



MARKET OUTLOOK

Week: September 23 –October 4, 2019

Highlights

- **Unexpected higher activity in August.** August's Imacec (3.7%) was above consensus expectations (2.6%), driven by the dissipation of transient phenomena that affected the dynamism of services. This result reduces the possibility of further cuts in TPM at the next monetary policy meetings.
- **The exchange rate appreciated in line with the global weakness of the dollar.** Manufacturing and employment data in the US accentuated the concern for the US economy, which depreciated the dollar globally and boosted the peso, which closed the week at levels close to \$ 715. However, a greater deceleration of the American economy could generate aversion to higher risk assets and the factors that this week appreciated the local parity, would result in an increase.
- **Reduction to tax revenue projections.** The lower price of copper and the low expected growth have impacted government revenues, which in its latest Public Finance Report adjusted downwards the projections for 2019 and 2020 (0.7% and 4.5%, respectively). The budget proposal submitted to Congress considers an expansion of 3.6% in 2020, which would result in a deficit of 2% of GDP next year.

Unexpected higher activity in August and pauses further cuts in the MPR

August's Imacec had an expansion of 3.7% y / y, well above what was expected. The result is explained by a solid growth in mining (5.3%), demonstrating that the inconveniences of the beginning of the year have gone, and by a good performance of the non-mining sectors (3.5% y / y, 0.9% m / m seasonally adjusted).

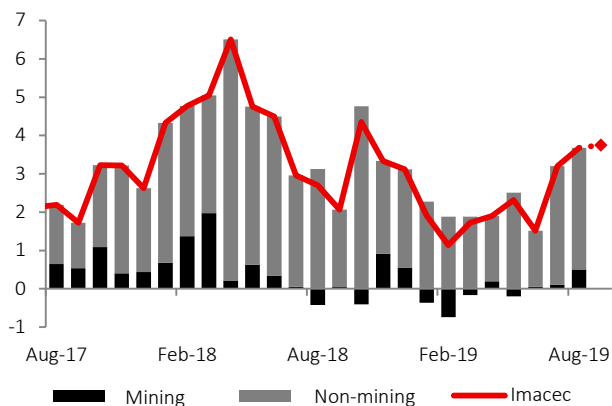
The growth of the non-mining sectors was influenced by services and construction. The latter has been showing high dynamism for several months, driven by real estate activity - benefiting from the drop in rates; while services have improved due to the end of the teachers' strike.

This surprise eliminates the possibility of a TPM cut in the next RPM in October. However, it is still too early to assess whether this surprise is temporary or marks a change in trend. We estimate that if the economy continues to show strength, the process of cuts would be suspended this year and the MPR would close at 2%. If the next Imacec surprises downwards, if inflation remains limited or if the risk of the external scenario increases, there may be an additional cut in December.

On the other hand, in September power generation shows an expansion of 0.4% y / y (0.7% in August), and business confidence is rather stable (IMCE without mining: 47.16 vs. 47, 74 in August). With this background, we project an Imacec between 3.5% and 4%. **We maintain our growth projection at 2.4% for the year. However, given**

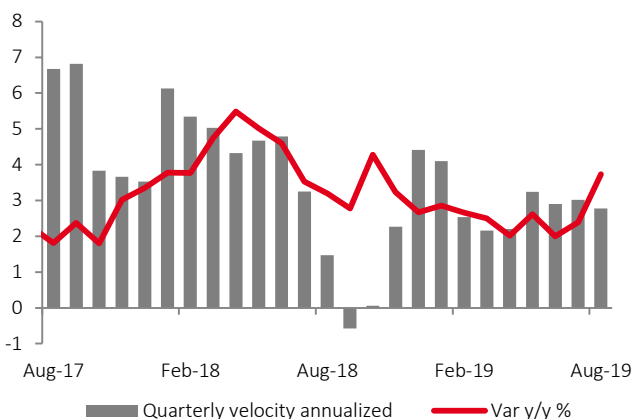
the positive surprise of the month, we estimate that the risks of further downward revisions have decreased considerably.

Graph 1: Imacec and components (annual var. %)



Source: BCCh and Santander

Graph 2: Imacec without mining seasonally adjusted (%)

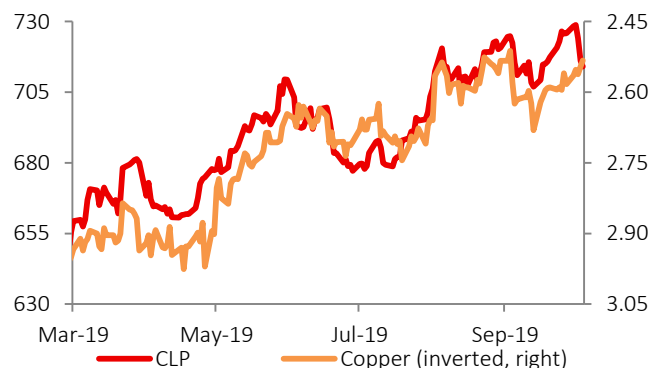


Source: BCCh and Santander

Exchange rate appreciated in line with the global weakness of the dollar

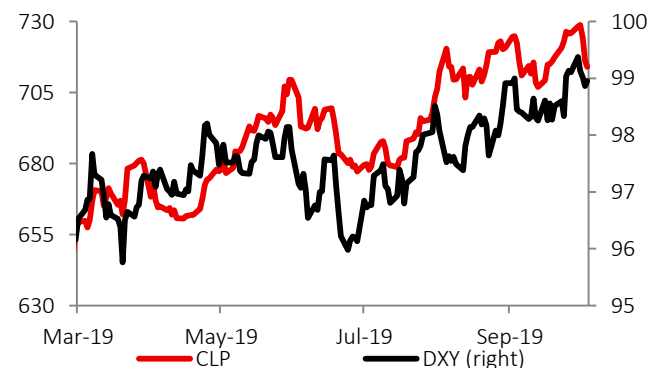
The local currency strengthened and went from trading at levels close to \$ 730 to under \$ 715. This appreciation of the peso was in line with the international trend and the weakening of the multilateral dollar. The trend of the American currency was explained by fears of a US slowdown. The September manufacturing indicator was below what was expected by the market and reached the lowest level since 2009. In addition, job creation was under the estimate of the surveys (136 thousand versus 145 thousand expected) and wages grew at a rate of 2.9%, the lowest in a year. In contrast, the unemployment rate continued to decline and stood at a minimum of 3.5%.

Graph 3: Exchange rate and Copper price (\$/US\$, US\$/lb.)



Source: Bloomberg and Santander

Graph 4: Exchange rate and DXY (\$/US\$, Index)



Source: Bloomberg and Santander

The lower pressure on wages gives the Federal Reserve more space to continue increasing the monetary impulse, which could subtract pressure on the peso. However, a greater slowdown in the US economy would generate

aversion to higher risk assets and the factors that appreciated the peso this week would eventually push up the local currency.

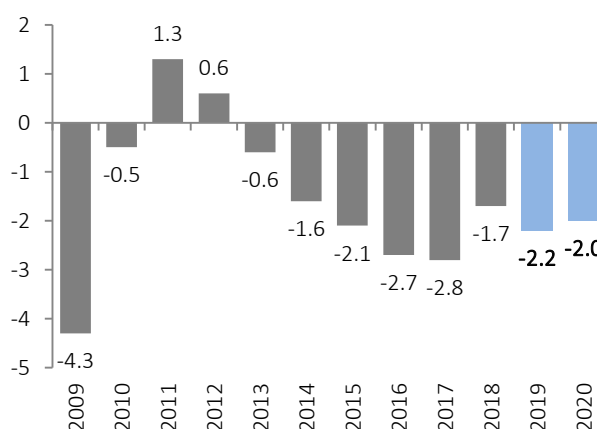
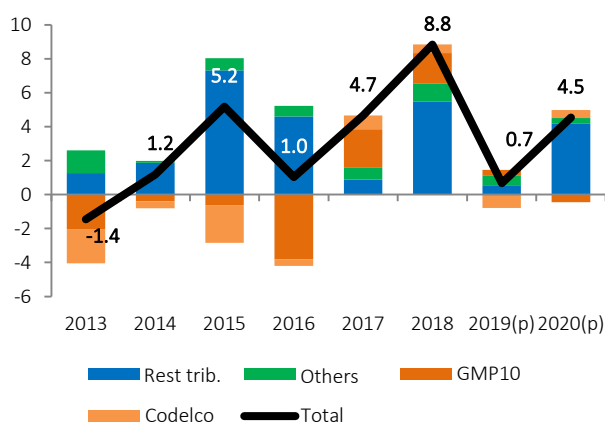
Government projects lower tax revenues in 2019 and 2020

The Public Finance Report (IFP), released by the Ministry of Finance, provided details regarding the impact of the deterioration of the macro context on public finances. In the document it is estimated that fiscal revenues would close this year with a real expansion of 0.7%, in contrast to 1.6% in June and well below the March estimate, which was steep above 5%. Notwithstanding the foregoing, the fall in the price of copper and the lower effective growth imply that the cyclical gaps are wider than previously estimated, which generates a positive impact on structural revenues. Thus, the Government estimated that the structural deficit will close 2019 at 1.4% of GDP, two tenths below the goal announced for the year.

Regarding the fiscal proposal for 2020, the IFP projects that revenues will grow 4.5% (versus 6% projected in June), mainly driven by the taxation of non-mining taxpayers. This estimate assumes a recovery in activity - with a GDP expanding 3.3% and domestic demand growing 3.6% -, a price of copper averaging US \$ 2.85 per pound, in addition to assuming the effects of the Tax Reform from January 2020. Although these assumptions are plausible, they do not appear to be conservative in a context of high uncertainty regarding both the external scenario and the final impact of the tax reform.

The budget proposal of the Executive considers an increase in expenditure of 3.6% compared to the estimated execution for this year, with which the fiscal deficit would reach 2% of GDP in 2020. In our baseline scenario we consider that both GDP and the price of copper will be somewhat smaller than estimated in the IFP. In a scenario like that, the fiscal deficit could be between 2.2% and 2.4% of GDP, so that the government's debt could next close over 28% of GDP.

Graph 5: Government income by component (annual var. %) **Graph 6: Effective fiscal balance (% of GDP)**



Note: 2019 and 2020 projections correspond to the IFP of the Ministry of Finance. Source: Dipres and Santander

DATA THAT WAS PUBLISHED / this week

DAY	COUNTRY	INDICATOR	PERIOD	PREVIOUS	ESTIMATION	ACTUAL
MONDAY 30	Chile	Unemployment rate	August	7.2%	7.2%	7.2%
	Chile	Industrial production y/y	August	2.6%	2.0%	1.4%
	Chile	Manufacturing production	August	5.7%	-2.3%	-1.5%
	Eurozone	Unemployment rate	August	7.5%	7.5%	7.4%
	China	PMI Official manufacturing	September	49.5	49.6	49.8
	China	PMI Caixin manufacturing	September	50.4	50.2	51.4
TUESDAY 1	Chile	IMACEC	August	3.2%	2.6%	3.7%
	US	PMI Markit manufacturing	September	51.0	51.0	51.1
	Eurozone	PMI Markit manufacturing	September	45.6	45.6	45.7
	Eurozone	Underlying inflation y/y	September	0.9%	1.0%	1.0%
WEDNESDAY 2	US	Employment ADP	September	195k	140k	135k
THURSDAY 3	Chile	Retail sales	August	1.8%	1.2%	2.3%
	US	Unemployment requests (thous)		213k	215k	219k
	US	PMI Markit Services	September	50.9	50.9	50.9
	US	PMI ISM non-manufacturing	September	56.4	55.0	52.6
	US	Durable goods orders	August	0.2%	--	0.2%
	Eurozone	PMI Markit Services	September	52.0	52.0	51.6
	Eurozone	Retail sales	August	2.2%	2.0%	2.1%
FRIDAY 4	US	Non- agriculture job creation	September	130k	145k	136k
	US	Unemployment rate	September	3.7%	3.7%	3.5%
	US	Salaries per hour y/y	September	3.2%	3.2%	2.9%
	US	Commercial balance	August	-\$54.0b	-\$54.5b	-\$54.9b

DATA THAT WILL BE PUBLISHED / next week

DAY	COUNTRY	INDICATOR	PERIOD	PREVIOUS	ESTIMATE
MONDAY 7	Chile	Commercial balance	September	\$143m	--
	Chile	Nominal salaries y/y	August	5.0%	--
	Chile	Car sales	September	33059	--
	Eurozone	Sentix confidence		-11.1	-12.5
	China	International reserves	September	\$3107.18b	\$3104.00b
	China	PMI Caixin Composed	September	51.6	--
	China	PMI Caixin Services	September	52.1	52.0
TUESDAY 8	Chile	Inflation m/m	September	0.2%	0.3%
	Chile	Inflation y/y	September	2.3%	--
	US	Producer price index y/y	September	1.8%	--
WEDNESDAY 9	US	Employment survey (JOLTS)	August	7217	--
	US	Minutes FOMC		--	--
THURSDAY 10	Chile	Economic expectations survey		0	0
	US	Inflation m/m	September	0.1%	0.1%
	US	Inflation y/y	September	1.7%	1.9%
	US	Underlying inflation y/y	September	2.4%	2.4%
	US	Unemployment requests (thous)		219k	--
FRIDAY 11	US	Consumer Confidence U. of Michigan	October	93.2	92.3


Research

FINANCIAL DIVISION


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

CONTACT

 (56 2) 2320 1021

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