Additional Policies to Support Households & Firms from the COVID-19 Shock

Ministry of Finance, Republic of Chile

April 13th, 2020

The Ministry of Finance announced an Economic Emergency Plan in mid-March of ~USD12 billion (4.8% of GDP) that is designed to ensure the availability of fiscal resources for the public health sector, protect incomes and jobs, and inject liquidity into the real economy.

On April 8th, additional complementary policy measures were announced for up to USD5 billion (2% of GDP), with the objective of supporting economic activity and protect incomes. This memo briefly summarizes these measures, their fiscal cost, and sources of financing.

I. Economic Emergency Plan: Phase I

The Economic Emergency Plan is a fiscal package announced in mid-March that amounts to ~USD12 billion (4.8% of GDP) with measures across three broad dimensions: boosting availability of fiscal resources for public health, measures that protect jobs and support incomes, and transitory policy measures that free-up working capital to the private sector.

Practically all of the Plan's measures are already being implemented. Policies that required legislation such as the transitory suspension of jobs, the capitalization of Banco Estado, the cash transfer for the most vulnerable, and the transitory reduction of the Stamp & Seals Tax, were enacted and are already in force. Separately, tax measures that required administrative adjustments have also been implemented by the Ministry of Finance and the tax authority. Accelerated payments to invoices related to public procurement contracts were initiated this month.

II. Phase II: Additional Policy Measures

On April 8th, the Government of Chile announced additional complementary measures totaling fiscal resources of up to USD5 billion (2% of GDP) with the objective of protecting economic activity and incomes.

The overall economic impact of these measures stretches far beyond the announced fiscal resources as a large share of these resources is intended to mobilize additional capital to the private sector across the economy.

Plan to Protect Economic Activity

In order to ensure that the credit channel continues to operate effectively, this plan considers an injection of up to USD3 billion to the *Fondo de Garantía para Pequeños Empresarios* (FOGAPE), a state credit-guarantee facility available to the banking sector and managed by

Banco Estado. This policy has the objective of injecting liquidity to firms, both small and large, to cover their working capital needs with access to private capital at a reasonable cost, as these new loans will be guaranteed by the State. The capitalization of FOGAPE of up to USD3 billion is expected to provide the private sector with access to loans with credit guarantees of up to USD24 billion, roughly 10% of GDP.

To enhance the scale and scope of this policy, the universe of firms that are eligible to obtain credit guarantees via FOGAPE is to be increased significantly. The current annual sales threshold of ~USD12 million is to be temporarily increased to ~USD34 million. In doing so, new credit will be mobilized to 99,8% of all firms and 84% of the economy's formal workers.

Moreover, FOGAPE will also increase limits on guaranteed loans and maximum coverage.

Table 1: Guaranteed Loan Limits and Maximum Coverage per Annual Sales Threshold

Annual Sales (UF)	Guaranteed Loan Limit (UF)		Maximum Coverage	
	Current	**New**	Current	**New**
< 25,000	5,000	**6,500**	80%	**85%**
25,000 - 100,000	15,000	**25,000**	50%	**80%**
100,000 - 600,000*	50,000	**150,000**	30%	**70%**
600,000 - 1,000,000	-	**250,000**	-	**60%**

Source: Ministry of Finance.
*Legislation approved in January, 2020 created a new transitory threshold for firms with annual sales between 100,000-350,000; current guaranteed loan limits and maximum coverage in Table 1 refer to this transitory range.

FOGAPE's capitalization and the adjustments described above require legislation, with discussion to begin in the Senate on Monday April 13th, 2020.

In order to enhance the effectiveness of this policy measure, all banks have agreed to provide eligible firms access to new loans capped at three-month average sales (10/2018-10/2019) at a maximum nominal interest rate equal to 3% plus the monetary policy rate (currently at 0.5%), that is, equivalent to a real interest rate of approximately 0%. These loans will have a 6-month grace period and shall be paid in quotas between a 24/48-month period. Banks have also agreed to defer payments on installments of outstanding loans for at least 6 months.

This policy has been coordinated with the Central Bank of Chile (CBC) and the Financial Markets Commission (CMF) to ensure the maximum impact and availability of credit and working capital to firms.

Plan to Protect Incomes

The Ministry of Finance will set up a fund of up to USD2 billion (0.8% of GDP) to finance policies that protect the incomes of the most vulnerable, expected to benefit up to 3 million people. Use of the fund's resources is expected to be flexible, allowing for a timely and tailored response by the Government to the evolving COVID-19 shock.

Other Measures

The Ministry of Finance will send a bill that modifies the CBC's Organic Law so that a larger set of formal financial institutions, such as savings and loans cooperatives supervised by the CMF, will have access to the institution's liquidity facilities.

This reform should further strengthen the CBC's ability to fulfill its financial stability mandate of fostering the stability and efficiency of the financial system, ensuring the normal functioning of internal and external payments.

Table 2 provides an overview of the economic policy measures announced thus far.

Table 2: Overview of Policy Measures Announced since March 19th

Phase	Dimension	Policy	Amount (USD million)
Phase 1	Fiscal Resources for Public Health	Additional fiscal resources for health expenditures	$ 1,400
		New Fund to Finance Medical Expenditures	$ 260
	Measures to Protect Employment and Support Incomes	Injection to the UI Solidarity Fund	$ 2,000
		Cash transfer for the most vulnerable	$ 167
		Municipal Solidarity Fund	$ 100
	Injecting Liquidity into the Economy	Suspension of corporate tax payments	$ 2,400
		Deferred VAT payments	$ 1,500
		Early corporate tax refunds for SMEs	$ 770
		Deferred corporate tax payments for SMEs	$ 600
		Deferred payment on property taxes	$ 670
		Accelerated personal income tax refund for self-employed	$ 200
		Advance on personal income tax refund for self-employed (withheld Jan. & Feb. 2020)	$ 118
		Reduction of the Stamp & Seals Tax	$ 420
		Accelerated Payments on public procurement obligations	$ 1,000
		New Capitalization of Banco Estado	$ 500
	Subtotal		**$ 12,105**
Phase 2	Plan to Protect Economic Activity	Capitalization of FOGAPE	$ 3,000
	Plan to Protect Incomes		$ 2,000
	Subtotal		**$ 5,000**
TOTAL			**$ 17,105**

Source: Ministry of Finance.

III. Costs & Sources of Financing for 2020

Although these policy measures imply resources of up to ~USD17.1 billion, the actual cost of the measures during 2020 is estimated at up to USD12.1 billion. The difference is due to the fact that several policies imply an intra-annual adjustment of the Central Government's financial programming, while others are expected to be only partly disbursed this year. In contrast, revenue losses in 2020 due to the transitory suspension of monthly corporate tax payments, deferred VAT payments, and advances on personal income taxes for self-employed will be recovered in 2021.

Phase II measures consider a capitalization of FOGAPE of up to USD3 billion to take place over time accordingly as the value of credit guarantees increases. The Plan to Protect Incomes through a fund of up to USD2 billion will be sourced from budget reallocations. Our preliminary estimate of the fiscal cost during 2020 of these measures is estimated at up to USD12.1 billion (Table 3).

Table 3: Fiscal Cost of Economic Policy Measures for 2020

Phase	Dimension	Policy	Amount (USD million)
Phase 1	Fiscal Resources for Public Health	Additional fiscal resources for health expenditures	$ 1,400
		New Fund to Finance Medical Expenditures	$ 260
	Measures to Protect Employment and Support Incomes	Injection to the UI Solidarity Fund (partial)	$ 1,000
		Cash transfer for the most vulnerable	$ 167
		Municipal Solidarity Fund	$ 100
	Injecting Liquidity into the Economy	Suspension of corporate tax payments (*)	$ 2,400
		Deferred VAT payments (*)	$ 750
		Advance on personal income tax refund for self-employed (withheld Jan. & Feb. 2020) (*)	$ 118
		Reduction of the Stamp & Seals Tax	$ 420
		New Capitalization of Banco Estado	$ 500
Subtotal			**$ 7,115**
Phase 2	Plan to Protect Economic Activity	Capitalization of FOGAPE (†)	$ 3,000
	Plan to Protect Incomes		$ 2,000
Subtotal			**$ 5,000**
TOTAL			**$ 12,115**

Source: Ministry of Finance.
* Tax revenues from the transitory suspension of monthly corporate tax payments will be recovered in 2020 & 2021, whereas deferred VAT payments and advances on personal income taxes for self-employed in 2021. † The table considers the full capitalization to take place in 2020, although the actual schedule may vary, as needed.

Additional financing needs are planned to be met by a combination of debt issuance of up to USD4 billion, budget reallocations, Treasury assets, eventually a larger withdrawal from the Economic & Social Stabilization Fund, a larger withdrawal from the Pension Reserve Fund, and the deferral of contributions to funds, as described in Table 4. The sources of additional financing may eventually change, either in case of unforeseen changes in market conditions and/or adjustments in funding needs of the government.

Table 4: Sources of Additional Financing for 2020

Source	Amount (USD million)
Additional Debt Issuance	$ 4,000
Budget Reallocations	$ 2,500
Treasury Assets	$ 1,600
Economic & Social Stabilization Fund (*)	$ 1,500
Additional withdrawal of the *Fondo de Reserva de Pensiones*	$ 1,000
Deferral of Contributions to:	
Fondo de Contingencia Estratégico	$ 936
Fondo de Reserva de Pensiones	$ 650
	$ 12,186

Source: Ministry of Finance.
* Resources to complete the capitalization of FOGAPE in 2020, as needed.

The following section provides additional details on the sources of additional financing:

Debt Issuance Plans for 2020.

In line with the 2020 National Budget Law, the Ministry of Finance initially announced a plan to issue Treasury bonds for a total of USD8.7 billion during 2020, of which USD5.4 billion were in local currency and USD3.3 billion in foreign currency. The entire foreign currency portion of this plan was issued in January-2020.[1]

In the context of the COVID-19 shock, the Ministry of Finance was authorized by law to issue Treasury Bonds for an additional USD4 billion, placing total 2020 issuance plans at USD12.7 billion. As mentioned previously, USD3.3 billion were already issued.

The local currency Treasury bond issuance plan for the second quarter of 2020[2] considers issuances of up to USD4.88 billion, all to be issued through the SOMA system of the Central Bank of Chile, acting as Fiscal Agent of the Republic of Chile. This plan considers the issuance of new short-term notes (6, 12 months), and bonds that mature in 2025, all in nominal and inflation-linked instruments. The Ministry of Finance will also continue implementing liability management operations.

Additional information on the issuance plan for the remaining ~USD4.8 billion will be appropriately informed.

Budget reallocation.

As a result of the ongoing interruption of normal economic activity, the Budget Office estimates that planned expenditures of the 2020 National Budget are likely to be under-executed. In addition, the Budget Office has outlined several austerity measures that will free up resources (described below).

- Freezing of all new hires and salary increases in the public sector (with the exception of the Ministry of Health);
- Public sector overtime to be cut by 90% and travel expenses to be reduced significantly (domestic and international);
- Cuts in government programs that have a lower probability of execution due to the pandemic, including programs related to tourism, sports, culture;
- Strict monitoring of public purchases and contracts related to the health emergency;
- Reduction in the cost of office supplies;
- Cuts in ceremonial and protocol expenses;
- Purchases of vehicles and non-financial assets are suspended for the rest of 2020;
- Review of payments and quotas to international organizations.

Treasury Assets.

The Ministry of Finance and the Budget Office have recently implemented administrative measures that are expected to further improve the adequate use of public financial resources, including seasonal cash surpluses across the State.

Economic & Social Stabilization Fund (FEES).

As of the end of February-2020, the market value of the FEES was ~USD12.4 billion. Macro-fiscal projections published in the *Informe de Finanzas Públicas* of February-2020 estimated withdrawals for USD3.16 billion during 2020.

The capitalization of FOGAPE for a total of up to USD3 billion would initially be sourced from Treasury Assets, and if needed would be completed with resources from the FEES.

[1] More information at: https://www.hacienda.cl/english/press-room/news/archive/chile-obtains-historical-yields-in-euro.html
[2] Available at: https://www.hacienda.cl/english/public-debt-office/news/ministry-of-finance-announces-the.html

Additional Withdrawal of the Pension Reserve Fund.

As of 2016, annual withdrawals from the Pension Reserve Fund (PRF) were capped at an amount equal to a **third** of the difference between pension liabilities expenses in the year, and the inflation-adjusted pension liabilities expenses in 2008.

However, recently approved legislation allows for exceptional withdrawals only during 2020 and 2021 of the **entire** difference between these expenses. As a result, the estimated annual withdrawal from the PRF during 2020 has been increased from USD650 million to ~USD1.6 billion.

Deferral on Contributions to Funds.

Recently approved legislation increased the window to contribute USD936 million to the Fondo de Contingencia Estratégico from 6 to 24 months, and also suspended annual contributions to the PRF for 2020 and 2021. Annual contributions to the PRF are equivalent to at least 0.2% of GDP of the previous year, with internal estimates originally placing the 2020 contribution at USD650 million.

IV. Updated Macro-fiscal data to be published in April-2020

In line with the Republic of Chile's fiscal institutional framework, the updated quarterly macro-fiscal data (*Informe de Finanzas Públicas*) will be published during April-2020.