CÁMARA
CHILENO BRITÁNICA
DE COMERCIO

Chilean Economic Report
Second Quarter 2024

2nd Edition 2024 — Produced since 1922

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Dear Members and Friends,

I am pleased to introduce the latest edition of our Chilean Economic Report, designed specifically for businesses looking to understand the dynamics shaping the Chilean economy.

Reflecting on the current economic landscape, I am encouraged by the resilience displayed as Chile's economy continues to grow. This expansion, driven by rising consumption and recoveries in several sectors, positions Chile for its strongest performance in three years, with projected growth between 2.25% and 3.00%. However, challenges remain, particularly as inflation exceeds 4.0%, influenced by a weakened Chilean peso and rising energy costs. While the Central Bank of Chile is committed to steering inflation towards its 3% target by 2026, recent adjustments in monetary policy indicate a cautious approach to further easing.

The economy's growth is highlighted by significant advances in the commodities sector, especially in copper. Record-high prices and strategic initiatives in lithium underscore Chile's pivotal role in global markets, boosting exports and narrowing the current account deficit. This quarter's report delves into the progress of President Boric's lithium strategy over the past year, including public/private partnerships aimed at expanding lithium production—demonstrating Chile's ambition to solidify its global leadership in this critical industry.

In recent months, we have noted a decline in business confidence, signalling ongoing challenges in key sectors such as construction and retail. Additionally, media

Elle Denton

Executive Director

British Chilean Chamber of Commerce

Santiago, Chile

attention has focused on rising energy prices as the government phases out subsidies introduced during the pandemic. This transition aims at fiscal sustainability, , but presents immediate challenges for Chilean families and businesses, with expected increases in household bills starting this July.

Amidst these economic shifts, Chile's social and political landscapes are evolving, supported by growing public backing for recent policy announcements on student debt and abortion laws. These developments set the stage for the upcoming regional elections.

I would like to extend my gratitude to Tom Azzopardi and the Chamber's Economic Editorial Board for their efforts in compiling this edition. Their dedication and expertise have once again produced a valuable resource for our members.

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Key points

• The Chilean economy has continued to grow into the second quarter, driven by rising consumption and recoveries in several sectors.

• Although growth will slow down in the second half, the Central Bank expects the economy to expand by 2.25-3.00% in 2024, its fastest rate in three years.

• The weaker Chilean peso and higher energy prices have contributed to a rise in annual inflation to over 4.0%. Convergence with the Central Bank's 3% target rate has been delayed until 2026.

• In response, the Central Bank has slowed its loosening of monetary policy, implementing a 25-basis point cut at its most recent meeting in June and playing down the likelihood of further cuts.

• As the economy heats up, unemployment has fallen to 8.3% but remains far above pre-pandemic levels.

• Despite the rise in economic activity and the fall in inflation since last year, business and consumer confidence remain in negative territory.

• Copper prices soared to record levels above US$5.00/lb in May, boosted by supply shocks and speculative buying. These have boosted exports, widening Chile's trade surplus and narrowing its current account deficit this year.

• The Chilean peso recovered against the US dollar to around CLP910/ dollar by mid-July, reflecting higher copper prices and convergence of monetary policy in both countries.

• State copper company Codelco has signed a deal to take control SQM's lithium operations in Chile, a key part of President Boric's lithium strategy

• Support for the government has risen ahead of regional elections later this year following government announcements on student debt cancellation and liberalisation of abortion laws.

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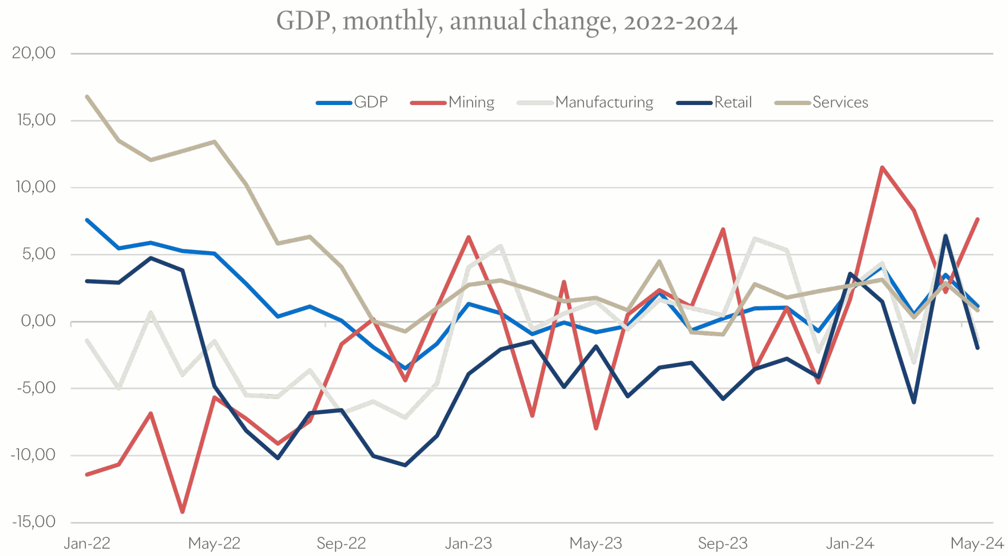
Domestic Economic Performance

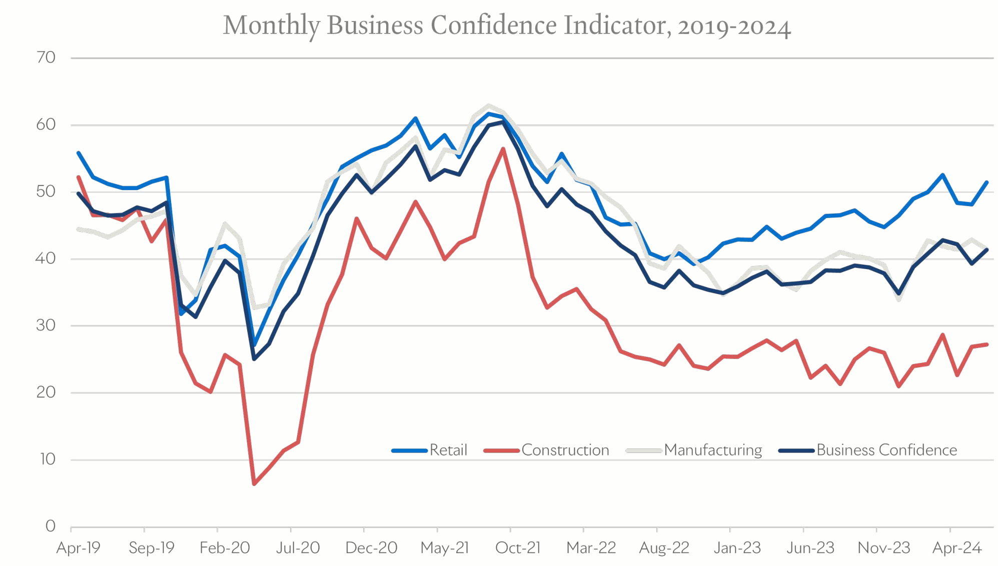
1



Source: Central Bank of Chile

The Chilean economy has begun to grow again after a contraction in 2022-2023, driven by a recovery in consumption. After expanding by 2.3% in the first three months of the year, preliminary data suggests that activity expanded by 3.5% in April and 1.1% in May. In April, growth was led by the services sector (up 2.9%), which accounts for 50% of GDP, as well as manufacturing and retail. In May, slower growth in services was compounded by a fall in retail activity.

Growth is expected to continue into the second half of the year although at a slower pace, reflecting the higher base of comparison. In its latest Monetary Policy Report, the Central Bank predicted that the economy would grow by 2.25-3.0% this year (compared with 2.0-3.0% predicted in March). The expansion would be driven by consumption which should expand by 2.8% (up from 2.0% forecast in March), including a 2.5% increase in household consumption. Meanwhile, investment is expected



Source: Central Bank of Chile

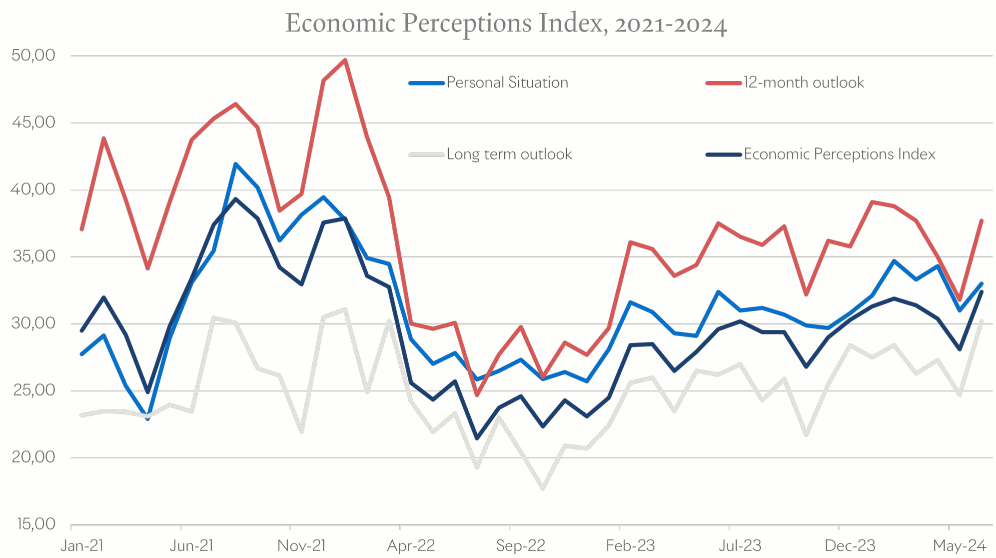
to be less of a drag on growth than previously expected, contracting by just 0.3% in 2024, compared with 2.0% forecast three months earlier.

The Bank forecast that activity would slow to 1.5-2.5% in 2025 and 2026 as a recovery in investment is offset by a slowdown in consumption.

Business Confidence

Business confidence has stabilized in recent months but remains in negative territory. The Monthly Business Confidence Indicator, produced by Adolfo Ibáñez University and business organisation ICARE, reached 41.37 points in June, up five points from twelve months earlier. While confidence in the construction industry remains near record lows (27.27 points in June), confidence in the retail sector moved back into positive territory.

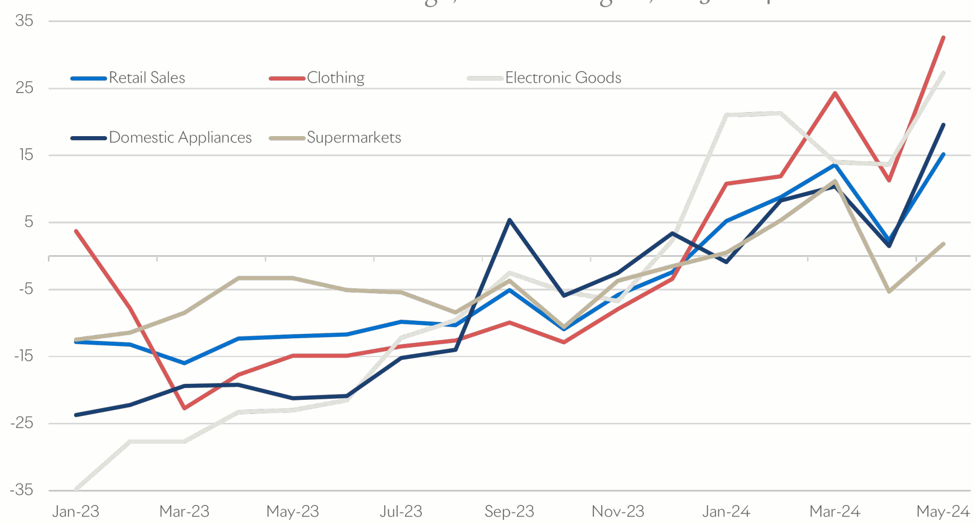
Consumer Confidence



Source: GfK

Consumer confidence has strengthened in recent months albeit from historically low levels. In June, GfK's Economic Perceptions Index reached 32.4 points, its highest level in more than two years, reflecting increased optimism about the economic outlook.

Retail Sales in Santiago, annual change %, 2023-2024



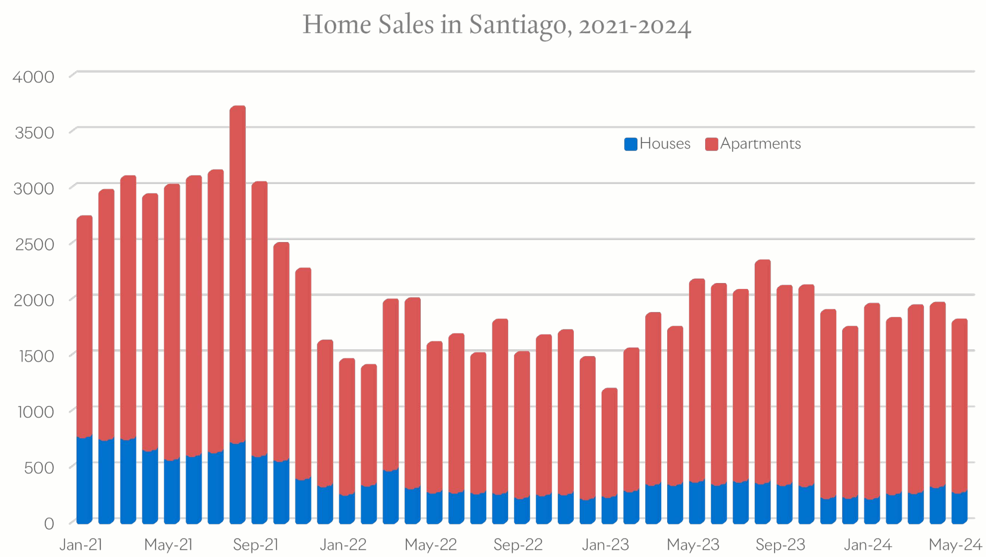
Source: National Retail Chamber

Retail has continued to recover from the slump triggered two years ago by the rise in inflation and the end of pensions withdrawals and other pandemic support measures. Retail sales in Santiago rose by 15.2% in the year to May, after declining 10% last year, driven by increased sales of electronic goods, clothing and domestic appliances.

The recovery has not spread to car sales which declined by 10.2% in the first six months of the year, after falling by more than a quarter in 2023.

Construction

There has been no let-up for the building industry where activity has continued to decline in line with falling investment, high interest rates and low home sales. The IMACON index produced by the Chilean Chamber of Construction fell to a record low in March, reflecting declines in sales of building materials, construction authorisations and other indicators.



Source: InfoInmobiliaria

Despite the fall in interest rates since mid-2023, the housing market has seen no improvement this year with home sales in the greater Santiago area falling in May to their lowest level since last December.

Manufacturing

Manufacturing activity fell 2.2% in the year to May, driven by a drop in the production of plastics and machinery, offset by a rise in machinery maintenance on increased orders from the mining industry.

Bottling the sun

Chile is set to become a leading country in the deployment of energy storage systems, attracting significant investment and strengthening the efficiency and reliability of its electricity system.

By developing its huge potential for renewable technologies such as wind and solar, the country has transformed its electricity system over the last decade, reducing its reliance on imported fossil fuels and associated carbon emissions and cutting energy costs.

But further development is limited by the intermittent nature of solar and wind power as well as the lack of transmission capacity required to move electricity from solar parks and wind farms largely located in the far north to the population centres around Santiago.

Chile's lengthy environmental approval means new power lines cannot be built quickly. Some renewable plants have even faced bankruptcy as the shortage of transmission capacity means they are unable to supply customers.

An alternative solution would be to store renewable power as it is generated and sell it to local customers e.g. mining companies or power distributors when it is needed. Typically, this involves a lithium battery - similar to the ones found in electric vehicles but on a much larger scale - either linked to a renewable energy facility or stand-alone. HYDROGEN??? DATA CENTER&AI????

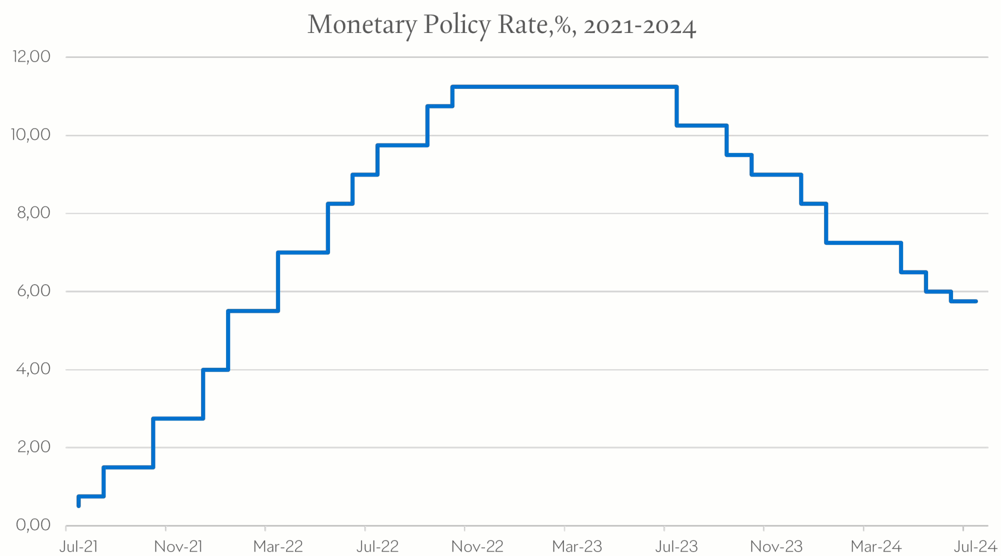
Energy firm AES Andes installed Chile's first battery energy storage system (BESS) in 2009. But the technology received a major boost in 2022 when Congress approved legislation allowing storage facilities to receive capacity payments like conventional generators.

Following the regulatory change, investment is booming. According to renewable energy association ACERA, storage capacity is expected to rise from 177MW at the end of 2023 to 869MW by next December. The National Electricity Commission now estimates that 4GW of energy storage could be installed in Chile by 2032.

Earlier this year, Engie installed a 139 MW unit, the largest in Latin America, at its Coya solar plant in Antofagasta. But companies are now looking at even larger capacities using alternative technologies, such as molten salt and stored hydropower.

Last year, AES was granted approval for a US$450 million facility that could store energy in the form of molten salt. Colbún plans to invest US$1.4 billion in an 800MW plant that would generate electricity by moving water between two reservoirs.

Another option gaining ground would be to use renewable power to produce hydrogen which could be transported to where it is needed.



Source: Central Bank ofChile

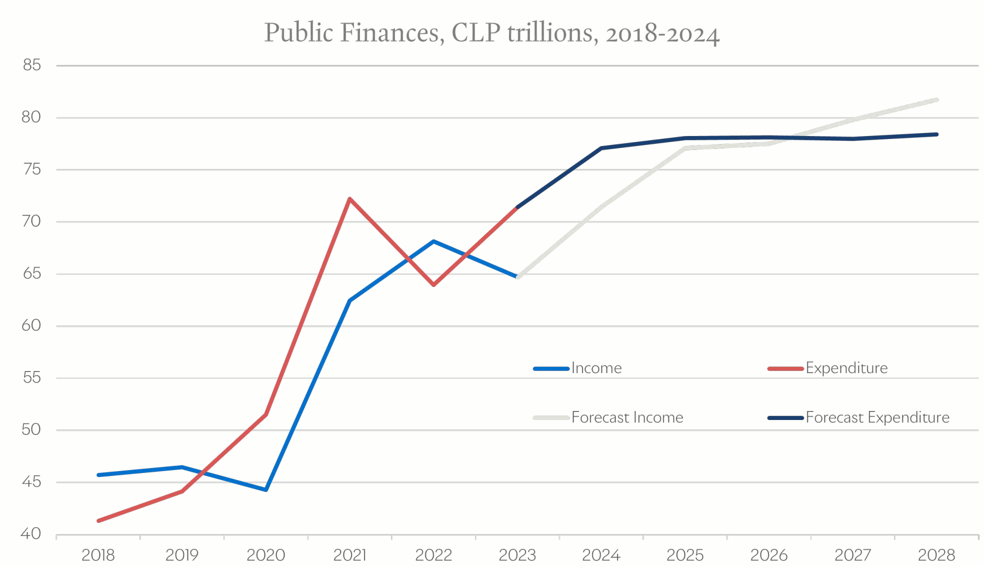
The Central Bank has slowed the loosening of monetary policy following a surge in inflation in recent months (See 1.5 Domestic Prices). On June 18th, the board voted unanimously to reduce its benchmark interest rate to 5.75%, the rate's lowest level in more than two years. But the cut of just 25 basis points is the smallest since the Bank began reducing rates a year ago.

With inflation now not expected to return to the Bank's medium term target rate of 3.0% until 2026, analysts surveyed in early July expected the rate to end the year at 5.25%, compared with 4.25% predicted in February.

Chile's public deficit is expected to reach CLP 5.6 trillion (US$6.1 billion) this year, the equivalent to 1.9% of GDP, according to the Budget Office's latest forecast, down 2.4% in 2023 and unchanged from the government's previous forecast made last February.

Spending is expected to rise by 4.9% in real terms to CLP 77.1 trillion (US$83.3 billion), in line with the budget legislation passed by Congress last year. Government income is expected to grow by 10.4% to CLP 71.4 trillion (US$77.1 billion), as stronger economic activity boosts tax revenues.

The government expects to receive an additional US$1.0 billion as a result of the higher copper prices, which are now expected to average US$4.20/lb this year, up from US$3.84/lb forecast in April. However, much of the gain will be offset by the sharp drop in lithium prices over the last year.



Source: Budget Office

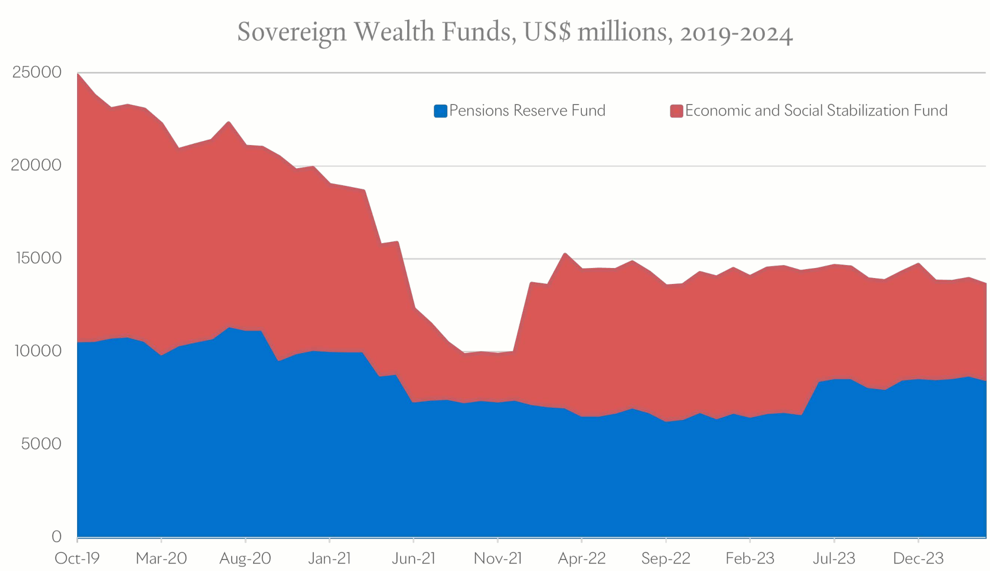
The government continues to expect that it will be able to close the structural public deficit (calculated using long-term forecasts for GDP growth and copper prices) by the end of its four-year term in 2026. This forecast assumes that government revenues will rise by over 5.0% annually during the next five years (as the economy grows by more than 2% annually) while public expenditure will remain flat.

Credit Ratings

Fitch Ratings	A- (stable)
S&P Global Ratings	A (negative)
Moody's	A2 (stable)
JCR	AA- (stable)

Despite significant market expectation following the expansion of Chile's sovereign debt over the last two years, there has been no downgrade of the country's sovereign rating. Fitch Ratings and Moody's have both recently reaffirmed their current ratings (A- and A2 respectively) and stable outlooks, citing the country's stable macroeconomic framework and relatively low GDP-debt ratio. S&P Global Ratings has made no change since lowering its outlook to negative last October

Sovereign Wealth Funds



Source: Ministry of Finance

By the end of April, Chile's two sovereign wealth funds held assets worth US$13.6 billion, down 6.6% from a year earlier, reflecting losses on investment and withdrawals made from the funds late last year.

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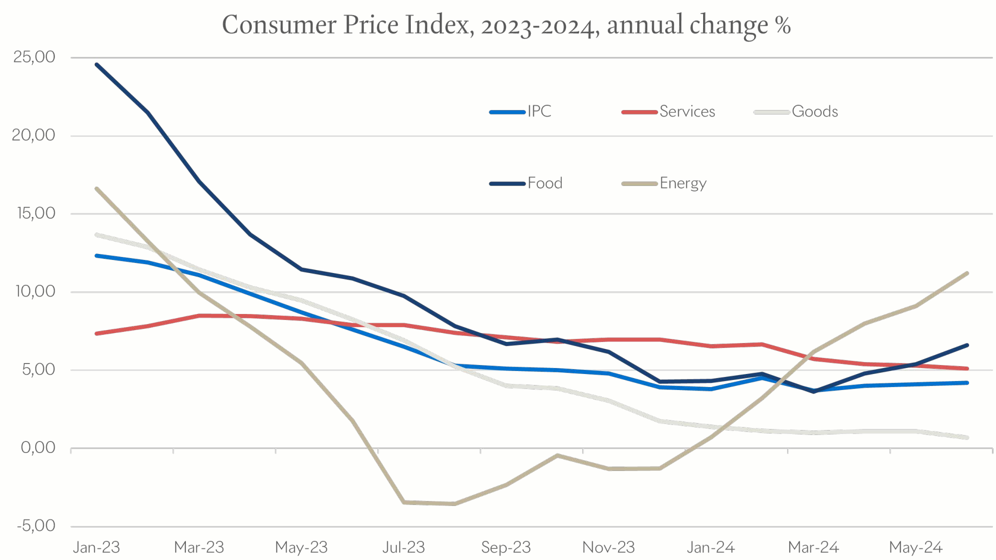

Source: National Statistics Institute

After declining sharply during 2023, inflation has begun to rise again driven by rising food and energy prices. After increases of 0.5% and 0.3% in April and May, the government's Consumer Price Index fell by 0.1% in June, lifting annual inflation to 4.2%, up from 3.9% at the end of last year.

The surge has been driven by the depreciation of the Chilean peso and rise in oil prices earlier in the year as well as changes to the basket of goods introduced in January. A major driver has been petrol prices which rose to over CLP1,400 a litre (US$1.57) in May before declining.

The fall in monthly inflation in June reflected declines in some important divisions, including clothing and footwear and food and drink. However, these were largely offset by a 7.2% rise in electricity prices.

As inflation has bounced back so have inflation expectations for this year and next. In June, the Central Bank forecast that the index would end the year at 4.2%, up from 3.8% predicted in March, and end 2025 at 3.6%, rather than returning to the bank's medium term target rate of 3.0% as previously estimated. Its forecast matches those of private analysts.


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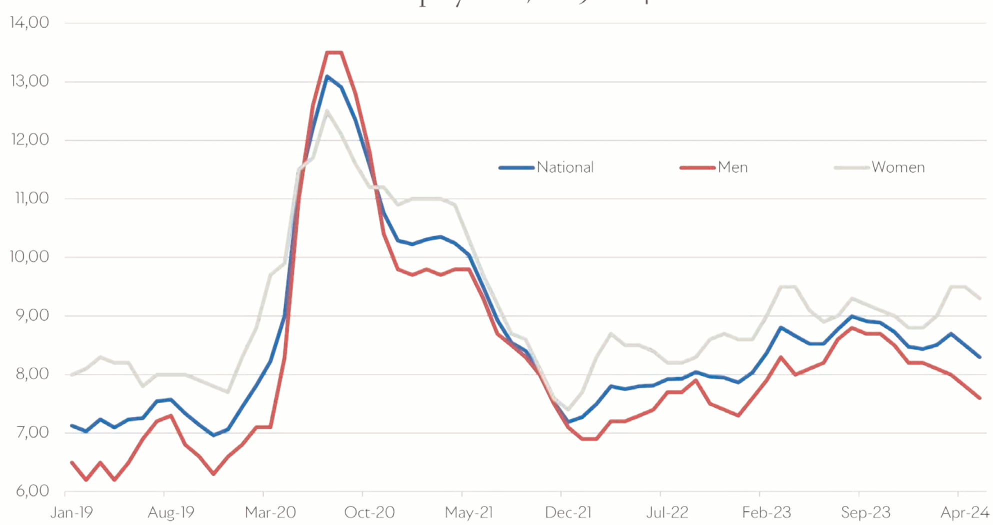
Unemployment, 2019-2024



Source: National Statistics Institute

Unemployment averaged 8.3% during the three months to May, down from 8.5% in the previous quarter and the same period of last year. While male unemployment fell to 7.6%, its lowest level in more than a year, female unemployment reached 9.3%.

The slight fall in unemployment reflects the net creation of more than 100,000 jobs since the start of the year with expansions in construction, professional services and especially public administration, offsetting losses in manufacturing, farming, and hospitality. However, the number of people out of work remains well above pre-pandemic levels even despite a large number of older people leaving the workforce prematurely.

In May, regulations came into force reducing the working week from 45 hours to 44 hours. Legislation passed last year will gradually reduce working times to 40 hours from 2028 onwards.

Wage growth slowed to 6.0% in May, down from 10.3% a year ago. In real terms, they grew by just 2.0%, their slowest rate in over a year.

On July 1st, the monthly minimum wage rose to CLP 500,000 (US$534), from CLP 460,000 previously, in line with legislation passed last year by Congress.

Source: Santiago Stock Exchange

Shares listed on the Santiago Stock Exchange have continued to rally into the second quarter, mirroring higher copper prices and the improved economic outlook. The IPSA index of the thirty largest companies listed on the exchange reached a new high of 6,810 points in late May, up almost 10% from the end of last year, before falling 3.3% in June.

Banking

Bank lending has continued to slow, with the value of outstanding loans reaching CLP 258.0 trillion (US$277 billion) at the end of May, down 1.5% from twelve months earlier. While the value of commercial loans fell 2.0% to CLP 140 trillion (US$150.8 billion), consumer lending fell 1.2% to CLP 29.4 trillion (US$31.7 billion) and mortgage lending was unchanged CLP 86.7 trillion (US$93.4 billion).

Profits in the banking sector reached CLP 2.1 trillion (US$2.2 billion) during the first five months of the year, up 1.9% from a year ago, but the after-tax return on profits fell to 15.0%, down from 18.2% in 2023.

The proportion of non-performing loans has continued to rise, reaching 2.3% of the total portfolio, including almost 3.0% for consumer loans, up from 1.9% a year ago.

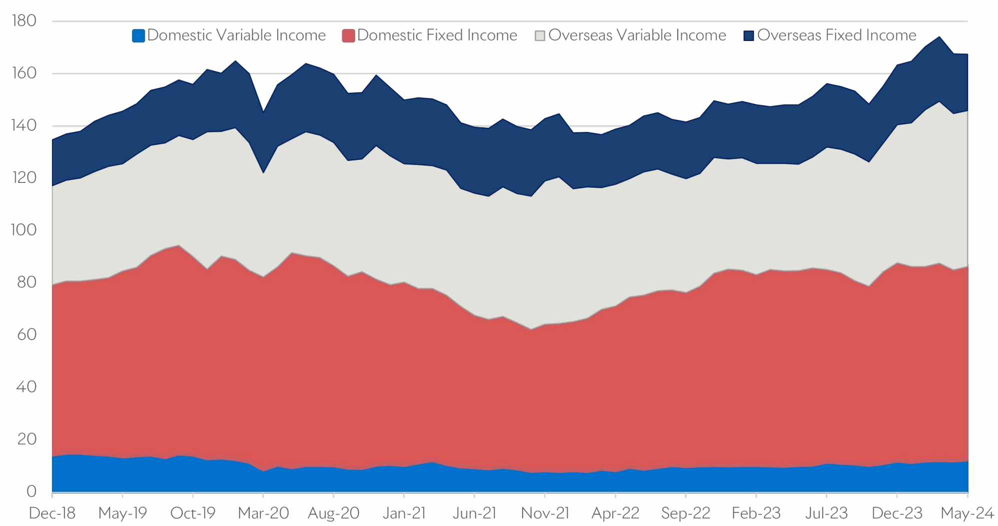
Type of fund	Amount (billions of pesos)	Change July 2023 – June 2024 (%, real in pesos)	Return July 2023 – june 2024 (%, adjusted for inflation)	Limits on equity investments (% of fund assets) Maximum	Minimum
A Funds	28,737	33.6	17.31	80	40
B Funds	35,039	33.1	13.27	60	25
C Funds	59,821	11.4	5.69	40	15
D Funds	29,342	3.9	-1.76	20	5
E Funds	20,647	-15.9	-4.21	5	0
Total	170,721	13.2			

Source: Superintendence of Pensions

By the end of June, Chile's pensions fund administrators (AFPs) held assets worth CLP170.7 trillion (US$ 187.8 billion), up 13.2% from twelve months earlier. While the riskiest A funds gained 17.3% over the last year, the conservative E funds lost 4.2%.

In April, the Central Bank announced that the proportion that pension funds can invest in alternative assets will rise from 13% currently (for A funds) to 15% from August 1st this year and then gradually to 20% by 2027.

AFPs by asset class, US$ billions, 2018-2024



Source: Superintendence of Pensions

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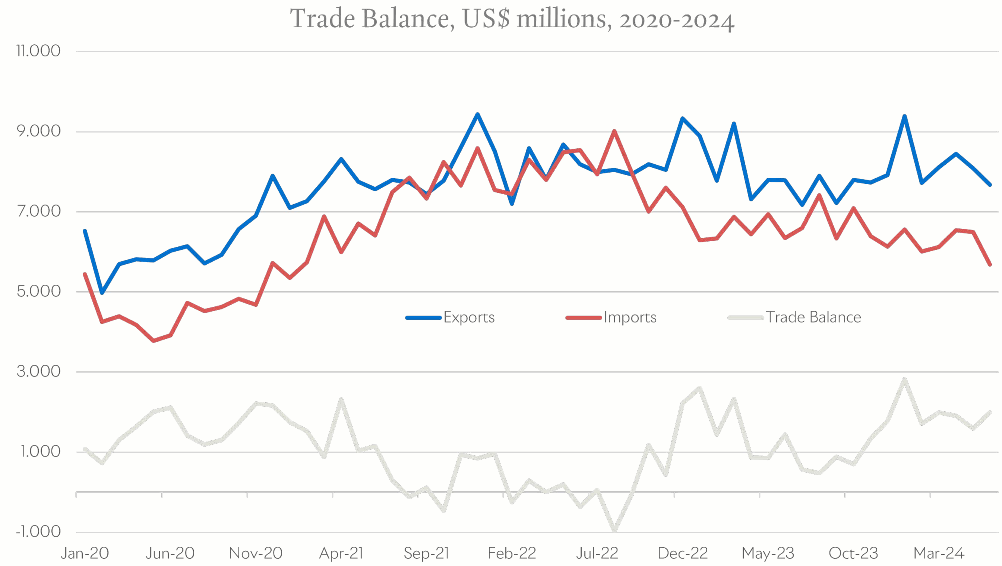
External Sector

2

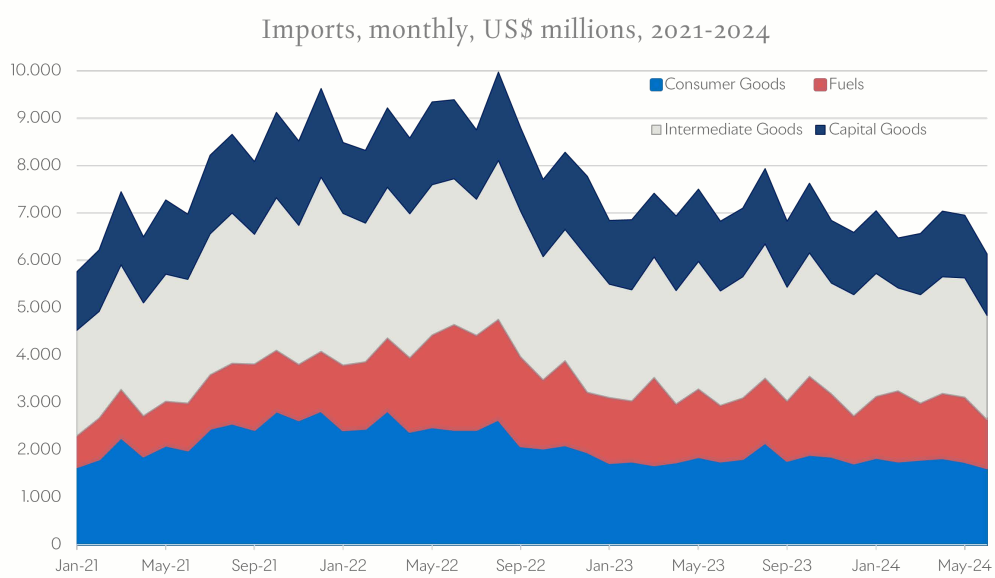
Chile's trade balance in goods reached US$12.0 billion during the first six months of the year, up from US$9.6 billion in the same period of last year, as exports rose, and imports fell. Exports rose 1.4% to US$49.5 billion, while imports fell 4.6% to US$37.4 billion.



Source: Central Bank of Chile

Imports

Reflecting the recovery in retail activity, imports of consumer goods stabilized at US$10.7 billion during the six months of the year, up 0.5% from twelve months earlier. Increased imports of electronic goods and food products were offset by a 9.6% decline to car imports to US$1.1 billion and a 28% drop in petrol imports (reflecting the maintenance closure of a major oil refinery last year).



Source: Central Bank of Chile

Higher oil and diesel imports was offset by sharp declines in imports of coal (down 30.4%) and liquified natural gas (down 32.2%) as Chile closed more coal-fired power plants and imported more natural gas from neighbouring Argentina.

Fuel imports during the first half fell 7.5% to US$7.6 billion, as lower volumes offset higher imports. The West Texas Intermediate oil price, which state oil company ENAP uses to price imports, averaged US$80/barrel during the half, up from US$75/barrel a year earlier. As well as lower oil and diesel imports, there were sharp declines in imports of coal (down 38.2%) and liquified natural gas (down 36.1%) as Chile closed more coal-fired power plants and imported natural gas from neighbouring Argentina.

West Texas Intermediate, 2022-2024, US$/barrel

Source: St Louis Federal Reserve

Imports of non-fuel intermediate goods during the half fell 3.7% to US$14.2 billion with falls in imports of chemicals, fertilizers, metallic products and spare parts for construction and mining equipment.

Reflecting the slump in investment, imports of capital goods decreased 12.1% to US$7.8 billion as imports of lorries, construction and mining equipment and motors, generators and transformers all fell sharply. However, imports during the second quarter reached US$4.0 billion, a 9.6% increase from the previous three months.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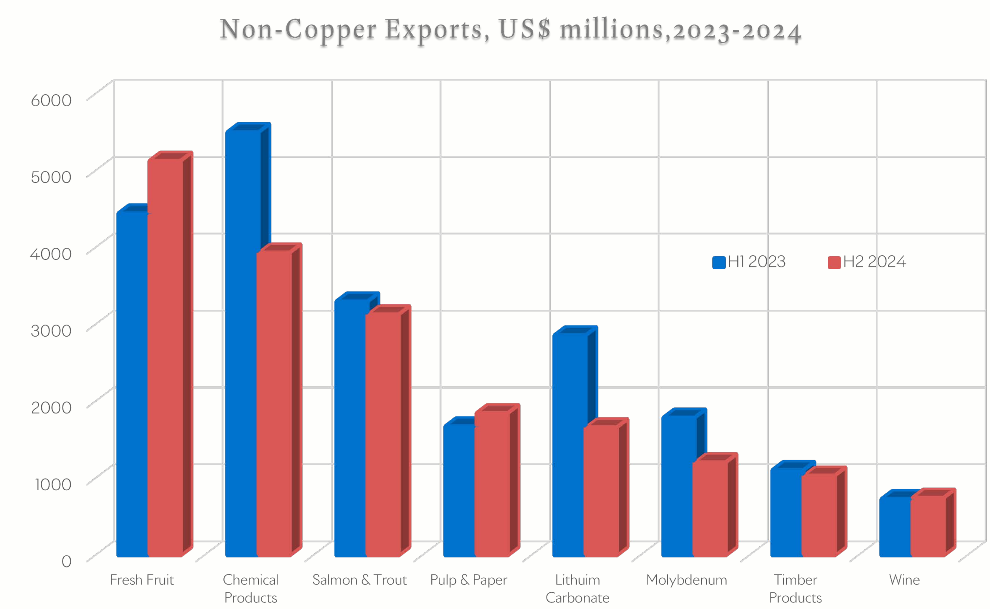
Exports



Source: Central Bank of Chile

Chile's exports during the first six months of the year rose 1.4% to US$49.5 billion, driven by higher mineral and agricultural exports.

Agricultural exports rose 11.7% to US$5.6 billion during the period, driven by a 15.4% increase in fruit exports to US$5.1 billion. Cherry exports rose 22.9% to US$2.2 billion while grape exports rose 22.1% to US$1.1 billion.

Exports of chemicals declined 28.4% to US$3.9 billion over the same period, reflecting lower prices for minerals including molybdenum oxide, lithium hydroxide and lithium sulphate.

Pulp and paper exports rose 10.2% to US$1.9 billion during the first half on increased pulp shipments. Exports of short-fibre pulp (made from eucalyptus) rose 40.8% to US$720 million while exports of long-fibre pulp (made from radiata pine) fell 20.2% to US$518 million. According to producer Arauco, the increase reflects both higher production following the launch of its Mapa project last year and higher prices. Prices in China for long-fibre pulp reached US$820/tonne in May, up 19% from a year ago.

Salmon exports during the first six months declined 4.4% to US$3.0 billion, on lower volumes and prices. Wine exports reached US$750 million, up 2.4% from the same period of last year.

Source: Chilean Copper Commission

Copper prices rallied to record levels during the second quarter, reflecting a tight supply and demand balance (following cuts to production in Central America and China) as well as speculation by financial investors in the metals markets. After breaking briefly above US$5.00/lb, prices quickly retreated but remained above levels seen in previous years, averaging US$4.42/lb in the quarter versus U$3.84/lb a year earlier.

The rally has lifted price expectations in the medium term. In May, the Chilean Copper Commission lifted its forecast to US$4.30/lb for 2024 and US$4.20/lb in 2025 (up from US$3.85/lb previously) while the Central Bank predicted in June that prices would average US$4.30/lb over the next three years.

Driven by the higher copper price, Chile's mineral exports reached US$27.7 billion during the first half of the year, up 6.9% from the same period of 2023. Copper exports rose 14.0% to US$24.0 billion, including 29.9% increase in shipments of copper concentrate to US$14.6 billion.

As well as higher prices, exports have been boosted by a recovery in mine production after the industry's dire performance in 2022-23. Production during the first five months of the year reached 2.1 million tonnes, up 3.2% from twelve months earlier. The government expects production to reach 5.5 million tonnes this year, up 5% from 2023, driven largely by output from Teck's newly expanded Quebrada Blanca mine.

Shipments of lithium carbonate fell 41.8% to US$1.7 billion during the six-month period, as higher export volumes were offset by lower prices for the mineral. Prices have fallen by more than 80% since late 2022 to around US$14,000/tonne in recent weeks.

Exports of molybdenum, a byproduct in many copper mines, fell to US$1.2 billion in the first half, down 32.4% from a year ago, reflecting lower prices and production. Mine output during the first five months of the year reached 15,153 tonnes, down 16.8%, while prices have fallen by almost 50% since early 2023.

Shipments of iron ore totalled US$881 million in the first half, up 14.1% Exports of precious metals rose 16.7% to US$911 million, reflecting higher prices.

President Boric's lithium strategy one year on

A year on since President Gabriel Boric launched the government's National Lithium Strategy, designed to boost production of the mineral as well as state participation in the industry, significant progress has been made on many fronts.

In May, following twelve months of negotiations, state copper company Codelco signed a definitive partnership to take a majority stake in SQM's lithium operation in Chile from January 2025 in exchange for extending mining rights. SQM will continue to manage the joint venture until 2031 when Codelco will assume control.

With the implementation of new extraction technologies, Codelco estimates that they could increase lithium production from the Atacama salt-flat to over 300,000 tonnes annually within a decade, from around 200,000 tonnes annually today.

However, the two companies still need approval from local indigenous communities who have expressed opposition to the deal.

Following its acquisition of Lithium Power International earlier this year, Codelco is looking for a partner to develop a smaller lithium operation on the Maricunga salt-flat, the country's second richest resource behind Atacama, with a deal expected in early 2025.

Economic development agency CORFO, which owns the claims at Atacama, has reached a deal with Albemarle, Chile's second largest producer allowing it to produce an additional 1.2 million tonnes of lithium (almost double its previous quota) during the remaining 16 years of its rental agreement.

Meanwhile, the government has opened up dozens of smaller salt-flats to private development with 36 companies showing interest in a recent Request for Information. Together these initiatives could help lift Chilean lithium production to well over 400,000 tonnes annually within a decade, Mining Minister Aurora Williams has said.

Although this would confirm Chile's position as one of the world's largest producers of the mineral, it may not be the boon to public finances that politicians had predicted. Prices for the mineral have fallen by around 80% since late 2022 as global production has boomed.

The glut of lithium in the market could affect Chile's ability to attract investment in downstream lithium industries with guaranteed supplies at preferential prices, another key part of the government's lithium strategy. A previous attempt to attract downstream investment failed in 2018 when companies walked away from contracts following a slump in prices.

Last year, the government signed deals with two Chinese firms for such investments with operations due to begin next year. BYD, the world's largest producer of electric vehicles, has since paused its US$290 million project to produce lithium cathode material in Chile although steel producer Tsingshan is continuing to make progress.

The government plans to hold another process for up to 9,500 tonnes of lithium carbonate produced by Albemarle later this year.

Trade between Chile and the United Kingdom reached US$452 million during the first five months of the year, up 16.4% from the same period of 2023.

Chilean exports to the UK rose 19.0% to US$250 million, led by increased shipments of fresh fruit and wine. Fruit exports rose 16.9% to US$104 million while Chile exported US$44 million worth of bottled wine to the UK, up 29.5%.

UK exports to Chile rose 13.4% to US$202 million. This increase was led by a 39.5% increase in shipments of intermediate goods to US$109 million while exports of capital goods to Chile fell 8.3% to US$46 million.

Finance Minister Mario Marcel will lead a delegation of Chilean business leaders and officials to London for the annual Chile Day events on September 9th-10th.

Chile recorded a current account deficit of US$104 million in the first three months of the year, equivalent to just 0.1% of GDP, down from US$3.7 billion in the previous quarter, but compared to a surplus of US$513 million twelve months ago.

The shrinking of the deficit since the end of the year reflects the expansion of the trade surplus in goods as exports rose and imports shrank.

In June, the Central Bank predicted that Chile would end the year with a current deficit of US$7.9 billion (equivalent to 2.1% of GDP), down from US$11.9 billion in 2023, as rising exports bolster the trade balance.

Financial Account

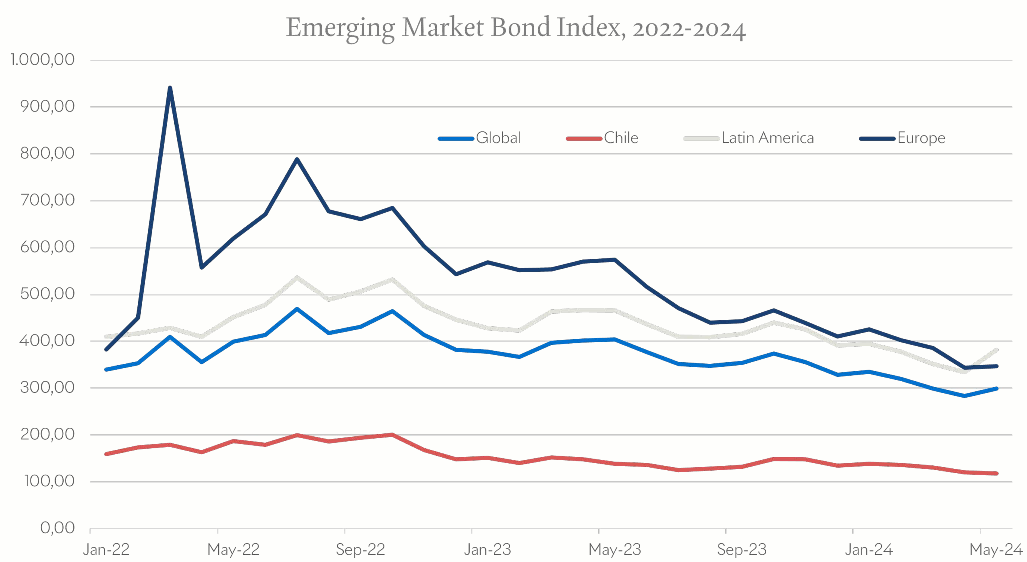
Chile's financial account deficit fell to US$683 million in the quarter down from US$887 million in the final quarter of 2024, but compared to a surplus of US$569 million twelve months earlier.

Foreign Direct Investment into Chile increased by US$4.2 billion while Chilean investment abroad reached US$1.6 billion. Foreign investment in Chilean financial assets rose by US$3.6 billion as the government and companies emitted debt abroad.

By the end of March, Chile's foreign debt reached US$241.7 billion, equivalent to 82.7% of GDP, up from US$ 241.0 billion at the end of last year. The increase was driven by corporate debt while government and banks both reduced their foreign debt as the fall in the value of Chilean peso reduced the value of debt in the local market owned by non-residents.

The fall in the value of the Chilean peso also significantly strengthened the country's net international investment position, which fell to a debt of US$53.8 billion, down US$10.1 billion from the end of last year. The fall reflected the increase in the value of assets held abroad by Chileans as a result of the peso's depreciation as well as the rally in stock markets, and the fall in the value of debts.

Country Risk

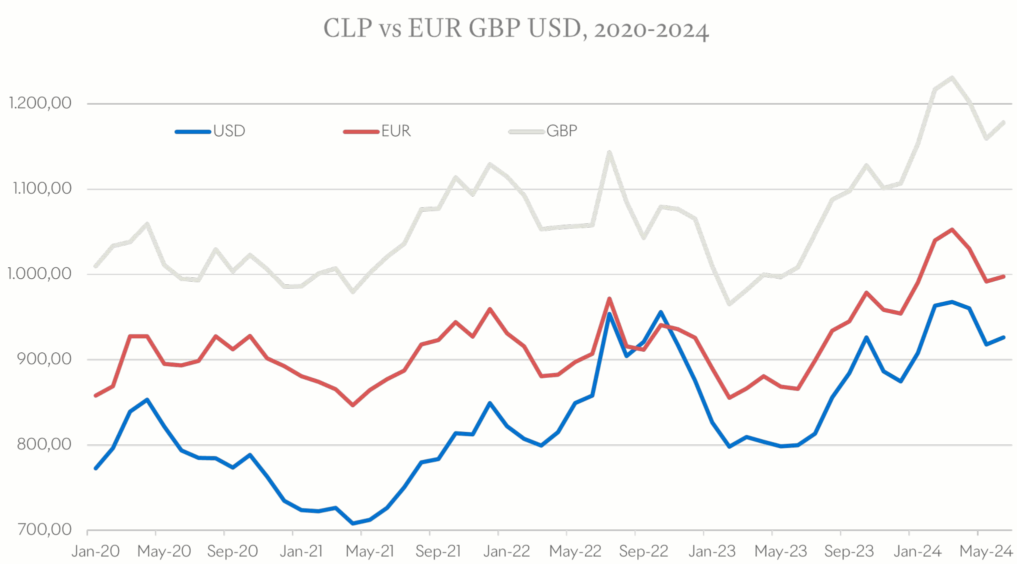


Source: JP Morgan Chase

As risk premiums have declined around the world, JP Morgan's Emerging Market Bond Index for Chile fell to 118 points in May, down from a peak of 148 points in November last year and its lowest level in more than six years.

Source: Central Bank of Chile

After falling to near record lows against the US dollar in early 2024, the Chilean peso appreciated in May to around CLP 900/dollar, driven by the higher copper prices as well as expectations that the difference in interest rates between Santiago and Washington DC are likely to narrow in the coming months. The exchange rate remains significantly higher than a year ago, keeping Chilean exports competitive but risking higher inflation.



Source: Central Bank of Chile

The Chilean peso has appreciated against all major currencies with the multilateral exchange rate (TCM) rising by 6% during the quarter.

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Quarterly Insight

3

Chilean families and businesses are going to suffer a sharp increase in electricity prices as the government withdraws energy subsidies introduced over the last five years.

Under legislation passed by Congress first during the 2019 social unrest and then the pandemic, lawmakers sought to prevent electricity bills from rising just when Chilean families were suffering unprecedented hardships.

Electricity bills had been expected to start falling from the start of the decade especially after the boom in renewable energy led to collapse in the long-term power prices in tenders to supply regulated clients.

But the cancellation of many renewable projects as well as the depreciation of the Chilean peso against the US dollar and the rise in oil prices following Russia's invasion of Ukraine threatened sharp increases in electricity bills.

The subsidies were financed with a promissory note from the government to the power companies that covers the difference between the frozen tariffs and actual costs. This debt must be paid back within a decade of the last law's approval in 2022.

With the pandemic over, the economy growing and inflation falling, the government has decided to gradually withdraw the price freeze for almost all consumers.

As a result, household electricity bills are expected to rise by around 30% from July 1st and by up to 60% by the end of next year as power firms adjust tariffs in line with market realities.

Given that electricity accounts for around 2% of household spending on average (and more for those for poorer families), this implies another significant increase in the cost of living for most people just when inflation seemed to be fading. Subsidies are planned to partially shield the 40% most vulnerable households from the increase although they must sign up online to be eligible.

By withdrawing the subsidies now, the government wants to avoid the situation in countries like Argentia and Bolivia where energy subsidies have become a major and permanent part of public expenditure, and which are very difficult to end due to political reasons.

But unravelling a short-term fix is proving to have multiple long-term consequences on the economy.

As well as higher costs for families, the jump in power prices is likely to impact prices throughout the economy. Statistics agency INE has already pointed to higher power prices as a key factor in the rise in inflation during the second quarter. In its latest Monetary Policy Report, the Central Bank has warned it could be a persistent factor into next year, pushing up the prices of other goods and services, delaying a fall in interest rates and weighing on economic growth.

With the end of the price freeze, the government now has to repay the energy companies.

The bill is estimated to total around US$6.0 billion, equivalent to almost 8% of annual public spending. But as well as having almost a decade to pay the debt, the government decided it will finance the transfer through a surcharge on electricity tariffs paid by large consumers (more than 5,000kWh/month).

The move, approved by Congress in April, has raised significant complaints from the mining industry and manufacturing sector which will bear the brunt of the bill

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Political Context

4

The government has made slow progress advancing its flagship reforms in pensions and taxation through Congress, straining relations with the opposition and the private sector.

After the government ordered the Senate to prioritise debate of its pension reforms, experts for the main parties reached a partial agreement on the legislation in early July, including the new 6% contribution by employers that was previously rejected in the Chamber of Deputies.

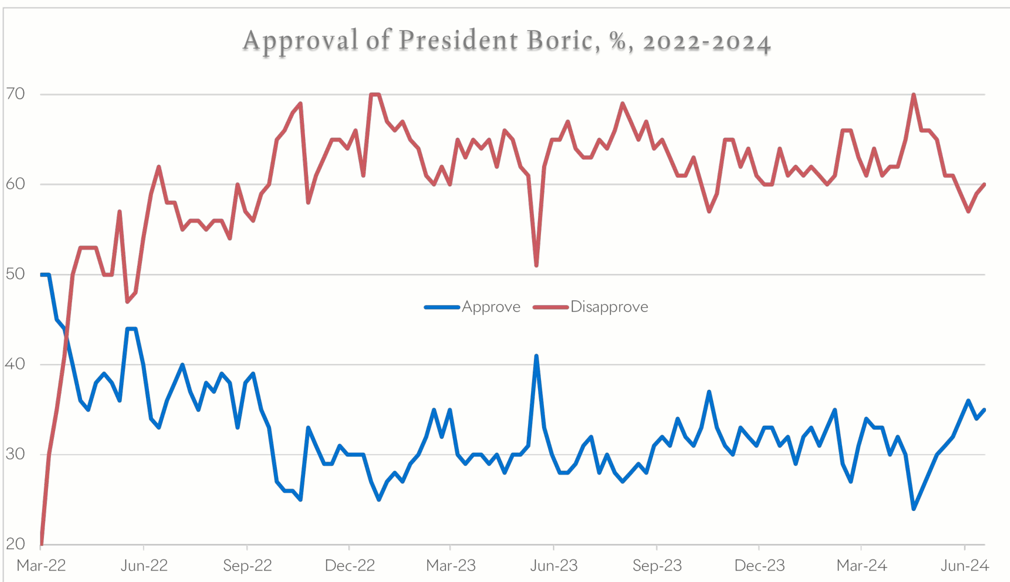
Meanwhile, Finance Minister Mario Marcel has delayed presentation of legislation to overhaul income tax until the second half of the year (but before the budget debate in September). It is expected to raise taxes on higher income earners while cutting corporation taxation.

In April, President Boric accused business leaders of working to block his legislative agenda, while some supporters warned that public frustration could spill over into street protests.

With its flagship reforms bogged down in Congress, the government has started to advance other policies designed to please supporters.

In May, Finance Minister Mario Marcel said that the government would send legislation to Congress by September to condone student debt, a key demand of supporters. Estimated to cost up to US$11.7 billion (or more than the annual education budget), the proposal was dismissed by the government's opponents and more moderate allies as an expensive gimmick ahead of this year's regional elections.

During his annual address to Congress on June 1st, President Boric said that the government would seek to lift restrictions on abortion, a key issue for his base but causing some right-wing legislators to abandon the chamber.



Source: Cadem

However, these announcements appear to have bolstered support for the government in recent weeks, according to the weekly poll by CADEM. After falling to a record low of 24% in early May (after three policemen were ambushed and murdered in southern Chile, reawakening concerns about crime levels), approval of President Boric had climbed to over 35% by late June, its highest level in over a year.

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Economic Outlook

5

As it emerges from the post-pandemic slump, the Chilean economy is set to grow this year at its fastest pace in three years. Household and government consumption are rising faster than expected while investment is now expected to contract by less than previously predicted, thanks to high metals prices and infrastructure spending.

A growing economy should help to bring down unemployment which remains stubbornly above pre-pandemic levels even when many older workers appear to have withdrawn permanently from the workforce.

However, stronger economic activity combined with the weaker peso and higher energy prices is stoking inflation. The Central Bank now expects the government's Consumer Price Index to end the year at 4.2% (unchanged from current levels) while a return to its medium-term target of 3% has been postponed until 2026.

As a result, the loosening of monetary policy begun in mid-2023 will likely end prematurely. The Central Bank could even be forced to hike rates before the end of the year if global events – war in Ukraine and the Near-East, US-Chinese tensions and the rise of populist politicians in Europe and North America – trigger price rises.

This year's moderate growth spurt is unlikely to last. As consumption slows, growth is expected to slow to less than 2.0% from next year in line with trend growth calculated by the Central Bank. Although investment is expected to recover next year, achieving the kind of sustained economic growth which saw income levels soar in previous decades will require conditions that give companies the confidence to bet big on Chile.

In fact, the government led by President Gabriel Boric has made encouraging investment a top priority for its remaining two years in office, with plans to cut red-tape for new investment projects and lower corporate tax rates. But it is not clear that it has the support necessary to push these reforms through Congress by March 2026 as politicians instead focus on next year's congressional and presidential races.

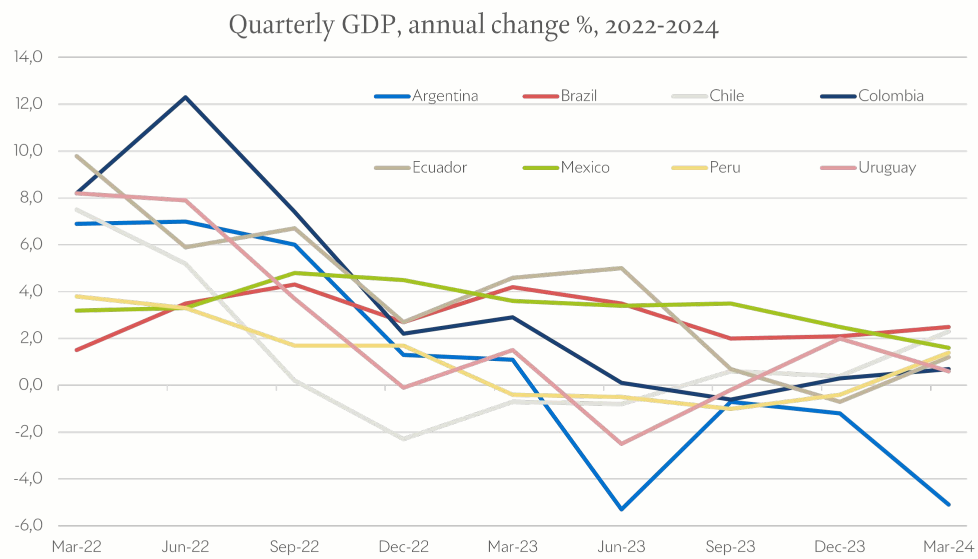
Economic Forecasts, 2024	Central Bank 1/	Finance Ministry 2/	Private analysts 3/
GDP (% annual variation)	2.25-3.00	2.7	2.6
Inflation (% annual variation)	4.2	3.7	3.9
Monetary-policy interest rate (% annual, nominal, end-year)	NA	NA	4.75
Exchange rate (pesos/US$)	NA	928	880 4/
Copper price (US$/lb)	4.30	4.20	NA

1/ Monetary Policy Report, July 2024
2/ Public Finances Report, May 2024
3/ Average of selected private analysts surveyed by Central Bank, July 2024

Latin America

Regional News

6



Source: Trading Economics

Argentina: President Javier Milei's radical measures (spending cuts and higher interest rates) to correct the economy are taking effect. Monthly inflation fell to 4.6% in June (from 25.5% in December) although economic activity contracted by 5.5% in the first quarter. In June, Congress approved his legislation to widen presidential powers, attract investment, privatise state companies and reform labour laws.

Brazil: Severe flooding killed 151 people and paralyzed economic activity in Rio Grande do Sul from April 29th onwards. Growth is expected to slow to 2.1% this year, down from 2.9% in 2023, while inflation will reach 3.7%, as the disaster hit food production.

Colombia: Growth slowed to just 0.7% in the first quarter amid uncertainty among investors over government policy. President Gustavo Petro has called for a national assembly to draft a new constitution and threatened to halt debt payments if Congress does not lift a debt ceiling.

Ecuador: President Daniel Noboa easily won a referendum in April to grant police and armed forces more powers to tackle organised crime. But increased crime levels and the crackdown is hurting economic activity which is expected to grow by just 1.0% this year.

Mexico: Claudia Sheinbaum, President Andrés López Obrador's chosen successor, won the presidential election attracting 60% of the votes cast as well as a majority of seats in Congress. After growing more than 3% in 2023, the economy is set to slow this year.

Peru: The Central Reserve Bank has continued to cut interest rates (reaching 5.75% in May) as inflation returned to target levels and the economy has begun to grow again. However, political instability continues to weigh on investment after police searched President Dina Boluarte's residence in a corruption probe.

Uruguay: A recovery in farm exports and consumer spending are expected to lift growth to over 3% this year. Yamandú Orsi of the centre-left Frente Amplio is the current favourite to win next October's presidential vote after winning primary elections on June 30th.

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