

Withdrawal from pension funds will partially contain deterioration of the activity

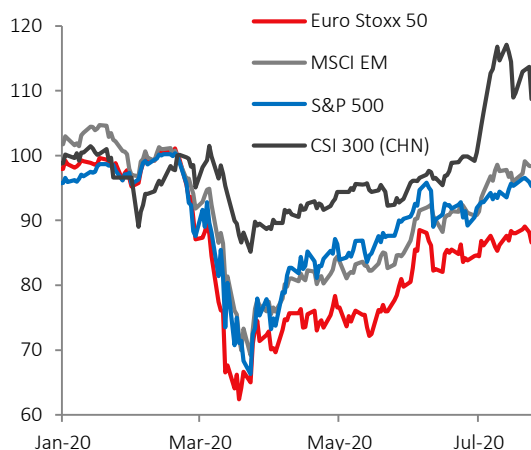
Mixed movements were recorded in global markets as evidence of the economic recovery has been tempered by outbreaks of the pandemic.

Approval of historic fund marks new step in European tax integration

The agreement for the constitution of a € 750,000 million fund, financed through joint debt issues of the countries of the European Union (mutual loans), marks a new milestone in the fiscal integration of the member countries. This, because the European Union will be obliged to pay the debt through its budget. If necessary, it could obtain additional resources from the states that make up the community. Of the total, € 360,000 million will go to loans and the remaining € 390,000 million to grants. The foci of the initiatives financed with these instruments are (1) the European Green Pact, (2) digitalization and (3) resilience to new situations such as the one generated by the pandemic. The distribution of funds in 2021 and 2022 between geographies will be linked to the evolution of unemployment in the countries during the period between 2015 and 2019 and in 2023 it will be replaced by a criterion based on the evolution of GDP. The European Council, by qualified majority, must approve the plans presented by the countries.

The announcement led to a strong appreciation of the Euro (1.7% for the week). This agreement, added to promising news about a vaccine, brought temporary optimism in the markets. However, the fear that a slow recovery in employment will slow the recovery has dampened expectations. Thus, the S&P500 fell 0.1% in the week, the Eurostoxx50 falling 1.5% and the Shanghai Stock Exchange losing 0.9%. Meanwhile, long term rates remained relatively stable.

Concern over medium-term economic recovery pushes back stock indices



Source: Bloomberg and Santander

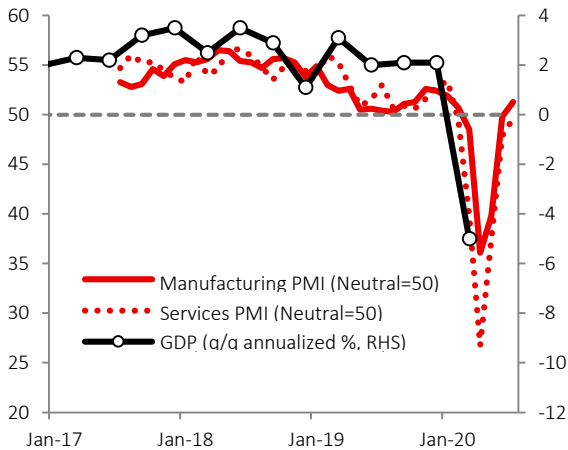
Approval of the European fund leads to a strong appreciation of the Euro



Source: Bloomberg and Santander

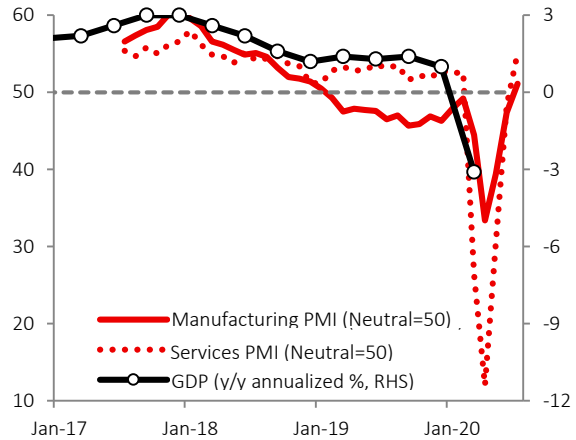
On the activity side, July PMIs in the US continued to show progress in the economic recovery, but slower than in May and June. The manufacturer scored 51.3 points, somewhat below what was expected, while the service sector remained in the contraction zone (49.6). This, in a scenario where mobility has slowed again due to the outbreaks of the pandemic. In Europe, PMIs were located in the expansion zone, led by the recovery in France and Germany.

The US PMIs reflected a slowdown in the process of opening up the economy



Source: Bloomberg and Santander

In Europe the recovery has been quicker



Source: Bloomberg and Santander

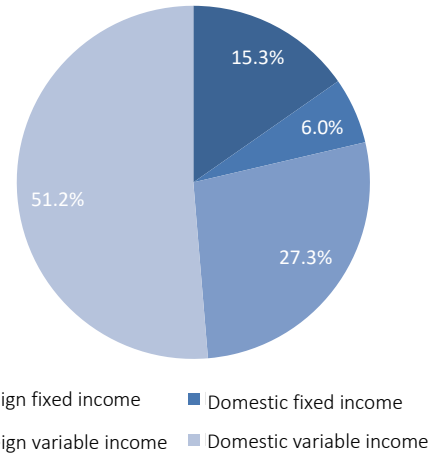
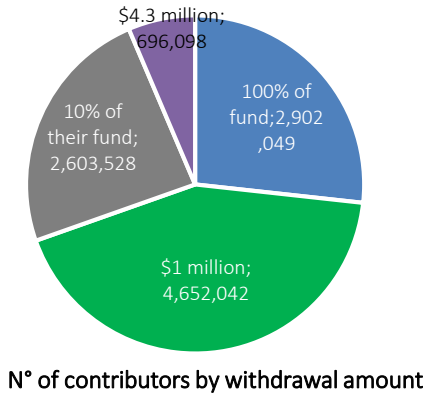
Withdrawal from pension funds will provide a temporary and limited stimulus to the economy

This week the constitutional reform was approved that allows each member of the AFP system - including pensioners for old age or disability - to withdraw 10% of the balance of their individual accounts, with a minimum of 35 UF, in case they have that amount saved, and a maximum of 150 UF. If an affiliate has less than 35 UF (approx. Ch\$ 1 million) they will be able to withdraw their entire balance. Based on the latest statistics on balances in individual accounts, we estimate that the maximum amount to be withdrawn would be between US \$ 17.5 billion and US\$ 18 billion. Most of the contributors (43%) will be able to withdraw the minimum of 35 UF, while 27% could withdraw the full balance of their funds.

It is expected that the greatest effect of the liquidation of funds will be observed in interest rates, since more than 50% of the portfolio is invested in national fixed income. However, at the closing of this report, the Central Bank announced that it would substantially increase the amounts of purchase of bank bonds (US\$ 4.6 billion), thereby mitigating the possible impact on rates. On the other hand, since local equities only represent 6% of the portfolio, the effects on the stock market should be less. On the other hand, it is not ruled out that a relevant fraction of the withdrawn funds are reinvested in instruments with a composition similar to that of current portfolios, which should also mitigate the impact on prices.

Almost 70% of contributors could withdraw \$ 1 million or less, and 27% could withdraw the total of their funds

The fund assets are invested mainly in domestic fixed income instruments



Source: Santander based on Superintendency of Pensions

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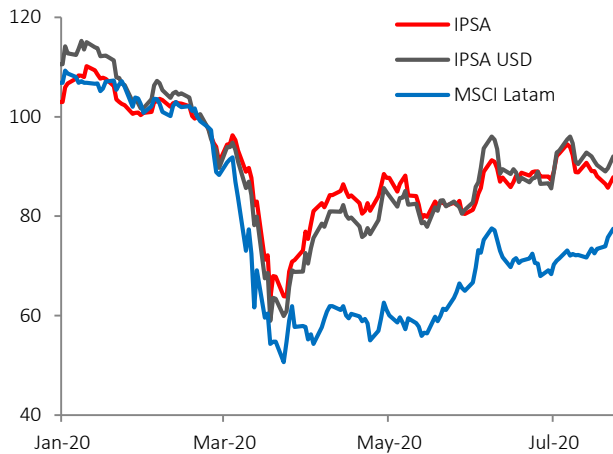
The withdrawal of funds implies a very substantial injection of liquidity into the economy. In the case of people who have suffered significant falls in their income, it is expected that they will exercise the possibility of withdrawing their funds. In the case of the least affected people, the fact that withdrawals do not constitute income for tax purposes - and therefore are exempt from paying taxes - can constitute an important incentive in the same direction. If all funds are withdrawn, the injection of liquidity would be of the order of 7% of annual GDP. A fraction of these resources, which could be more than half, will be saved under a different legal framework or used to amortize debts of a different nature. The remaining resources will be used for consumption of both habitual and durable goods. The latter tend to be produced abroad, so imports will increase. For its part, depending on the quarantine situation, the local supply may respond to the greater demand by increasing production, which will translate into a higher level of activity. In the event that there is no response capacity of supply, it will generate pressure on prices. Given these elements, it is possible to foresee that the net effect on activity will be between 1pp and 2pp and will be concentrated in the second half of the year. In our next Monthly Economic Outlook we will update the growth projections for the year, incorporating the possible impact of the withdrawal of funds.

On the other hand, this withdrawal will have important fiscal consequences. According to estimates by the Budget Office, the fiscal impact would be of the order of US \$ 6,000 million in the long term, mainly due to the greater demand for basic solidarity pensions (US \$ 3,876 million in present value according to DIPRES). In the short term, the tax expense generated by the fact that withdrawals are not subject to income tax is of the order of US \$ 750 million, while the tax benefits of those taxpayers who transfer the funds from their Mandatory account to Voluntary Pension Savings could amount to US \$ 1,370 million.

Local markets react cautiously

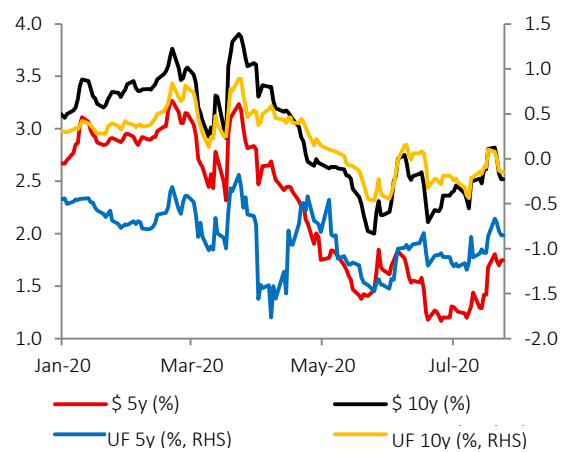
Since the project was approved in general in the Chamber of Deputies, the IPSA accumulates a decrease of 5%, in a context where Latin American markets showed progress. In the last week, however, the stock market showed greater stability, realizing that most of the effects are probably already incorporated in prices. In the case of fixed income, after increases in long term rates during the past week, this week there have been reductions after the Central Bank indicated t it would take safeguards to avoid excessive volatility, which translated into the announcement of the purchase of bank bonds reported today.

The evolution of the IPSA shows that the effects of the liquidation should be limited



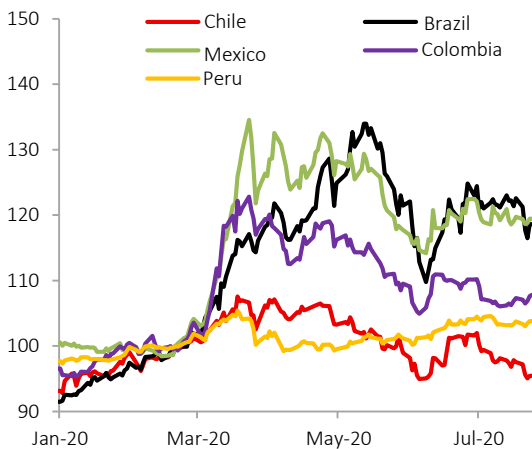
Source: Bloomberg and Santander

Rates reducing in the recent days, after two weeks of increases



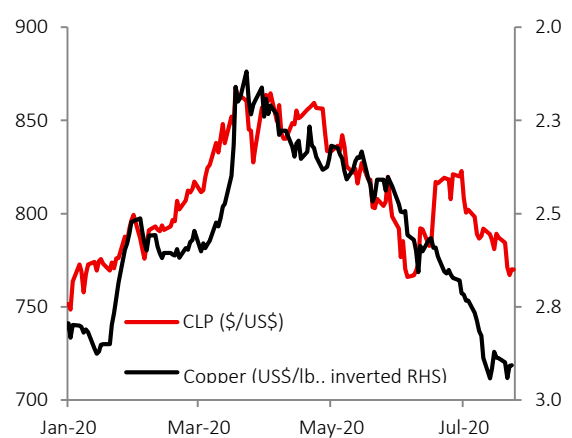
Source: BCCh, RiskAmerica and Santander

The Peso appreciated 2% in a week where emerging currencies remained stable...



Source: Bloomberg and Santander

... and copper tended to recede, although maintaining high levels



Source: BCCh, RiskAmerica and Santander

The exchange rate has appreciated intensively (around 2% in the week), which is consistent with the expectation of liquidation of funds abroad that would increase the flow of foreign currency to the country, in a context where the copper price has remained high.

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