MONTHLY ECONOMIC OUTLOOK

Optimism returns to the markets after weeks of uncertainty

In Chile, activity data show an acceleration in the recovery driven by the easing of lockdown measures and liquidity injections received by households.

Highlights

- **Election results in the United States and positive news about the Pfizer-BioNTech vaccine return optimism to the markets.** Less likelihood of dramatic shifts in US economic policy and the prospects for a solution to the pandemic has boosted global stock markets in recent days and driven up commodity prices.
- **Activity in Chile is accelerating its pace of recovery.** Progress in the easing of lockdown and the injection of liquidity to households have stimulated consumption. Progress in the normalisation of activity in several sectors and low benchmarks will result in a fourth quarter with positive figures.
- **The employment situation is starting to improve, but job creation is still slow.** As of September, there were still 1.5 million fewer jobs than in March, and nearly 600,000 workers remained under the employment protection programme. The unemployment rate has remained relatively moderate (12.3%) due to low labour participation.
- **Global optimism spreads to local markets.** Local stock index IPSA has risen by approximately 13% in just a few days, taking it to its highest level since the end of August. The exchange rate has appreciated again, helped by a high copper price and a relatively weak dollar, while long-term interest rates have remained stable.
- **A possible second withdrawal of pension funds could mean an additional injection of US$16 billion into the economy.** We assess that about 15% of affiliates will have no funds to withdraw, while 35% will be left without savings. If implemented, this second withdrawal could give an additional temporary boost to demand during the first quarter, but less intense than the first.
- **Accelerated inflation will be transitory.** The high CPI records for September and October are explained by the easing of lockdown measures and the consumption impulse of the liquidity shock received by households. In the future, economy gaps will take the pressure off prices, although a possible further withdrawal of pension funds could lead to one-off increases.
- **Complex processing of the 2021 budget.** Tensions between the government and opposing parliamentarians have hampered progress on the Budget Law for next year. One of the issues where there is no agreement pertains the mechanism to use Covid Fund resources, which next year will amount to US$ 5.2 billion. On the other hand, public spending expanded by 28% YoY in the third quarter.

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Vaccine progresses and the US election are improving expectations.

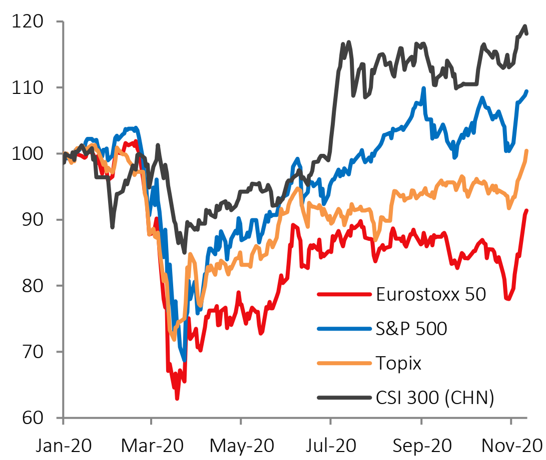
The last few days have been marked by two milestones that have boosted asset prices globally: the result of the US elections and the advance of the Covid-19 vaccine being developed by Pfizer in conjunction with the German company BioNTech.

In the case of the US elections, the victory of the Democratic candidate, Joe Biden, and the eventual renewal of the Republicans' control of the Senate –a situation to be settled in a second round for the state of Georgia during January—was celebrated by the markets. The new government is expected to further the control of the pandemic and to implement major economic stimulus measures with a new fiscal package. It will also be relevant in the fight against climate change, such as the return to the Paris Agreement. Still, the possibility of implementing a more radical agenda, in terms of spending, tax burden and environmental protection, will be limited by Congress. Regarding the relationship with China, disputes will persist, but there will be a change of approach, with emphasis on a multilateral strategy.

This week it was reported that the vaccine developed by Pfizer with BioNTech succeeded in preventing more than 90% of Covid-19 infections in a large-scale study. This result is much more promising than was expected and could soon allow authorisation for the use of this vaccine in at-risk populations. The news comes at a time when pandemic outbreaks in Europe and the US continue to escalate, beginning to impact service sectors and threatening global recovery.

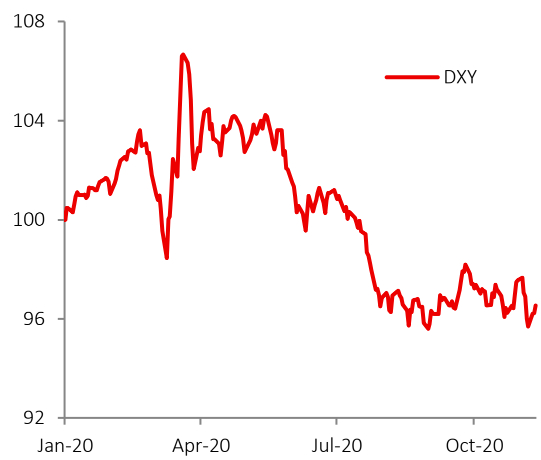
Asset prices reacted favourably to both the US election result and the news of the vaccine, after weeks of poor results due to the worsening of the health situation. The S&P500 rose 6% in the last week, the Eurostoxx50 rose 13%, and stock volatility as measured by the VIX fell to 24%. Long rates on US Treasury bonds tended to increase moderately, but the dollar has remained relatively weak.

US Election results and progress on Covid vaccine boost stock markets



Source: Reuters and Santander

Dollar remains weak

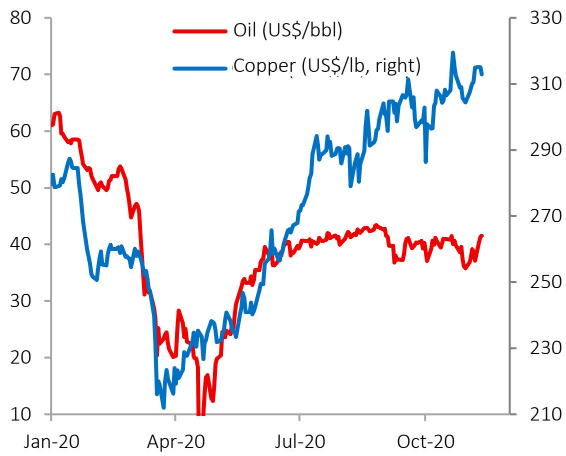


Source: Reuters and Santander

Recently, the need for further stimulus to counter the impact of the pandemic's resurgence led the Bank of England to increase its asset purchase programme, and the European Central Bank is expected to do the same at its December meeting. The Fed, meanwhile, has been less clear about its next steps, pending definitions on a new tax package.

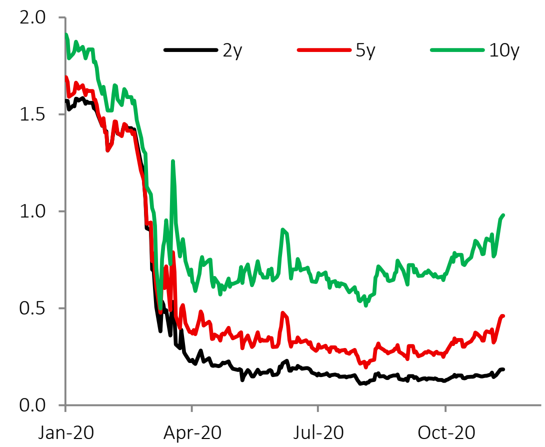
As in the case of financial assets, commodity prices reacted upwards to the news of the week. The price of copper rose to around US$3.13 per pound, while the price of oil reached US$42 per barrel. However, this value is still well below the levels seen at the end of last year, reflecting the weak outlook for oil demand provoked not only by weak growth but also by the expected changes in countries' energy matrices.

Rise in raw material prices



Source: Reuters and Santander

Long-term rates in the US rise again with the prospect of further fiscal stimulus

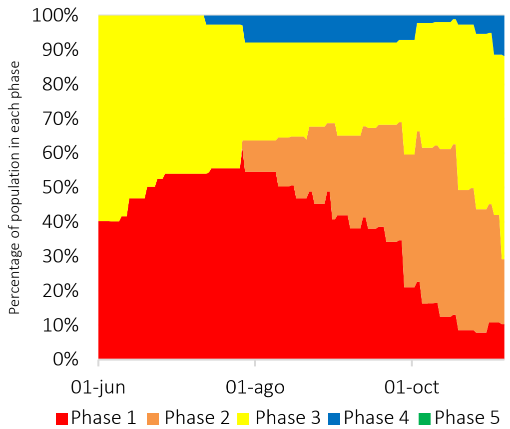


Source: Reuters and Santander

Local activity continues its vigorous recovery

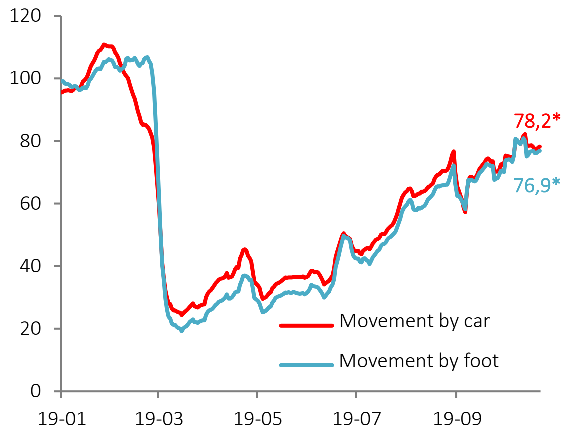
As expected, the easing of the lockdown and the strong impulse to consumption caused by the liquidity shock households received led the Imacec in September to show a significant increase over August (5.1% MoM, non-seasonal). Sectors contributing the most were trade, manufacturing and, to a lesser extent, business services. Mining maintained a similar performance to previous months, reflecting the restricted impact the pandemic has had on the sector. Additionally, construction continued to lag behind given a significant fraction of the population was still under quarantine until September.

Advances in the easing of lockdown measures



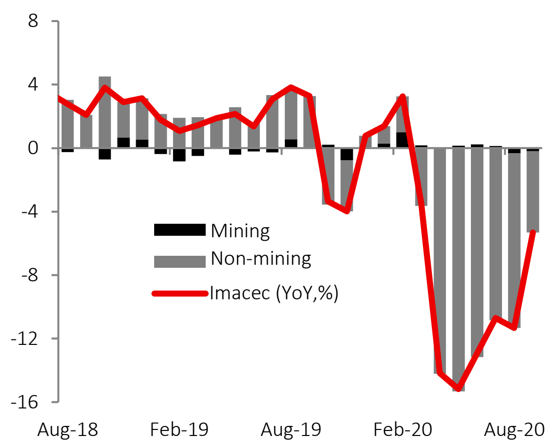
Source: Ministry of Health and Santander

Mobility has recovered but is still below the levels of an average year



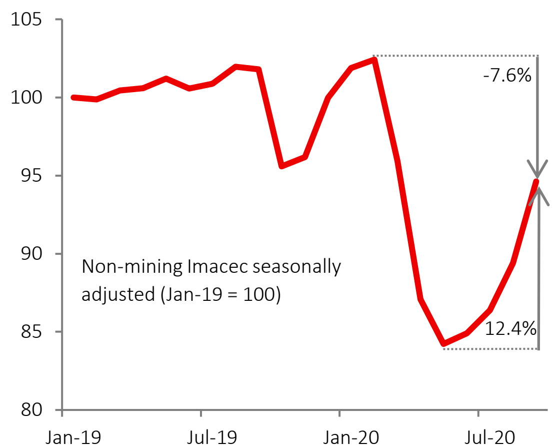
*: Excludes day of national plebiscite
Source: Apple Inc. and Santander

Activity speeds up recovery



Source: BCCh and Santander

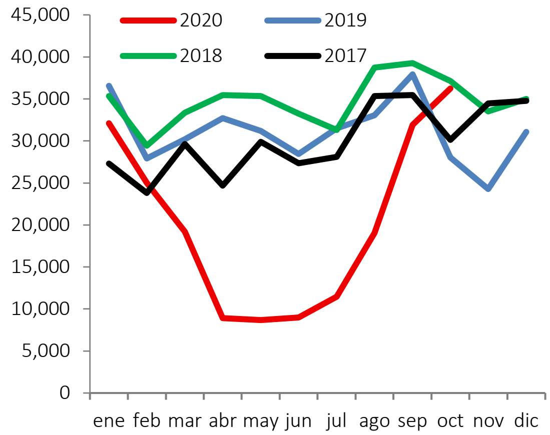
A significant gap remains from pre-pandemic situation



Source: BCCh and Santander

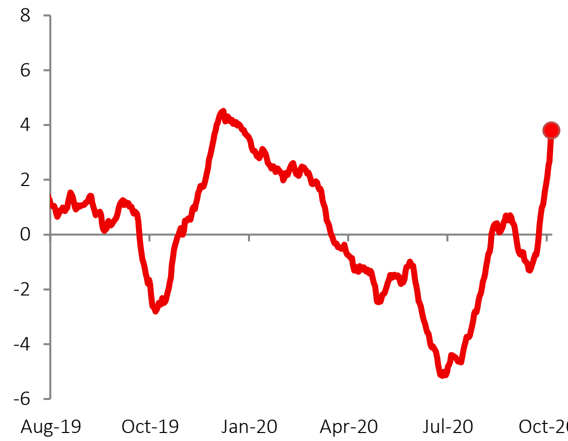
In recent weeks, the transition to more advanced stages of normalcy has continued to increase mobility and normalise activity in several sectors. Added to the weak benchmark of last year's social outbreak, this will make October's Imacec register the first year-on-year expansion since last February, which would fall between 1% YoY and 2% YoY. Several monthly indicators point precisely in that direction. New car sales increased by almost 30% YoY, electricity generation increased by 2.7% YoY (vs only 0.9% in September) and exports grew to double digits figures. At the same time, business expectations are on optimistic grounds for the first time in more than a year, with all sectors above the neutral level except for construction.

New car sales returned to pre-pandemic levels in October



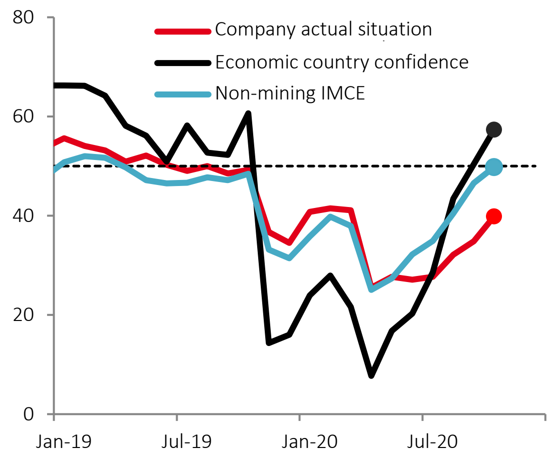
Source: ANAC and Santander

Growth in electricity generation shows a more dynamic activity



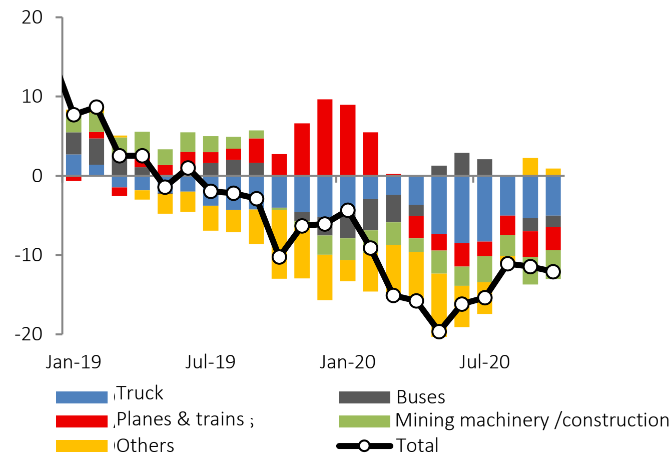
Source: CEN and Santander

Business confidence marks its best record since the social outbreak



Source: Icare-UAI and Santander

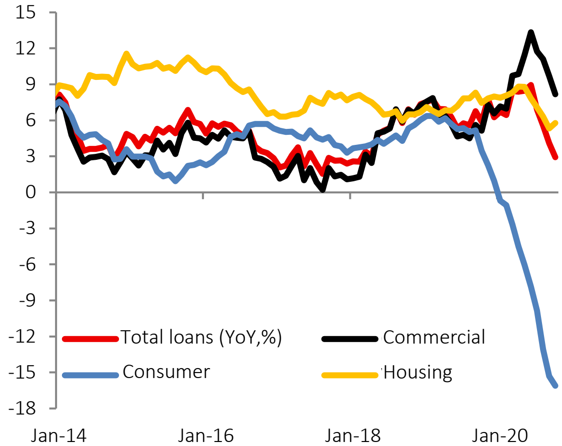
Capital goods imports remain weak



Source: BCCh and Santander

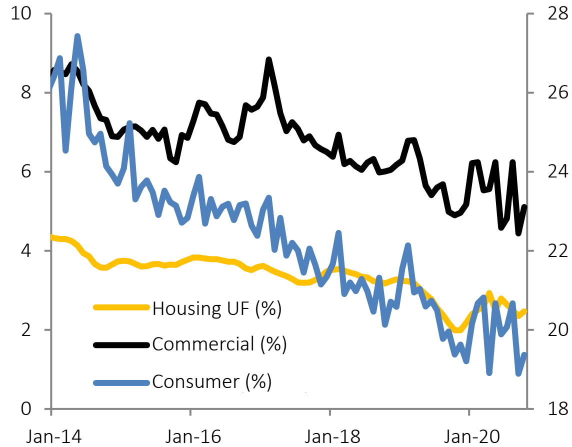
Nonetheless, imports of capital goods continue under pressure. Likewise, commercial loans have lost their momentum after having expanded at high rates until mid-year, caused by companies' demand for liquidity. This reflects the fact that the recovery in investment is still weak. Meanwhile, while mortgage loans have remained stable, consumer loans are still slow, in a context where interest rates are at very low levels.

Commercial loans lose momentum



Source: BCCh and Santander.

Interest rates remain at historically low levels



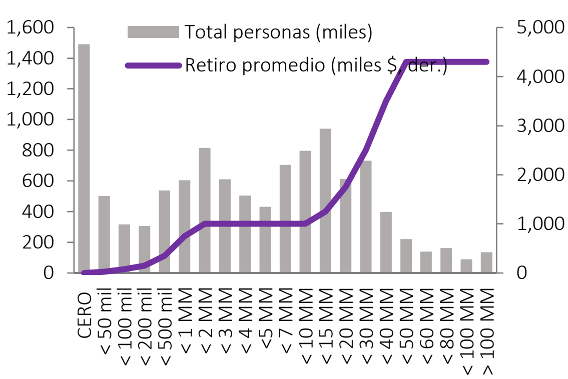
Source: BCCh and Santander.

Possible second pension fund withdrawal could reach US$ 16 billion

Payments for the first pension withdrawal – approved at the end of July– already amount to US$ 17 billion, in line with our estimates. This measure has resulted in 1.5 million contributors having a zero balance in their accounts, while 1.1 million have a balance of less than $200,000.

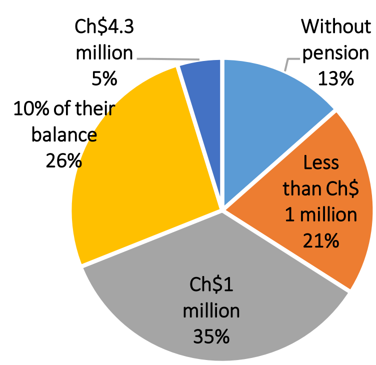
We estimate that a possible second withdrawal –which is currently being discussed in Congress— would imply a somewhat smaller reduction in pension savings than in the first case, with a maximum amount of around US$ 16 billion. About 13% of contributors (1.5 million people) have no balance in their accounts, so they could not make the second withdrawal. An additional 21% have less than 1 million saved, so making use of the facility could also leave them without savings.

About 1.5 million people have no balance to withdraw from their accounts



Source: Santander based on SPensiones

About 35% of contributors would be left without pension savings after a second withdrawal

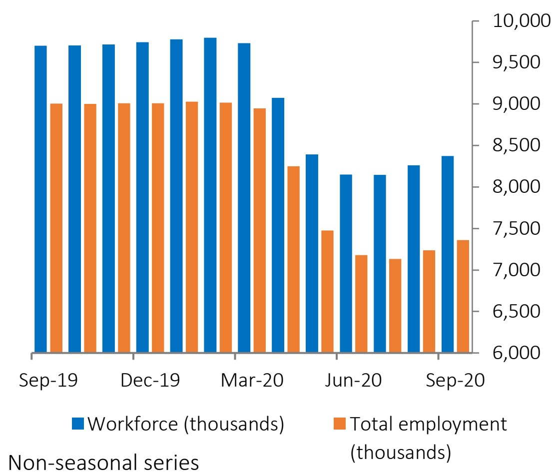


Source: Santander based on SPensiones

Labour market recovers at a slow pace

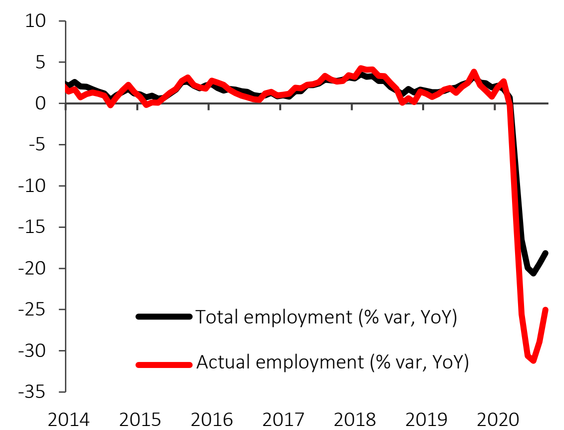
Consistent with the increase in activity, employment has shown an upturn in recent records, with almost 300,000 jobs created since July. Nevertheless, the employment situation remains weak, with 1.5 million fewer jobs than last March when the pandemic broke out. The number of absent workers is still high (around 600,000 more than in an average year) corresponding to those under the employment protection programme. Thus, while total employment fell by 18% YoY in the quarter ending in September, actual employment –which excludes absent workers– fell by 25%. Meanwhile, labour participation continues to be hit by the pandemic, affecting the unemployment rate which has fallen slightly to 12.3%.

Labour force and employment remain well below pre-pandemic levels



Non-seasonal series
Source: INE and Santander

Despite recovery, actual employment remains 25% below last year's levels

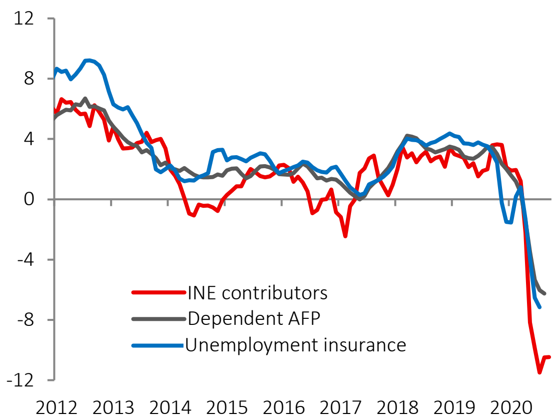


Actual employment excludes absent workers.
Source: INE and Santander

As we discussed in our September Monthly Economic Outlook, the fall in employment during the pandemic has been substantially greater than activity. While this can be explained in part by productivity gains and changes in sectoral composition, there are also indications that there may be an overestimation of job losses. Particularly when comparing the data from surveys against administrative records, it can be seen that the contraction of employment resulting from the latter is considerably less than that of the former (AFP dependent contributors marked a 6.3% decline YoY in August - the last data available - while the equivalent measurement from the National Institute of Statistics (INE) indicated a 10.5% YoY contraction in the same month). While discrepancies between the two data are well known, the magnitude of the gap has widened in the context of the pandemic.

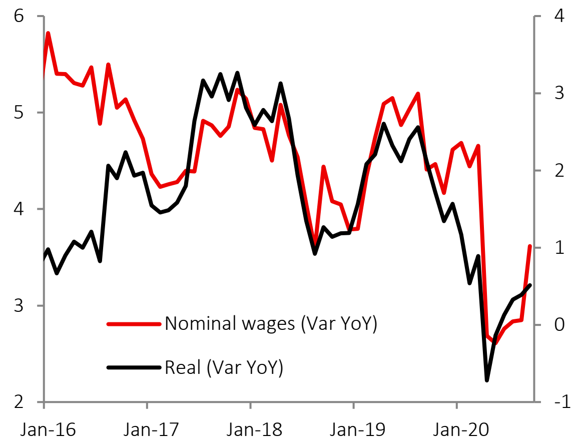
Wages have also shown a more moderate behaviour than employment, and in September they recorded an increase of 1% MoM (0.4% non-seasonal). In twelve months, the expansion reached 3.6%, a figure that is influenced by an 8.1% growth in trade remuneration. Despite this, September's high inflationary record contained the expansion of real wages, which grew at a rate of 0.5% YoY. Although September is usually a month in which the readjustment of the minimum wage accelerates this indicator, this year the project finished its processing in Congress only at the end of October, so the impact of the new figures would not yet be captured.

The gap between administrative records and INE figures widened in recent months



Source: SPensiones, INE and Santander

In real terms, the rebound in wages has been contained by higher inflation

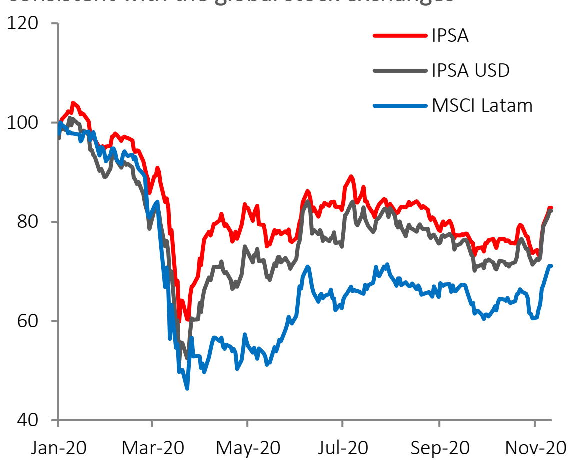


Source: INE and Santander

Global optimism spreads to local markets

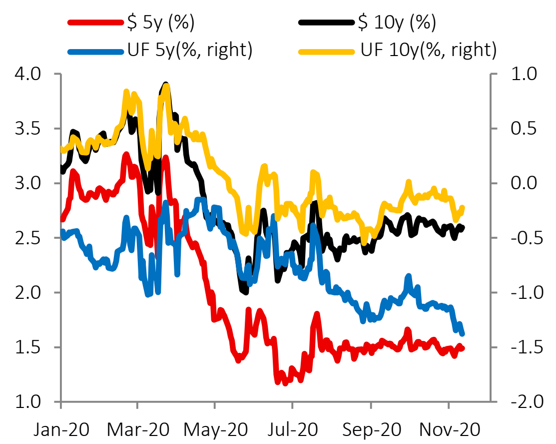
Until the first days of November, the local stock market showed a downward trend and the IPSA fell to 3,500 points, its lowest level since the end of March. However, recently the local market has adhered to the global optimism, rising sharply with a 13% increase. Thus, as of the date this report was issued, the IPSA was being traded at approximately 3,970 points. In the bond market, inflation surprises in recent months have pushed down indexed bonds, bringing 2 and 5-year UF bond rates to levels around -2.1% and -1.4%.

IPSA had a robust advance in the last days, consistent with the global stock exchanges



Source: INE and Santander

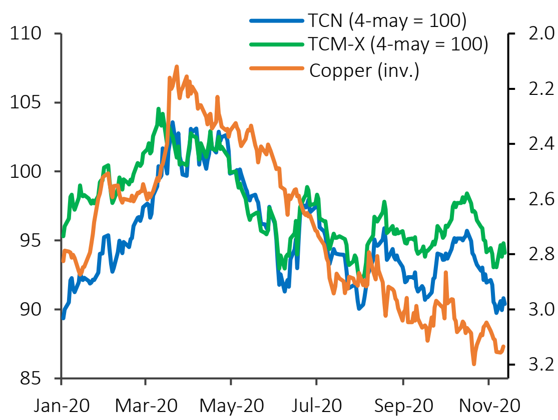
UF rates drop due to inflationary surprise



Source: BCCh, RiskAmerica and Santander

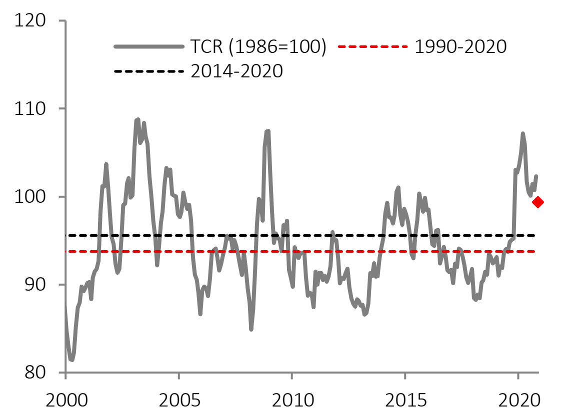
The Peso has maintained an appreciating trend, driven in recent weeks by an increased global risk appetite, high copper prices and portfolio adjustments in pension funds. Additionally, the Ministry of Finance has maintained foreign exchange sales to provide the necessary cash flow to finance expenditure in the latter part of the year. With this, the Peso/dollar parity descended from over $800 in mid-October to $755 in the last few days. The nominal appreciation of the currency has been reflected in the real exchange rate, which has fallen by around 7% since its peak in March, reaching its strongest level since October 2019. In the future, we estimate that some of the factors that explain this trend will display a reversal. Notably, the price of copper may fall towards levels closer to those consistent with its long-term values. On the other hand, if the US fiscal stimulus package is advanced, there should be an overall appreciation of the dollar. This could bring parity to around $780 by the end of the year.

The Peso has appreciated again, driven by a high price of copper



Source: BCCh, Bloomberg and Santander

Real exchange rate remains above historical averages



Note: Red dot corresponds to estimate for Nov-20 with a nominal exchange rate of $760.
Source: Ministry of Finance and Santander

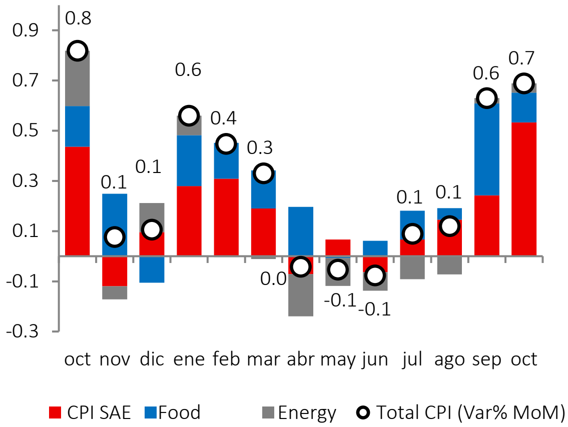
Rising inflation would be transitory

The October CPI showed a 0.7% monthly variation, well above market expectations (0.3%), bringing the 12-month inflation to just below the 3% target. The figure was affected by food, housing, durable goods and clothing. Furthermore, the end of the temporary reduction of the stamp duty - in force since April as a measure to deal with the pandemic - contributed almost a tenth to inflation.

Both the injection of liquidity that households have received - with the withdrawal of pension funds and the Emergency Family Income - and the easing of lockdown measures have given a stimulus to consumption, which would explain the inflationary impulse. Nevertheless, we believe that this is a transitional effect that will not be repeated in the coming months. Particularly for November and December, we project null or only slightly negative changes in the CPI, which would bring inflation to around 2.7% by the end of the year.

In 2021, capacity gaps will remain substantial, keeping price momentum restricted and pushing the CPI down to 2.5% in the first quarter. Nevertheless, a possible second withdrawal of pension funds could induce further short-term price pressures.

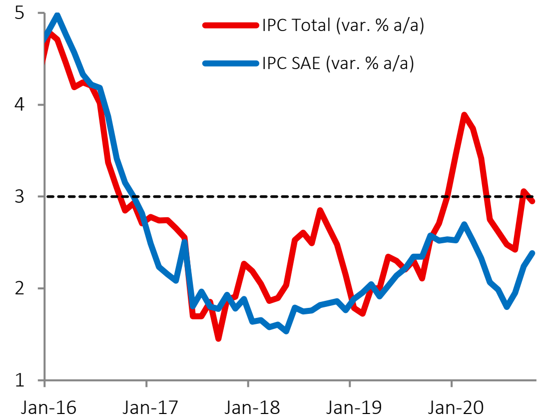
CPI surprised again in October



Source: INE and Santander

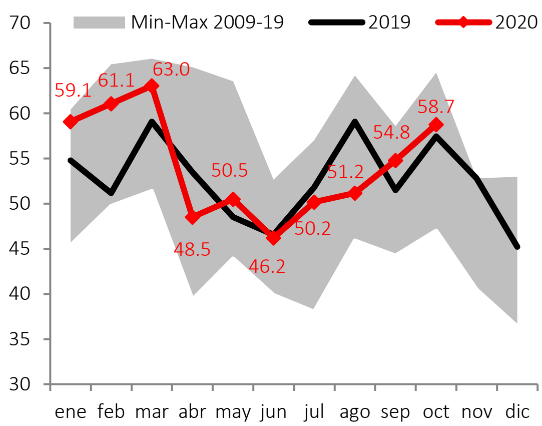
Note: SAE=sans food and energy

Inflation returned to the target of 3%



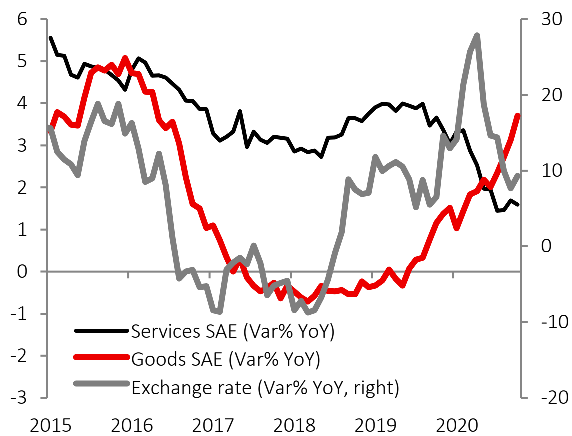
Source: INE and Santander

Price increases were widespread



Inflationary spread: percentage of products that increased in price in the month.
Source: INE and Santander

Underlying asset prices continue to accelerate, despite moderation in the exchange rate



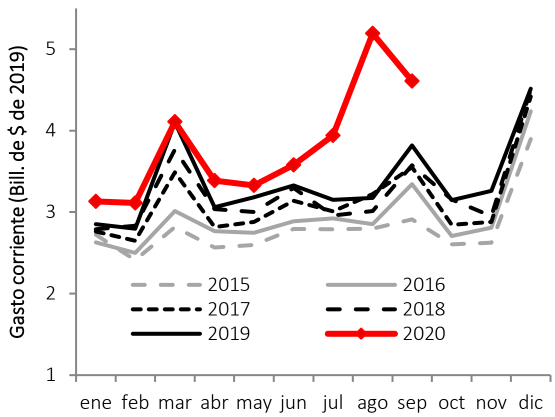
Source: INE and Santander

Budget discussion progresses with difficulty

Discussion of the 2021 fiscal budget began in early October, but progress has been slow due to disagreements between the government and opposition parliamentarians. One of the issues that has created contention is the mechanism for the use of Covid Fund resources, which for next year contemplate an amount close to US$ 5.2 billion. While the government emphasises the need for flexibility in order to allocate resources in the areas that most need it, opposition parliamentarians complain of a lack of transparency and demand guarantees that resources will be used appropriately.

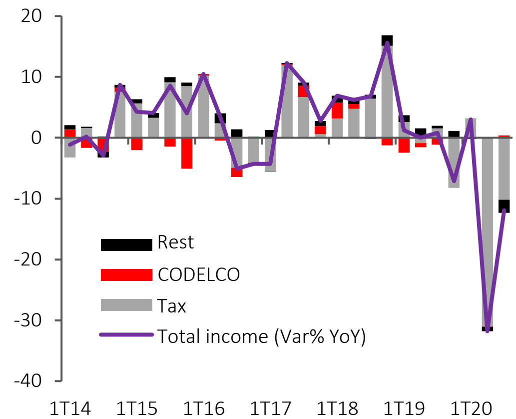
In terms of the execution of the current budget, the trend of recent months was maintained with a high expansion of expenditure (28.5% YoY in the third quarter) during September, driven by subsidies and donations. Meanwhile, revenues continued to contract (-12% YoY in the third quarter), albeit at a more moderate pace than the previous quarter. Overall, the fiscal deficit in the last twelve months already exceeds 7% of GDP and would close the year at around 8.5% of GDP.

Fiscal stimulus measures are reflected in strong expenditure growth



Source: Ministry of Finance and Santander

Fall in revenue eased by tax relief measures



Source: Ministry of Finance and Santander

Macroeconomic projections

National Accounts	2014	2015	2016	2017	2018	2019	2020 E	2021 P
GDP (real var. % YoY)	1.8	2.3	1.7	1.2	3.9	1.1	-6.0/-5.0	4.0/5.0
Internal demand (real var. % YoY)	-0.5	2.5	1.8	2.9	4.7	1.0	-9.0	7.0
Total consumption (real var. % YoY)	2.9	2.6	3.5	3.6	3.8	2.9	-9.0	8.0
Private consumption (real var. % YoY)	2.7	2.1	2.7	3.4	3.7	1.1	-9.5	8.0
Public consumption (real var. % YoY)	3.8	4.8	7.2	4.6	4.3	-0.3	-5.0	7.0
Gross fixed capital formation. (real var. % YoY)	-4.8	-0.3	-1.3	-3.1	4.8	4.2	-8.5	5.0
Exports (real var. % YoY)	0.3	-1.7	0.5	-1.5	5.0	-2.3	-1.5	2.5
Imports (real var. % YoY)	-6.5	-1.1	0.9	4.6	7.9	-2.3	-14.0	11.0
GDP (US$ billions)	260.6	244.3	250.6	277.1	298.9	282.7	245	265
GDP per capita (US$ thousands)	14.6	13.6	13.8	15.0	15.9	14.8	12.5	13.1
Population (millions)	17.8	18.0	18.2	18.4	18.8	19.1	19.5	19.7

Note: The GDP component projections will be updated following the publication of the 3Q20 Quarterly National Accounts (18 November).

Balance of Payments	2014	2015	2016	2017	2018	2019	2020 E	2021 P
Trade balance (US$ billions)	6.5	3.4	4.9	7.4	4.6	4.2	15.5	11.5
Exports (US$ billions)	75.1	62.0	60.7	68.8	75.2	69.9	69.5	71.5
Imports (US$ billions)	68.6	58.6	55.9	61.4	70.6	65.7	54.0	60.0
Current account (US$ billions)	-5.2	-5.7	-5.0	-6.4	-10.6	-10.9	-2.0	-4.0
Current account (GDP%)	-2.0	-2.4	-2.0	-2.3	-3.6	-3.9	-1.0	-1.5
Price of copper (annual average, US$/lbs.)	3.11	2.50	2.21	2.80	2.96	2.72	2.75	2.85
WTI oil price (annual average US$/bbl.)	93.1	48.7	43.2	50.9	64.8	57.0	39.0	48.0

Money and Exchange Market	2014	2015	2016	2017	2018	2019	2020 E	2021 P
CPI Inflation (var. YoY, % by December)	4.6	4.4	2.7	2.3	2.6	3.0	2.7	2.6
CPI Inflation (var. YoY, average %)	4.7	4.3	3.8	2.2	2.4	2.3	3.0	2.6
CPI sans food and fuel inflation (IPC-SAE) (var. YoY, % by December)	4.3	4.7	2.8	1.9	2.3	2.5	2.2	2.3
CLP/US$ exchange rate (year's exercise)	607	707	667	615	696	745	780	800
CLP/US$ exchange rate (year average)	570	654	677	649	640	703	795	790
Monetary policy rate (year's exercise, %)	3.00	3.50	3.50	2.50	2.75	1.75	0.50	0.50
Monetary policy rate (%, year average)	3.75	3.06	3.5	2.7	2.52	2.48	0.78	0.50

Fiscal Policy	2014	2015	2016	2017	2018	2019	2020 E	2021 P
Public expenditure (real var. % YoY)	6.4	7.4	3.8	4.8	3.5	4.1	11.5	0.0
Central Government balance (% GDP)	-1.6	-2.2	-2.7	-2.8	-1.6	-2.8	-8.3	-4.5%
Central Gov. gross debt (US$ billions)	36.6	39.0	53.4	68.9	70.2	74.4	84.2	95.0

Source: BCCh, INE and Santander

CONTACT

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https://banco.santander.cl/estudios