



# Observatorio Económico

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## President Bachelet announces economic measures amounting to US\$330 million in her annual budget

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- These measures focus on fighting the economic crisis and strengthening the social safety net.
- The fiscal cost of the measures in 2009 will amount to some US\$330 million, approximately 0.2% of GDP for the year, and will be financed from taxes on fuel, redistribution of the budget and the Public Treasury. However, this will not affect the sustainability of public finances.
- The reduction in the ceiling for fuel tax to 4.5 UTM (monthly tax units)/m<sup>3</sup> will reduce our 2009 inflation estimate from 0.9 percentage points to 0.6 percentage points.

President Michelle Bachelet announced a set of measures in her latest annual budget on 21 May. The economic measures introduced include the following:

- 1. Supplementary payment of \$40 thousand for family benefit:** This will be paid to the poorest families in August. Workers who receive Family or Maternal Benefits, and heads of households who receive benefits under the Family Subsidy and the Chile Solidario program will benefit from this measure. According to the Ministry of Finance, this measure will cost US\$265 million and will affect some 4 million family benefit recipients.
- 2. Bringing forward the Provisional Reform:** The timeframe for expanding the Social Pensions System will be brought forward from 1 July 2010 to 1 September 2009, which will lead to coverage of elderly adults with lower resources increasing from 45% to 50% by the latter date. Under this timeframe, by July there will be an increase in Basic Social Pensions (BSP) from \$60 thousand to \$75 thousand, and an increase in the maximum Provisional Social Contribution (PSC) to \$120 thousand. Under this new schedule, from September the BSP will increase from \$75 thousand in accordance with the CPI, and the maximum for the PSC will reach \$150 thousand. The cost of this reform in 2009 will be US\$45 million.
- 3. Home insurance:** The Government will finance unemployment insurance for people repaying a mortgage on a home bought with a subsidy. The insurance will cover four monthly payments, and is applicable to persons who are unemployed for at least 2 months. The estimated cost of this measure to the Finance Ministry is US\$14 million.
- 4. A new ceiling for fuel tax:** the specific fuel tax will be set at 4.5 UTM/m<sup>3</sup>. The tax is currently 3.5 UTM/m<sup>3</sup> resulting from a transitional decrease (decreed in 2008 but will be reapplied gradually from June) from the 6 UTM/m<sup>3</sup> established by law.

**Appraisal:**

Whilst the economic measures announced by the President also include others related to the operation of markets -such as prison sentences for the crime of collusion (which has been in the public eye following the revelation of this type of practice in the pharmaceutical sector) and a third round of reforms for capital markets- the centerpiece of the announcement was the package of measures to tackle the economic crisis and to reinforce the social safety net on which President Bachelet has placed great emphasis.

The general appraisal of this set of measures is positive, as it will increase the counter-cyclical nature of fiscal policy at a time when this is required to offset the decline in economic activity. The Finance Minister, Andrés Velasco, announced that the cost of these measures during 2009 will be US\$330 million. This represents around 0.2% of estimated 2009 GDP, and does not constitute an undue burden on public finances, given the net creditor position of the national Government. Mr. Velasco indicated that the set of measures would be financed in equal parts by the fuel tax, the reallocation of budgets and the Public Treasury.

The reduction in the ceiling on the specific fuel tax will, in our opinion, reduce inflation by 0.3 percentage points, bringing inflation at the end of 2009 down to 0.6%, rather than the 0.9% in our previous estimate. This forecast agrees with the Central Bank's forecast for the year.