Markets remain highly stressed by evolution of the Covid-19

Governments and central banks of the world implement strong stimulus measures and make regulatory adjustments to face the pandemic. Financial assets continued to decline during the week, but closed higher after various announcements by the authorities. Global interest rates increased due to the expectation of higher debt issuance to finance contingency measures.

Government of Chile announces measures to mitigate the economic impact of Covid-19. The package of measures for US$ 11,750 billion seeks to mitigate the negative impact that the virus will have. Most of the tax measures are transitory and aim to give liquidity to smaller companies. For its part, the health budget increases considerably, underpinned by the Constitutional 2% allowed by the declaration of a State of Catastrophe.

Drastic cut in the MPR and liquidity measures of the Central Bank contribute to give greater stability to the financial markets. However, further action by the authorities may be necessary to sustain liquidity and avoid a sharp contraction in credit.

CLAUDIO SOTO
Chief economist
claudio.soto.gamboa@santander.cl

GABRIEL CESTAU
Economist
gabriel.cestau@santander.cl

SINDY OLEA
Economist
sindy.olea@santander.cl

MIGUEL SANTANA
Economist
miguelpatricio.santana@santander.cl

FABIÁN SEPÚLVEDA
Economist
fabian.sepulveda@santander.cl

Stimulus measures contain market crash

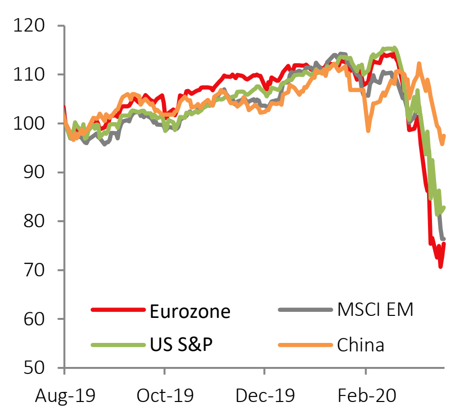
The rapid spread of the coronavirus (Covid-19) in different geographies and an acceleration in the number of new infections worldwide have meant drastic containment measures - ranging from border closures to total quarantine in some countries -, which in turn, has resulted in significant disruptions in production chains.

At the close of this report, the markets partially reversed the falls of the week.

In this context, the financial markets continued to show substantial falls. At the beginning of the week, the stock markets of developed economies decreased up to 11%, while the drop in emerging markets exceeded 20%. However, in recent days, large fiscal stimulus packages and liquidity measures announced by the authorities of the main economies have helped to partially reverse the downward trend in the markets.

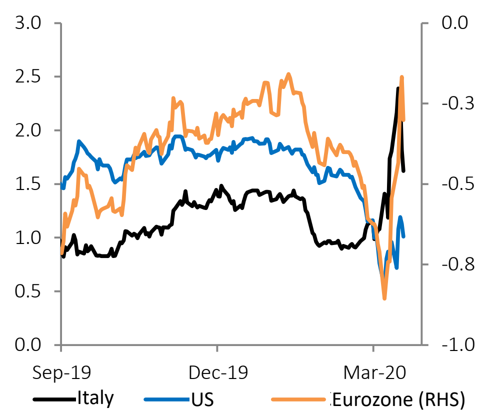
Contrary to what was observed in the previous weeks, significant outflows from global fixed income were recorded, with which interest rates increased substantially. This behavior is explained by the greater debt issuance that governments will have to carry out to face the emergency, the increased perception of risk and the uncertainty regarding the extent that this epidemic will have in the global economy.

Graph 1: International Exchanges (Index 100 = Aug.19)



Source: Bloomberg and Santander

Graph 2: Benchmark rate 10y (%)



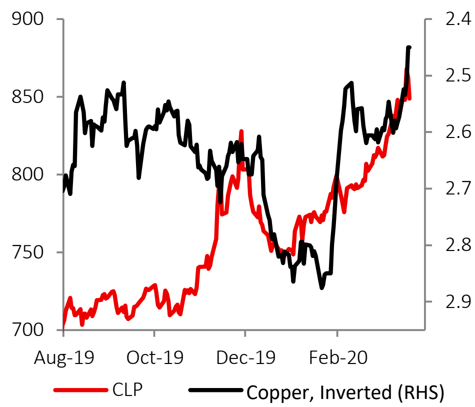
Source: Bloomberg and Santander

Local assets deteriorated in line with the international trend

The local market mirrored external movements. The IPSA closed the week with a drop of around 13%, while the exchange rate fell below $ 850. The depreciation of the peso was in line with the abrupt drop in the price of copper and the global strengthening of the dollar.

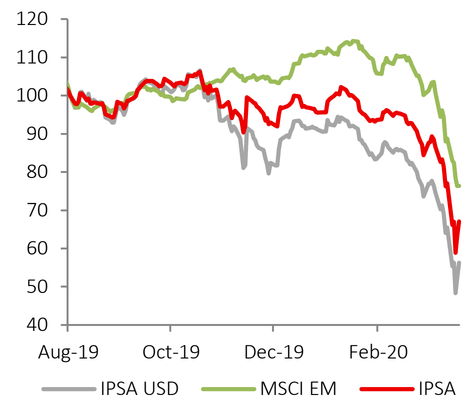
Local fixed income was a reflection of international rates and, although with fluctuations, increases in government rates predominated. In contrast, swap rates closed with significant falls in line with the rate drop that the Central Bank made earlier this week. Meanwhile, liquidity conditions are still tight.

Graph 3: Exchange rate and copper ($/US$, US$/lb.)



Source: Bloomberg and Santander.

Graph 4: Exchange markets (Index 100 = Aug.19)



Source: Bloomberg and Santander.

Central Bank cuts MPR to 1% and announces additional measures

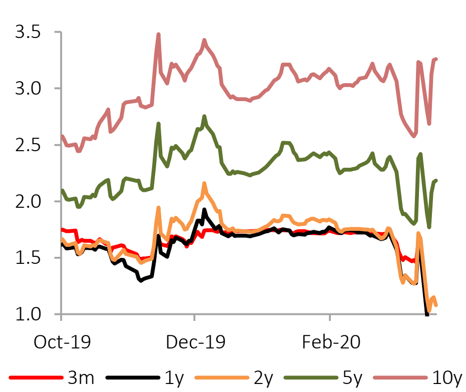
In an extraordinary meeting, the Central Bank reduced the Monetary Policy Rate (MPR) by 75bp to bring it up to 1%. Likewise, the issuing entity announced a series of unconventional measures to inject greater liquidity into the market and facilitate the credit channel.

New facility of the Central Bank (FCIC) will increase credit

One of them is the Conditional Credit Increase Facility (FCIC), where banks will be able to apply for financing at the current MPR - or less if it is reduced - for a term of up to four years. The amount of this facility will increase with loans in order to encourage credit.

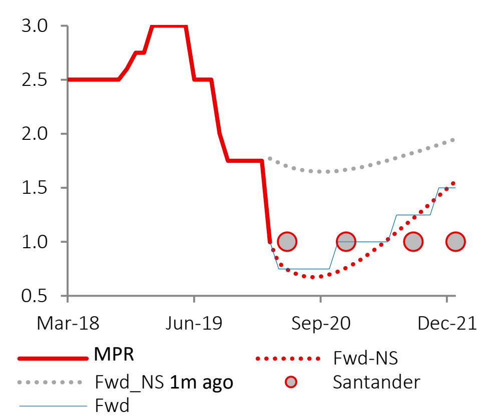
In addition, corporate bonds will be included within the eligible collaterals for all current liquidity operations in pesos and a program of purchase of bank bonds for up to US $ 4 billion will be implemented. Lastly, the Central Bank also announced that the foreign exchange sales program in the foreign exchange market will be extended until January 9, 2021.

Graph 5: Nominal swap rates (%)



Source: Bloomberg and Santander.

Graph 6: MPR expectations (%)



Source: Bloomberg and Santander.

Central banks around the world take interest rates to a minimum

The monetary authorities provide important monetary incentives.

The United States Federal Reserve (Fed) decided to meet extraordinarily for the second time in the month. On this occasion, it cut the interest rate to a range of 0% to 0.25%, announced new measures for the money market and opened a liquidity fund for the short-term financing of companies. Additionally, the first coronavirus fiscal stimulus plan was approved, while a new one for US $ 1.3 trillion is already being processed, of which US $ 500 billion would go to homes and US $ 500 billion to companies.

In turn, the European Central Bank announced a program to purchase public and private assets for € 750 billion, and its president left the door open for new measures. In turn, the Bank of England recently released the second cut in just over a week, lowering its rate to 0.1%, the lowest the UK has ever seen. In addition, it decided to expand its quantitative easing program by $ 235 billion, to a total of $ 740 billion.

Taiwan cut its rate by 25bp, Canada and South Korea by 50bp, New Zealand by 75bp and South Africa by 100bp. Meanwhile, the Reserve Bank of Australia had an extraordinary meeting, in which it reduced interest rates to a record low of 0.25%, the second cut made by the entity in two weeks. In addition, emergency plan was presented, including a line of credit for companies of $ 50 billion.

Brazil's governing body reduced the interest rate by 50bp, to a record low of 3.75%. Meanwhile, the country's growth expectations are cut to the range of 0% to 0.5%, well below the 2.1% forecast a few months ago. Its peer in Peru cut reference rates, in an extraordinary meeting by 100bp, placing it at 1.25% and indicated that the deterioration of domestic demand is important, which leaves the door open for future cuts. Also in Chile, the Central Bank cut the monetary policy rate by 75bp, bringing it down to 1%, and implemented quantitative stimulus programs.

In this way, efforts are multiplied to face the economic consequences of the coronavirus. Until now, monetary policy has been the first to react, but fiscal and regulatory efforts will slowly increase. However, the next few months will see the interruption in the logistics chains and the consequences on the activity will be severe.

Government announces measures to mitigate the economic impact of Covid-19

The Government announced a package of measures for US $ 11,750 million that seeks to mitigate the negative impact that the spread of the coronavirus will have on the economy. The announcements consider an increase in the budget of the Health System -using the constitutional 2%, which is equivalent to about US $ 1.2 billion-, tax benefits focused on SMEs and individuals, and the presentation of a bill that creates a mechanism to " suspend ”jobs for the duration of the health emergency. Banco Estado will also be capitalized so that it can expand its loan portfolio.

The tax measures are related to the postponement of different taxes - VAT and income - focused on small and medium-sized companies, and the transitory reduction of stamp taxes to 0%. Regarding job protection, a bill was announced so that people who work in sectors that will not be able to function in the event of a health emergency continue to receive income from their Unemployment Insurance, without terminating their employment relationship.

The tax announcements will reduce tax revenues by close to US $ 6 billion (just over 2% of GDP). The measures that contemplate more expenses, including the constitutional 2% for health, add up to around US $ 4.5 billion (1.6% of GDP). To this are added other movements, such as the capitalization of Banco Estado for US $ 500 million.

Most of the tax measures are transitory and aim to strengthen the liquidity of companies. Therefore, its impact on the annual collection of the Treasury should be limited. There will also be space for reallocations, since not all the initiatives contemplated in the original budget design will be able to be carried out. Thus, the final impact on the fiscal situation of these measures is still uncertain.

Market Summary

	Exchange rates				Exchange			10Y rates			
	Level	Weekly Var.	Accum. Mar.20	Accum. 2020	Weekly Var.	Accum. Mar.20	Accum. 2020	Level	Weekly Var.	Accum. Mar.20	Accum. 2020
			%			%				pb	
US	102.4	-3.5	-4.1	-5.5	-12.3	-19.6	-26.2	0.96	0	-19	-92
Eurozone	1.1	3.8	3.1	4.7	-1.3	-23.4	-31.9	-0.34	21	27	-15
UK	1.2	4.6	9.2	11.7	-3.3	-21.2	-31.6	0.54	13	9	-33
Japan	111.4	3.2	3.1	2.3	1.7	-15.1	-25.5	0.10	11	26	13
Chile	860.8	2.8	5.3	14.5	-15.8	-23.2	-32.2	3.68	37	9	53
Argentina	63.7	1.2	2.5	6.3	-13.4	-29.6	-40.9	46.5	1,106	2,100	2,545
Brazil	5.0	3.2	12.1	24.8	-16.2	-33.5	-40.1	9.06	98	228	225
Mexico	24.3	10.8	23.8	28.3	-9.8	-16.9	-21.3	7.77	12	92	92
Colombia	4,132	2.8	17.3	25.9	-20.6	-39.8	-43.9	9.00	100	317	292
Peru	3.5	-0.4	1.6	5.8	-9.1	-18.9	-25.7	5.65	87	166	144
China	7.1	1.3	1.5	1.6	-6.2	-7.3	-10.5	2.75	3	-4	-42
Turkey	6.6	3.6	5.1	10.4	-10.3	-19.1	-25.2	13.1	140	27	107
South Africa	17.5	7.5	11.7	24.0	-8.0	-20.8	-29.4	11.67	170	257	343
India	75.4	2.1	3.9	5.7	-12.3	-21.9	-28.0	6.26	-6	-11	-28
Indonesia	15,900	7.9	10.9	14.2	-14.5	-23.1	-33.4	8.10	80	121	100

COMMODITIES	Level	Weekly Var.	Accum. Mar.20	Accum. 2020
Copper	2.18	-11.7	-14.2	-22.7
Oil	23.6	-25.7	-47.3	-61.8
Gold	1,481.1	-3.2	-6.5	-2.2

INDICATORS OF RISK	Level	Weekly Var.	Accum. Mar.20	Accum. 2020
VIX (%)	64	6.6	24.3	49.6
Chile CDS 5y	133	32	65	93
Peru CDS 5y	129	30	64	89
Mexico CDS 5y	235	32	129	158
Brazil CDS 5y	296	36	162	198
Colombia CDS 5y	289	71	183	218

CONTACTO

(56 2) 2320 1021
Access our reports at:

http://saladecomunicacion.santander.cl/estudios
https://santandercl.gcs-web.com/investors/our-economy-and-financial-system