Gobierno de Chile

Republic of Chile

Ministry of Finance

December 2019

Debt Management Strategy: Debt policy goals and structure

➢ Debt Management Strategy:

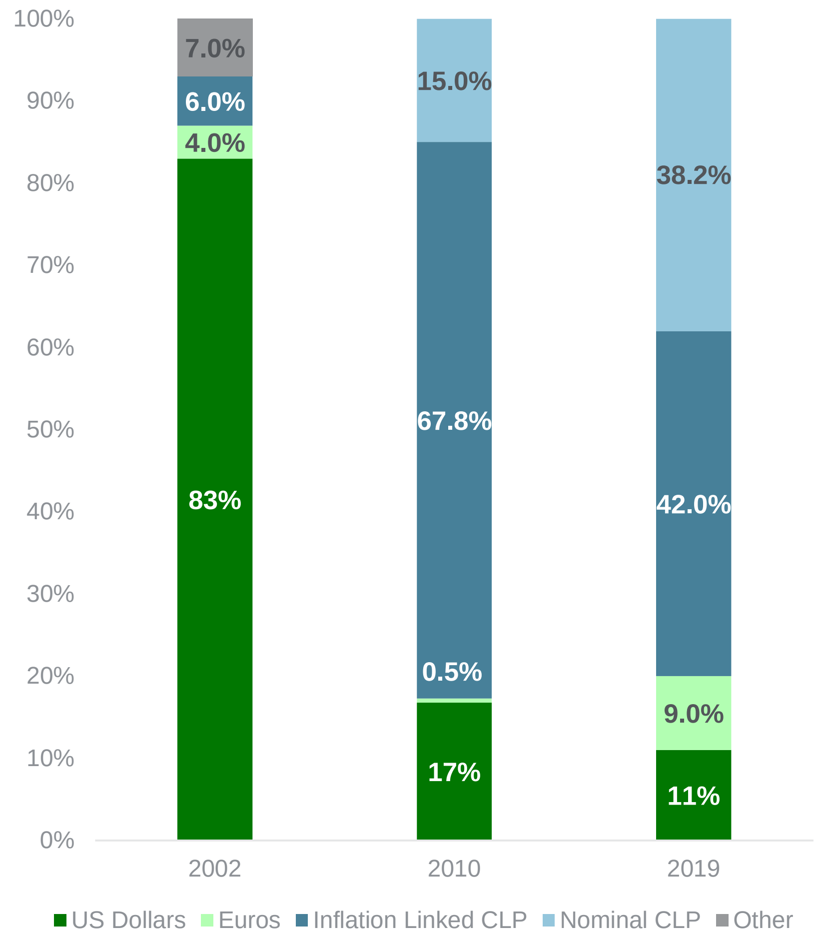
- ➢ **Domestic:** to develop and lengthen yield curves (nominal and real), while deepening liquidity by fostering greater participation of non-residents
  - Recent issuances have strengthened new benchmarks and have created longer tenors, extending the debt maturity profile in line with international standards

- ➢ **External:** to establish benchmarks for Chilean companies in international capital markets

- ➢ **In addition:** to promote the development of a green asset class (social/green bonds) that attracts foreign investment in support of the country's sustainable infrastructure needs, while diversifying the investor base

- ➢ **Strong commitment with depth and liquidity**

Debt Composition by Currency
Percent of total



Source: Ministry of Finance; Public Debt Report

Liquidity agenda increasing foreign investors' participation

Not high liquidity and low foreign participation justified a plan initiated in 2014:

- **Improving liquidity and promoting foreign investor participation**
  - Less auctions per bond and for a higher amount, instead the previous method of multiple auctions of smaller amounts
  - Continuous contact with investors in order to update about debt management operation and Chilean economy
  - Settlement adjustments in order to comply with international standard (T+2)
- **Continuous discussion with index research team in order to include Chilean bonds (nominal)**
  - Discussions with JP Morgan research team in order to be included in the GBI Emerging Market Bond Index
- **Modifications of Article 104 (exemption for capital gains)**
  - Simplification to Article 104 approved by Congress in 2016 and in force from February 1st, 2017
  - The Issuer is in charge to apply the retention, in order to simplify the mechanics
- **Liability Management executed in 2016**
  - In order to repurchase bonds that will not be used as benchmark, and replace them by tapping existing benchmarks

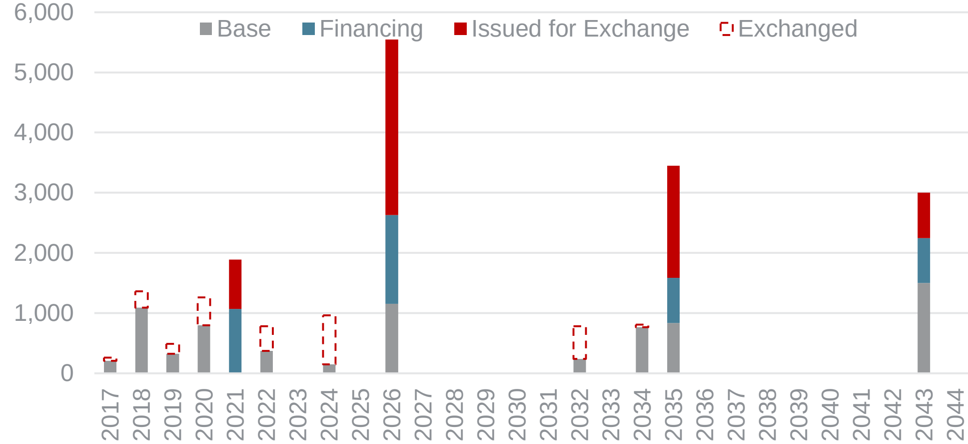
Source: Ministry of Finance

Liability Management executed in 2016

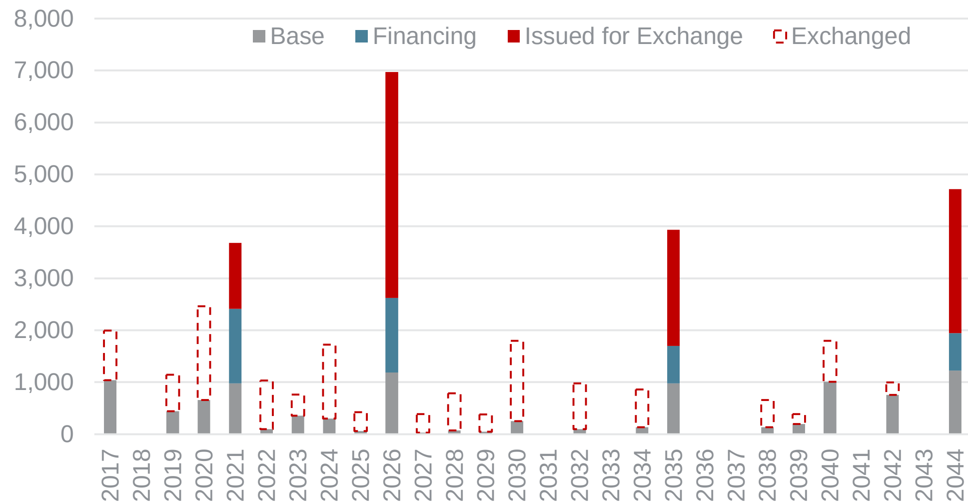
- **Modernization of the Sovereign Debt Plan and Strategy**
  - At the beginning of the year, the Maturity Profile showed:
    - Low liquidity
    - Absence of benchmarks
  - The participation of non-resident Investor in the local currency debt was approximately 3.4%

- **Other adjustments**
  - **Concentration of trading in key benchmarks, achieved by liability management operations in local currency bonds**
    - Strong references both in inflation-linked and nominal curves
    - Implemented by exchanging illiquid & low outstanding bonds (“non benchmark bonds”), with “benchmark bonds” with high liquidity and larger outstanding amounts
  - **First domestic Euroclearable bond**

Maturity Profile: Nominal Curve as of December 2016
USD billion



Maturity Profile: Inflation linked Curve (UF) as of December 2016
USD billion

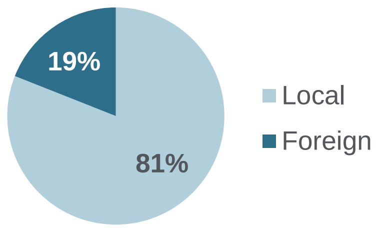


First Domestic Euroclearable Bonds for CLP 1.0 Trillion – January 2017

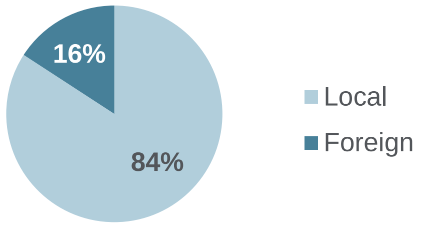
- **Euroclearable bonds and book building simultaneously with local and international investors**
  - January 18th, 2017: first time that the Republic of Chile offered CLP 1.0 Trillion domestic bonds to international investors and book-building process:
    - International investors could hold a direct interest in the bonds through Euroclear, as a DCV-Participant
    - Payments of principal and interest to investors will be made in Chilean Pesos (CLP) via the local clearing system, DCV
  - The Republic made public its intent to offer the bonds to domestic and international investors on Thursday January 12th, a week ahead of the trade
    - The trade was marketed to international investors through a global investor call, in which the Republic explained the details of the transaction
    - More than 100 international investors accessed the recording – a clear indication of interest by the international investment community
  - **Due to the successful story, it was repeated in 2017, 2018 and 2019**

Issuer	Republic of Chile
Local Currency Ratings	Aa3 / AA / AA- (Moody's / S&P / Fitch)
Distribution	▪ Local registration for domestic investors ▪ 144A / Reg. S. for international investors(1)
Currency	Chilean Peso (CLP); all payments payable in CLP
Size	**CLP 1.0 Trillion (~US$1.5 Billion)**
Maturity	February 28, 2021
Coupon	4.50% per annum, accruing from September 1, 2016
Yield ("TIR")	**3.80%**(2)
Issue price	**102.740%**(3)
Foreign exchange rate	657.85 CLP / USD(4)
Interest payment dates	March 1 and September 1
Amortization	Bullet
Use of Proceeds	General government purposes
Denominations	CLP 5,000,000 and integral multiples thereof
Settlement currency	All international investors settle primary allocation in USD
Clearing	**DCV / Euroclear**
Listing	Santiago Stock Exchange
Governing Law	Chilean Law

Allocation by investor
% of total



Demand by investor
% of total



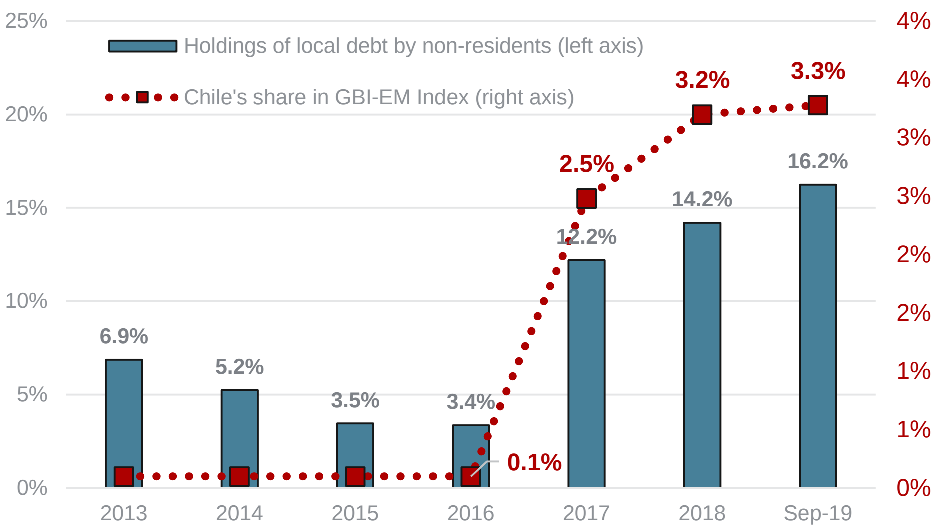
(1) With permanent restrictions: transfers in the U.S. are only to QIBs. (Unitary ISIN under existing ISIN). No registration rights; (2) Calculated per local ("SEBRA") conventions; (3) Plus accrued interest of CLP 2.9bn calculated pursuant to SEBRA conventions; (4) Dolar Observado published in the official gazette on the morning of the transaction – settlement to international investors in USD

Progress to improve liquidity in the local fixed income market in recent years

- **LM as a regular policy**
- **Greater weight in the GBI EM Bond index**
  - Three local Euro-clearable bonds issuances since February 2017. These have allowed for a broader inclusion of Chilean bonds in the GBI Emerging Market Bond Index.
  - Chile's share in this index increased from 0.10% in 2016 to 3.3% by Sep-2019.
- **Recent events and stability of non-residents investment**

Non-resident Holdings of LC Debt & GBI-EM Share

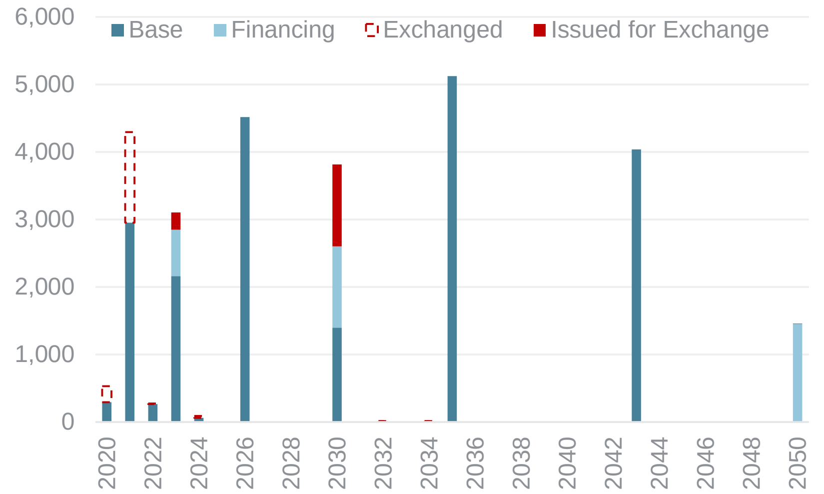
Percent of total



Source: JP Morgan and the Ministry of Finance

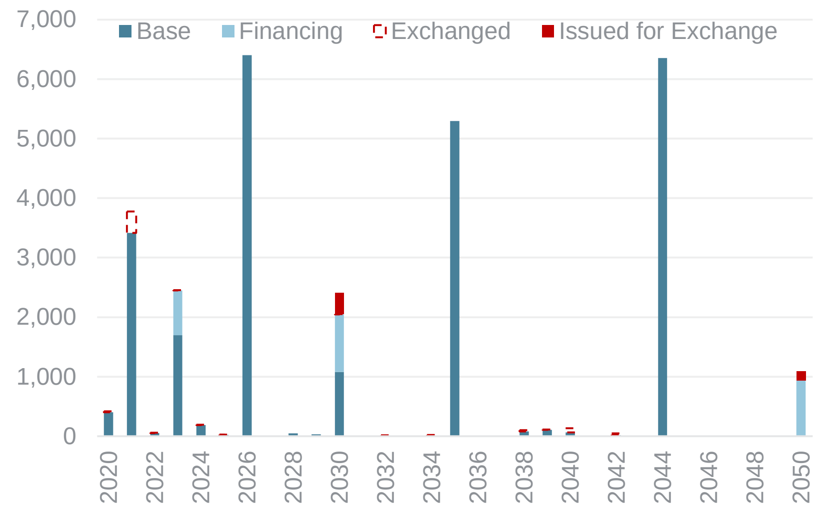
Maturity Profile: Nominal Curve as of December 2019

USD billion



Maturity Profile: Inflation linked Curve (UF) as of December 2019

USD billion



Source: Ministry of Finance

Diagnosis and Further Steps

Diagnosis:

- **Pros**
  - Investor diversification
  - Good experience when locals are going abroad
  - Signals of higher liquidity
- **Cons**
  - Liquidity requires a fluid movement between locals and foreigners, which could not be the case when the FX market has constraints
  - Foreign investor prefer book building, which add certain administrative constraints and difficulties for a good timing
  - Price tension is not necessary high, because international investor are price takers, or normally want an issue premium

Nonetheless, the Chilean experience shows that to improve foreign participation requires other complementary measures.

- **Still, additional measures are necessary or at least worth to analyze**
  - Market Makers
  - OTC for Pension Funds
  - ETF’s