Monthly Economic Update

March 30th, 2020

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EVENTS IN CHILE

The government has implemented increasingly strict measures to slow the spread of the Coronavirus outbreak in Chile, including closing borders to foreigners, imposing a nightly nationwide curfew and from March 26th, restricting all non-essential movement in much of Santiago, including the main business, commercial and government districts. Schools, universities, shopping malls and many businesses have been closed while hundreds of thousands of workers are being encouraged to work from home where possible. Sanitary cordons have been imposed to prevent the outbreak spreading to northern and southern regions while Chileans arriving from high-risk countries have been required to enter obligatory quarantine for two weeks.

Three weeks after the first case of Coronavirus was detected in Chile, the number of cases had risen to 1,306 (March 26th), the second highest figure in South America behind Brazil, while three people have died. Health Minister Jaime Mañalich has estimated that the number of cases will peak at around 40,000 by late April or early May.

The government has proposed a US$11.75 billion package to support companies and families through the expected shutdown of the Chilean economy. Corporate tax payments will be suspended until July while small and medium-sized businesses will be able to delay payment of Value-Added Tax for three months. The government will inject US$500 million into state-owned bank BancoEstado so it can boost lending to households and SMEs by around US$4.4 billion. Stamp duty on financial transactions will be cut to zero until September making it cheaper to renegotiate loans while low income families will also receive a payment of CLP50,000/dependent. This measure has been criticized by the opposition lawmakers who have a majority in Congress as insufficient to maintain families during the lockdown.

To fund the package (worth the equivalent of 4.75% of GDP), Finance Minister Ignacio Briones said that the government will suspend its annual contribution of US$500 million to the Pensions Reserve Fund for the next two years and seek authorization from Congress to borrow an additional US$4.0 billion.

At a special unscheduled meeting on March 16th, the board of the Central Bank agreed to reduce its benchmark interest rate by 75 basis points to 1.00%, the biggest rate cut in over a decade. The board said the move, which followed similar cuts by Central Banks around the world, was necessary to mitigate of the Coronavirus outbreak on the economy. The decision was divided with two board members recommending a 50bp cut. Prior to the outbreak, analysts had expected the bank to reduce the rate by just 25bp at its subsequent meeting in May.

As well as the rate cut, the Bank announced additional measure to ensure liquidity in financial markets, including a new six-month credit facility to banks that increase lending to businesses, a program to buy to US$4.0 billion worth of bank bonds and the extension of its existing swap programs until January 2021.

In late February, Congress completed approval of the government's tax reform bill, simplifying the corporate tax regime while raising taxes on high income earners and wealthy property owners. The bill is expected to raise an additional US$2.2 billion annually which will finance new social measures such as the new guaranteed minimum income of CLP300,000 and higher basic pensions. Lawmakers have begun debating the government's new pensions reform which would see employers contribute an additional 6% of wages, half of which would go to workers' individual pensions account and the rest to boost the pensions of the lowest paid.

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ECONOMIC STATISTICS

• The Chilean economy has performed better than expected in recent months, growing by 1.5% in January, after contracting by 2.1% in the final quarter of last year. Finance Minister Ignacio Briones has warned that the Coronavirus emergency will deal a severe though transitory blow to the economy. Analysts fear that this could see Chile could enter recession in the coming quarters. The Central Bank is expected to radically reduce its growth forecast of 0.5-1.5% for this year in its upcoming monetary policy report

• Unemployment rose to 7.4% in the November-to-January rolling quarter, the first to fully encompass the wake of last October's widespread unrest. So far, the Central Bank's warning that joblessness could exceed 10.0% has not been fulfilled. That is largely because many workers instead have moved into lower quality jobs with the number in informal employment rising by 17.5% in the year to January, compared to a 2.1% expansion of the total workforce. However, the impact of the Coronavirus outbreak will likely lead to further increases in unemployment.

• The US dollar has surged against the Chilean Peso in recent weeks as investors rush to buy dollars amid the shutdown of large parts of the global economy. By mid-March, it had reached record levels above CLP860/dollar against an average of CPL796/dollar in February and CLP702/dollar last year.

• Share prices in Chile have slumped as the number of cases of Coronavirus have multiplied around the world. By March 18th, the IPSA index of the Santiago Stock Exchange's forty largest companies had fallen to 2,876 points, down 38.7% since the start of 2020 and its lowest level in almost four years. However, the index recovered above 3,000 points after US lawmakers approved a massive economic stimulus package.

• The international copper price has plummeted since mid-January on fears that the Coronavirus outbreak will limit global growth and reduce demand for the metal. By mid-March, the price had fallen as low as US$2.09/lb, its lowest level since 2016 and down 25% since the start of the year. With prices now below the production costs of less efficient mines, some companies may be forced halt production. Several, including Anglo American, BHP and Codelco have already reduced staffing levels to slow the spread of the Coronavirus while work on major investment projects, including Teck's QB2 and Codelco's Chuquicamata Underground, has been suspended

• Prior to the Coronavirus outbreak, business confidence was improving with the Monthly Business Confidence Index produced by the ICARE business organization and the Adolfo Ibáñez University, reaching 43.91 points in February - still in negative territory but up 10 points from the record low reached last December.

• Consumers, however, remain gloomy. GfK's Economic Perceptions Index reached 32.7 points in February, up just four points from the record low reached last November, as pessimism about the country's long-term outlook outweighed improved short-term prospects.

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