

Ministerio de Hacienda



CHILE'S SHORT AND LONG-TERM CHALLENGES: AN AMBITIOUS AND REALISTIC AGENDA

Georgetown University, 2022
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Mario Marcel C. | Minister of Finance

Chile has faced two extremely negative shocks since late-2019:

Shock #1: the Oct-19 Social Unrest

Response: a new democratic Chilean Constitution

Challenge: promote a successful channeling of the process

Shock #2: Covid-19 Pandemic

Response: unprecedented economic policies undertaken by the MoF and the BCCh

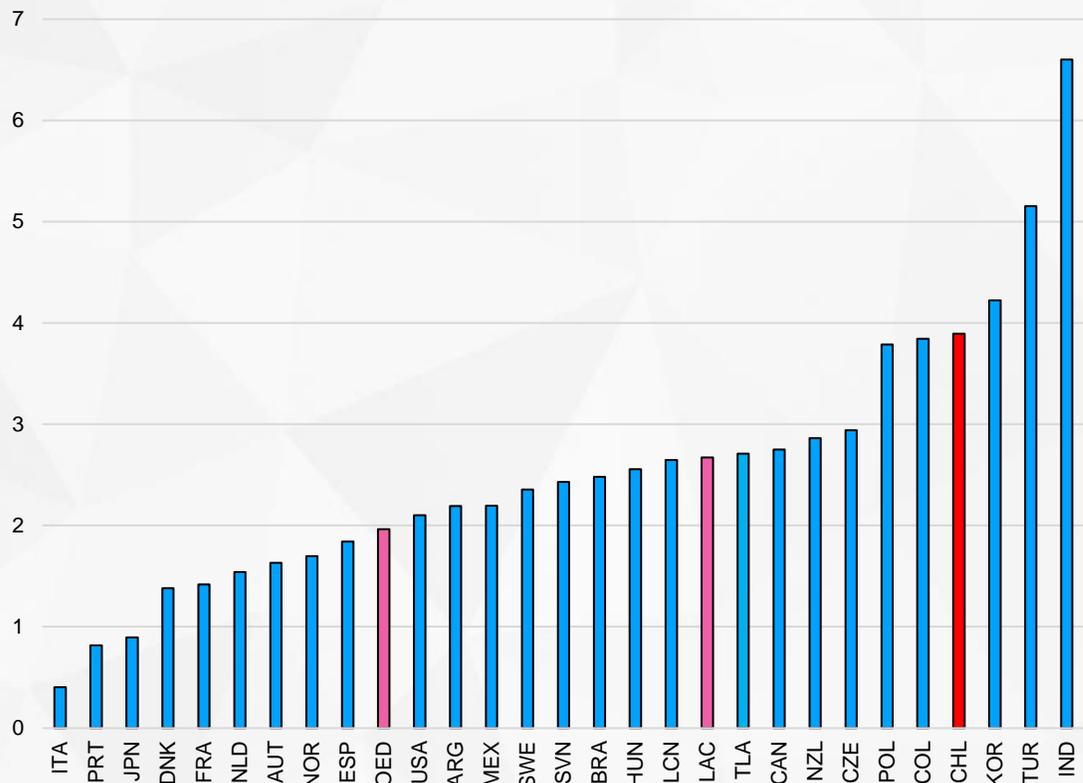
Challenge: to resolve the macroeconomic imbalances caused and build up new buffers

Our Government aims to contribute toward the resolution of both structural and pandemic-related challenges and imbalances that our country face.

Chile's 2019 social unrest: how did this happen?

Chile's economic growth has outperformed other countries, however, there is room for enhancing social needs

Average GDP growth between 2000-2018 (%)



Deprivations in Chile (2018 or latest available year)

17%
of the population live in relative income poverty.

53%
would be at risk of falling into poverty if they had to forgo 3 months of their income.

36%
of poor households spend more than 40% of their income on housing costs.

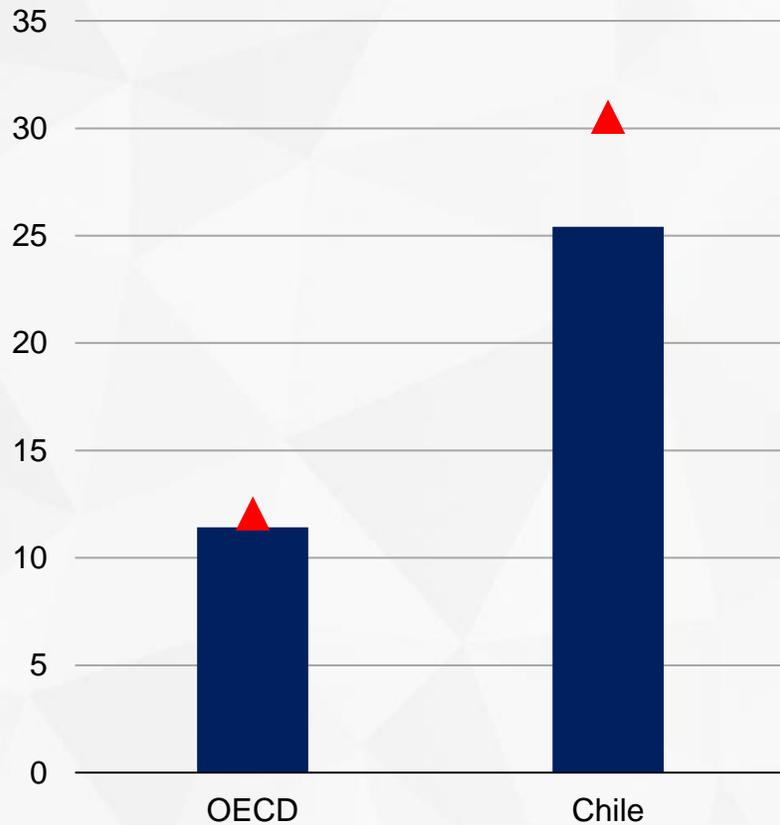
13%
say they have no friends or family to turn to in times of need



Inequality is still high and a lasting problem

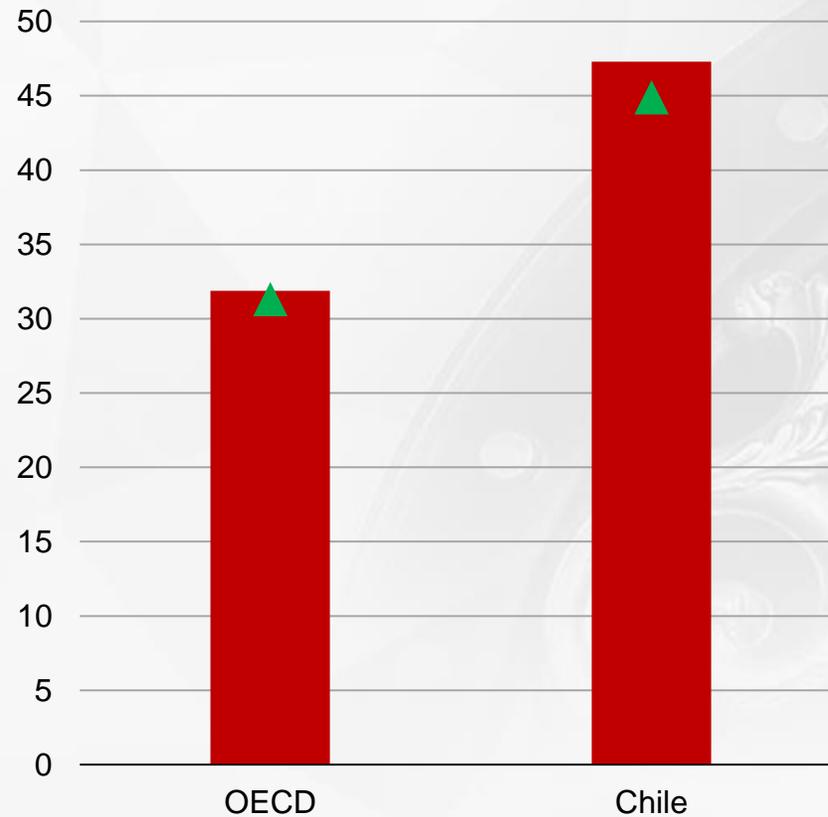
Share of temporary workers

- Share of temporary workers, 2020
- ▲ Share of temporary workers, 2010

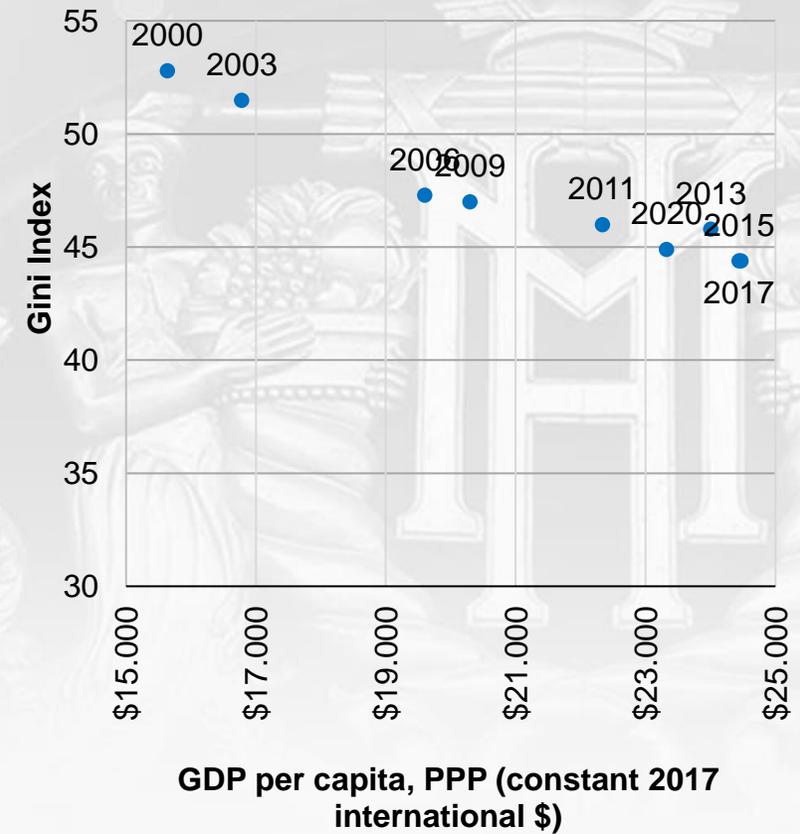


Gini Index

- Gini Index 2006 - 2007
- ▲ Gini Index 2020



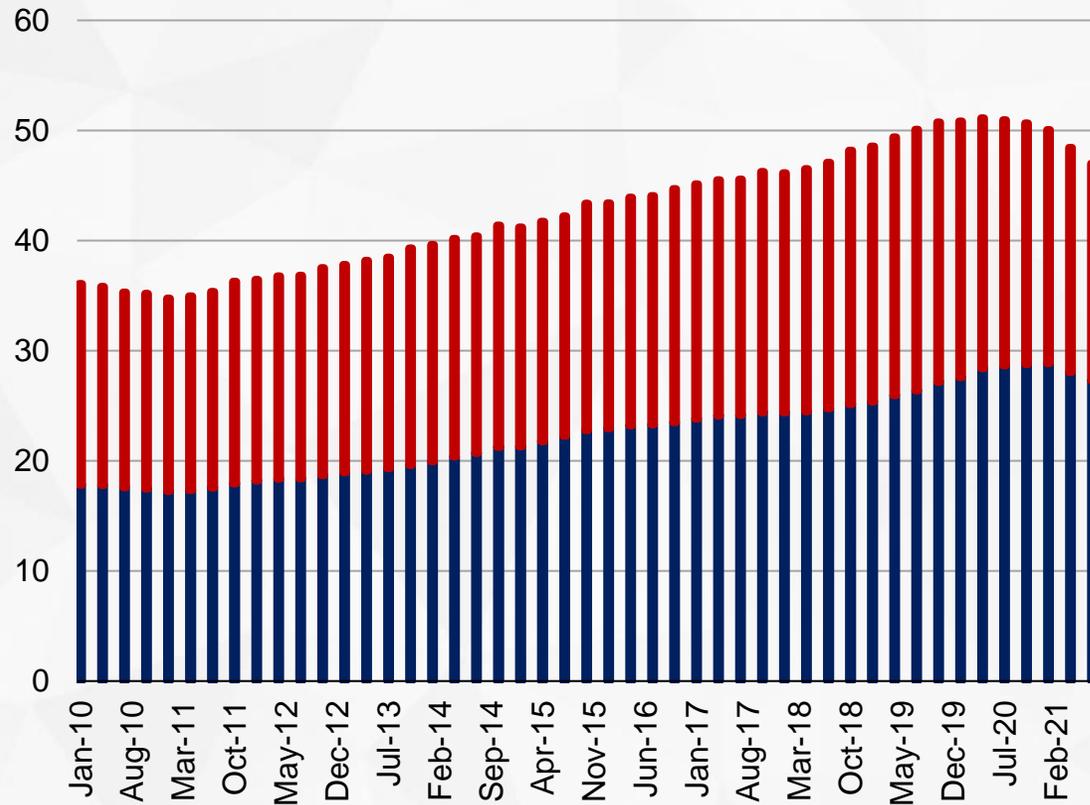
Gini coefficient and per capita income level (2000 - 2020)



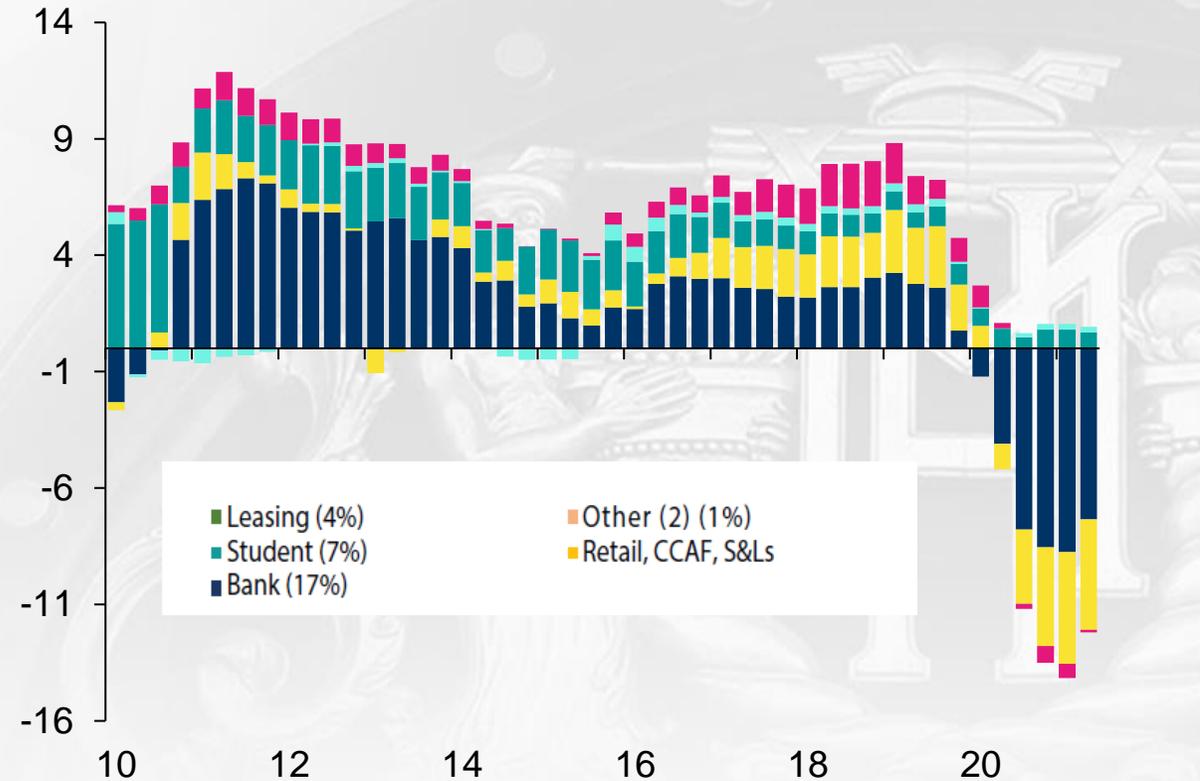
Household indebtedness has grown not only due to mortgages, but also due to consumer debt with non-banking institutions

Household indebtedness
(percent of GDP)

■ Mortgage ■ Non-mortgage



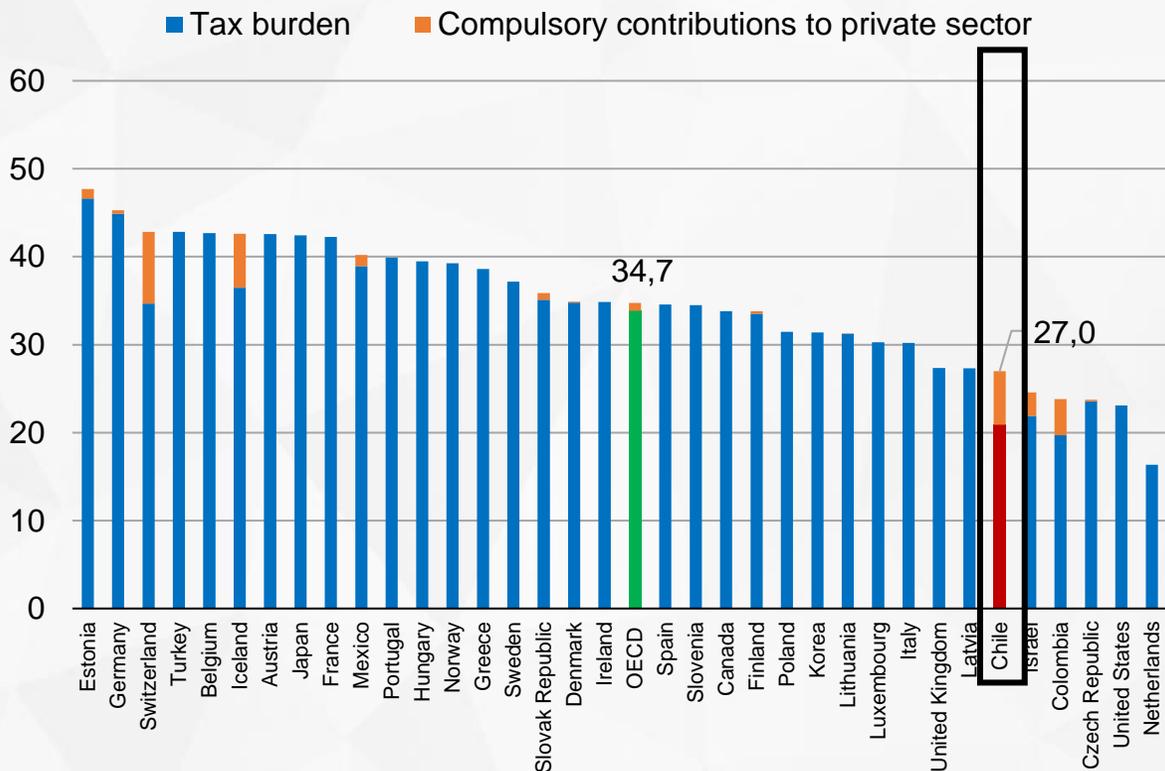
Non-mortgage debt
(annual change, percent)



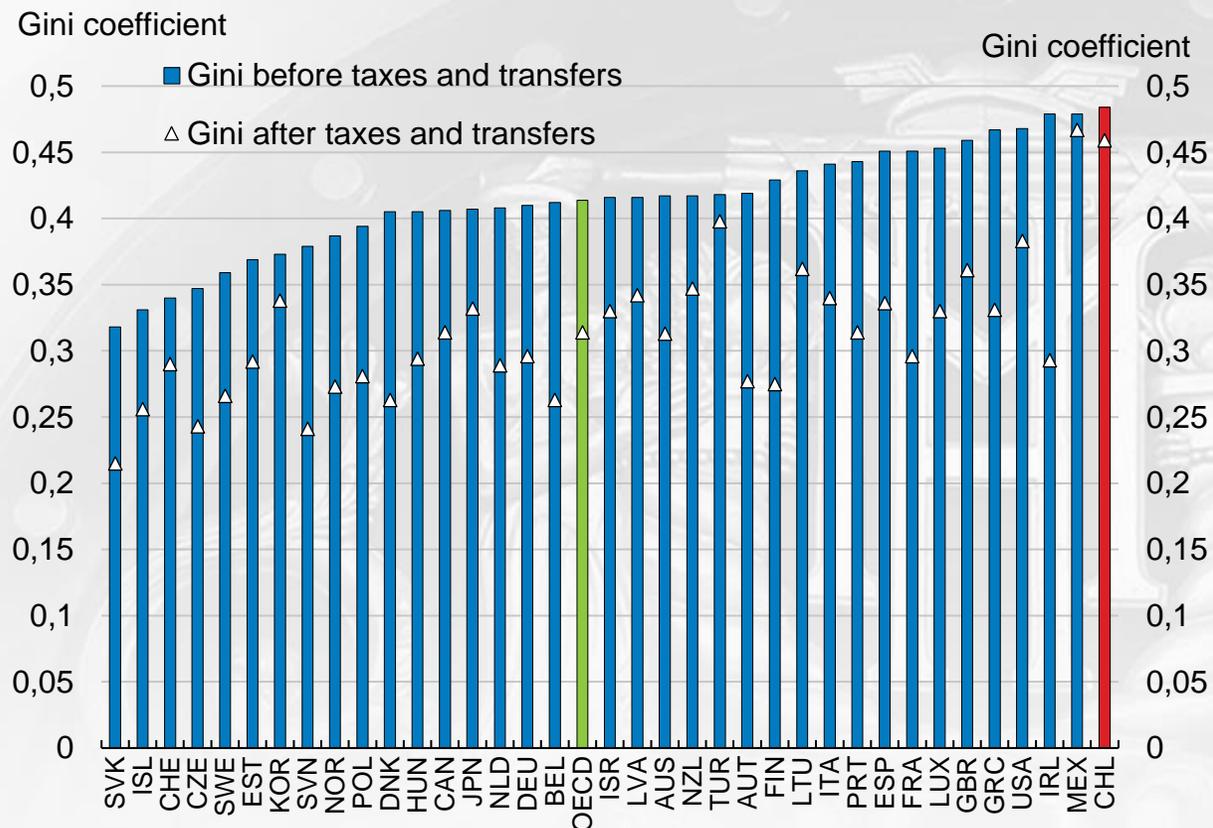
Source: Central Bank of Chile.

Chile's 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)

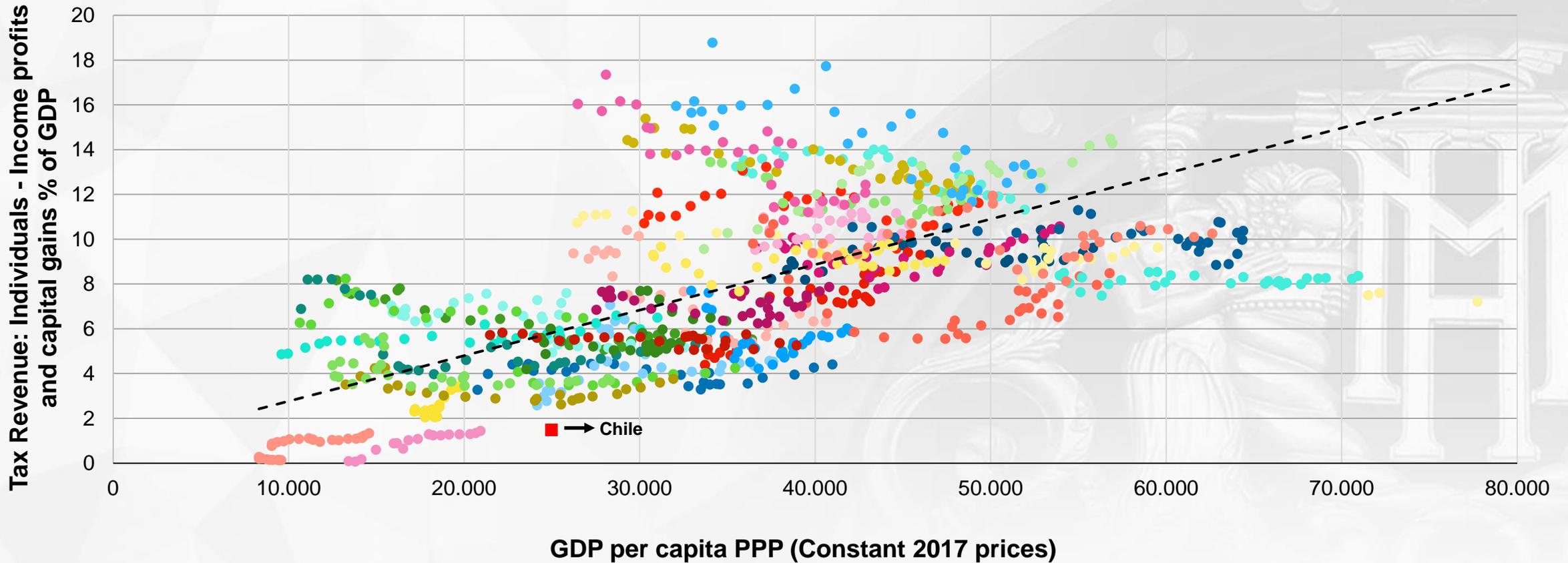


Note: green column stand for the OECD average and the red column for Chile.

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

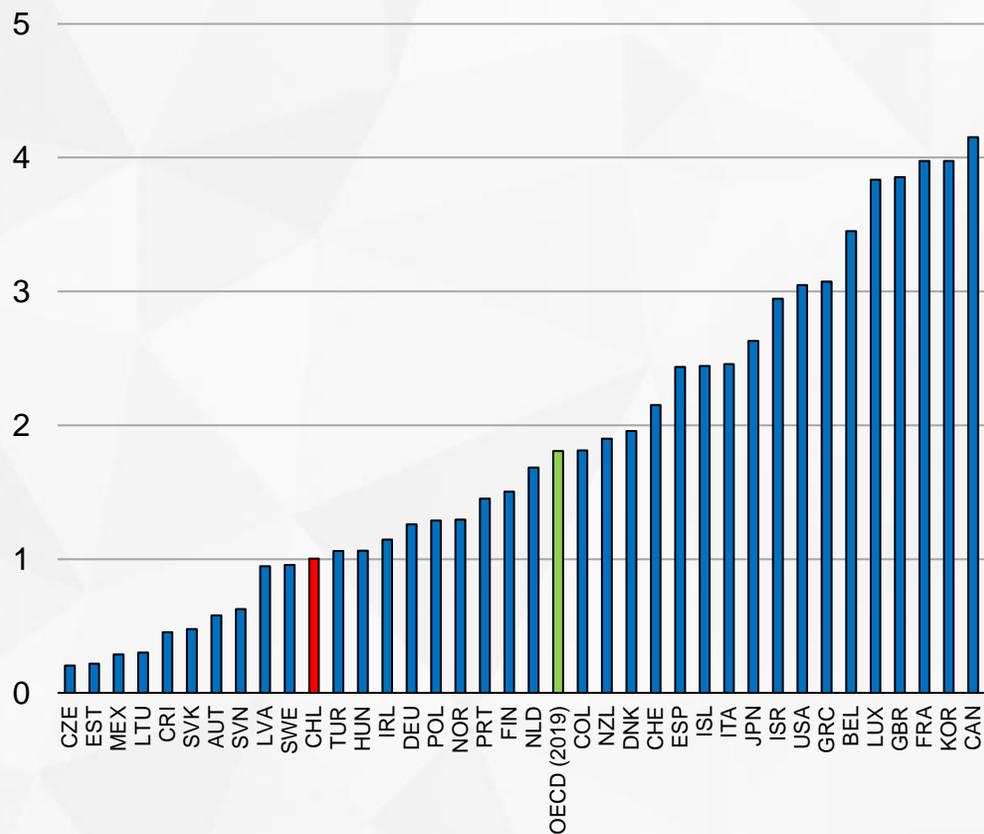


Note: each color accounts for a different OECD country in all years available data. Red mark accounts for latest Chile available data.

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)

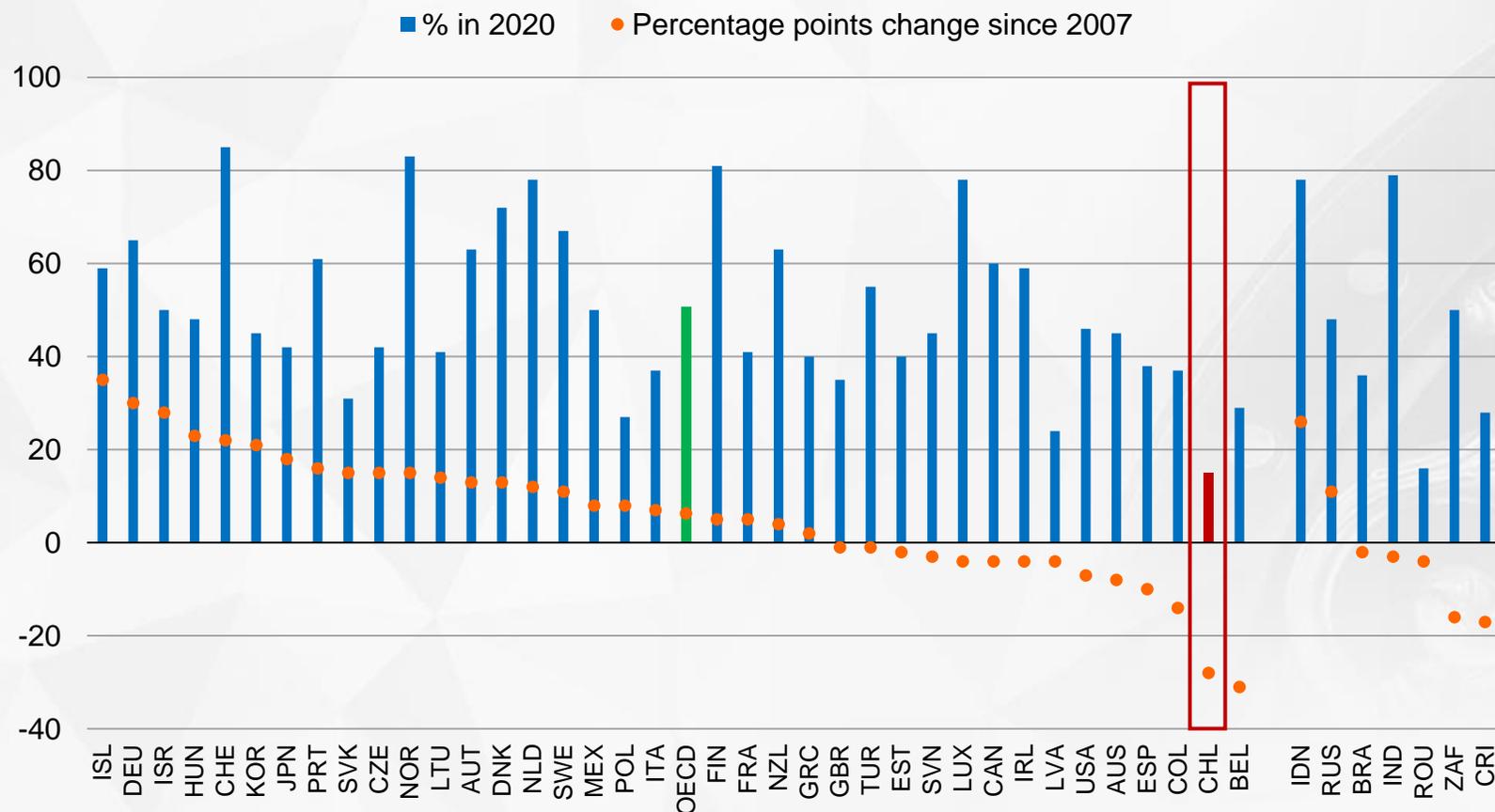
	Year introduced	US\$/ton CO2
Chile	2017	5
Colombia	2017	5
Denmark	1992	26
Finland	1990	65
France	2014	50
Ireland	2010	22
Japan	2012	3
Mexico	2014	1 a 3
Norway	1991	59
Portugal	2015	14
South Africa	2019	10
Sweden	1991	127
Switzerland	2008	96

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

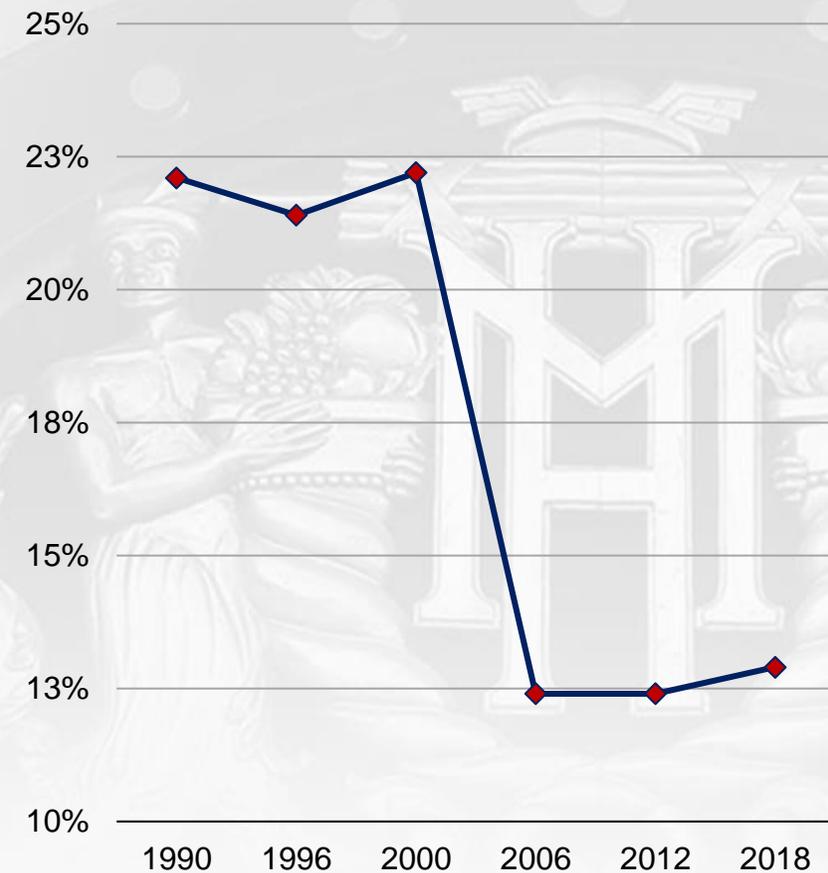
Source: OECD, IMF.

Confidence in government has been falling and stands below OECD countries. The same happens with confidence in other people

Confidence in national government in 2020 and its change since 2007
(percentage points)



Chile: Interpersonal confidence
(percentage of positive answers)

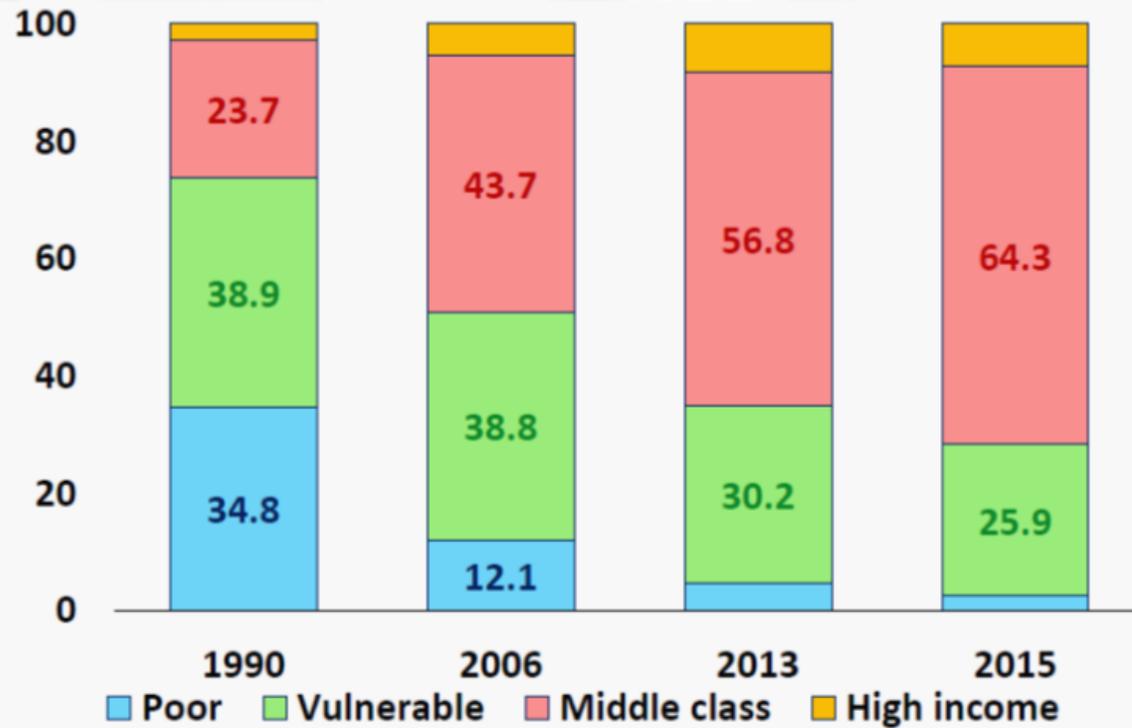


Note: Percentage who answered “yes” to “Do you have confidence in the national government?”

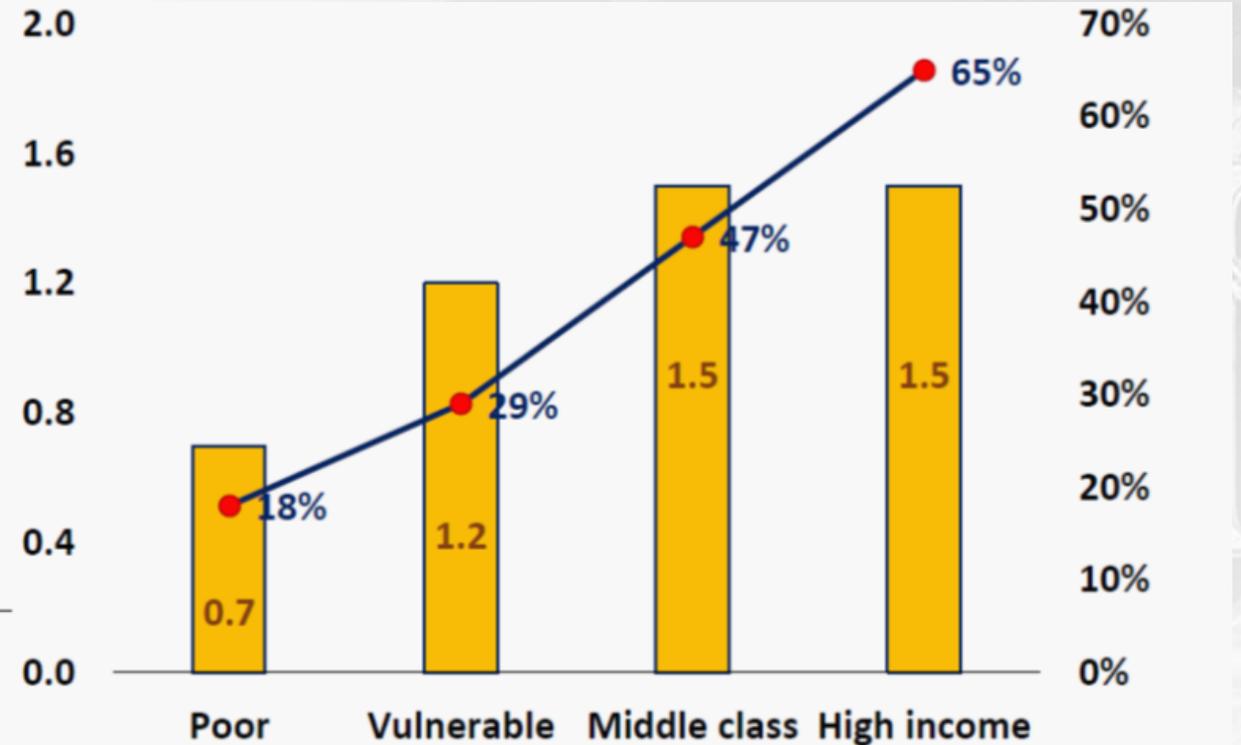
Source: OECD based on World Gallup Poll,

The development of Chile during the last decades has been marked by a significant growth of the middle class

Evolution of the population in Chile according to socioeconomic class, 1990 2015 (*)
(% of total population)



Employed by household and percentage with respect to total household members by socioeconomic class, 2015
(percent)

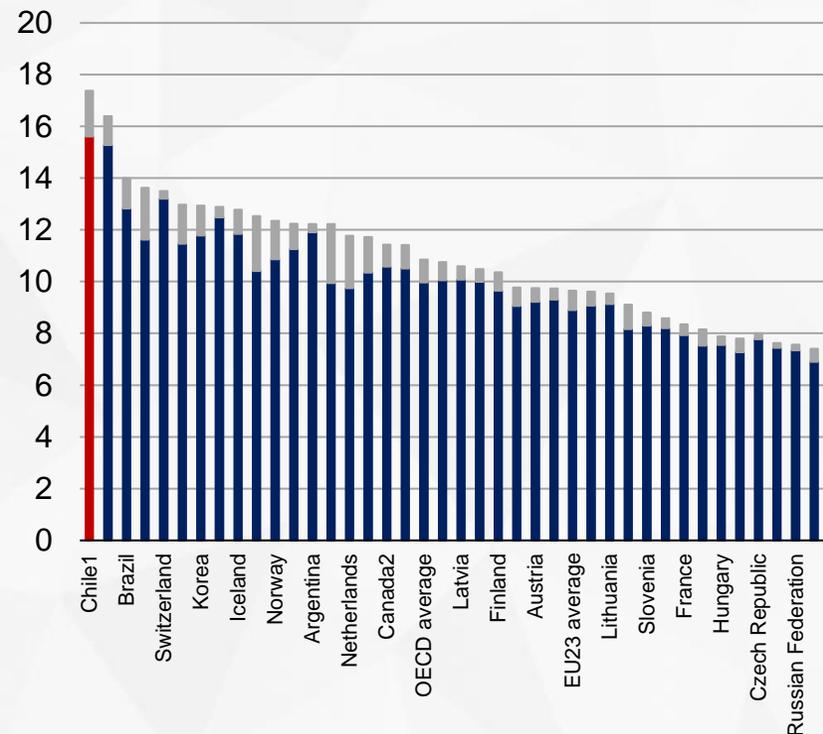


Although education expenditure is high, tests scores remain below other countries

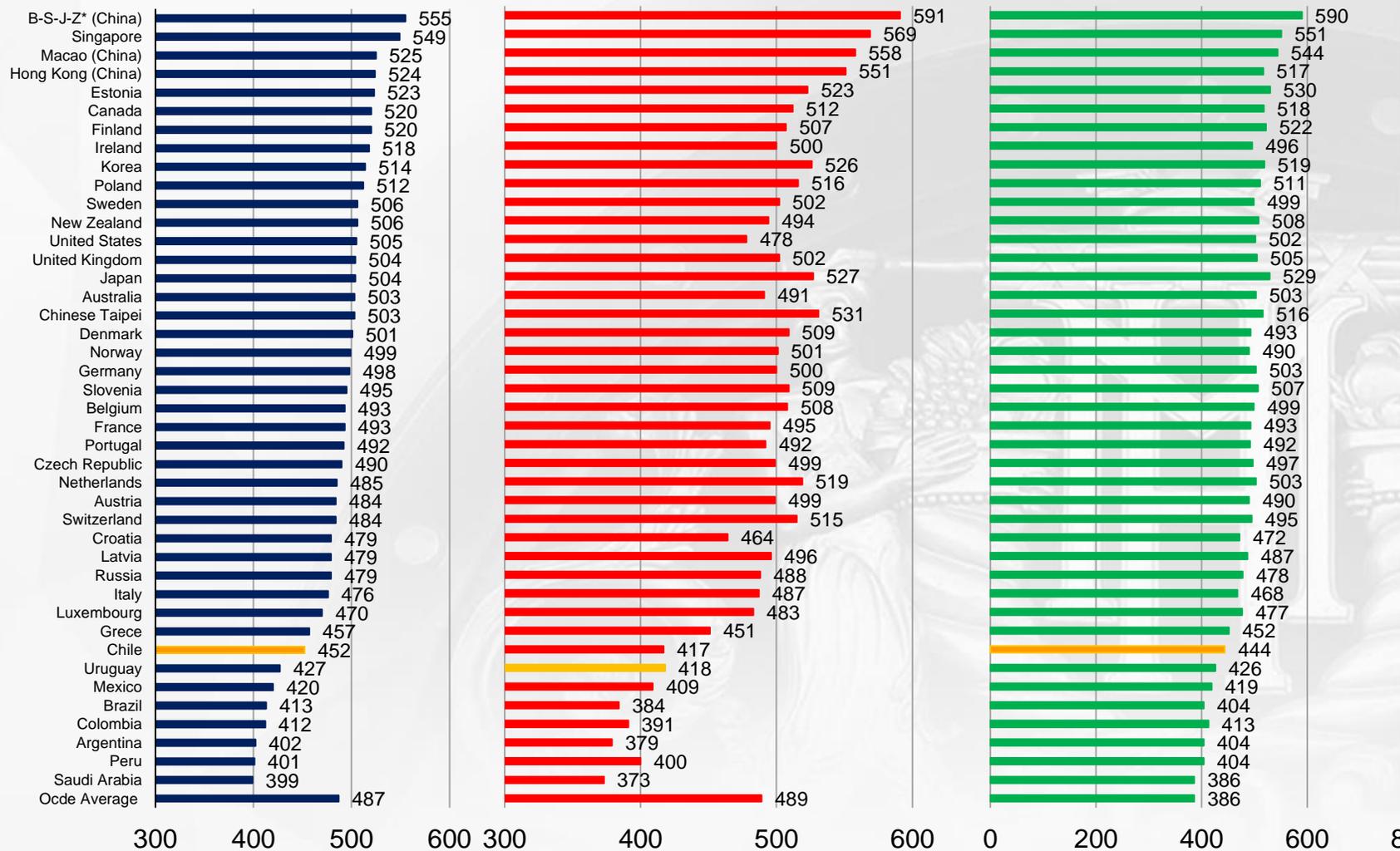
Total public expenditure on education-primary to tertiary education

(as a percentage of total government expenditure, 2016)

■ Public transfers and payments to the non-educational private sector
■ Direct public expenditure on educational institutions



PISA 2018 Results (snapshot of student's performance in reading, mathematics, and science)

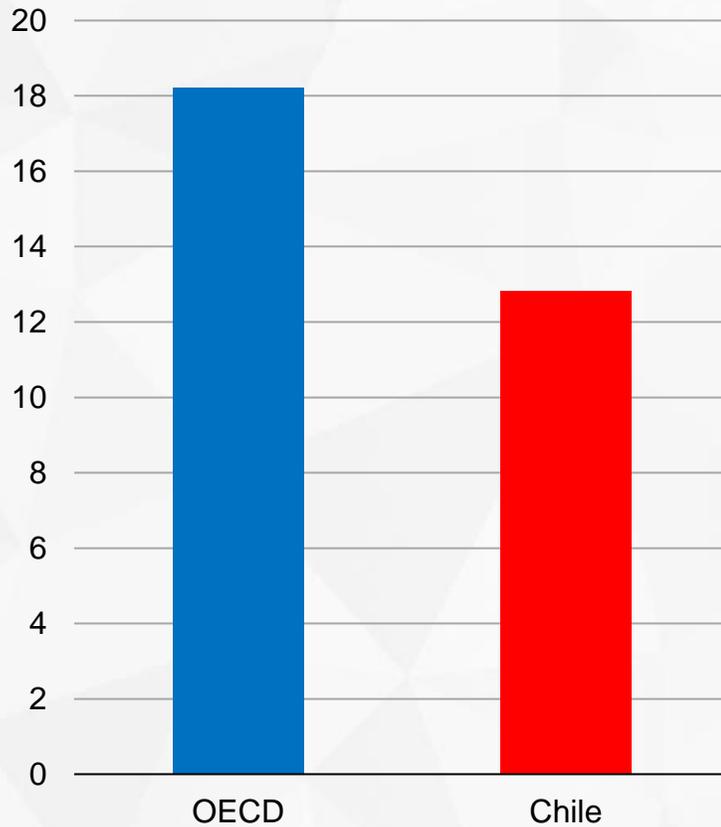


Note: (1) Year of reference 2017. (2) Primary education includes pre-primary programs. Countries are ranked in descending order of total public expenditure on education as a percentage of total government expenditure. Source: OECD/UIS/Eurostat (2019).

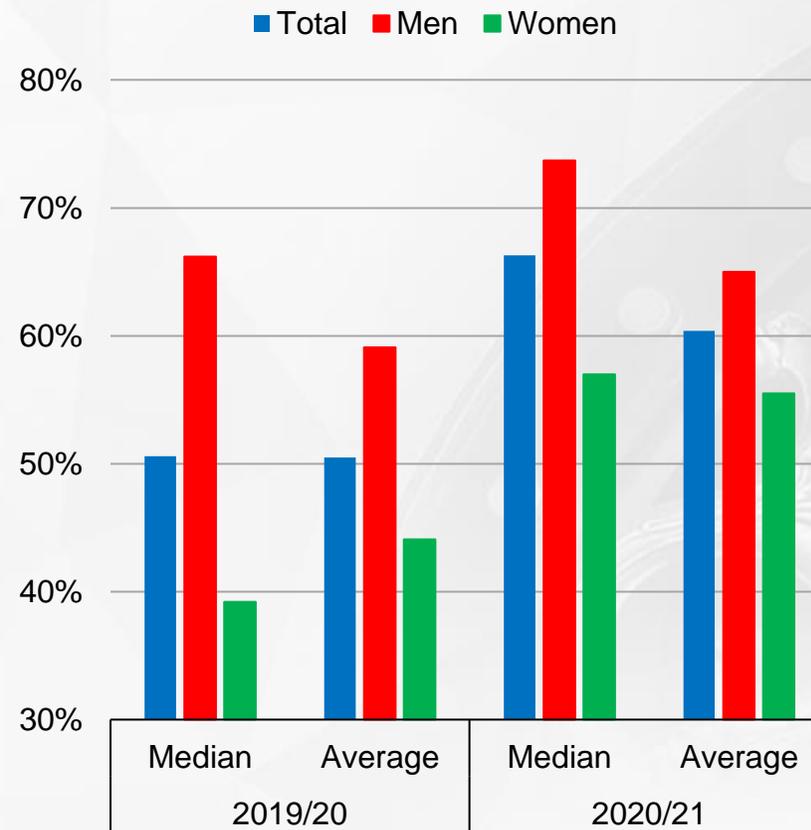
Source: OECD.

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

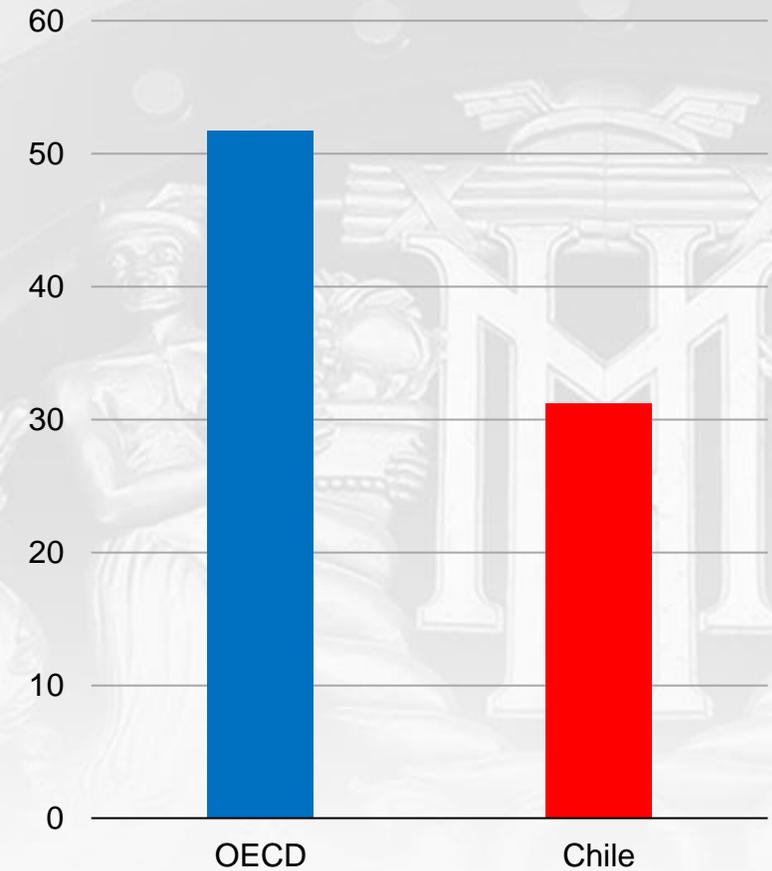
Effective contribution to the pensions system
(% gross income, 2020)



Chile's contribution density
(# months contributed over # months affiliated to the system)



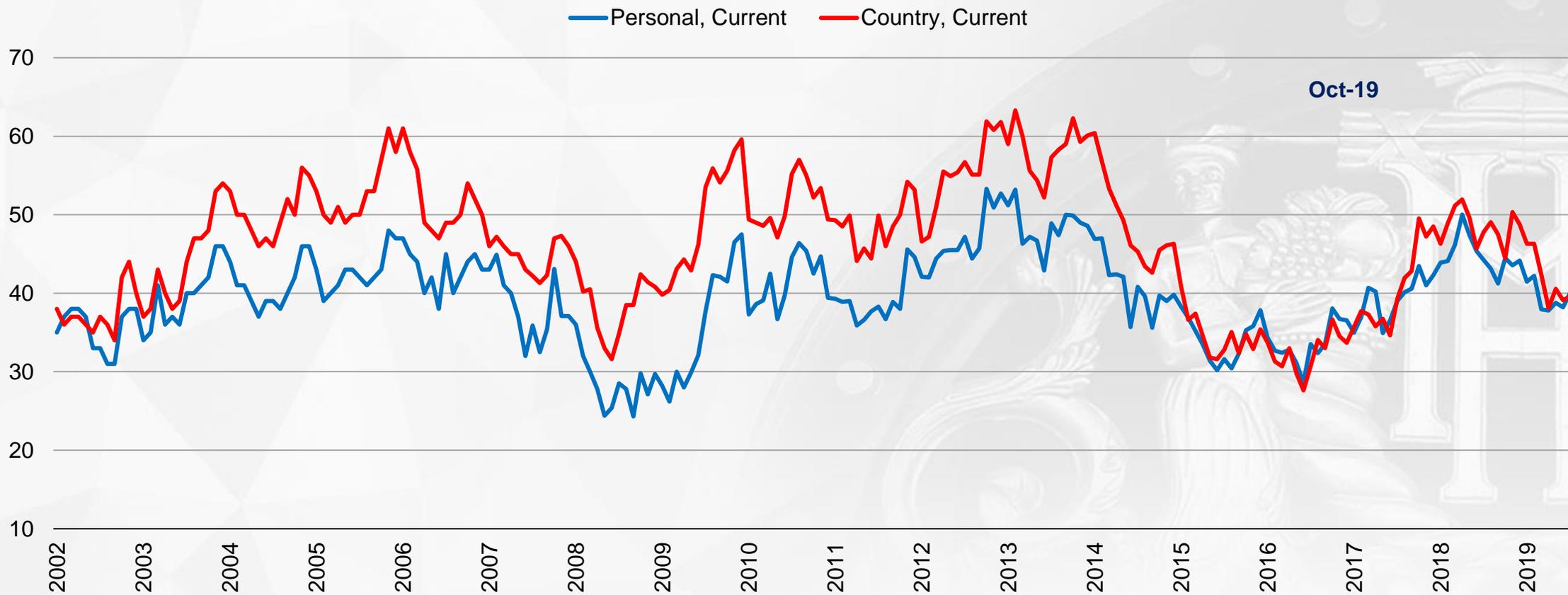
Gross replacement rate
(at retirement age, as of 2020)



Note: In Chile, figures include the disability insurance and fees paid to AFPs.
Source: OECD, IMF.

Early signs of the social unrest: a clear mismatch between the perception of the current personal and country economic situation

Consumer confidence: gap between personal situation and country economic situation
(index, 50 = neutral threshold)



Chile's 2019 social unrest:
how did this happen?

**Response: a new democratic Chilean
Constitution**

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

Number of articles in the Constitution

Current Constitution

143 articles and 50 transitory dispositions

Set 25 LOC subjects (Public declaration of interests and assets authorities, Public Electoral System, Central Bank, Armed Forces, Public Administration, Congress, among others)

Total constitutional articles + articles contained in the LOC referred to in the Constitution: 2410

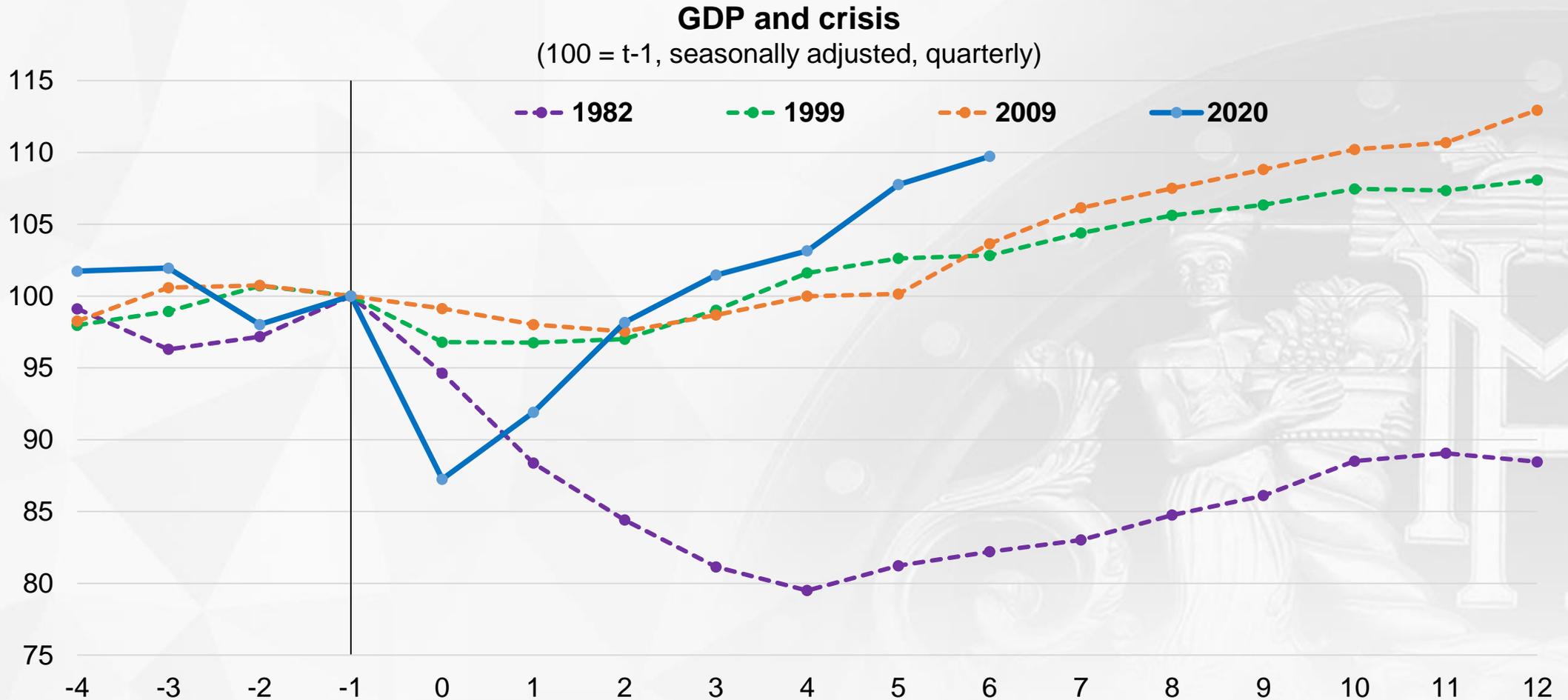
New Constitution proposal

281 arts (until 20-Apr.2022)

No LOC. Some of them have some arts in the new constitution.

The agenda of the new government aims at contributing towards the resolution of both structural and pandemic-related challenges

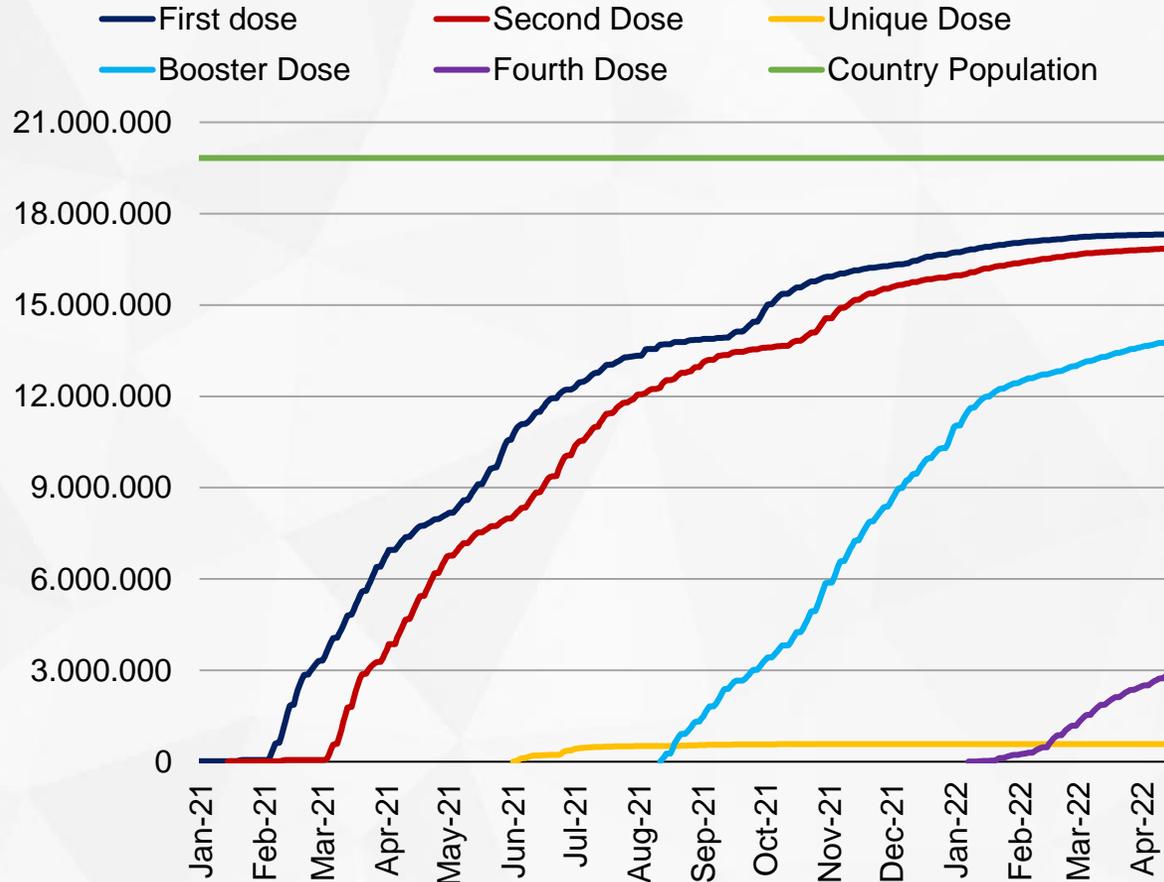
Chile recovered rapidly from the Covid-19 crisis, being the shortest crisis in the last 40 years



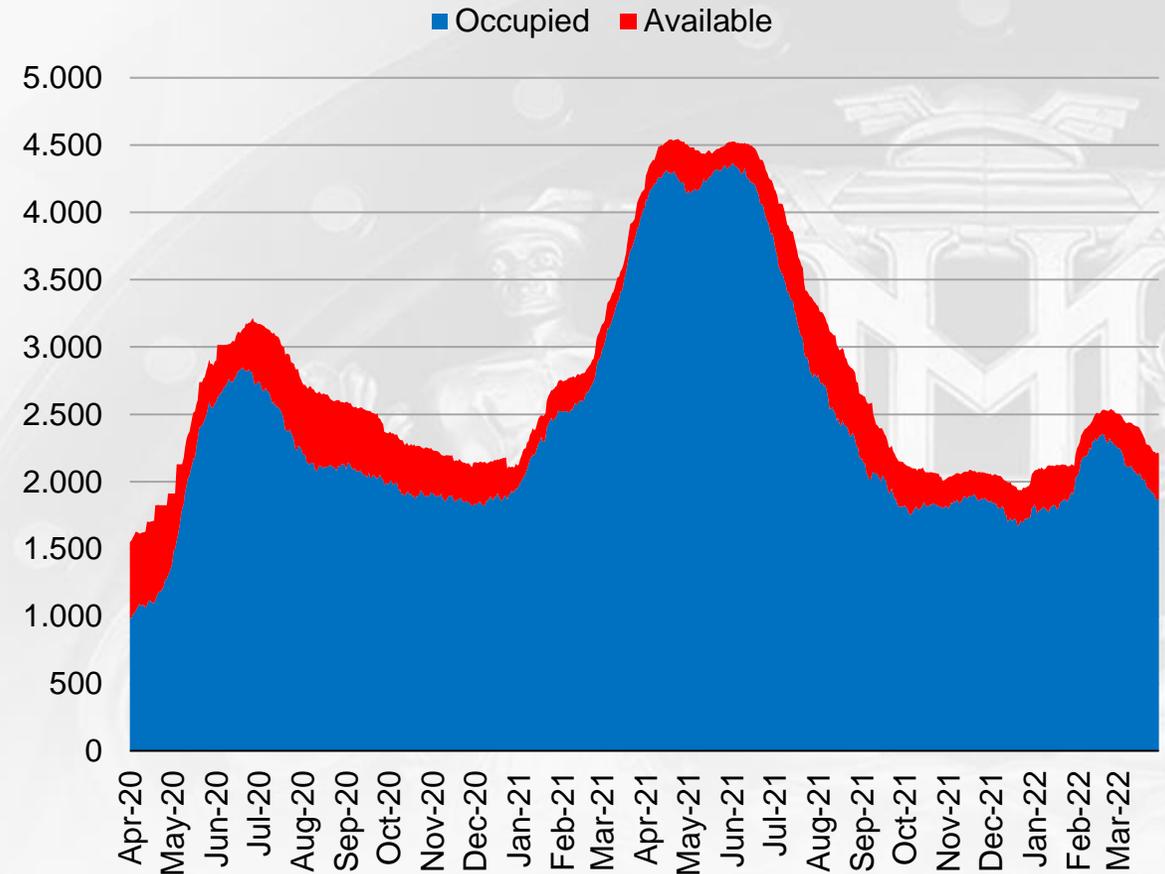
Note: T=0 in periods 1981.Q4, 1998.Q4, 2008.Q4, 2020.Q2 Official seasonally adjusted spliced series for all periods except 1982-83. For that period, the series contained in the volume “Economic and Social Indicators 1960-1988” was seasonally adjusted. **Source:** Central Bank of Chile

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

Chile's Vaccination campaign (# of persons)



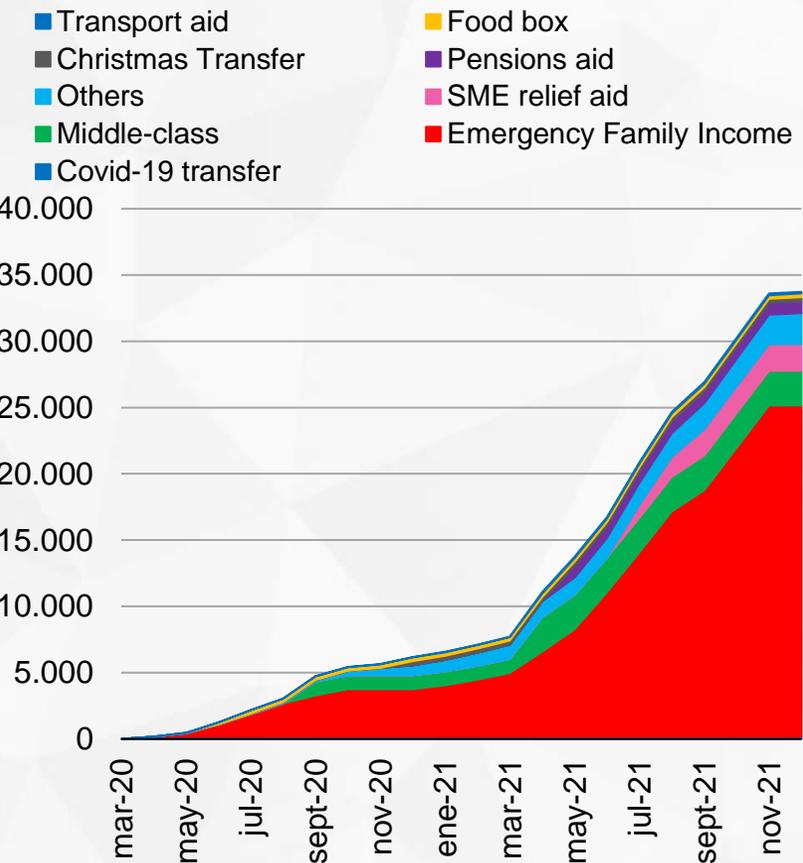
Chile: ICU availability (N° of beds)



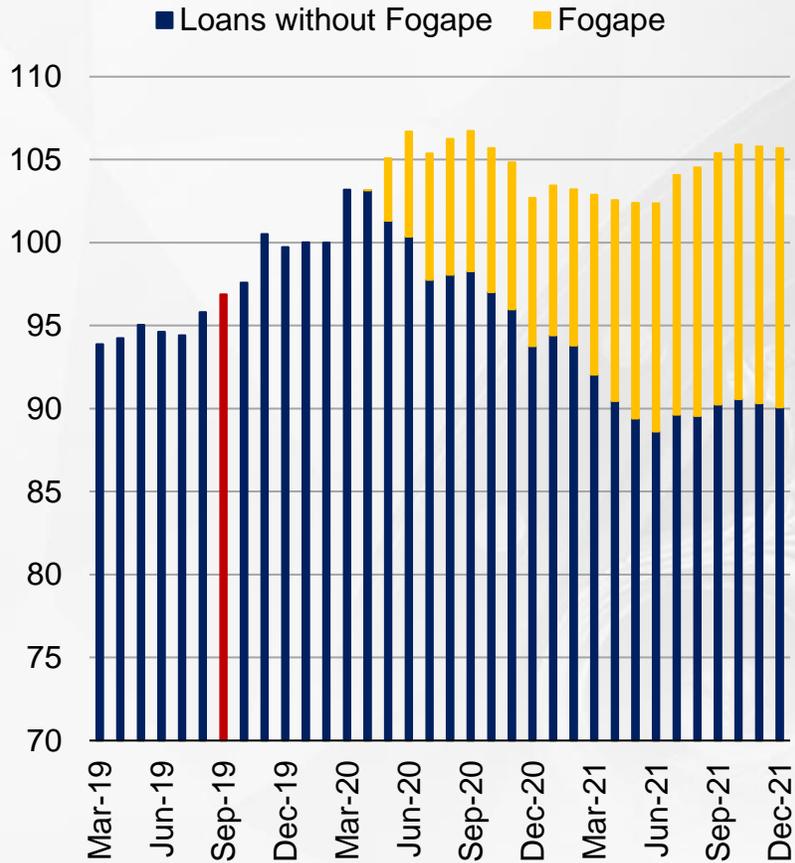
Source: Ministry of Health and Ministry of Science.

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

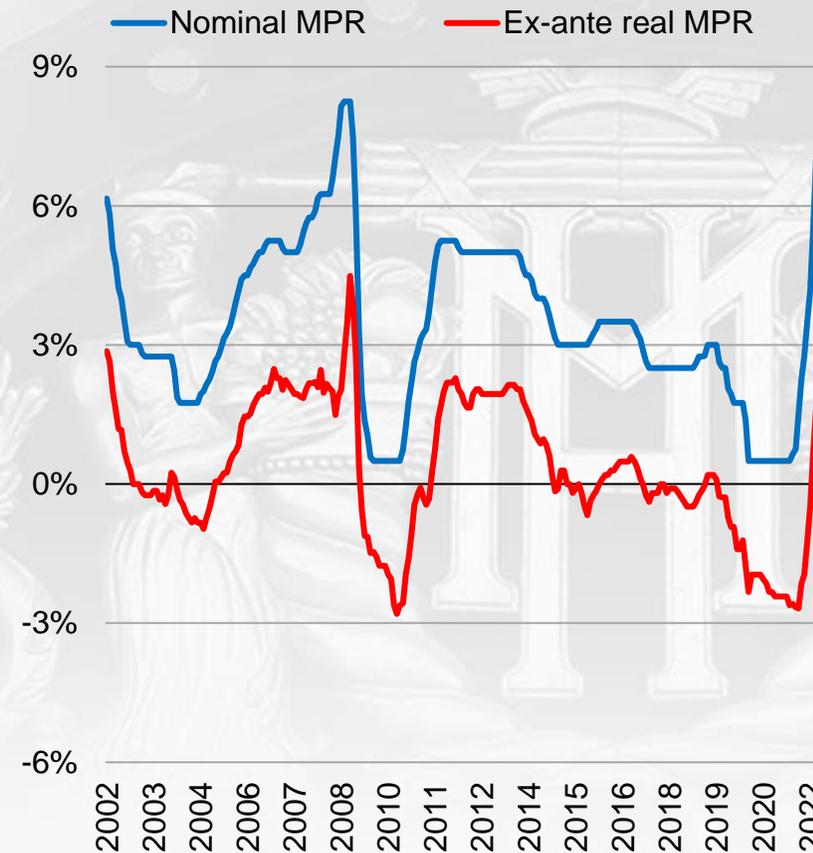
Covid-19 Fiscal Measures (US \$ million)



Real commercial loans balance (Index 100=feb 2020)



Monetary Policy Rate (*) (%)

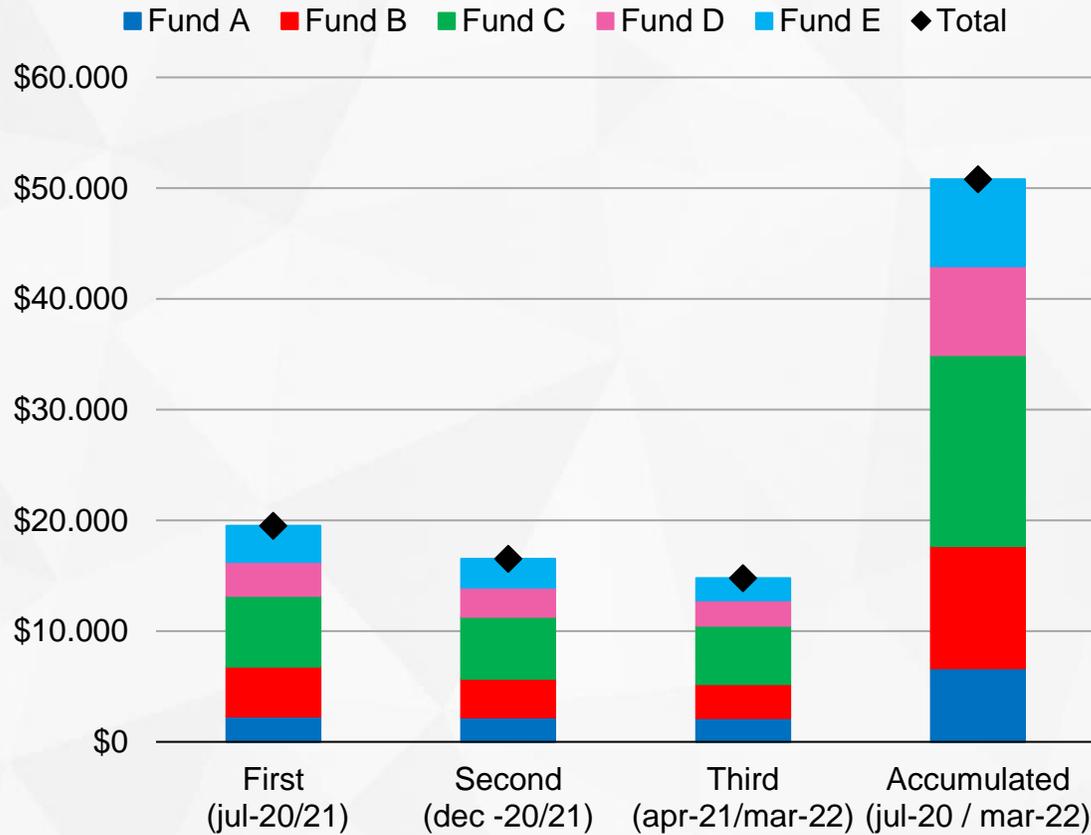


Note: (*) The nominal MPR series shows the average of the month. For March 2022, the nominal MPR is the rate decided in the last Central Bank monetary policy meeting on March 29 (7.00%). Ex-ante measure considers 11-months-ahead inflation expectations from the Economic Expectations Survey (EES).

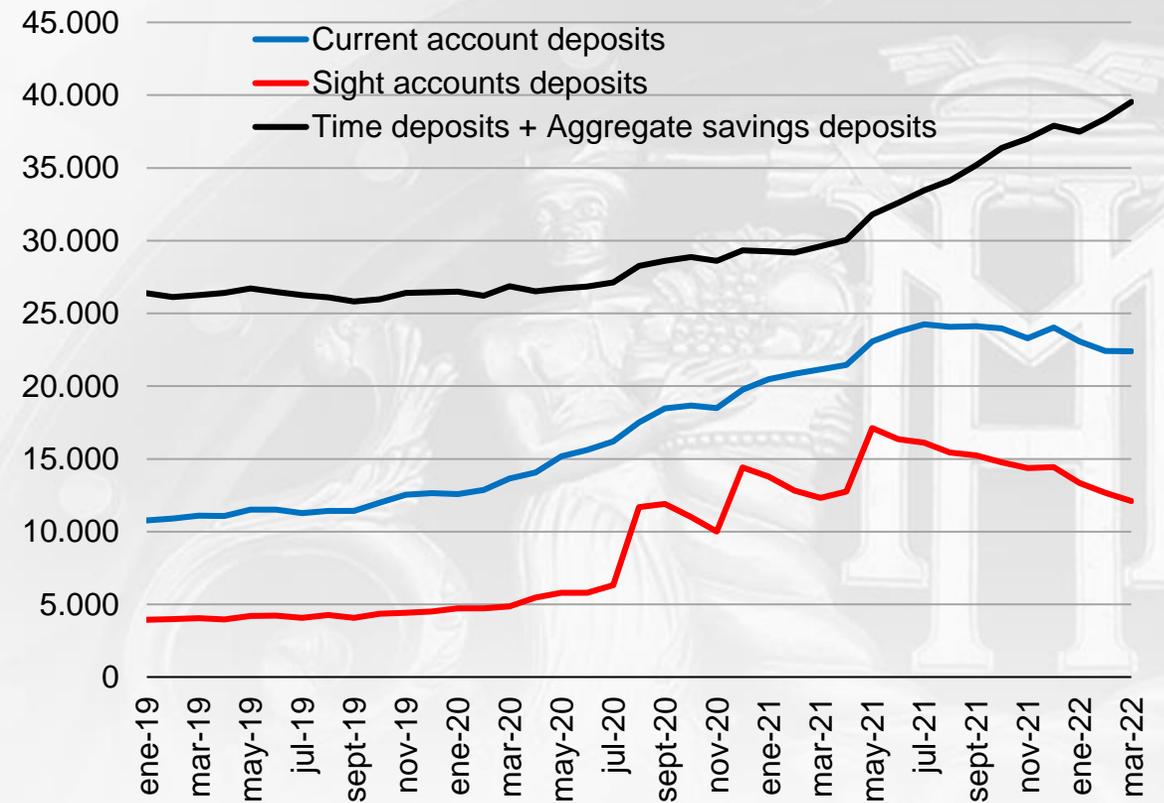
Source: Central Bank of Chile and Ministry of Finance.

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)

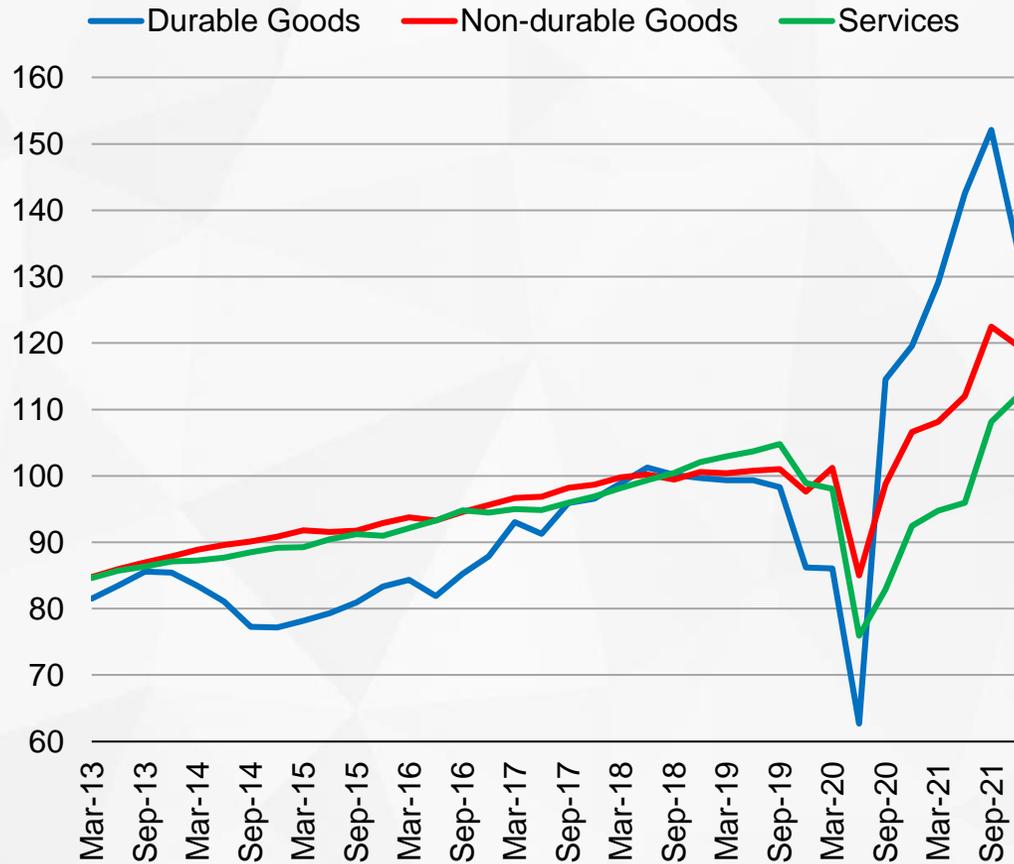


Note: Series in USD are calculated using an exchange rate of \$800 per dolar.

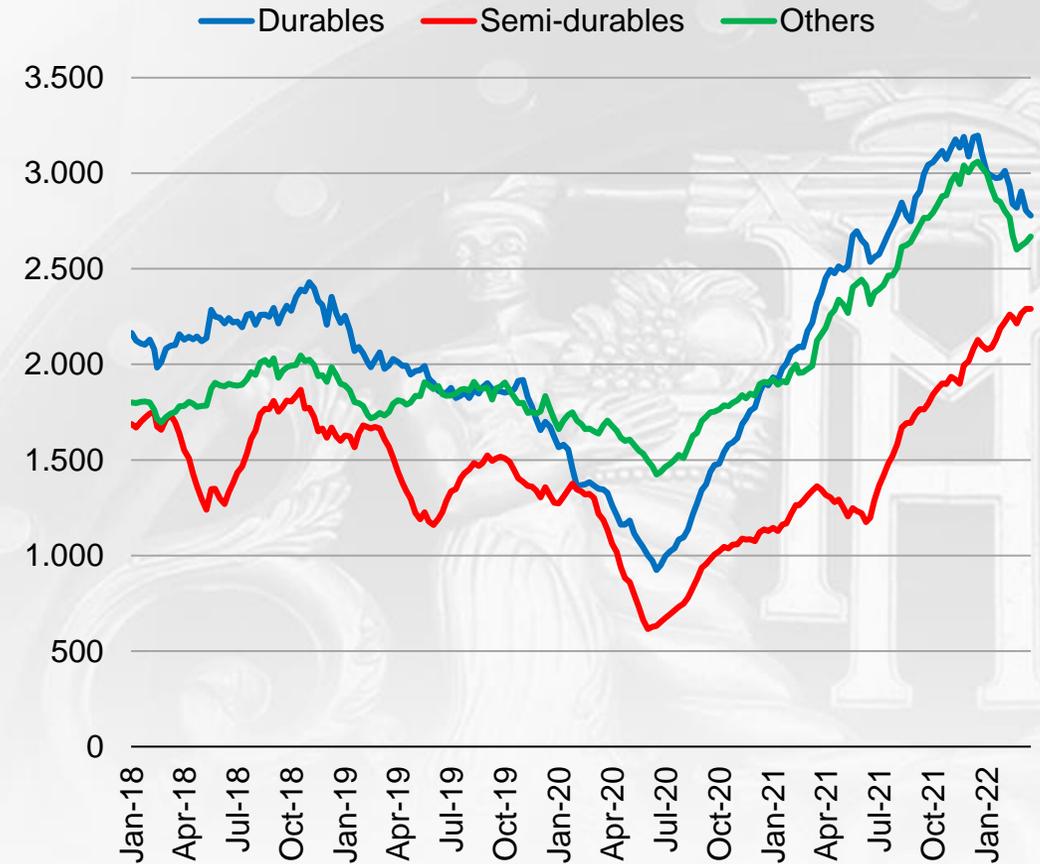
Source: Central Bank of Chile and Chilean Pensions Supervisor (SAFP).

These policies boosted private consumption beyond sustainable levels

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

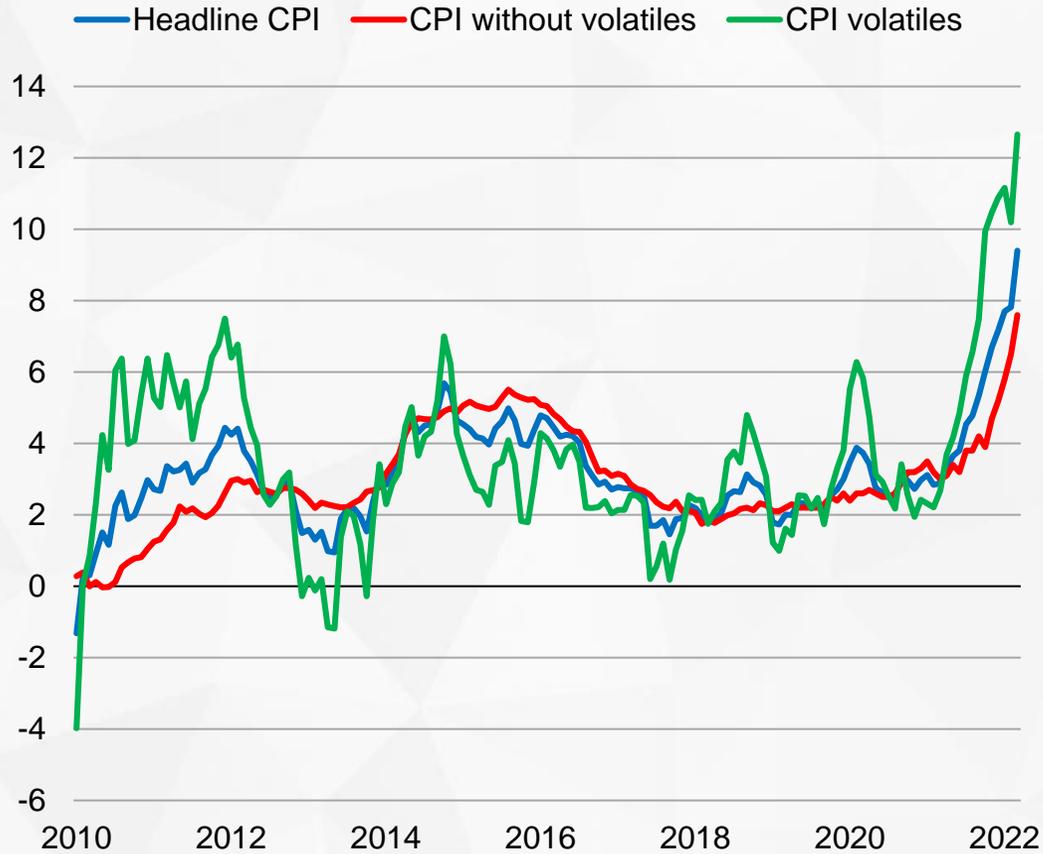


Consumer goods imports
(US\$ million, MA3m)

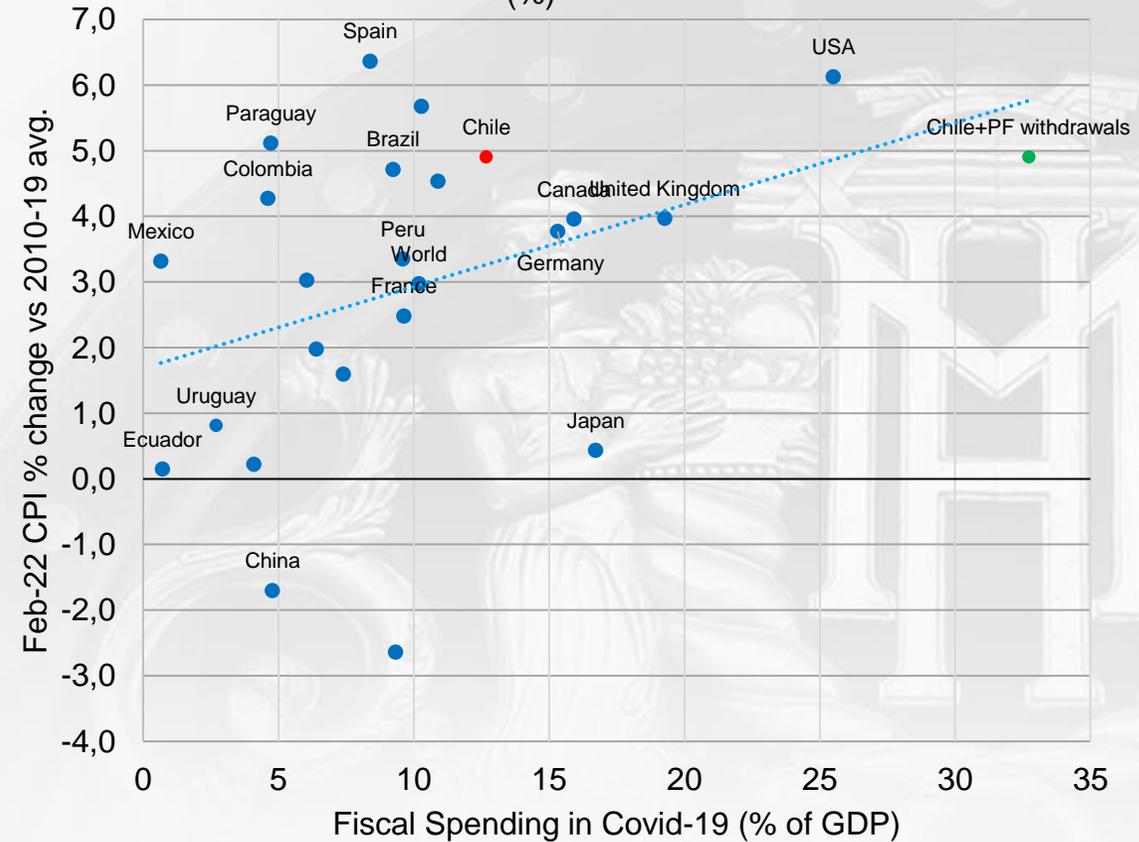


Pushing inflation up alongside supply-side constraints

Inflation
(annual change, %)



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



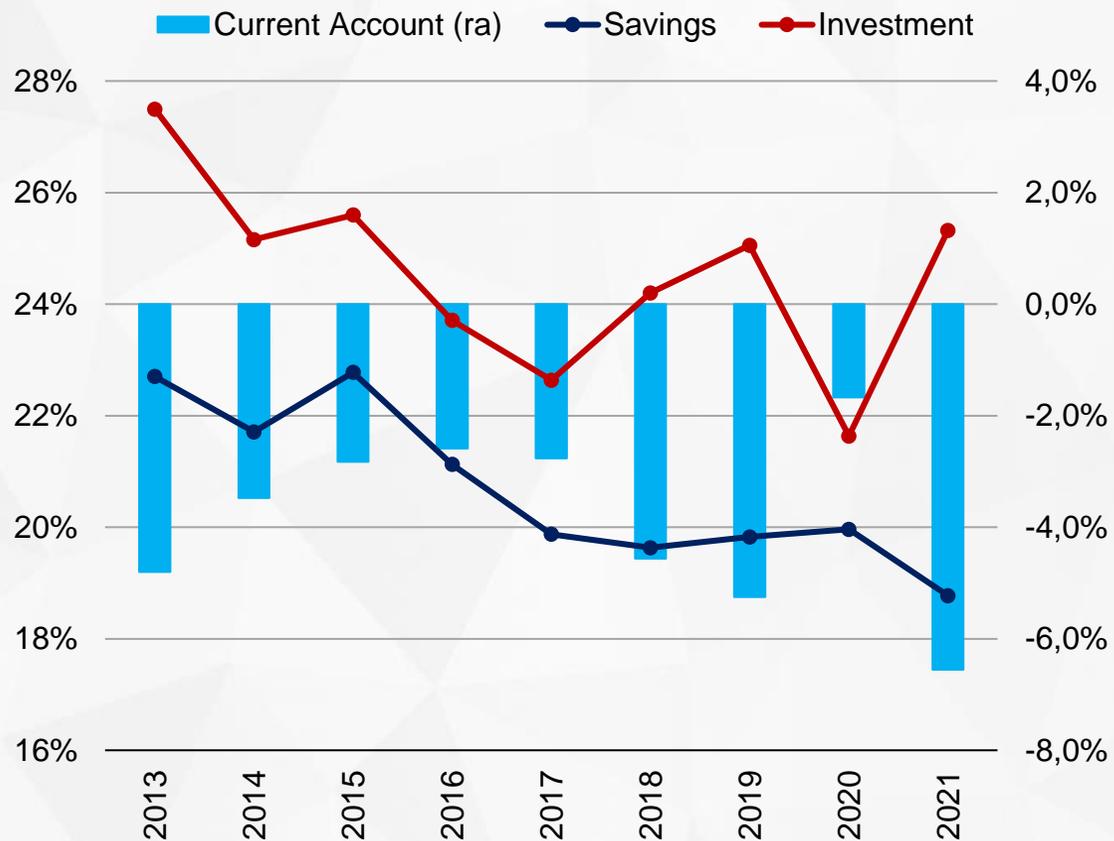
Note: (1) Fiscal above-the-line measures that governments have announced or taken in selected economies in response to the COVID-19 pandemic as of September 27th, 2021. (2) EES: Economic Expectations Survey and FTS: Financial Traders Survey.

Source: Central Bank of Chile, Bloomberg and IMF.

The macroeconomic imbalances that appeared are requiring a rapid reversion of the adopted policies

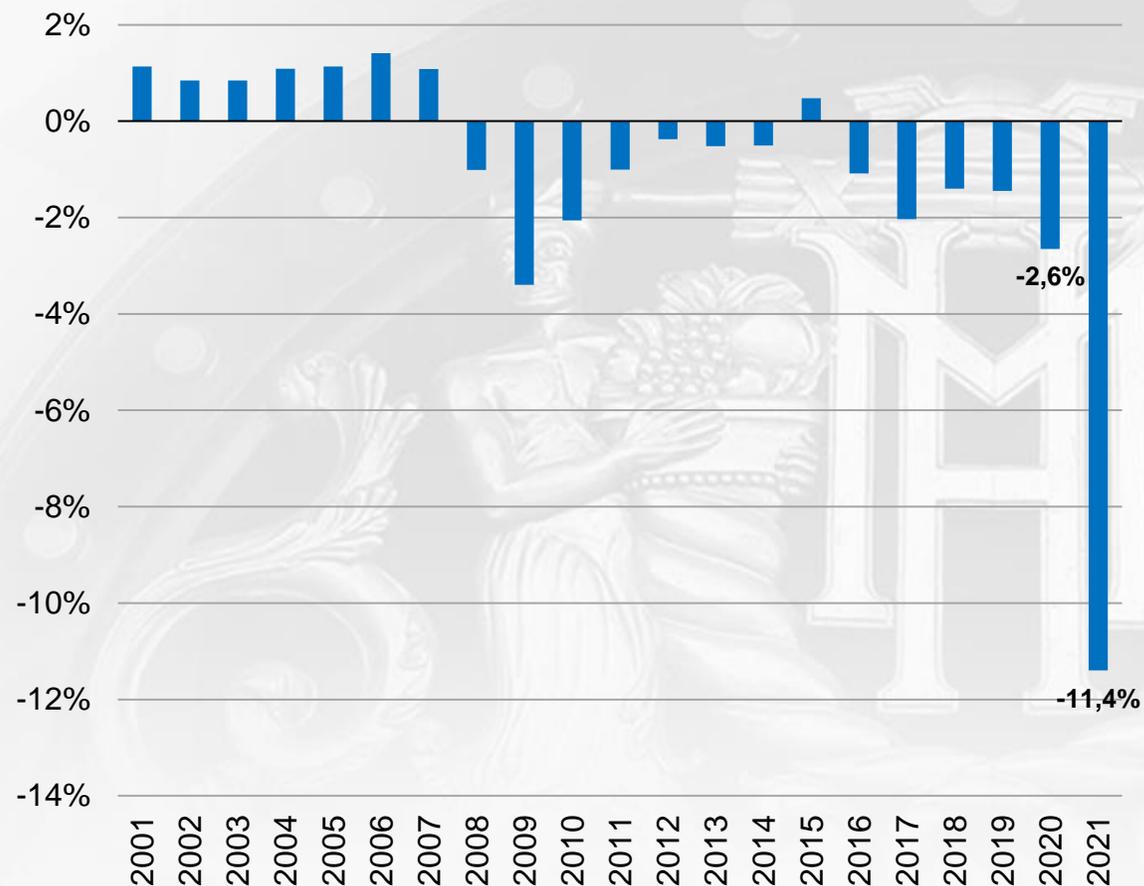
Domestic savings and investment rates

(% GDP)



Central Government Structural Balance (*)

(% GDP)

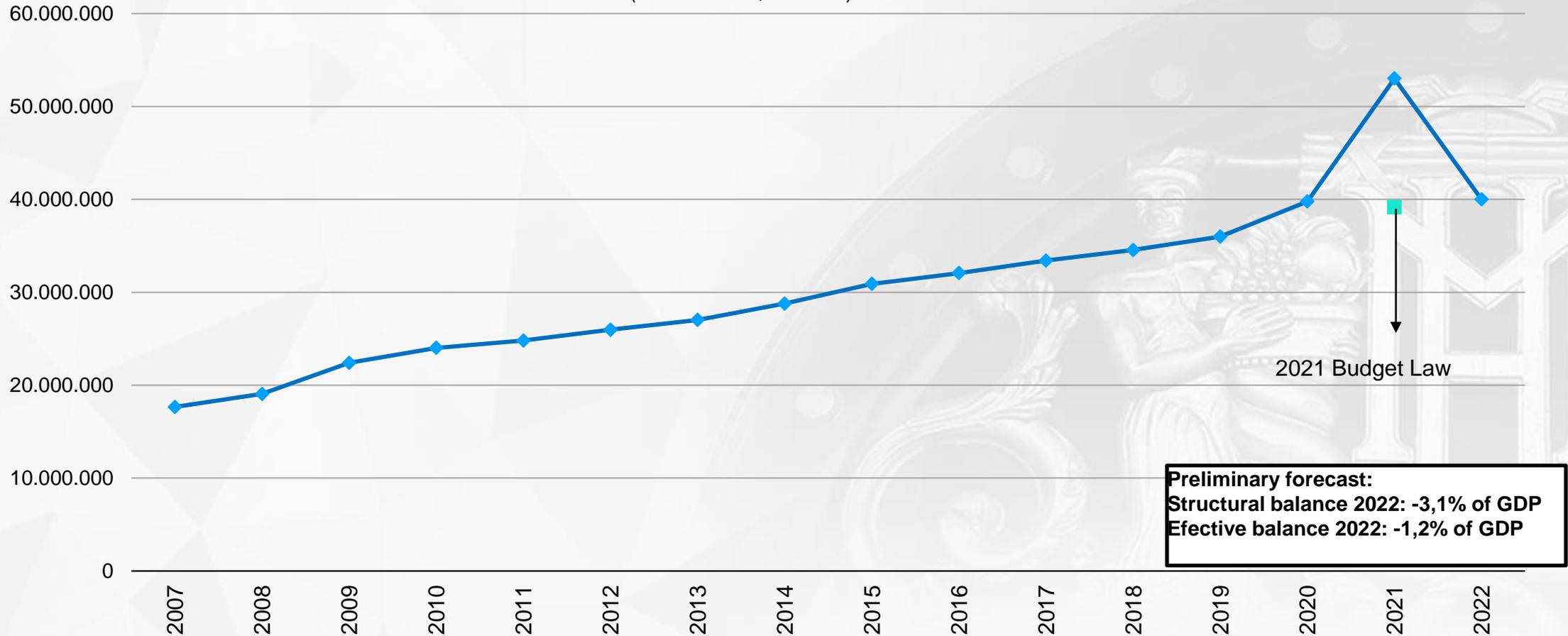


Note: 2021 data is preliminary.

Source: Central Bank of Chile.

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

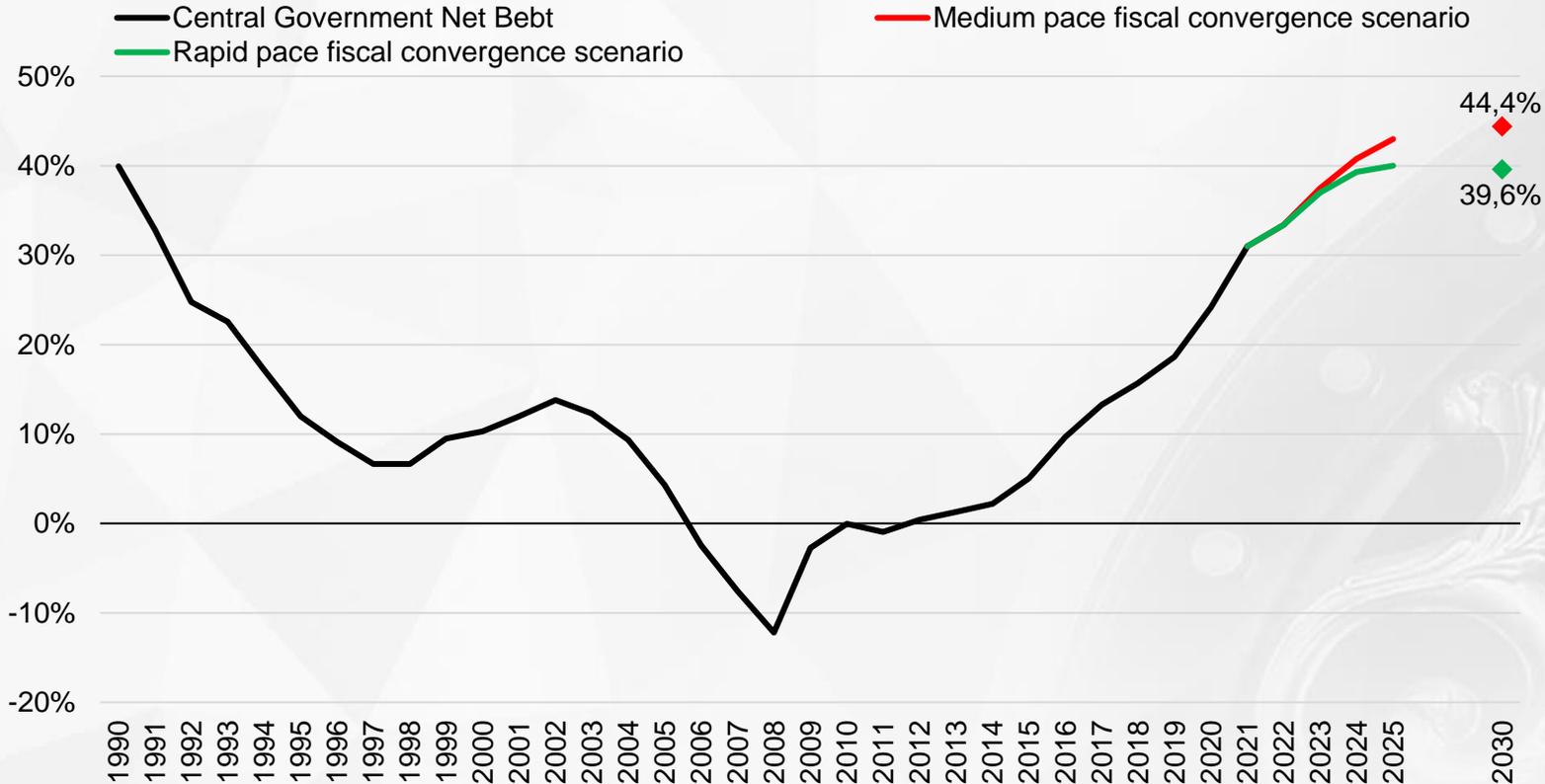
Central Government Expenditure (in 2009 CLP, millions)



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

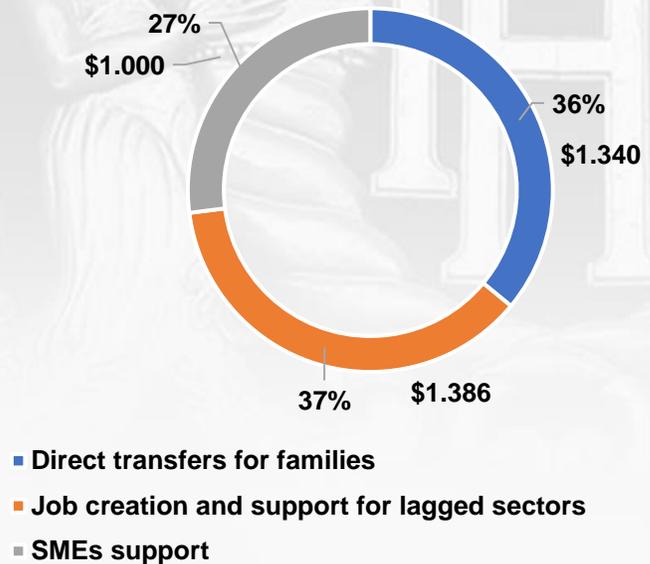


1) Inclusive Recovery Plan: support sectors that may be lagging in the recovery



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

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



Source: <https://www.gob.cl/chileapoya/>.

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

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.

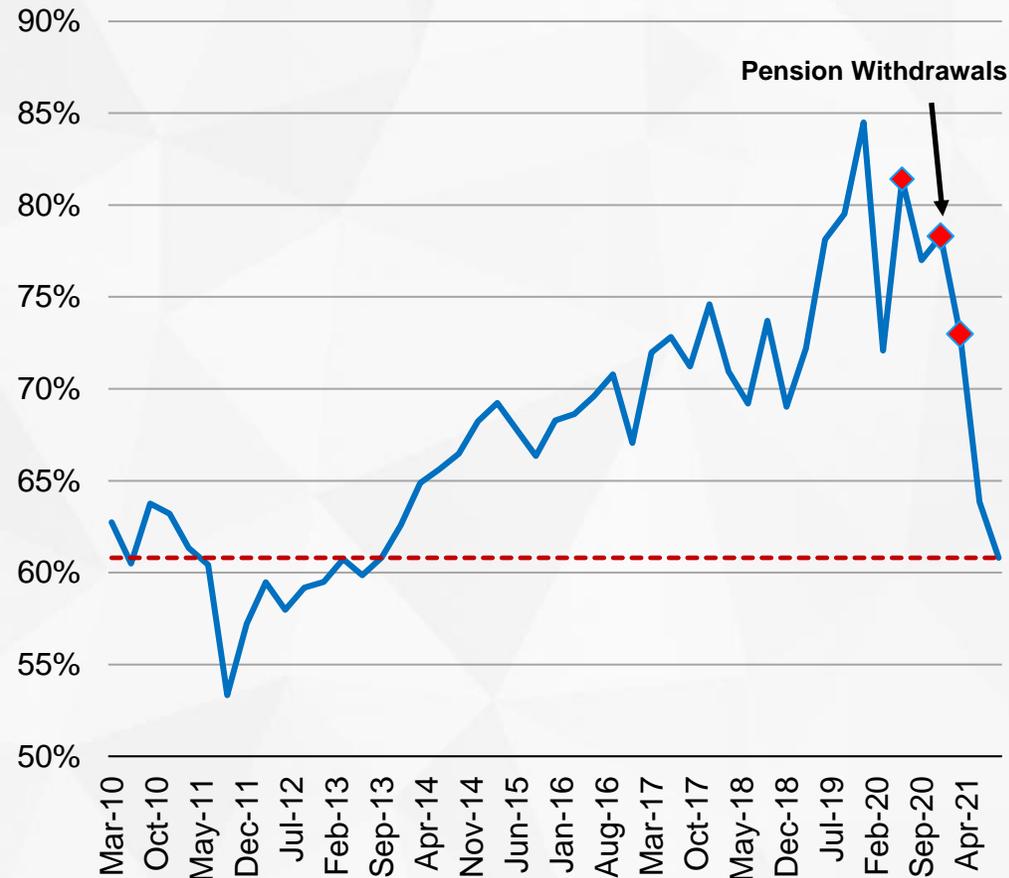
Presenting a proposal by 3Q2022.

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

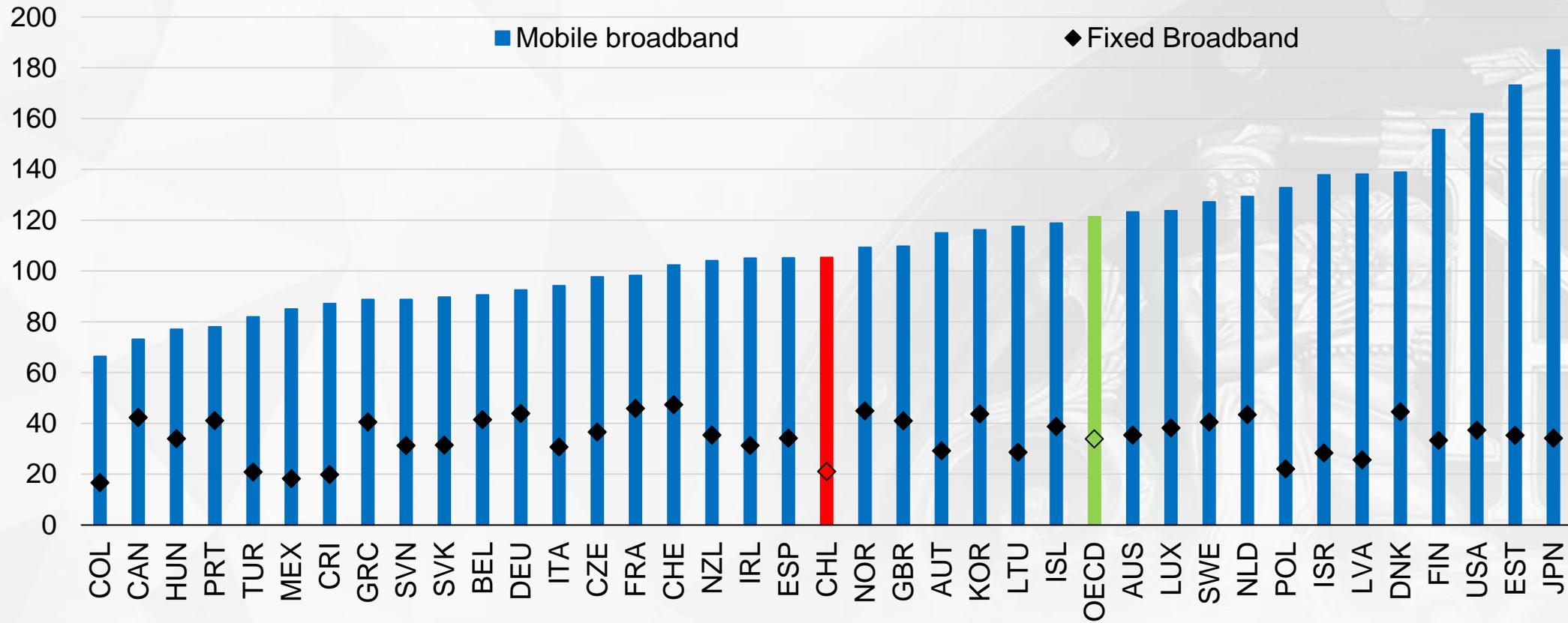
- Financial Innovation Bill. (Fintech)
- Internationalization of the CLP (simplified RUT).
- Resilience of the financial system and its infrastructure. (allow the Central Bank to grant liquidity to non-bank financial players)
- Legislative initiative that establishes a risk-based supervision system for 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).

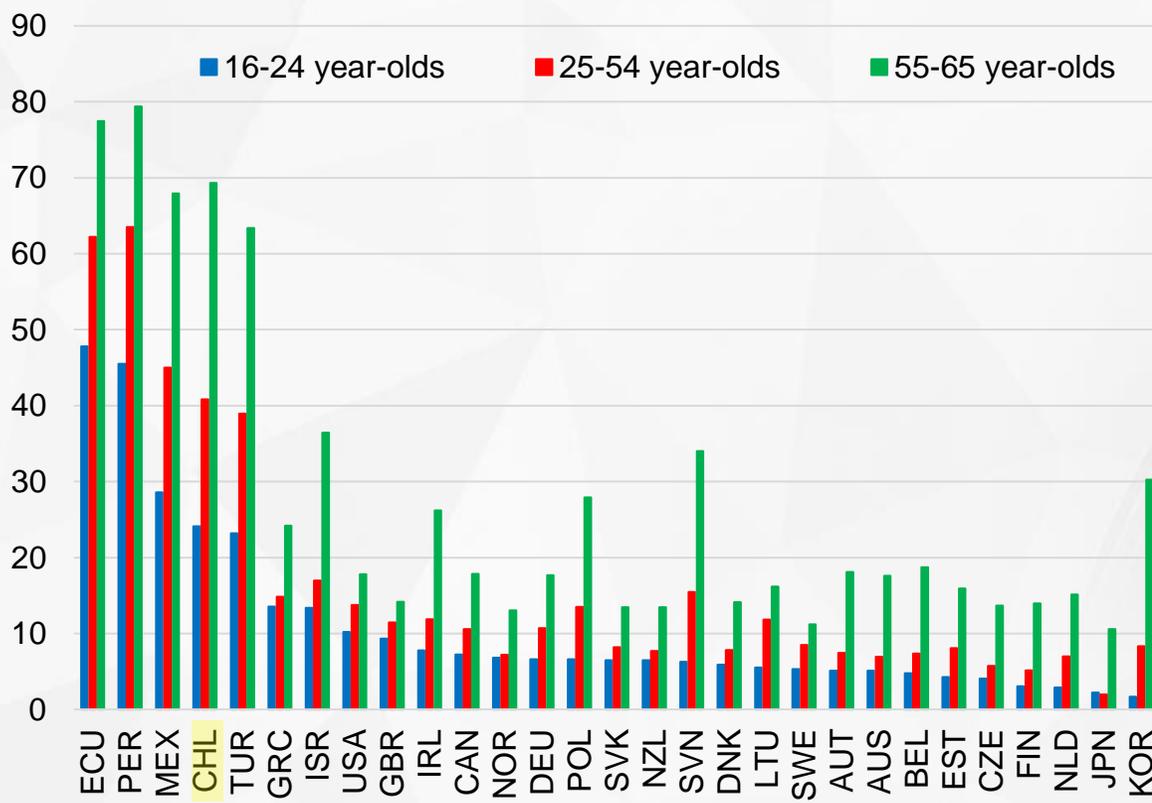
Improve productivity: There're some gaps to close in terms of digital transformation. Chile lags other countries in fixed broadband subscriptions.

Broadband subscriptions
(Subscriptions per 100 inhabitants, June 2021)

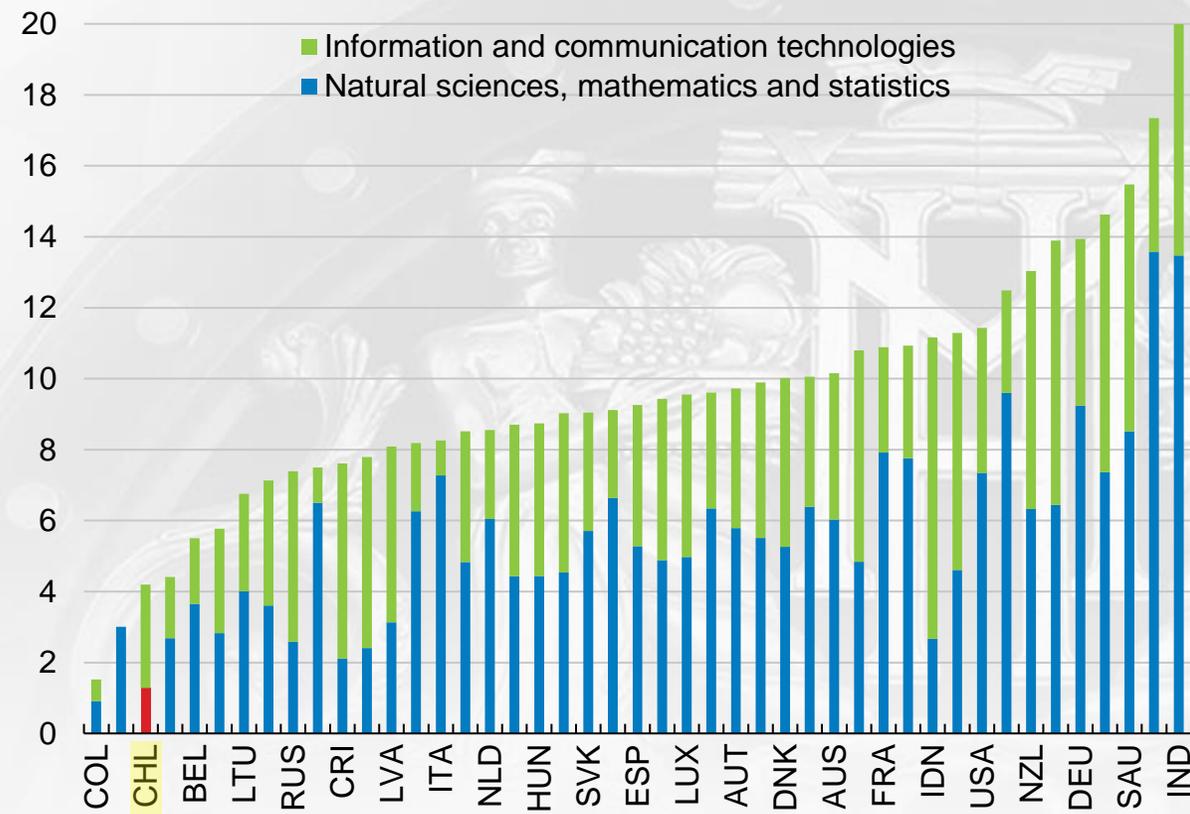


There's room for improvement in digital areas' skills and ICT tertiary-educated workers

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)

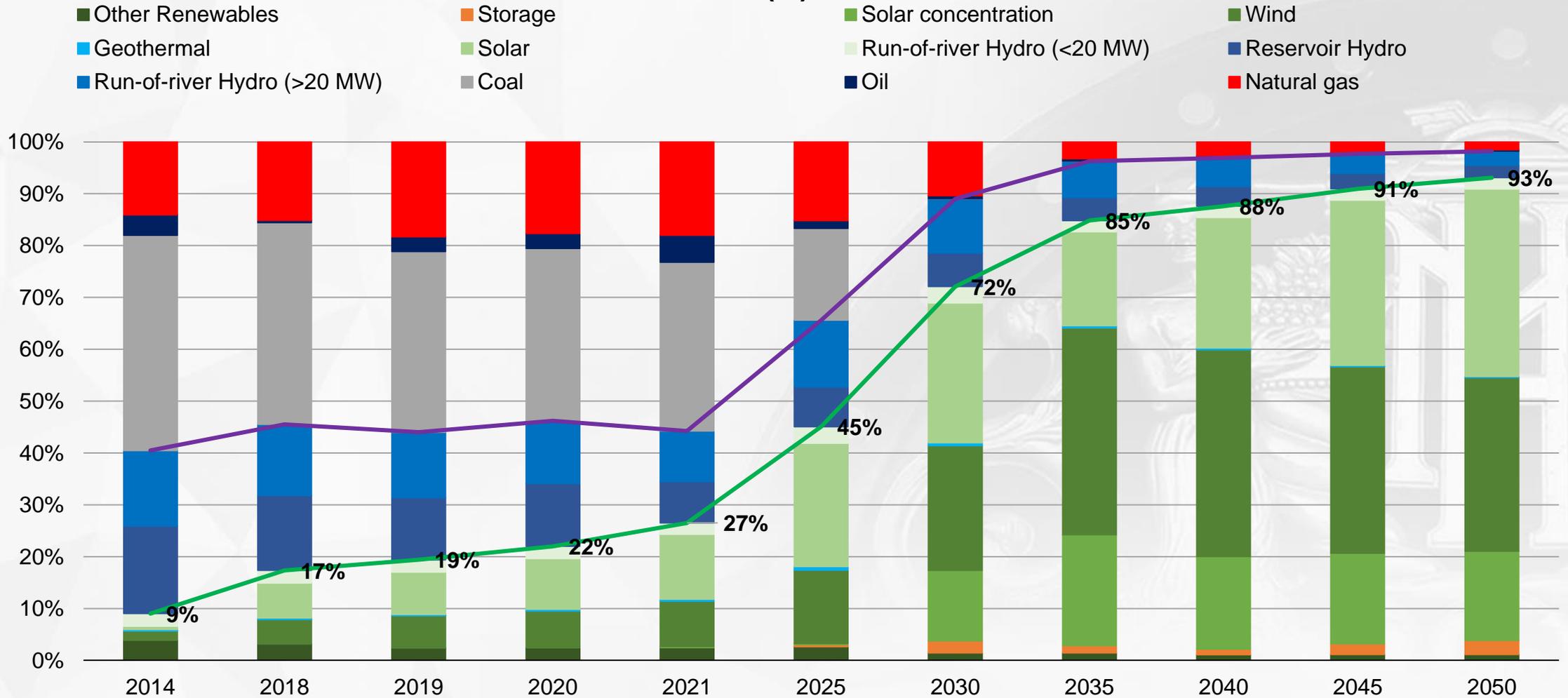


Note: (*) Chile, Greece, Israel, Lithuania, New Zealand, Slovenia and Turkey: Year of reference 2015. Ecuador, Mexico, Peru and United States: Year of reference 2017. All other countries: Year of reference 2012. Data for Belgium refer only to Flanders and data for the United Kingdom refer to England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

Source: OECD.

Green Transition: Transitions to low carbon electricity systems

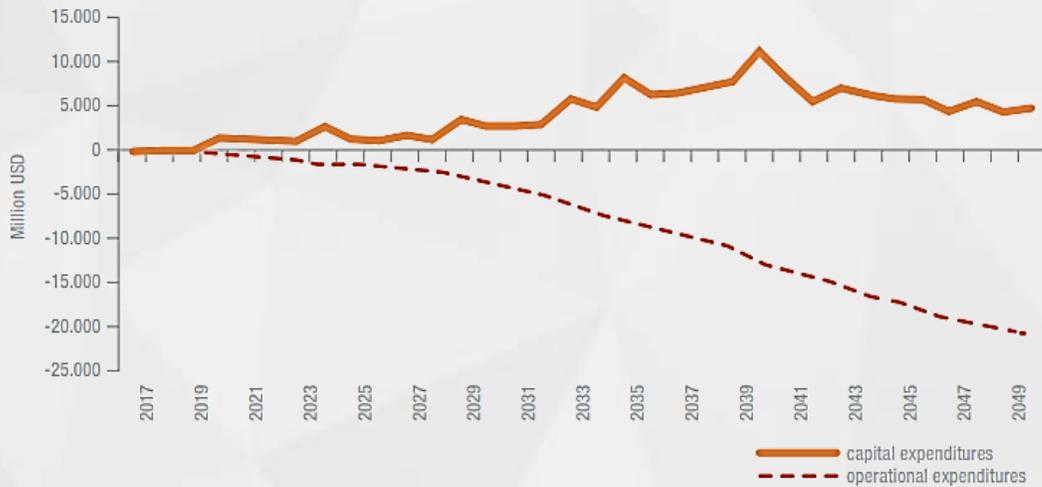
Energy matrix and NCRE participation (%)





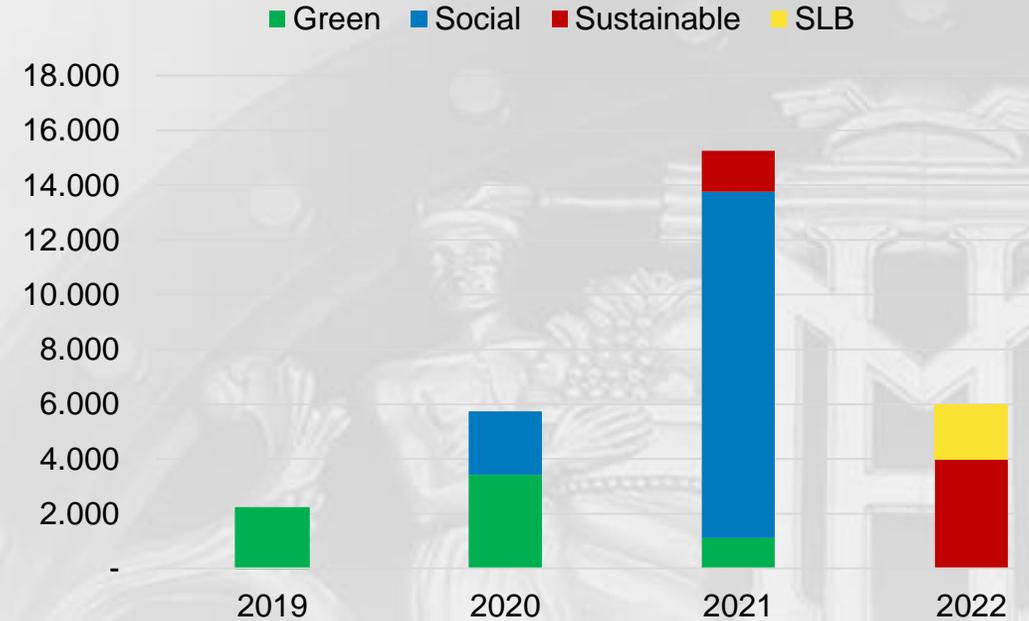
Green Transition: Key role of Green Finance in aligning financial flows towards climate action. Labelled bonds, including green bonds, have broadened Chile's investor base.

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.

Ministerio de Hacienda



CHILE'S SHORT AND LONG-TERM CHALLENGES: AN AMBITIOUS AND REALISTIC AGENDA

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Mario Marcel C. | Minister of Finance