

Chile



COUNTRY RISK CATEGORY

2/7

The country risk categories range from 0 to 7. The lower the number the better the credit rating the country has.



EKN'S OUTSTANDING GUARANTEES TO THE COUNTRY

SHORT-TERM TRANSACTIONS: SEK 407 MILLION

MEDIUM AND LONG-TERM TRANSACTIONS: SEK 1098 MILLION

DATE

07/04/2016

Economy stable but slowing down

The political situation in Chile is stable. The democratic agenda has been followed exemplarily since the military handed over power in 1990. The country also has a long tradition of responsible economic policies, which is appreciated by the international financial markets. Falling commodity prices and lower demand have however led to substantially lower growth for the time being. The major income disparities in the country serve as a factor of uncertainty. The centre-left coalition's return to power, led by President Michelle Bachelet, will seek to implement reforms geared toward income equalisation. The country's more recent tradition of consensus solutions will probably continue for the most part, but the changed majority situation in the parliament will increase the government's propensity toward unilateral solutions. However, it is highly likely that the situation will remain under control within the bounds of the country's parliamentary system.

THE COUNTRY'S STRENGTHS AND WEAKNESSES

Strengths

- Political consensus on economic policies
- Fundamental political stability
- Strong institutions and a robust banking system

Weaknesses

- Large income disparities could create political problems
- Lack of economic diversification and innovation
- Lack of domestic energy

Chile in country risk category 2 for a long time

Chile has been ranked in country risk category 2 since the late 1990s. The country has not been categorised within the OECD for a number of years because it is now categorised as an OECD high-income country. This is an expression of the stable economic growth in the country since the late 1980s.

WHAT MIGHT CAUSE A CHANGE IN THE COUNTRY POLICY?

The policy may be made less restrictive in the event of

- Increased export diversification and reduced dependence on copper
- Increased public savings to reduce the effects of commodity price fluctuations

The policy may be made more restrictive in the event of

- The lack of income equalisation reforms potentially leading to increased social conflict
- Continuing low international copper prices

EKN'S EXPOSURE AND EXPERIENCE

Chile keen to maintain its good reputation

EKN's payment experiences from Chile are on the whole very good. It is clear that the government is very keen to maintain its good relations with lenders. EKN's outstanding guarantees for transactions in Chile totalled just below SEK 1.1 billion, and the vast majority are guarantees for exports of buses for the public transport system in Santiago. In 2015, 135 guarantees were issued, totalling nearly SEK 600 million.

EKN's experience from guaranteeing transactions with Chile is good. However, the negative commodity price trends in recent years have had repercussions for the Chilean economy and thus the commercial conditions for companies. This has been reflected in a slight increase in the number of payment delays. In addition, EKN has experienced problems related to the public transport system in Santiago.

COUNTRY ANALYST



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Background

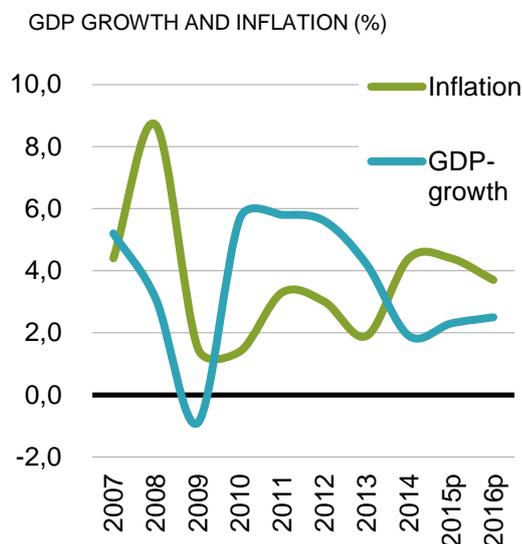
Political developments in Chile have been calm since democracy was restored in 1990. The country has been ruled by centre-left governments ever since, with the exception of the period from 2010 to 2013 when a right-wing alliance under Sebastian Piñera took power. His term of office was characterised by economic successes, but also social protests. However, the 2013 elections restored the old order and the centre-left coalition under former President Michelle Bachelet reclaimed power.

Domestic policy consensus

As regards economic policy, consensus between the various parties is relatively high – both the current and former governments have adopted orthodox economic policies with a clear market-economy orientation. The political climate is characterised by a strong consensus. This has been further accentuated by the constitution drafted during the period of military rule, which significantly complicates the ability to secure voting majorities in parliament for any of the political blocks. Another challenge for the government is to manage the large and increasing income disparities in the country. These disparities should also be seen in the context of the fact that there are a small number of groups that in practice control a large portion of economic activity in Chile. In addition, the country's energy situation will continue to be an Achilles heel in light of its lack of energy sources and the difficulty of developing nuclear power due to the risk of earthquakes. Chile is therefore dependent on energy supplies from neighbouring countries, with which Chile has complicated relations.

Most recent trends

Michelle Bachelet has set a key objective to overhaul the tax system and, in particular, reform



Macroeconomic control in Chile. Source: IMF

the educational sector. Constitutional reform is also high on the agenda. Bachelet is under heavy domestic policy pressure to change the educational system in particular, and in recent years this has been manifested as extensive student demonstrations. On the other hand, the actual implementation of these reforms has moved slowly, despite the government's relatively comfortable parliamentary situation. Lower economic growth, rapidly declining popularity for the president, corruption scandals and disagreements within the governing majority have led to demands for moderation of the reforms. The domestic policy situation in particular has led to a decrease in confidence from the Chilean business sector, which in

turn is reflected in falling investment levels.

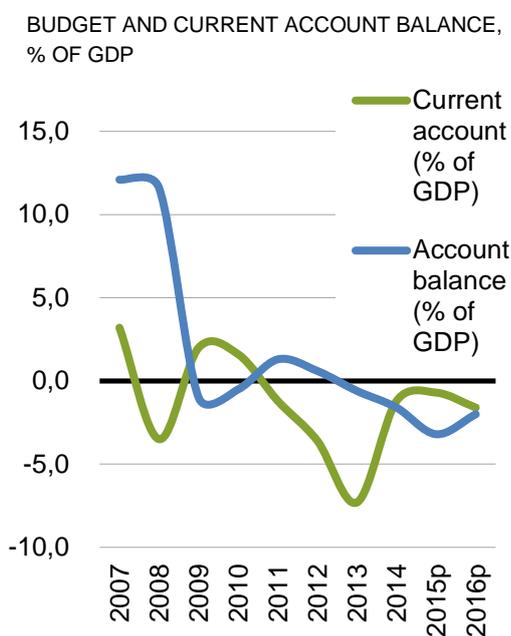
Copper dominates the Chilean economy and has traditionally accounted for nearly 40 per cent of export revenue. The high copper prices of past years have enabled the creation of a stabilisation fund, which can now be utilised given today's significantly lower copper prices.

Exports are relatively evenly divided between the US, the EU and Latin America, with China becoming an increasingly important trade partner.

However, reduced demand from China over the past year, and the resulting drop in copper prices, has left its mark on the Chilean economy. Growth only came in at slightly more than 2 per cent in 2015 and is expected to remain at that level. The level of investment has fallen a couple of percentage points over a couple years to just below 24 per cent of GDP. This is partially related to a decrease in investments in the mining sector due to the lower copper prices, but is also due to greater uncertainty within the Chilean business community as a result of the government's proposed tax reforms – which include higher corporate tax rates. The ongoing economic slowdown is partially being counterbalanced by the fact that the Chilean export industry is benefiting from the North American recovery, but also the fiscal and monetary easing which has led to a more competitive exchange rate. The country's good public finances thus give the country room for manoeuvre in a tougher economic environment. The combination of steady growth and price stability are likely to continue to be features of the Chilean economy in the future.

Long-term trends

Meanwhile, Chile's long-term growth potential is increasingly being called into question. The low level of education in Chile in particular is restricting the potential to raise productivity in existing industries – which is something that the proposed education reform aims to change. Arguably, the most important problem to tackle, however, is the lack of economic diversification. The question is therefore ultimately about the future potential of the country's



Balanced growth in Chile. Source: IMF

country's outlet markets.

commodity-based export model, in the absence of any new export products. Raw materials, particularly copper, continue to dominate and make Chile vulnerable to fluctuations in international commodity prices.

However, the economic problems can be managed from a position of strength. The country's traditionally austere fiscal policies have paved the way for balanced growth in the public sector and created scope for countermeasures when the country was exposed to external shocks. The political consensus on fundamental economic policies has created long-term stability and international confidence. Overall, it is highly likely that the Chilean economy will move forward steadily in the long-term, but at a lower rate, given the weak trend in the

A few groups of owners are dominant

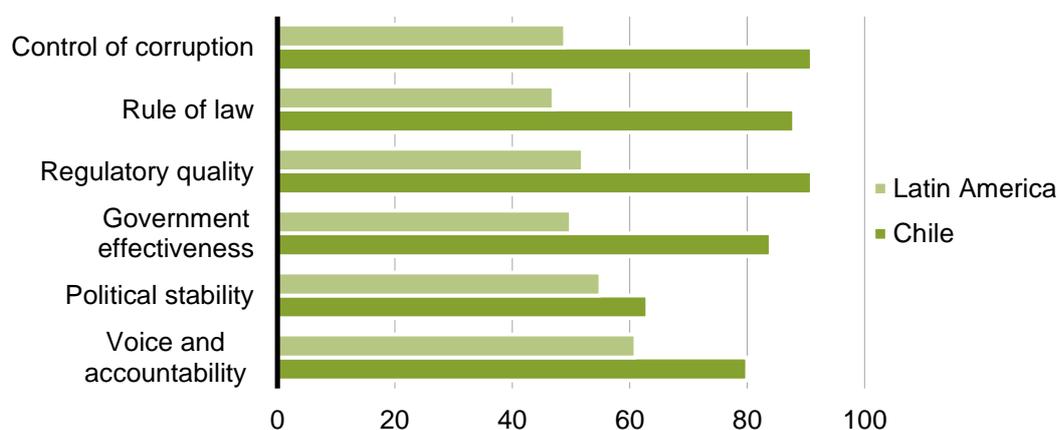
Chile's stable macroeconomic climate has facilitated the growth of a healthy and relatively well-managed business sector. However, ownership is highly concentrated to a few groups of owners who also largely dominate the media sector and public opinion. The availability of financial information on private buyers is good, and imports on open credit terms are common. Letters of credit are rare. Demand for financing solutions via EKN is also limited in a relatively mature market such as Chile.

The World Bank's Doing Business Indicators rank Chile 48th (out of 189). Chile is just behind Mexico in Latin America. The lack of a higher ranking reflects a general Latin American problem: the slow legal system (albeit less pronounced in Chile). In other business environment aspects, such as rule of law, control of corruption and transparency, the country is at par with the other OECD countries

Institutionally, Chile is a relatively highly developed country where leading institutions such as the ministry of finance, central bank and the banking regulatory authority all have a very good reputation. In particular, the banking regulatory authority's strict regulation of the financial sector has led to Chile currently having Latin America's strongest and most developed banking system. The banking system's assets are equal to over 90 per cent of the country's GDP, far above the Latin American average. Lending in relation to GDP is high, while the proportion of credit losses is limited to just over two per cent.

BUSINESS ENVIRONMENT

Ranking from 0 (worst) to 100 (best)



The Chilean business environment is consistently far better than the regional average. Source: World Bank 2015

The loan-to-asset ratio in the Chilean banking system is high in regional terms, but the high confidence of depositors and the very limited short-term financing significantly reduce the refinancing risk. Foreign ownership is considerable (over 60 per cent) and market concentration is high. The four largest banks (one foreign-owned, two domestic privately owned and one government owned) account for around two-thirds of the loan market. Spanish banks (Santander, BBVA) play considerable roles in the Chilean market.