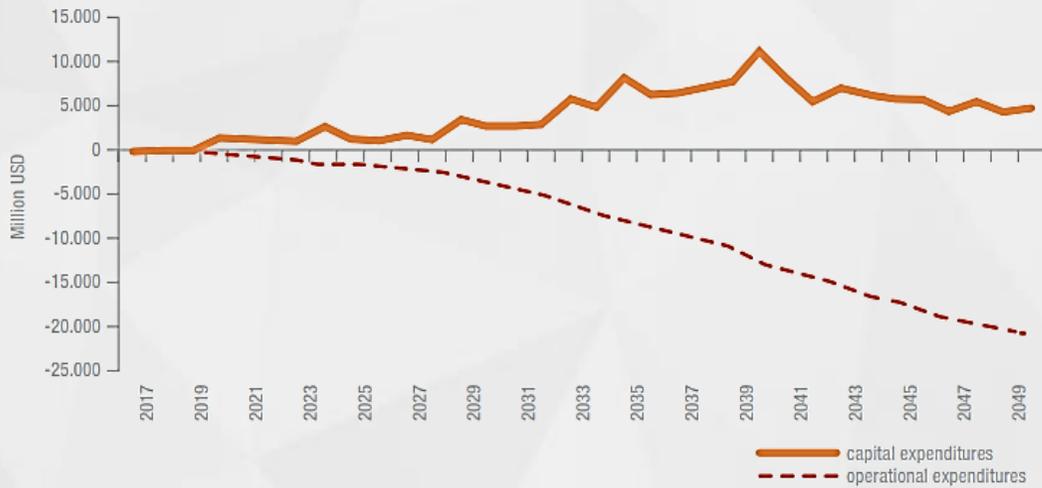
Energy matrix and NCRE participation (%)





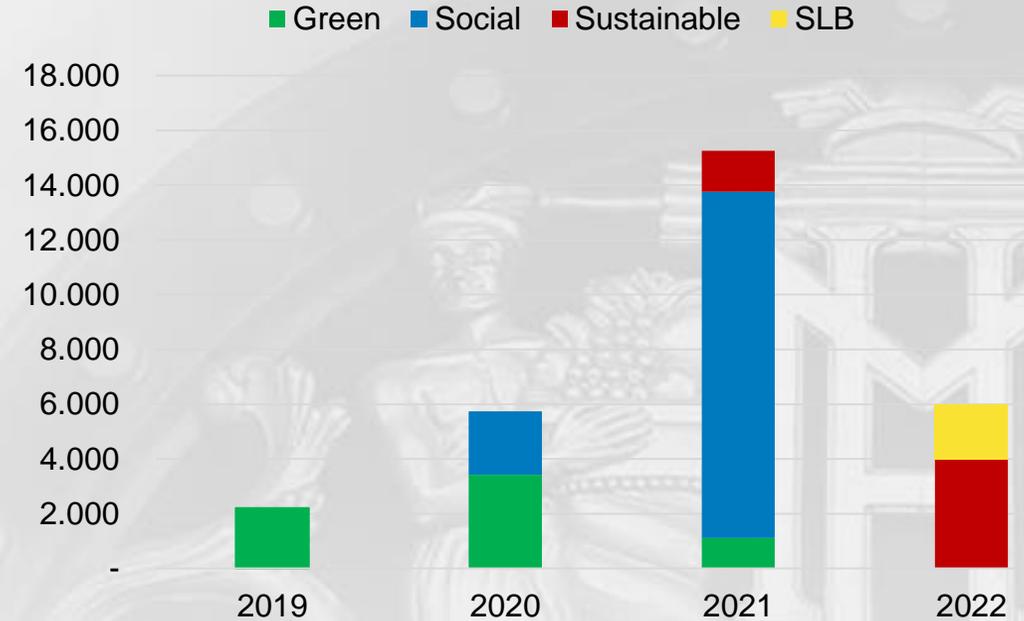
Green Transition: Key role of Green Finance in aligning financial flows towards climate action. Labelled bonds, including green bonds, have broadened Chile's investor base.

Total net capital and operational expenditures (in million USD) for net-zero emission target by 2050



Net present value of the investment required is around US\$48.600 million, and represents savings of about US\$80.100 million, giving a direct net gain of US\$31.500 million

ESG Issuances of Chile
(MM US\$ equivalent issued amount)



As of March-2022, the Ministry of Finance has issued **US\$33 billion in labelled bonds:**

- i. Social: US\$17.8 billion
- ii. Green: US\$7.7 billion
- iii. Sustainable: US\$5.5 billion

In sum, these reach **roughly 28.7% of Chile's Central Government debt**

Gathering of information necessary to promote green finance:

- Taxonomy of environmentally sustainable economic activities: Chile is currently working on the development of structural elements for a future taxonomy. This will allow investors to distinguish between “environmentally sustainable” and “non-environmentally sustainable” economic activities.
- Valuation of the Natural Capital: Chile formed a Natural Capital Committee to measure, evaluate, value, and advise the government on ecosystem services matters.
- Green Budgeting: Chile is developing a fiscal framework for measure de fiscal expenditure in climate change matters.

Continue the development and refinement of green financial instruments:

- Carbon price instruments: Chile is working on the implementation of a mixed system of these instruments, which works effectively and in a coordinated manner. In the case of the Green Tax, the country is evaluating the opportunity proposed by a new Tax reform for the improvement of the green tax.
- Given the unique conditions that the country presents for the Green Hydrogen industry, and its contribution in the path towards carbon neutrality, Chile is working on the promotion of financial instruments that promote such an industry.

Constitutional Process



Chile's Convention Calendar

July 5th, 2022:

Deadline for Constituents to propose a new Constitution

September 4th, 2022:

Referendum to approve or reject the proposal.

- “Approve” reached 78% of the votes, and “Reject” the remaining 22%.
- Drafting a new constitution through a Constitutional Convention reached 79%, above the 21% of the Mixed Convention.

May 15th-16th, 2021 - Election of Conventional Constituents

Some norms and procedures of the Convention...

- A two-thirds majority of the Convention members is needed to approve the text of the new Constitution.
- Convention may not intervene or exercise any other functions over other organs or authorities.

July 2022 – Convention delivers Text

July 2022 – A Commission in charge of harmonizing the final draft will conceal internal consistency mismatches

September 2022 – Plebiscite to ratify the Constitution

Do you approve the text of the New Constitution proposed by the Convention?
Approve or **Reject**

Approve

President ratifies New Constitution.

Reject

Current Constitution remains

- ✓ Mandatory participation
- ✓ Simple majority
- ✓ The text of the New Constitution to be ratified in a plebiscite must be in accordance with the status of Chile as a Republic, its democratic regime, the judicial sentences, and the international treaties ratified by Chile.

After more than 9 months and over 1,300 norms proposed, the Convention has already approved 196 articles that will be embedded in the Constitutional proposal

33 Committees and subcommittees

Active (17/33)

- Political System
- Constitutional Principles
- State form
- Fundamental Rights
- Environment
- Justice System
- Culture, Science, Tech.
- Among others...

1,354 norms proposed

E.g., Central Bank-related Bulletins and initiatives proposed:

#937-6 // #936-6 // #866-6 //
#717-6 // #643-6 // #412-6 //
#349-6 // #04-6 // #172-6

Ex.2: Fiscal sustainability and responsibility:

#867-5

196 articles approved

So far, none has been included in the final draft

Ch. II – Constitutional Principles

29th art.: *“Public finances will be conducted through fiscal sustainability and responsibility principles, which will guide the state action in all its institutions and levels.” (*)*

35th art.: *Fiscal Budget: almost identical to current Constitution*

Other

18/20th art.: *Property tax: “Every person, has the right to property..”*

“No person can be deprived of their property, except by virtue of a law...”

Note: (*) Original version (in Spanish) prevails.

Source: Constitutional Convention website - www.chileconvencion.cl

Ministerio de Hacienda



CHILE MACRO OUTLOOK AND POLICY PRIORITIES AND PROSPECTS

IMF Spring Meeting, 2022
April 20, 2022

Mario Marcel C. | Minister of Finance