

BANCO SANTANDER CHILE  
Form 6-K  
November 27, 2006

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**FORM 6-K**  
**SECURITIES AND EXCHANGE COMMISSION**  
**Washington, D.C. 20549**

**Report of Foreign Issuer**

**Pursuant to Rule 13a-16 or 15d-16 of  
the Securities Exchange Act of 1934**

**For the month of June 30, 2006**

**Commission File Number: 001-14554**

**Banco Santander Chile**  
**Santander-Chile Bank**

*(Translation of Registrant's Name into English)*

**Bandera 140**  
**Santiago, Chile**

*(Address of principal executive office)*

Indicate by check mark whether the registrant files or will file annual reports under cover of Form 20-F or Form 40-F:

Form 20-F

Form 40-F

Indicate by check mark if the registrant is submitting the Form 6-K in paper as permitted by Regulation S-T Rule 101(b)(1):

Yes

No

Indicate by check mark if the registrant is submitting the Form 6-K in paper as permitted by Regulation S-T Rule 101(b)(7):

Yes

No

Indicate by check mark whether by furnishing the information contained in this Form, the Registrant is also thereby furnishing the information to the Commission pursuant to Rule 12g3-2(b) under the Securities Exchange Act of 1934:

Yes

No

If  Yes is marked, indicate below the file number assigned to the registrant in connection with Rule 12g3-2(b): N/A



**TABLE OF CONTENTS**

Cautionary Statement Concerning Forward-Looking Statements	3
Certain Terms and Conventions	6
Presentation of Financial Information	7
Item 1. Key Information	9
Item 2. Information on the Company	24
Item 3. Operating and Financial Review and Prospects	43
Item 4. Directors, Senior Management and Employees	98
Item 5. Major Shareholders and Related Party Transactions	103
Item 6. Financial Information	106
Item 7. The Offer and Listing	107
Item 8. Quantitative and Qualitative Disclosures about Market Risk	108
Item 9. Principal Accountant Fees and Services	128
Item 10. Purchases of Equity Securities by the Issuer and Affiliated Purchasers	129
Item 11. Exhibits	129

**CAUTIONARY STATEMENT CONCERNING  
FORWARD-LOOKING STATEMENTS**

We have made statements in this report on Form 6-K that constitute forward-looking statements within the meaning of the Private Securities Litigation Reform Act of 1995. These statements appear throughout this report and include statements regarding our intent, belief or current expectations regarding:

asset growth and alternative sources of funding

growth of our fee-based business

financing plans

impact of competition

impact of regulation

exposure to market risks:

interest rate risk

foreign exchange risk

equity price risk

projected capital expenditures

liquidity

trends affecting:

our financial condition

our results of operation

The sections of this report which contain forward-looking statements include, without limitation, [Item 1: Key Information] Risk Factors, [Item 2: Information on the Company] Strategy, [Item 3: Operating and Financial Review and Prospects], [Item 6: Financial Information] Legal Proceedings and [Item 8: Quantitative and Qualitative Disclosures About Market Risk]. Our forward-looking statements also may be identified by words such as "believes," "expects," "anticipates," "projects," "intends," "should," "could," "may," "seeks," "aim," "combined," "estimates," "practices," "target," "goal," "objective," "future" or similar expressions.

You should understand that the following important factors, in addition to those discussed elsewhere in this report and in the documents which are incorporated by reference, could affect our

future results and could cause those results or other outcomes to differ materially from those expressed in our forward-looking statements:

- changes in capital markets in general that may affect policies or attitudes towards lending to Chile or Chilean companies
- changes in economic conditions
- the monetary and interest rate policies of the Central Bank
- inflation or deflation
- unemployment
- unanticipated turbulence in interest rates
- movements in foreign exchange rates
- movements in equity prices or other rates or prices
- changes in Chilean and foreign laws and regulations
- changes in taxes
- competition, changes in competition and pricing environments
- our inability to hedge certain risks economically
- the adequacy of loss allowances
- technological changes
- changes in consumer spending and saving habits
- increased costs
- unanticipated increases in financing and other costs or the inability to obtain additional debt or equity financing on attractive terms
- changes in, or failure to comply with, banking regulations
- our ability to successfully market and sell additional services to our existing customers
- disruptions in client service
- natural disasters

- successful implementation of new technologies
- an inaccurate or ineffective client segmentation model

You should not place undue reliance on such statements, which speak only as of the date that they were made. The forward-looking statements contained in this report speak only as of the date of this report, and we do not undertake to update any forward-looking statement to reflect events or circumstances after the date hereof or to reflect the occurrence of unanticipated events.

### CERTAIN TERMS AND CONVENTIONS

As used in this report on Form 6-K, "Santander-Chile", "the Bank", "we," "our" and "us" mean Banco Santander-Chile and its consolidated subsidiaries, the bank resulting from the merger of Santiago and Old Santander-Chile.

When we refer to "Santiago" in this report, we refer to Banco Santiago and its consolidated subsidiaries prior to its merger with Old Santander-Chile. When we refer to "Old Santander-Chile" in this report, we refer to the former Banco Santander-Chile and its consolidated subsidiaries, which ceased to exist upon its merger into Santiago, effected on August 1, 2002.

As used in this report on Form 6-K, the term "billion" means one thousand million (1,000,000,000).

In this report, references to "\$", "US\$", "U.S.\$", "U.S. dollars" and "dollars" are to United States dollars, references to "Chilean pesos," "pesos" or "Ch\$" are to Chilean pesos and references to "UF" are to Unidades de Fomento. The UF is an inflation-indexed Chilean monetary unit with a value in Chilean pesos that changes daily to reflect changes in the official Consumer Price Index ("CPI") of the Instituto Nacional de Estadísticas (the Chilean National Institute of Statistics) for the previous month. See "Item 3: Operating and Financial Review and Prospects" and Note 1(c) to the Unaudited Consolidated Financial Statements.

In this report, references to the "Audited Consolidated Financial Statements" are to the audited consolidated financial statements of Santander-Chile at December 31, 2004 and 2005 and for the years ended December 31, 2003, 2004 and 2005 (together with the notes thereto) contained in Santander-Chile's Annual Report on Form 20-F for the fiscal year ended December 31, 2005. References to the "Unaudited Consolidated Financial Statements" are to the unaudited consolidated financial statements of Santander-Chile at and for the six-months ended June 30, 2005 and 2006 (together with the notes thereto) included elsewhere in this report on Form 6-K.

In this report, references to the Audit Committee are to the Bank's *Comité de Directores y Auditoría*. This committee is the successor of the Directors Committee created under Law 19,705 in 2000 and the Audit Committee created by the Board of Directors of Banco Santiago in 1995. On September 22, 2004, the Superintendency of Banks authorized that the functions of the Audit Committee be performed by the Directors Committee. On October 19, 2004, the Board of Directors of Banco Santander Chile, by resolution No. 357, approved the merger of both committees and the transfer of all functions of both committees to the *Comité de Directores y Auditoría*, which was created on the same date.

In this report, references to "BIS" are to the Bank for International Settlement, and references to "BIS ratio" are to the capital adequacy ratio as calculated in accordance with the Basel Capital Accord.



## PRESENTATION OF FINANCIAL INFORMATION

### Currency and Accounting Principles

Santander-Chile is a Chilean bank and maintains its financial books and records in Chilean pesos and prepares its audited and unaudited consolidated financial statements in conformity with generally accepted accounting principles in Chile and the rules of the *Superintendencia de Bancos e Instituciones Financieras* (the Superintendency of Banks and Financial Institutions, which is referred to herein as the "Superintendency of Banks"), which together differ in certain significant respects from generally accepted accounting principles in the United States ("U.S. GAAP"). References to "Chilean GAAP" in this report on Form 6-K are to accounting principles generally accepted in Chile, as supplemented by the applicable rules of the Superintendency of Banks. See Note 27 to the Audited Consolidated Financial Statements and Note 26 to the Unaudited Consolidated Financial Statements for a description of the principal differences between Chilean GAAP and U.S. GAAP, as they relate to Santander-Chile, and a reconciliation to U.S. GAAP of net income and shareholders' equity.

Pursuant to Chilean GAAP, amounts expressed in the Unaudited Consolidated Financial Statements and all other amounts included elsewhere throughout this report on Form 6-K at all dates other than the year end and for all periods other than full years expressed in Chilean pesos are expressed in constant Chilean pesos as of June 30, 2006. Amounts at any year end and for any full year period expressed in Chilean pesos are expressed in constant pesos as of December 31, 2005. The monetary correction factor for amounts as of June 30, 2006 compared to December 31, 2005 was 1.13% . See Note 1(c) to the Unaudited Consolidated Financial Statements.

### Loans

Unless otherwise specified, all references herein (except in the Unaudited Consolidated Financial Statements) to loans are to loans and financial leases before deduction for loan loss allowance, and, except as otherwise specified, all market share data presented herein are based on information published periodically by the Superintendency of Banks. Non-performing loans include loans for which either principal or interest is overdue, and which do not accrue interest. Restructured loans for which no payments are overdue are not ordinarily classified as non-performing loans. Past due loans include, with respect to any loan, only the portion of principal and interest that is overdue for 90 or more days, and do not include the installments of such loan that are not overdue or that are overdue for less than 90 days, unless legal proceedings have been commenced for the entire outstanding balance according to the terms of the loan, in which case the entire loan is considered past due within 90 days after initiation of such proceedings. This practice differs from that normally followed in the United States, where the amount classified as past due would include the entire amount of principal and interest on any and all loans which have any portion overdue. See *Item 3E: Asset and Liability Management/Selected Statistical Information/Loan Portfolio/Classification of Loan Portfolio/Classification of Loan Portfolio Based on the Borrower's Payment Performance.*

According to the regulations established by the Superintendency of Banks, Santander-Chile is required to write-off commercial loans no later than 24 months after being classified as past due, if unsecured, and if secured, no later than 36 months after being classified as past due. When an installment of a past due corporate loan (whether secured or unsecured) is written-off, we must write-off all installments which are overdue, notwithstanding our right to write-off the entire amount of the loan. Once any amount of a loan is written-off, each subsequent installment must be written-off as it becomes overdue, notwithstanding our right to write-off the entire amount of the loan. In the case of past due consumer loans, a similar practice applies, except that after the first installment becomes three months past due, Santander-Chile must write-off the entire remaining part of the loan. We may write-off any loan (whether commercial or consumer) before the first installment becomes overdue, but only in accordance with special procedures established by the Superintendency of Banks. Loans



are written-off against the loan-loss reserve to the extent of any required allowances for such loans; the remainder of such loans is written-off against income. See *Item 3. [Operating and Financial Review and Prospects][Assets and Liability Management][Analysis of Loan Loss Allowance.]*

Outstanding loans and the related percentages of Santander-Chile's loan portfolio consisting of corporate and consumer loans in the section entitled *[Item 2C: Business Overview]* are categorized based on the nature of the borrower. Outstanding loans and related percentages of the loan portfolio of Santander-Chile consisting of corporate and consumer loans in the section entitled *[Item 3 E: Asset and Liability Management][Selected Statistical Information]* are categorized in accordance with the reporting requirements of the Superintendency of Banks, which are based on the type and term of loans.

### **Effect of Rounding**

Certain figures included in this report and in the Unaudited Consolidated Financial Statements have been rounded for ease of presentation. Percentage figures included in this report have not in all cases been calculated on the basis of such rounded figures but on the basis of such amounts prior to rounding. For this reason, certain percentage amounts in this report may vary from those obtained by performing the same calculations using the figures in the Unaudited Consolidated Financial Statements. Certain other amounts that appear in this report may not sum due to rounding.

### **Economic and Market Data**

In this report, unless otherwise indicated, all macro-economic data related to the Chilean economy is based on information published by the *Banco Central de Chile* (the [Central Bank]), and all market share and other data related to the Chilean financial system is based on information published by the Superintendency of Banks and our analysis of such information. Information regarding the consolidated risk index of the Chilean financial system as a whole is not available.

### **Exchange Rates**

This report contains translations of certain Chilean peso amounts into U.S. dollars at specified rates solely for the convenience of the reader. These translations should not be construed as representations that the Chilean peso amounts actually represent such U.S. dollar amounts, were converted from U.S. dollars at the rates indicated in preparing the audited and unaudited consolidated financial statements, could be converted into U.S. dollars at the rates indicated or were converted at all.

Unless otherwise indicated, all the U.S. dollar amounts at any year end or for any full year have been translated from Chilean pesos based on the observed exchange rate reported by the Central Bank on December 30, 2005 (the latest practicable date, as December 31, 2005 was a banking holiday in Chile), which was Ch\$514.21 per US\$1.00, and all the U.S. dollar amounts at and for the six-months ended June 30, 2005 and 2006 have been translated from Chilean pesos based on the observed exchange rate reported by the Central Bank on June 30, 2006, which was Ch\$547.31 per US\$1.00. The observed exchange rates reported by the Central Bank on December 31, 2005 and June 30, 2006 are based upon the actual exchange rates as of December 29, 2005 and June 29, 2006, respectively, and are the exchange rates specified by the Superintendency of Banks for use by Chilean banks in the preparation of their financial statements for the periods ended December 31, 2005 and June 30, 2006, respectively. The observed exchange rate on November 24, 2006 was Ch\$529.17 per US\$1.00, reflecting an accumulated appreciation of 3.3% from June 30, 2006. The Federal Reserve Bank of New York does not report a noon buying rate for the Chilean peso. For more information on the observed exchange rate see *[Item 1: Exchange Rates.]*



**ITEM 1. KEY INFORMATION**

**A. Selected Financial Data**

The following table presents historical financial information about us at the dates and for each of the periods indicated. The following table should be read in conjunction with, and is qualified in its entirety by reference to, our Audited Annual Consolidated Financial Statements as appearing in our 2005 Form 20-F and our Interim Unaudited Consolidated Financial Statements at and for the six-month period ended June 30, 2005 and 2006 included in this report on Form 6-K. Our Audited Annual Consolidated Financial Statements and our Interim Unaudited Consolidated Financial Statements are prepared in accordance with Chilean GAAP, which differs in certain significant respects from U.S. GAAP. Note 27 to our Audited Annual Consolidated Financial Statements in our Form 20-F provides a description of the material differences between Chilean GAAP and U.S. GAAP and a reconciliation to U.S. GAAP of net income for the years ended December 31, 2003, 2004 and 2005 and shareholders' equity at December 31, 2004 and 2005. Note 26 to our Interim Unaudited Consolidated Financial Statements provides a description of the material differences between Chilean GAAP and U.S. GAAP and a reconciliation to U.S. GAAP of net income for the six-month periods ended June 30, 2005 and 2006 and shareholders' equity at June 30, 2005 and 2006.

	At and for the years ended December 31,					At and for the year ended	At and for the year ended
	2001	2002	2003	2004	2005	2005	2005
	(in millions of constant Ch\$ of December 31, 2005)(1)					(in thousands of U.S.\$)(1)(2)	(in millions of U.S.\$)(3)
<b>CONSOLIDATED INCOME STATEMENT DATA</b>							
<b>Chilean GAAP:</b>							
Interest revenue	639,738	1,105,866	651,540	812,032	985,669	1,916,860	445,131
Interest expense	(360,962)	(549,012)	(330,119)	(326,743)	(439,790)	(855,273)	(185,095)
Net interest revenue	278,776	556,854	321,421	485,289	545,879	1,061,587	260,036
Provisions for loan losses	(38,886)	(70,831)	(71,592)	(83,677)	(63,532)	(123,554)	(30,199)
Total fees and income from services, net	53,357	109,497	118,762	126,013	138,366	269,085	65,100
Other operating income, net (3)	13,808	(14,815)	169,373	20,555	(12,514)	(24,336)	13,000
Other income and expenses, net	11,013	(34,259)	2,132	(4,206)	(21,468)	(41,749)	(20,300)
Operating expenses	(169,970)	(307,487)	(265,749)	(277,989)	(279,053)	(542,683)	(136,560)
Loss from price-level restatement	(8,408)	(13,962)	(8,179)	(12,417)	(18,140)	(35,227)	(4,900)
Income before income taxes	127,177	198,054	266,169	253,570	289,538	563,073	146,100
Income (taxes) benefits	3,908	(29,409)	(46,382)	(47,578)	(49,828)	(96,902)	(25,700)
Net income	131,084	168,645	219,786	205,991	239,710	466,171	120,400
Net income per share	1.33	0.89	1.17	1.09	1.27	0.00247	0.6
Net income per ADS (4).	1,376.64	929.83	1,211.82	1,135.71	1,321.61	2.57	663.8
Dividends per share (5)	1.03	1.33	0.89	1.17	1.09	0.00212	1.0
Dividends per ADS (5)	1,068.90	1,376.64	929.83	1,211.82	1,135.71	2.21	1,135.7
Weighted-average shares outstanding (in millions)	98,934.2	188,446.1	188,446.1	188,446.1	188,446.1		188,446
<b>U.S. GAAP:</b>							
Net interest income (6)	513,803	552,831	299,796	464,832	553,121	1,075,671	273,800
Provision for loan losses	(76,785)	(70,912)	(91,093)	(67,493)	(64,561)	(125,554)	(31,200)
Amortization of goodwill	43,040						
Net income	170,949	148,071	189,778	206,130	226,042	439,591	109,700
Net income per Share (7)	0.91	0.79	1.01	1.10	1.20	0.00233	0.5
Net income per ADS (7).	942.55	816.41	1,046.34	1,136.50	1,246.26	2.42	605.2
Weighted-avg. shares outstanding (in millions)	188,446.1	188,446.1	188,446.1	188,446.1	188,446.1		188,446
Weighted-avg. ADS outstanding (in millions)	181.377	181.377	181.377	181.377	181.377		181.377



	At and for the years ended December 31,					At and	
	2001	2002	2003	2004	2005	2005	2005
	(in millions of constant Ch\$ of December 31, 2005)(1)					(in thousands of U.S.)(1)(2)	(in millions of U.S.)(1)(2)
<b>CONSOLIDATED BALANCE SHEET DATA</b>							
<b>Chilean GAAP:</b>							
Cash and due from banks	613,247	1,048,680	1,044,980	982,576	1,224,962	2,382,221	1,397,221
Investments (8)	1,042,365	2,679,370	2,032,066	2,061,505	1,249,495	2,429,931	1,483,111
Loans, net of allowances	5,458,235	8,253,544	7,911,569	8,752,111	9,996,407	19,440,321	9,606,000
Loan loss allowances	(104,268)	(179,727)	(178,639)	(179,559)	(147,866)	(287,560)	(177,900)
Derivatives (9)	□	□	□	□	□	□	131,600
Other assets	348,494	218,599	303,873	433,377	347,923	676,617	1,365,900
Total assets (6)	7,462,341	12,500,190	11,596,376	12,507,481	13,096,821	25,469,791	13,984,111
Deposits	3,837,001	6,522,038	5,868,778	6,991,517	8,075,521	15,704,714	5,468,900
Other interest-bearing liabilities	2,499,893	4,203,590	3,600,611	3,279,243	2,842,461	5,527,824	3,138,500
Derivatives (9)	□	□	□	□	□	□	115,800
Shareholders' equity	594,907	1,032,570	1,080,366	1,069,103	1,081,832	2,103,872	992,200
<b>U.S. GAAP:</b>							
Total assets	12,856,751	12,152,674	11,220,032	12,256,764	13,837,675	26,910,552	13,960,500
Long-term borrowings	3,999,436	3,314,851	2,545,906	1,870,374	1,427,677	2,776,447	1,676,700
Shareholders' equity	1,513,766	1,917,506	1,920,773	1,911,668	1,898,262	3,691,608	1,854,900
Goodwill	555,624	789,779	789,779	789,779	789,779	1,535,908	798,700



	At and for the year ended December 31,					At and for the six-months ended June 30,	
	2001	2002	2003	2004	2005	2005	2006
<b>CONSOLIDATED RATIOS</b>							
<b>Chilean GAAP:</b>							
Profitability and performance:							
Net interest margin(10)	4.5%	4.8%	3.0%	4.4%	4.7%	4.5%	4.7%
Return on average total assets(11)	1.9%	1.3%	1.8%	1.7%	1.8%	1.8%	1.9%
Return on average shareholders' equity(12)	23.2%	16.2%	22.1%	20.2%	24.1%	23.1%	26.1%
Capital:							
Average shareholders' equity as a percentage of average total assets	8.1%	8.3%	8.1%	8.2%	7.4%	7.8%	7.4%
Total liabilities as a multiple of shareholders' equity	11.5	11.1	9.7	11.7	12.1	14.1	14.0
Credit Quality:							
Substandard loans as a percentage of total loans(13)	2.2%	3.2%	3.6%	3.7%	2.6%	3.2%	3.0%
Allowance for loan losses as percentage of total loans	2.1%	2.1%	2.2%	2.0%	1.5%	1.9%	1.3%
Past due loans as a percentage of total loans(14)	1.3%	2.1%	2.2%	1.5%	1.1%	1.3%	0.8%
Operating Ratios:							
Operating expenses/operating revenue(15)	49.1%	47.2%	43.6%	44.0%	41.5%	40.4%	37.0%
Operating expenses/average total assets (16)	2.4%	2.3%	2.2%	2.2%	2.1%	2.0%	1.9%
Ratio of earnings to fixed charges(17):							
Including interest on deposits	1.35	1.36	1.81	1.77	1.65	1.82	1.67
Excluding interest on deposits	1.68	1.65	2.34	2.26	2.46	2.57	2.61
<b>U.S. GAAP(18):</b>							
Profitability and performance:							
Net interest margin (19)	4.5%	4.7%	2.8%	4.3%	4.8%	4.7%	4.9%
Return on average total assets (20)	1.4%	1.2%	1.6%	1.8%	1.7%	1.6%	1.9%
Return on average shareholders' equity (21)	11.7%	8.6%	9.9%	10.8%	11.9%	11.6%	14.4%

Ratio of earnings to fixed charges(17):

Including interest on deposits	1.36	1.37	1.83	1.87	1.71	1.88	1.73
Excluding interest on deposits	1.71	1.67	2.35	2.43	2.51	2.65	2.70

#### OTHER DATA

Inflation Rate(22)	2.6%	2.8%	1.1%	2.4%	3.7%	2.7%	3.9%
Revaluation (devaluation) rate (Ch\$/U.S.\$) at period end(22)	14.6%	8.6%	(15.9%)	(6.6%)	(8.1%)	(5.5%)	(9.1%)
Number of employees at period end(23)	4,489	8,314	7,535	7,380	7,482	7,383	7,782
Number of branches and offices at period end	169	347	345	315	352	327	367

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- (1) Except per share data, percentages and ratios, share amounts, employee numbers and branch numbers.
  - (2) Amounts stated in U.S. dollars at and for the year ended December 31, 2005 have been translated from Chilean pesos at the observed exchange rate of Ch\$514.21 = U.S.\$1.00 at December 30, 2005. Amount stated in U.S. dollars at and for the six-months ended June 30, 2006 have been translated from Chilean pesos at the observed exchange rate of Ch\$547.31 = U.S. \$1.00 at June 30, 2006. See "Item 1: Key Information" Exchange Rates" for more information on the observed exchange rate.
  - (3) Includes in the six months ended June 30, 2006, a gain of Ch\$7,089 million resulting from the application of new accounting principles in that period. See "Item 3: Operating and Financial Review and Prospects" New Accounting Standards for Financial investments and Derivatives" and Note 1 of our Unaudited Consolidated Financial Statements.
  - (4) 1 ADS = 1,039 shares of common stock.
  - (5) The dividends per share of common stock and per ADS are determined based on the previous year's net income. The dividend per ADS is calculated on the basis of 1,039 shares per ADS.
  - (6) Net interest income and total assets on a U.S. GAAP basis have been determined by applying the relevant U.S. GAAP adjustments to net interest income and total assets presented in accordance with Article 9 of Regulation S-X. See Note 27 to our Consolidated Financial Statements at and for the years ended December 31, 2001, 2002, 2003, 2004 and 2005 and Note 26 of our Unaudited Consolidated Financial Statements at and for the six months ended June 30, 2005 and 2006.
  - (7) Net income per share and per ADS in accordance with U.S. GAAP has been calculated on the basis of the weighted-average number of shares or ADSs, as applicable, outstanding during the period.
  - (8) Includes principally Chilean government securities, corporate securities, other financial investments and investment collateral under agreements to repurchase.
  - (9) At June 30, 2006, derivatives are valued at market price and classified as a separate line item in the balance sheet. At prior dates, derivatives are classified under "other assets" and "other liabilities", and generally recorded at net notional amount. Our derivatives holdings at June 30, 2005 have been reclassified from "other assets" and "other liabilities" to "derivatives", but have not been marked to market as would be required under currently applicable accounting principles. Amounts at December 31, 2005 and at dates prior to June 30, 2005 have not been reclassified. See "Item 3: Operating



and Financial Review and Prospects—New Accounting Standards for Financial Investments and Derivatives— and Note 1 of our Unaudited Consolidated Financial Statements.

- (10) Net interest revenue (net interest revenue for the six months ended June 30, 2005 and 2006 is annualized (multiplied by 2)) divided by average interest earning assets (as presented in —Item 3: Selected Statistical Information—).
- (11) Net income (net income for the six months ended June 30, 2005 and 2006 is annualized (multiplied by 2)) divided by average total assets (as presented in —Item 3: Selected Statistical Information—).
- (12) Net income (net income for the six months ended June 30, 2005 and 2006 is annualized (multiplied by 2)) divided by average shareholders' equity (as presented in —Item 3: Selected Statistical Information—).
- (13) Substandard loans in the old rating system included all loans rated B- or worse. In the new loan risk classification system which took effect in 2004, substandard loans include all consumer and mortgage loans rated B- or worse and commercial loans rated C1 or worse. See —Item 3E-Asset and Liability Management-Analysis of Substandard Loans and Amounts Past Due— .
- (14) Past due loans are loans the principal or interest amount of which is overdue for 90 or more days, and do not include the installments of such loans that are not overdue or that are less than 90 days overdue, unless legal proceedings have been commenced for the entire outstanding balance according to the terms of the loan.
- (15) Operating revenue includes —Net interest revenue,— —Total fees and income from services, net— and —Other operating income, net—.
- (16) For the six months ended June 30, 2005 and 2006, operating expenses have been annualized (multiplied by 2).
- (17) For the purpose of computing the ratios of earnings to fixed charges, earnings consist of earnings before income tax and fixed charges. Fixed charges consist of gross interest expense and the proportion deemed representative of the interest factor of rental expense.
- (18) The following ratios have been calculated using U.S. GAAP figures except for net interest margin. See footnote 18 regarding calculation of net interest margin.
- (19) Net interest margin has been determined by applying the relevant U.S. GAAP adjustments to net interest income for the six month periods ended June 30, 2005 and 2006 amortized (multiplied by 2) presented in accordance with Article 9 of Regulation S-X divided by interest earning assets which is calculated on a Chilean GAAP basis. See Note 27(y) to our Consolidated Financial Statements at and for the years ended December 31, 2001, 2002, 2003, 2004 and 2005 and Note 26(y) of our Unaudited Consolidated Financial Statements at and for the six months ended June 30, 2005 and 2006. For the six months ended June 30, 2005 and 2006, net interest margin is annualized (multiplied by 2).
- (20) Net income divided by average total assets. Average total assets were calculated as an average of the beginning and ending balance for each year, and total assets on a U.S. GAAP basis has been determined by applying the relevant U.S. GAAP adjustments to total assets presented in accordance with Article 9 of Regulation S-X. See Note 27 to our Consolidated Financial Statements at and for the years ended December 31, 2001, 2002, 2003, 2004 and 2005 and Note 26 of our Unaudited Consolidated Financial Statements at and for the six months ended June 30, 2005 and 2006. For the six months ended June 30, 2005 and 2006, net income has been annualized (multiplied by 2).
- (21) Average shareholders' equity was calculated as an average of the beginning and ending balance for each year. Shareholders' equity on a U.S. GAAP basis has been determined by applying the relevant U.S. GAAP adjustments to shareholders' equity presented in accordance with Article 9 of Regulation S-X. See Note 27(y) to our Consolidated Financial Statements at and for the years ended December 31, 2001, 2002, 2003,

2004 and 2005 and Note 26(y) of our Unaudited Consolidates Financial Statements at and for the six months ended June 30, 2005 and 2006. For the six months ended June 30, 2005 and 2006, net income has been annualized (multiplied by 2).

(22) Based on information published by the Central Bank.

(23) The number of employees presented in this table at December 31, 2001 are those of Santiago only, excluding subsidiaries, because consolidated employee information was not available in that year.

**Exchange Rates**

Chile has two currency markets, the *Mercado Cambiario Formal*, or the Formal Exchange Market and the *Mercado Cambiario Informal*, or the Informal Exchange Market. Under Law 18,840, the organic law of the Central Bank, or the Central Bank Act (*Ley Orgánica Constitucional del Banco Central de Chile*), the Central Bank determines which purchases and sales of foreign currencies must be carried out in the Formal Exchange Market. Pursuant to Central Bank regulations which are currently in effect, all payments, remittances or transfers of foreign currency abroad which are required to be effected through the Formal Exchange Market may be effected with foreign currency procured outside the Formal Exchange Market. The Formal Exchange Market is comprised of the banks and other entities so authorized by the Central Bank. The conversion from pesos to U.S. dollars of all payments and distributions with respect to the ADSs described in this Report must be transacted at the spot market rate in the Formal Exchange Market. Current regulations require that the Central Bank be informed of certain transactions and that they be effected through the Formal Exchange Market.

Purchases and sales of foreign currencies performed may be legally carried out in the Informal Exchange Market. The Informal Exchange Market reflects transactions carried out at informal exchange rates by entities not expressly authorized to operate in the Formal Exchange Market. There are no limits imposed on the extent to which the rate of exchange in the Informal Exchange Market can fluctuate above or below the observed exchange rate. On June 30, 2006, the exchange rate in the Informal Exchange Market was Ch\$538.85 or 1.5% lower than the published observed exchange rate for such date of Ch\$547.31 per U.S.\$1.00.

The following table sets forth the annual low, high, average and period-end observed exchange rate for U.S. dollars for each of the following periods, as reported by the Central Bank. We make no representation that the Chilean peso or the U.S. dollar amounts referred to herein actually represent, could have been or could be converted into U.S. dollars or Chilean pesos, as the case may be, at the rates indicated, at any particular rate or at all.

Year	Daily Observed Exchange Rate Ch\$ Per U.S.\$(1)			
	Low (2)	High(2)	Average (3)	Period End (4)
2001	557.13	716.62	634.94	656.20
2002	641.75	756.56	689.24	712.38
2003	593.10	758.21	691.54	599.42
2004	559.21	649.45	609.55	559.83
2005	509.70	592.75	559.86	514.21
Month				
May 2006	512.76	532.92	520.79	531.11
June 2006	529.91	549.63	542.46	547.31
July 2006	537.56	545.93	540.62	539.41
August 2006	530.69	545.36	538.53	537.77
September 2006	536.63	540.80	538.65	538.22
October 2006	524.12	537.63	530.95	525.99
November 2006 (5)	523.34	529.66	526.86	529.17

Source: Central Bank.

- (1) Nominal figures.
- (2) Exchange rates are the actual low and high, on a day-by-day basis for each period.
- (3) The average of monthly average rates during the year.
- (4) As reported by the Central Bank the first business day of the following period.
- (5) Period from November 1 through November 24, 2006.

#### Dividends

Under the current General Banking Law, a Chilean bank may only pay a single dividend per year (i.e., interim dividends are not permitted). Santander-Chile's annual dividend is proposed by its Board of Directors and is approved by the shareholders at the annual ordinary shareholders' meeting held the year following that in which the dividend is generated. For example, the 2005 dividend must be proposed and approved during the first four months of 2006. Following shareholder approval, the proposed dividend is declared and paid. Historically, the dividend for a particular year has been declared and paid no later than one month following the shareholders meeting. Dividends are paid to shareholders of record on the fifth day preceding the date set for payment of the dividend. The applicable record dated for the payment of dividends to holders of ADSs will, to the extent practicable, be the same.

Under the General Banking Law a bank must distribute cash dividends in respect of any fiscal year in an amount equal to at least 30% of its net income for that year, as long as the dividend does not result in the infringement of minimal capital requirements. The balances of our distributable net income are generally retained for use in our business (including for the maintenance of any required legal reserves). Although our Board of Directors currently intends to pay regular annual dividends, the amount of dividend payments will depend upon, among other factors, our then current level of earnings, capital and legal reserve requirements, as

well as market conditions, and there can be no assurance as to the amount or timing of future dividends.

Dividends payable to holders of ADSs are net of foreign currency conversion expenses of the depositary and will be subject to the Chilean withholding tax currently at the rate of 35% (subject to credits in certain cases as described in "Taxation" Chilean Tax Considerations See "Item 10E: Taxation" of our Annual Report on 20-F for the fiscal year ended December 31, 2005. Owners of the ADSs will not be charged any dividend remittance fees by the depositary with respect to cash or stock dividends.

Under the Foreign Investment Contract (as defined herein), the Depositary, on behalf of ADS holders, is granted access to the Formal Exchange Market to convert cash dividends from Chilean pesos to U.S. dollars and to pay such U.S. dollars to ADS holders outside Chile, net of taxes, and no separate registration by ADS holders is required. In the past, Chilean law required that holders of shares of Chilean companies who were not residents of Chile to register as foreign investors under one of the foreign investment regimes contemplated by Chilean law in order to have dividends, sale proceeds or other amounts with respect to their shares remitted outside Chile through the Formal Exchange Market. On April 19, 2001, the Central Bank

deregulated the Exchange Market eliminating the need to obtain approval from the Central Bank in order to remit dividends, but at the same time this eliminated the possibility of accessing the Formal Exchange Market. These changes do not affect the current Foreign Investment Contract, which was signed prior to April 19, 2001, which grants access to the Formal Exchange Market with prior approval of the Central Bank. See *Item 10D: Exchange Controls* of our Annual Report on 20-F for the fiscal year ended December 31, 2005.

The following table presents dividends paid by us in nominal terms in the following years:

Year	Dividend Ch\$ mn (1)	Per share Ch\$/share (2)	Per ADR Ch\$/ADR (3)	% over earnings(4)
2003	157,315	0.83	867.40	100
2004	206,975	1.10	1,141.16	100
2005	198,795	1.05	1,096.06	100
2006	155,812	0.83	859.08	65

(1) Million of nominal pesos.

(2) Calculated on the basis of 188,446 million shares

(3) Calculated on the basis of 1,039 shares per ADS.

(4) Calculated by dividing dividend paid in the year by net income for the previous year.

## B. Risk Factors

You should carefully consider the following risk factors, as well as all the other information presented in this Report before investing in securities issued by us. The risks and uncertainties described below are not the only ones that we face. Additional risks and uncertainties that we do not know about or that we currently think are immaterial may also impair our business operations. Any of the following risks, if they actually occur, could materially and adversely affect our business, results of operations, prospects and financial condition.

We are subject to market risks that are presented both in this subsection and in *Item 3: Operating and Financial Review and Prospect.* and *Item 8: Quantitative and Qualitative Disclosures About Market Risk*

### Risks Associated with Our Business

#### **Increased competition and industry consolidation may adversely affect results of our operations.**

The Chilean market for financial services is highly competitive. We compete with other Chilean private-sector domestic and foreign banks, with Banco del Estado, a public-sector bank, with department stores and the larger supermarket chains that make consumer loans and sell other financial products to a large portion of the Chilean population. The lower-middle to middle-income segments of the Chilean population and the small and medium-sized corporate segments have become the target markets of several banks, and competition in these segments is likely to increase. As a result, net interest margins in these segments are likely to decline. Although we believe that demand for financial products and services from individuals and for small and medium-sized companies will continue to grow during the remainder of the decade, we cannot assure you that net interest margins will be maintained at their current levels.

We also face competition from non-bank and non-finance competitors (principally department stores) with respect to some of our credit products, such as credit cards, consumer loans and insurance brokerage. In addition, we face competition from non-bank finance competitors, such as leasing, factoring and automobile finance companies, with respect to credit products, and from mutual funds, pension funds and insurance companies, with respect to savings products. Currently, banks continue to be the main suppliers of leasing, factoring and mutual funds, and the insurance sales business has seen rapid growth.



The increase in competition within the Chilean banking industry in recent years has led to, among other things, consolidation in the industry. For example, in January 2002, Banco de Chile and Banco de A. Edwards, the third and fifth largest banks in Chile respectively, merged to become the largest Chilean bank at that time. We expect the trends of increased competition and consolidation to continue and result in the formation of new large financial groups. Consolidation, which can result in the creation of larger and stronger competitors, may adversely affect our financial condition and results of operations by decreasing the net interest margins we are able to generate. In addition, Law No. 19,769 allows insurance companies to participate and compete with us in the residential mortgage and credit card businesses.

***Our allowances for impairment losses may not be adequate to cover our future actual losses to our loan portfolio.***

At June 30, 2006, our allowance for impairment losses on loans was Ch\$147,583 million, and the ratio of our allowance for impairment losses to total loans was 1.32% . The amount of allowances is based on our current assessment of and

expectations concerning various factors affecting the quality of our loan portfolio. These factors include, among other things, our borrower's financial condition, repayment ability and repayment intention, the realizable value of any collateral, the prospects for support from any guarantor, Chile's economy, government macroeconomic policies, interest rates and legal and regulatory environment. Many of these factors are beyond our control. If our assessment of and expectations concerning the above-mentioned factors differ from actual developments, or if the quality of our loan portfolio deteriorates or the future actual losses exceed our estimates, our allowance for impairment losses may not be adequate to cover actual losses and we may need to make additional provisions for impairment losses, which may materially and adversely affect our results of operations and financial condition.

***Our exposure to individuals and small businesses could lead to higher levels of past due loans, allowances for loan losses and charge-offs.***

A substantial number of our customers consists of individuals (approximately 41.4% of the value of the total loan portfolio at June 30, 2006) and, to a lesser extent, small and medium-sized companies (those with annual sales of less than US\$2.2 million) which comprised approximately 15.1% of the value of the total loan portfolio at June 30, 2006. As part of our business strategy, we seek to increase lending and other services to small companies and individuals. Small companies and individuals are, however, more likely to be adversely affected by downturns in the Chilean economy than large corporations and high-income individuals. In addition, at June 30, 2006, our residential mortgage loans represented 25.0% of our total loans. If the economic conditions and real estate market in Chile experience a significant downturn, our asset quality, results of operations and financial condition may be materially and adversely affected. As a result of these factors, in the future we may experience higher levels of past due loans, which could result in higher provisions for loan losses. There can be no assurance that the levels of past due loans and subsequent write-offs will not be materially higher in the future.

***If we are unable to maintain the quality of our loan portfolio, our financial condition and results of operations may be materially and adversely affected.***

At June 30, 2006, our past due loans were Ch\$88,559 million, and the ratio of our past due loans to total loans was 0.79% . For additional information on our asset quality, see [Item 3E: Asset and Liability Management] Selected Statistical Information] in our 2006 Interim Report. We seek to continue to improve our credit risk management policies and procedures. However, we cannot assure you that our credit risk management policies, procedures and systems are free from any deficiency. Failure of credit risk management policies may result in an increase in level of non-performing loans and adversely affect the quality of our loan portfolio. In addition, the quality of our loan portfolio may also deteriorate due to various other reasons, including factors beyond our control. If such deterioration were to occur, it would materially and adversely affect our financial conditions and results of operations.

***The value of the collateral securing our loans may not be sufficient, and we may be unable to realize the full value of the collateral securing our loan portfolio.***

The value of the collateral securing our loan portfolio may significantly fluctuate or decline due to factors beyond our control, including macroeconomic factors affecting Chile's economy. However, we may not have current information on the value of collateral, which may result in an inaccurate assessment for impairment losses of our loans secured by such collateral. If this were to occur, we may need to make additional provisions to cover actual impairment losses of our loans, which may materially and adversely affect our results of operations and financial condition.

Additionally, there are certain provisions under Chilean law that may affect our ability to foreclose or liquidate residential mortgages granted to us by our customers if the affected real estate has been declared as [family property] by a court. Furthermore, foreclosure will be extremely limited if any party using the real estate has filed with a court a petition requesting that such real estate be declared as family property.

***The growth of our loan portfolio may expose us to increased loan losses.***

From December 31, 2000 to June 30, 2006, our aggregate loan portfolio (on an unconsolidated combined basis) grew by 48.8% in nominal terms to Ch\$11,156,529 million (US\$20,384 million), while our consumer loan portfolio grew by 123.7% in nominal terms to Ch\$1,382,600 million (US\$2,526 million), excluding lines of credit and calculated in accordance with the loan classification system of the Superintendency of Banks. Because the method of classification of loans used by the Superintendency of Banks for its public information differs in minor

respects from that used by us for internal accounting purposes, the foregoing figures may differ from the figures included in our financial statements. The further expansion of our loan portfolio (particularly in the consumer, small and mid-sized companies and real estate segments) can be expected to expose us to a higher level of loan losses and require us to establish higher levels of provisions for loan losses.

***Our loan portfolio may not continue to grow at the same rate.***

There can be no assurance that in the future our loan portfolio will continue to grow at the same or similar rates as the historical growth rate previously experienced by Santiago or Old Santander-Chile. Average loan growth has remained significant in the last five years. According to the Superintendency of Banks, from December 31, 2000 to June 30, 2006, the aggregate amount of loans outstanding in the Chilean banking system (on an unconsolidated basis) grew 74.1% in nominal terms to Ch\$48,873,852 million (US\$89,298 million) at June 30, 2006. A reversal of the rate of growth of the Chilean economy, a slowdown in the growth of customer demand, an increased in market competition or changes in governmental regulations, could adversely affect the rate of growth of our loan portfolio and our risk index and, accordingly, increase our required allowances for loan losses.

***The effectiveness of our credit risk management is affected by the quality and scope of information available in Chile.***

In assessing customers' creditworthiness, we rely largely on the credit information available from our own internal databases, the Superintendency of Banks, Dicom (a nationwide credit bureau) and other sources. Due to limitations on the availability of information and the developing information infrastructure in Chile, our assessment of the credit risks associated with a particular customer may not be based on complete, accurate or reliable information. In addition, although we have been improving our credit scoring systems to better assess borrowers' credit risk profiles, we cannot assure you that our credit scoring systems collect complete or accurate information reflecting the actual behavior of customers or that their credit risk can be assessed correctly. Without complete, accurate and reliable information, we have to rely on other publicly available resources and our internal resources, which may not be effective. As a result, our ability to effectively manage our credit risk may be materially and adversely affected.

***Fluctuations in the rate of inflation may affect our results of operations.***

Although Chilean inflation has been moderate in recent years, Chile has experienced high levels of inflation in the past. High levels of inflation in Chile could adversely affect the Chilean economy and have an adverse effect on our business, financial condition and results of operations. In 2005, inflation rate reached 3.7% compared to 2.4% in 2004. The annualized CPI inflation rate reached 3.9% as of June 2006 compared to 2.7% as of June 2005.

Our assets and liabilities are denominated in Chilean pesos, UF and foreign currencies. The UF is revalued in monthly cycles. On each day in the period beginning the tenth day of the current month through the ninth day of the succeeding month, the nominal peso value of the UF is indexed up (or down in the event of deflation) in order to reflect a proportional amount of the change in the Chilean Consumer Price Index during the prior calendar month. One UF equaled to Ch\$17,489.25 and Ch\$18,151.40 at June 30, 2005 and 2006, respectively. The effect of any changes in the nominal peso value of our UF denominated assets and liabilities is reflected in our results of operations as an increase (or decrease, in the event of deflation) in interest revenue and expense, respectively. Our net interest revenue will be positively affected by an inflationary environment to the extent that our average UF denominated assets exceed our average UF denominated liabilities. Our net interest revenue will be negatively affected by inflation in any period in which our average UF denominated liabilities exceed our average UF denominated assets. Our average UF denominated assets exceeded our average UF denominated liabilities by Ch\$1,108,952 million and Ch\$2,140,729 million for the six-months ended June 30, 2005 and 2006, respectively. We generally have more UF denominated financial assets than UF denominated financial liabilities and, therefore, benefits from positive monthly inflation figures and we actively manage the size of this gap in accordance with our views of futures inflation expectations. Although we currently benefit from moderate levels of inflation in Chile, due to the current structure of our assets and liabilities (i.e., a significant portion of our loans are indexed to the inflation rate, but there are no corresponding features in deposits, or other funding sources that would increase the size of our funding base), there can be no assurance that our business, financial condition and result of operations in the future will not be adversely affected by changing levels of inflation, especially in a period of deflation.

***Our results of operations are affected by interest rate volatility.***

Our results of operations depend to a great extent on our net interest revenue. In the first half of 2006, net interest revenue represented 86.5% of our net operating revenue. Changes in market interest rates could affect the interest rates earned on our interest-earning assets differently from the interest rates paid on our interest-bearing liabilities leading to a reduction in our net interest revenue or result in a decrease in customer's

demand for our loan or deposit products. Interest rates are highly sensitive to many factors beyond our control, including the reserve policies of the Central Bank, deregulation of the financial sector in Chile, domestic and international economic and political conditions and other factors. Any volatility in interest rates

could adversely affect our business, our future financial performance and the price of our securities. The following table shows the yields on the Chilean government's 90-day note as reported by the Central Bank of Chile at year-end for the last five years.

Year	Period-end 90 day note (%)
2002	2.88
2003	2.58
2004	2.32
2005	4.75
2006 (through June 30, 2006)	4.82

Source: Central Bank.

***Since our principal sources of funds are short-term deposits, a sudden shortage of funds could cause an increase in costs of funding and an adverse effect on our revenues.***

Customer deposits are our primary source of funding. At June 30, 2006, 80.3% of our customer deposits had remaining maturities of one year or less, or were payable on demand. A significant portion of our assets have longer maturities, resulting in a mismatch between the maturities of liabilities and the maturities of assets. If a substantial portion of our depositors withdraws their demand deposits or do not roll over their time deposits upon maturity, our liquidity position, results of operations and financial condition may be materially and adversely affected. We cannot assure you that in the event of a sudden or unexpected shortage of funds in the banking system, any money markets in which we operate will be able to maintain levels of funding without incurring high funding costs or the liquidation of certain assets. If this were to happen, our results of operations and financial condition may be materially and adversely affected.

***We may be unable to meet requirements relating to capital adequacy.***

We are required by the General Banking Law to maintain regulatory capital of at least 8% of our risk-weighted assets, net of required loan loss allowance and deductions, and paid-in capital and reserves (basic capital) of at least 3% of our total assets, net of required loan loss allowances. As a result of the merger between Old Santander-Chile and Santiago, we were required to maintain a minimum regulatory capital to risk-weighted assets ratio of 12%, which was reduced to 11% as of January 1, 2005. At June 30, 2006, the ratio of our basic capital to total assets, net of loan loss allowance, was 6.1%, and the ratio of our regulatory capital to risk-weighted assets, net of loan loss allowance and deductions, was 12.2%. Certain developments could affect our ability to continue to satisfy the current capital adequacy requirements applicable to us, including:

- the increase of risk-weighted assets as a result of the expansion of our business;
- the failure to increase our capital correspondingly;
- losses resulting from a deterioration in our asset quality;
- declines in the value of our investment instrument portfolio; and
- changes in accounting rules or in the guidelines regarding the calculation of the capital adequacy ratios of banks in Chile.

We may also be required to raise additional capital in the future in order to maintain our capital adequacy ratios above the minimum-required levels. Our ability to raise additional capital may be limited by numerous factors, including: our future financial condition, results of operations and cash flows; any necessary government regulatory approvals; our credit ratings; general market conditions for capital-raising activities by commercial banks and other financial institutions; and domestic and international economic, political and other conditions.

If we require additional capital in the future, we cannot assure you that we will be able to obtain such capital on favorable terms, in a timely manner or at all. Furthermore, the Superintendency of Banks may increase the minimum capital adequacy requirements applicable to us. Accordingly, although we currently meet the applicable

capital adequacy requirements, we may face difficulties in meeting these requirements in the future. If we fail to meet the capital adequacy requirements, we may be required to take corrective actions. These measures could materially and adversely affect our business reputation, financial condition and results of operations. In addition, if we are unable to raise sufficient capital in a timely manner, the growth of our loan portfolio and other risk-weighted assets may be restricted, and we may face significant challenges in implementing our business strategy. As a result, our prospects, results of operations and financial condition could be materially and adversely affected.

***Our business is highly dependant on proper functioning and improvement of information technology systems.***

Our business is highly dependant on the ability of our information technology systems to accurately process a large number of transactions across numerous and diverse markets and products in a timely manner. The proper functioning of our financial control, risk management, accounting, customer service and other data processing systems is critical to our business and our ability to compete effectively. We have backup data for our key data processing systems that could be used in the event of a catastrophe or a failure of our primary systems, and have established alternative communication networks where available. However, we do not operate all of our redundant systems on a real-time basis and cannot assure you that our business activities would not be materially disrupted if there were a partial or complete failure of any of these primary information technology systems or communication networks. Such failures could be caused by, among other things, software bugs, computer virus attacks or conversion errors due to system upgrading. In addition, any security breach caused by unauthorized access to information or systems, or intentional malfunctions or loss or corruption of data, software, hardware or other computer equipment, could have a material adverse effect on our business, results of operations and financial condition.

Our ability to remain competitive and achieve further growth will depend in part on our ability to upgrade our information technology systems and increase our capacity on a timely and cost-effective basis. Any substantial failure to improve or upgrade information technology systems effectively or on timely basis could materially and adversely affect our competitiveness, results of operations and financial condition.

***Operational problems or errors can have a material adverse impact on our business, financial condition and results of operations.***

Santander-Chile, like all large financial institutions, is exposed to many types of operational risks, including the risk of fraud by employees and outsiders, failure to obtain proper internal authorizations, failure to properly document transactions, equipment failures and errors by employees. Fraud or other misconduct by employees or third parties may be difficult to detect and prevent and could subject us to financial losses and sanctions imposed by governmental authorities as well as seriously harm our reputation. Although Santander-Chile maintains a system of operational controls, there can be no assurance that operational problems or errors will not occur and that their occurrence will not have a material adverse impact on our business, financial condition and results of operations.

***Banking regulations may restrict our operations and thereby adversely affect our financial condition and results of operations.***

We are subject to regulation by the Superintendency of Banks. In addition, we are subject to regulation by the Central Bank with regard to certain matters, including reserve requirements and interest rates and foreign exchange mismatches and market risks. During the Chilean financial crisis of 1982 and 1983, the Central Bank and the Superintendency of Banks strictly controlled the funding, lending and general business matters of the banking industry in Chile.

Pursuant to the *Ley General de Bancos, Decreto con Fuerza de Ley No. 3 de 1997*, or the General Banking Law, all Chilean banks may, subject to the approval of the Superintendency of Banks, engage in certain businesses other than commercial banking depending on the risk associated with such business and the financial strength of the bank. Such additional businesses include securities brokerage, mutual fund management, securitization, insurance brokerage, leasing, factoring, financial advisory, custody and transportation of securities, loan collection and financial services. The General Banking Law also applies to the Chilean banking system a modified version of the capital adequacy guidelines issued by the Basle Committee on Banking Regulation and Supervisory Practices and limits the discretion of the Superintendency of Banks to deny new banking licenses. There can be no assurance that regulators will not in the future impose more restrictive limitations on the activities of banks, including us, than those currently in effect. Any such change could have a material adverse effect on our financial condition or results of operations.

Historically, Chilean banks have not paid interest on amounts deposited in checking accounts. However, since June 1, 2002, the Central Bank allows banks to pay interest on checking accounts. Currently, there are no applicable restrictions on the interest that may be paid on checking accounts. We have begun to pay interest on some checking accounts under certain conditions. If competition or other factors lead us to pay higher interest



rates on checking accounts, to relax the conditions under which we pay interest or to increase the number of checking accounts on which we pay interest, any such change could have a material adverse effect on our financial condition or results of operations.

We must maintain higher regulatory capital to risk — weighted assets than other banks in Chile. The merger of Old Santander-Chile and Santiago required a special regulatory preapproval of the Superintendency of Banks, which was granted on May 16, 2002. The resolution granting this preapproval imposed a mandatory minimum regulatory capital to risk-weighted

assets ratio of 12% for the merged bank compared to the 8% minimum for other banks in Chile. Effective January 1, 2005, the Superintendency of Banks lowered our minimum regulatory capital to risk-weighted assets ratio to 11%. Although we have not failed in the past to comply with our capital maintenance obligations, there can be no assurance that we will be able to do so in the future.

***We are subject to regulatory inspections and examinations.***

We are also subject to various inspections, examinations, inquiries, audits and other regulatory requirements by Chilean regulatory authorities. We cannot assure you that we will be able to meet all the applicable regulatory requirements and guidelines, or that we will not be subject to sanctions, fines and other penalties in the future as a result of non-compliance. If sanctions, fines and other penalties are imposed on us for failure to comply with applicable requirements, guidelines or regulations, our business, financial condition, results of operations and our reputation and ability to engage in business may be materially and adversely affected.

**Risks Relating to Chile**

***Our growth and profitability depend on the level of economic activity in Chile.***

A substantial amount of our loans are to borrowers doing business in Chile. Accordingly, the recoverability of these loans in particular, our ability to increase the amount of loans outstanding and our results of operations and financial condition in general, are dependent to a significant extent on the level of economic activity in Chile. Our results of operations and financial condition could be affected by changes in economic or other policies of the Chilean government, which has exercised and continues to exercise a substantial influence over many aspects of the private sector, or other political or economic developments in Chile. We cannot assure you that the Chilean economy will continue to grow in the future or that those future developments in or affecting Chile's exports will not materially and adversely affect our business, financial condition or results of operations.

***Economic problems encountered by other countries may adversely affect the Chilean economy, our results of operations and the market value of our securities.***

The prices of securities issued by Chilean companies, including banks, are to varying degrees influenced by economic and market considerations in other countries. We cannot assure you that future developments in or affecting the Chilean economy, including consequences of economic difficulties in other markets, will not materially and adversely affect our business, financial condition or results of operations.

We are directly exposed to risks related to the weakness and volatility of the economic and political situation in Latin America, especially in Argentina and Brazil. Although the government have stimulated economic growth in Argentina, if Argentina's economic environment significantly deteriorates or does not further improve, the economy in Chile, as both a neighboring country and a trading partner, could also be affected and could experience slower growth than in recent years. The recent cuts in gas exports from Argentina to Chile could also adversely affect economic growth in Chile. Our business could be affected by an economic downturn in Brazil. This could result in the need for us to increase our loan allowances, thus affecting our financial results, our results of operations and the price of our securities. At June 30, 2006, approximately 3.9% of our loans were held abroad and 0.45% of our loans were comprised of loans to companies in Latin American countries. We cannot assure you that crisis and political uncertainty in other Latin American countries will not have an adverse effect on Chile, the price of our securities or our business.

***Currency fluctuations could adversely affect our financial condition and results of operations and the value of our securities.***

Any future changes in the value of the Chilean peso against the U.S. dollar could affect the dollar value of our securities. The peso has been subject to large devaluations and appreciations in the past and could be subject to significant fluctuations in the future. Our results of operations may be affected by fluctuations in the exchange rates between the peso and the dollar despite our policy and Chilean regulations relating to the general avoidance of material exchange rate exposure. In order to avoid material exchange rate exposure, we enter into forward exchange transactions. At June 30, 2006, the net position of our foreign currency-denominated assets and Chilean peso-denominated assets that contain repayment terms linked to changes in foreign currency exchange rates exceeded our foreign currency-denominated liabilities and Chilean peso-denominated liabilities that contain repayment terms linked to changes in foreign currency exchange rates by Ch\$95,458 million

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(US\$174.4 million). The following table shows the value of the Chilean peso relative to the U.S. dollar as reported by the Central Bank at year-end for the last four years.

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Year	Exchange rate (Ch\$) Year-end	Devaluation (Revaluation) (%)
2002	712.38	8.6%
2003	599.42	(15.9%)
2004	559.83	(6.6%)
2005	514.21	(8.1%)
2006 (through June 30, 2006)	547.31	6.4%

Source: Central Bank.

We may decide to change our policy regarding exchange rate exposure. Regulations that limit such exposures may also be amended or eliminated. Greater exchange rate risk will increase our exposure to the devaluation of the peso, and any such devaluation may impair our capacity to service foreign-currency obligations and may, therefore, materially and adversely affect our financial condition and results of operations. Notwithstanding the existence of general policies and regulations that limit material exchange rate exposures, the economic policies of the Chilean government and any future fluctuations of the peso against the dollar could affect our financial condition and results of operations.

Furthermore, Chilean trading in the shares underlying our ADSs will be conducted in pesos. Cash distributions with respect to our shares of common stock are received in Chilean pesos by the depositary which then will convert such amounts to U.S. dollars at the then-prevailing exchange rate for the purpose of making payments in respect of our ADSs. If the value of the Chilean peso falls relative to the U.S. dollar, the dollar value of our ADSs and any distributions to be received from the depositary will be reduced. In addition, the depositary will incur customary current conversion costs (to be borne by the holders of our ADSs) in connection with the conversion and subsequent distribution of dividends or other payments.

***Chile's banking regulatory and capital markets environment is continually evolving and may change.***

Chilean laws, regulations, policies and interpretations of laws relating to the banking sector and financial institutions are continually evolving and changing. For example, legislation is being discussed regarding the elimination of reserve requirements, permissions to enter the pension fund business and modifications to maximum lending rates. Changes in banking regulations may materially and adversely affect the bank's business, financial condition and results of operations.

In addition, certain aspects of Chilean legislation governing the capital markets is currently being reviewed by the Chilean Congress and a new law known as *Mercado de Capitales II* (MK2) is expected to be passed soon. MK2 is expected to, among other things, modify certain provisions set forth in the General Banking Law that limit the lending activity of banks. Under current legislation, banks are not allowed to grant unsecured loans to one individual or entity in an aggregate amount in excess of 5% of the regulatory capital of the bank. This limit is expected to be increased to 25% if the amount that exceeds said 5% corresponds to loans secured by collateral with an aggregate value equal to or higher than such excess. MK2 is expected to increase these limits to 10% and 30% of the regulatory capital of the bank, respectively, unless the loans are granted to individuals or entities directly or indirectly related to the property or management of the bank, in which case the limits are expected to be maintained in 5% and 25%, respectively. Although any such decrease may increase our lending activity, it may also increase the risks associated with the growth of our loan portfolio. See *Risks Related to Our Business* *The growth of our loan portfolio may expose us to increased loan losses.*

***Any downgrading of Chile debt credit rating for domestic and international debt by international credit rating agencies may adversely affect our business, our future financial performance, stockholder's equity and the price of our shares and ADSs.***

Our ratings are equivalent to the Chilean sovereign ratings. In 2006, Moody's improved its rating for the Republic of Chile and also for us. Any adverse revisions to Chile's credit ratings for domestic and international debt by international rating agencies may adversely affect our ratings, and our business, future financial

performance, stockholder's equity and the price of our equity shares and ADSs.

***Chile has different corporate disclosure and accounting standards than those you may be familiar with in the United States.***

We prepare our financial statements in accordance with Chilean GAAP, which requires management to make estimates and assumptions with respect to certain matters that are inherently uncertain. The consolidated financial statements include various estimates and assumptions, including but not limited to the adequacy of the allowance for loan losses, estimates of the fair value of certain financial instruments, the selection of useful lives of certain assets and the valuation and recoverability of

goodwill and deferred taxes. We evaluate these estimates and judgments on an ongoing basis. Management bases its estimates and judgments on historical experience and on various other factors that are believed to be reasonable under the circumstances. Actual results in future periods could differ from those produced by such estimates and assumptions, and if these differences were significant enough, our reported results of operations would be affected materially.

Accounting, financial reporting and securities disclosure requirements in Chile differ from those in the United States. Accordingly, the information about us available to you will not be the same as the information available to shareholders of a U.S. financial institution. There are also material differences between Chilean and U.S. accounting and financial reporting standards. As a result, Chilean financial statements and reported earnings generally differ from those reported based on U.S. accounting and reporting standards.

As a regulated financial institution, we are required to submit to the Superintendency of Banks unaudited unconsolidated balance sheets and income statements, excluding any note disclosure, prepared in accordance with Chilean GAAP and the rules of the Superintendency of Banks on a monthly basis. Such disclosure differs in a number of significant respects from information generally available in the United States with respect to U.S. financial institutions.

The securities laws of Chile, which govern open or publicly listed companies such as us, have as a principal objective promoting disclosure of all material corporate information to the public. Chilean disclosure requirements, however, differ from those in the United States in some material respects. In addition, although Chilean law imposes restrictions on insider trading and price manipulation, applicable Chilean laws are different from those in the United States and in certain respects the Chilean securities markets are not as highly regulated and supervised as the U.S. securities markets.

***Our status as a controlled company and a foreign private issuer exempts us from certain of the corporate governance standards of the New York Stock Exchange, limiting the protections afforded to investors.***

We are a "controlled company" and a "foreign private issuer" within the meaning of the New York Stock Exchange corporate governance standards. Under the New York Stock Exchange rules, a controlled company is exempt from certain New York Stock Exchange corporate governance requirements. In addition, a foreign private issuer may elect to comply with the practice of its home country and not to comply with certain New York Stock Exchange corporate governance requirements, including the requirements that (1) a majority of the board of directors consist of independent directors, (2) a nominating and corporate governance committee be established that is composed entirely of independent directors and has a written charter addressing the committee's purpose and responsibilities, (3) a compensation committee be established that is composed entirely of independent directors and has a written charter addressing the committee's purpose and responsibilities and (4) an annual performance evaluation of the nominating and corporate governance and compensation committees be undertaken. We currently use these exemptions and, following this offering, intend to continue using these exemptions. Accordingly, you will not have the same protections afforded to shareholders of companies that are subject to all New York Stock Exchange corporate governance requirements.

***Chile imposes controls on foreign investment and repatriation of investments that may affect your investment in, and earnings from, our ADSs.***

Equity investments in Chile by persons who are not Chilean residents have generally been subject to various exchange control regulations which restrict the repatriation of the investments and earnings therefrom. In April 2001, the Central Bank eliminated the regulations that affected foreign investors except that investors are still required to provide the Central Bank with information related to equity investments and conduct such operations within Chile's Formal Exchange Market. The ADSs are subject to a contract, dated May 17, 1994, among the depositary, us and the Central Bank that remains in full force and effect. The ADSs continue to be governed by the provisions of such contract subject to the regulations in existence prior to April 2001 (the "Foreign Investment Contract"). The contract grants the depositary and the holders of the ADSs access to the Formal Exchange Market, which permits the depositary to remit dividends it receives from us to the holders of the ADSs. The contract also permits ADS holders to repatriate the proceeds from the sale of shares of our common stock withdrawn from the ADR facility, or that have been received free of payment as a consequence of spin-offs, mergers, capital increases, wind-ups, share dividends or preemptive rights transfers, enabling them to acquire

the foreign currency necessary to repatriate earnings from such investments. Pursuant to Chilean law, the contract cannot be amended unilaterally by the Central Bank, and there are judicial precedents (although not binding with respect to future judicial decisions) indicating that contracts of this type may not be abrogated by future legislative changes or resolutions of the Advisory Council of the Central Bank. Holders of shares of our common stock, except for shares of our common stock withdrawn from the ADS facility or received in the manner described above, are not entitled to the benefits of the contract, may not have access to the Formal Exchange Market, and may have restrictions on their ability to repatriate investments in shares of our common stock and earnings therefrom.

Holders of ADSs are entitled to receive dividends on the underlying shares to the same extent as the holders of shares. Dividends received by holders of ADSs will be paid net of foreign currency exchange fees and expenses of the depository and will be subject to Chilean withholding tax, currently imposed at a rate of 35.0% (subject to credits in certain cases). If for any reason, including changes in Chilean law, the depository were unable to convert Chilean pesos to U.S. dollars, investors would receive dividends and other distributions, if any, in Chilean pesos.

We cannot assure you that additional Chilean restrictions applicable to holders of our ADSs, the disposition of the shares underlying them or the repatriation of the proceeds from such disposition or the payment of dividends will not be imposed in the future, nor can we advise you as to the duration or impact of such restrictions if imposed.

***ADS holders may not be able to effect service of process on, or enforce judgments or bring original actions against, us, our directors or our executive officers, which may limit the ability of holders of ADSs to seek relief against us.***

We are a Chilean corporation. None of our directors are residents of the United States and most of our executive officers reside outside the United States. In addition, a substantial portion of our assets and the assets of our directors and executive officers are located outside the United States. As a result, it may be difficult for ADS holders to effect service of process outside Chile upon us or our directors and executive officers or to bring an action against us or such persons in the United States or Chile to enforce liabilities based on U.S. federal securities laws. It may also be difficult for ADS holders to enforce in the United States or in Chilean courts money judgments obtained in United States courts against us or our directors and executive officers based on civil liability provisions of the U.S. federal securities laws. If a U.S. court grants a final money judgment in an action based on the civil liability provisions of the federal securities laws of the United States, enforceability of this money judgment in Chile will be subject to the obtaining of the relevant "exequatur" (i.e., recognition and enforcement of the foreign judgment) according to Chilean civil procedure law currently in force, and consequently, subject to the satisfaction of certain factors. The most important of these factors are the existence of reciprocity, the absence of a conflicting judgment by a Chilean court relating to the same parties and arising from the same facts and circumstances and the Chilean courts' determination that the U.S. courts had jurisdiction, that process was appropriately served on the defendant and that enforcement would not violate Chilean public policy. Failure to satisfy any of such requirements may result in non-enforcement of your rights.

***We cannot assure you of the accuracy or comparability of facts, forecasts and statistics contained in this report with respect to Chile, its economy and global banking industries.***

Facts, forecasts and statistics in this document relating to Chile, Chile's economy and Chilean global banking industries, including market share information, are derived from various official and other publicly available sources generally believed to be reliable. However, we cannot guarantee the quality and reliability of such official and other sources of materials. In addition, these facts, forecasts and statistics have not been independently verified by us and, therefore, we make no representation as to the accuracy of such facts, forecasts and statistics, which may not be consistent with other information compiled within or outside of Chile and may not be complete or up to date. We have taken reasonable care in reproducing or extracting the information from such sources. However, because of possible flawed or ineffective methodologies underlying the published information or discrepancies between the published information and market practice and other problems, these facts, forecasts or statistics may be inaccurate and may not be comparable from period to period or to facts, forecasts or statistics produced for other economies, and you should not unduly rely upon them.

**Risks Relating to our ADSs**

***There may be a lack of liquidity and market for our shares and ADSs.***

The ADSs are listed and traded on the NYSE. The common stock is listed and traded on the Santiago Stock Exchange, the Chile Electronic Stock Exchange and the Valparaiso Stock Exchange, which we refer to collectively as the Chilean Stock Exchanges, although the trading market for the common stock is small by international standards. At June 30, 2006, we had 188,446,126,794 shares of common stock outstanding. The Chilean securities markets are substantially smaller, less liquid and more volatile than major securities markets in the United States. According to Article 14 of the *Ley de Mercado de Valores, Ley No. 18,045*, or the Chilean Securities Market Law, the *Superintendencia de Valores y Seguros*, or the Superintendency of Securities and



Insurance, may suspend the offer, quotation or trading of shares of any company listed on one or more Chilean Stock Exchanges for up to 30 days if, in its opinion, such suspension is necessary to protect investors or is justified for reasons of public interest. Such suspension may be extended for up to 120 days. If, at the expiration of the extension, the circumstances giving rise to the original suspension have not changed, the Superintendency of Securities and Insurance will then cancel the

relevant listing in the registry of securities. In addition, the Santiago Stock Exchange may inquire as to any movement in the price of any securities in excess of 10% and suspend trading in such securities for a day if it deems necessary.

Although the common stock is traded on the Chilean Stock Exchanges, there can be no assurance that a liquid trading market for the common stock will continue. Approximately 15.86% of our outstanding common stock is held by the public (i.e., shareholders other than Banco Santander Central Hispano, S.A., to which we refer as Banco Santander Central Hispano, and its affiliates), including our shares that are represented by ADSs trading on the NYSE. A limited trading market in general and our concentrated ownership in particular may impair the ability of an ADS holder to sell in the Chilean market shares of common stock obtained upon withdrawal of such shares from the ADR facility in the amount and at the price and time such holder desires, and could increase the volatility of the price of the ADSs.

***You may be unable to exercise preemptive rights.***

The *Ley Sobre Sociedades Anónimas, Ley No. 18,046* and the *Reglamento de Sociedades Anónimas*, which we refer to collectively as the Chilean Companies Law, and applicable regulations require that whenever we issue new common stock for cash, we grant preemptive rights to all of our shareholders (including holders of ADSs), giving them the right to purchase a sufficient number of shares to maintain their existing ownership percentage. Such an offering would not be possible unless a registration statement under the U.S. Securities Act of 1933, as amended, were effective with respect to such rights and common stock or an exemption from the registration requirements thereunder were available.

Since we are not obligated to elect to make a registration statement available with respect to such rights and the common stock, you may not be able to exercise your preemptive rights. If a registration statement is not filed or an applicable exemption is not available, the depository will sell such holders' preemptive rights and distribute the proceeds thereof if a premium can be recognized over the cost of any such sale.

***You may have fewer and less well defined shareholders' rights than with shares of a company in the United States.***

Our corporate affairs are governed by our estatutos, or bylaws, and the laws of Chile. Under such laws, our shareholders may have fewer or less well-defined rights than they might have as shareholders of a corporation incorporated in a U.S. jurisdiction. For example, under legislation applicable to Chilean banks, our shareholders would not be entitled to appraisal rights in the event of a merger or other business combination undertaken by us.

## **ITEM 2. INFORMATION ON THE COMPANY**

### **A. History and Development of the Company**

#### **Overview**

We were formed on August 1, 2002 by the merger of Santiago and Old Santander-Chile, both of which were subsidiaries of our controlling shareholder, Banco Santander Central Hispano. We are the largest bank in Chile in terms of total assets, total deposits, loans and shareholders' equity. At June 30, 2006, we had total assets of Ch\$15,206,926 million (US\$27,785 million), loans net of allowances outstanding of Ch\$11,005,488 million (US\$20,108 million), deposits of Ch\$6,645,164 million (US\$12,142 million) and shareholders' equity of Ch\$1,084,985 million (US\$1,982 million). At June 30, 2006, we employed 7,782 people and had the largest private branch network in Chile with 367 branches. Our headquarters are located in Santiago and we operate in every major region of Chile.

We provide a broad range of commercial and retail banking services to our customers, including Chilean peso and foreign currency denominated loans to finance a variety of commercial transactions, trade financing, foreign currency forward contracts, credit lines and a variety of retail banking services, including mortgage financing. We seek to offer our customers a wide range of products while providing high levels of service. In addition to our

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traditional banking operations, we offer a variety of financial services including financial leasing, financial advisory services, mutual fund management, securities brokerage, insurance brokerage and investment management.

The legal predecessor of Santander-Chile was Banco Santiago (Santiago). Santiago was incorporated by public deed dated September 7, 1977 granted at the Notary Office of Alfredo Astaburuaga Gálvez. Santiago received its permission to incorporate and function as a bank by Resolution No. 118 of the Superintendency of Banks on October 27, 1977. The Bank's bylaws were approved by Resolution No. 103 of the Superintendency of Banks on September 22, 1977. In January 1997, Santiago merged with Banco O'Higgins with Santiago being the surviving entity. In 1999, Santiago became a controlled subsidiary of Banco Santander Central Hispano. At June 30, 2002, Santiago was the second largest private sector bank in Chile in terms of total assets, deposits, loans and shareholders' equity.

Old Santander-Chile was established as a subsidiary of Banco Santander Central Hispano in 1978. In 1982, Old Santander-Chile acquired a significant portion of the assets and liabilities of Banco Español-Chile, a domestic bank that had become insolvent. In July 1996, Old Santander-Chile was merged into Banco Osorno y la Unión becoming "Banco Santander-Chile", the third largest private bank in terms of outstanding loans at that date.

Our principal executive offices are located at Bandera 140, Santiago, Chile (our telephone number is 011-562-320-2000 and our website is [www.santandersantiago.cl](http://www.santandersantiago.cl)). None of the information contained on our website is incorporated by reference into, or forms part of, this Report.

### **Relationship with Banco Santander Central Hispano**

We believe that our relationship with our controlling shareholder, Banco Santander Central Hispano, offers us a significant competitive advantage over our peer Chilean banks. Banco Santander Central Hispano is one of the largest financial groups in Latin America, in terms of total assets measured on a region-wide basis. It is the largest financial group in Spain and is a major player elsewhere in Europe, including the United Kingdom through its Abbey subsidiary and Portugal, where it is the third-largest banking group. Through Santander Consumer Finance it also operates a leading consumer finance franchise in Germany, Italy, Spain and several other European countries.

Our relationship with Banco Santander Central Hispano provides us with access to the group's client base, while its multinational focus allows us to offer international solutions to our clients' financial needs. We also have the benefit of selectively borrowing from Banco Santander Central Hispano's product offerings in other countries as well as benefiting from their know-how in systems management. We believe that our relationship with Banco Santander Central Hispano will also enhance our ability to manage credit and market risks by adopting policies and know-how developed by Banco Santander Central Hispano. Our internal auditing function has been strengthened and is more independent from management as a result of the addition of an internal auditing department that concurrently reports directly to our Audit Committee and the Audit committee of Banco Santander Central Hispano. We believe that this structure leads to greater monitoring and control of our exposure to operational risks.

Banco Santander Central Hispano's support includes the assignment of managerial personnel to key supervisory areas of Santander-Chile, like Risks, Auditing, Accounting and Financial Control. Santander-Chile does not pay any management fees to Banco Santander Central Hispano in connection with these support services.

### **B. Organizational Structure**

Banco Santander Central Hispano controls Santander-Chile through its holdings in Teatinos Siglo XXI and Santander-Chile Holding, which are controlled subsidiaries, and through the indirect ownership of ADRs representing 7.23% of Santander-Chile's outstanding capital stock held by Grupo Empresarial Santander, S.L. This gives Santander Central Hispano control over 84.14% of the shares of the Bank and actual participation when excluding minority shareholders that participate in Santander-Chile Holding is 83.96% .

<b>Shareholder</b>	<b>Number of Shares</b>	<b>Percentage</b>
Teatinos Siglo XXI S.A.	78,108,391,607	41.45%
Santander-Chile Holding	66,822,519,695	35.46
Grupo Empresarial Santander, S.L. vía ADRs	13,626,663,708	7.23%

### **Management Team**

The chart below sets forth the names and areas of responsibility of our senior commercial managers.



The chart below sets forth the names and areas of responsibilities of our operating managers.

### C. Business Overview

We have 367 total branches, 99 of which operated under the Santander Banefe brand name. The remaining 268 branches are operated under the Santander Santiago brand name. We provide a full range of financial services to corporate and individual customers. We divide our clients into five general categories: Retail, Middle-market, Wholesale, Institutional and Treasury.

Retail is comprised of individuals and small business clients as follows:

*Lower-middle to middle-income (Santander Banefe)*, consisting of individuals with monthly income between Ch\$120,000 (US\$219) and Ch\$400,000 (US\$ 731), which are served through our Banefe branch network. This segment accounts for 4.9% of our loans as of June 30, 2006. This segment offers customers a range of products, including consumer loans, credit cards, auto loans, residential mortgage loans, debit card accounts, savings products, mutual funds and insurance brokerage.

*Middle- and upper-income*, consisting of individuals with a monthly income greater than Ch\$400,000 (US\$731). Clients in this segment account for 36.5% of our loans as of June 30, 2006 and are offered a range of products, including consumer loans, credit cards, auto loans, commercial loans, foreign trade financing, residential mortgage loans, checking accounts, savings products, mutual funds and insurance brokerage.

*Small businesses*, consisting of small companies with annual sales less than Ch\$1,200 million (US\$2.2 million). As of June 30, 2006, small companies represented approximately 14.4% of our total loans outstanding. Customers in this segment are offered a range of products, including commercial loans, leasing, factoring, foreign trade, credit cards, mortgage loans, checking accounts, savings products, mutual funds and insurance brokerage.

The Middle-market is comprised of mid-sized companies, companies in the real estate sector and large companies as follows:

*Mid-sized companies*, consisting of companies with annual sales over Ch\$1,200 million (US\$2.2 million) and up to Ch\$3,500 million (US\$6.4 million). Customers in this segment are offered a wide range of products, including commercial loans, leasing, factoring, foreign trade, credit cards, mortgage loans, checking accounts, cash management, treasury services, financial advisory, savings products, mutual funds and insurance brokerage. As of June 30, 2006, these clients represented 8.1% of our total loans outstanding.

*Real estate*. This segment also includes all companies in the real estate sector. As of June 30, 2006, these clients represented 5.0% of our total loans outstanding. To clients in the real estate sector we offer apart from traditional banking services, specialized services for financing primarily residential projects in order to increase the sale of residential mortgage loans.

*Large companies*, consisting of companies with annual sales over Ch\$3,500 million (US\$6.4 million). Customers in this segment are offered a wide range of products, including commercial loans, leasing, factoring, foreign trade, credit cards,



mortgage loans, checking accounts, cash management, treasury services, financial advisory, savings products, mutual funds and insurance brokerage. As of June 30, 2006, these clients represented 10.4% of our total loans outstanding.

The Wholesale segment is comprised of:

Companies that are foreign multinationals or part of a large Chilean economic group with sales over Ch\$3,500 million (US\$6.4 million). As of June 30, 2006, these clients represented 16.8% of our total loans outstanding. Customers in this segment are offered a wide range of products, including commercial loans, leasing, factoring, foreign trade, mortgage loans, checking accounts, cash management, treasury services, financial advisory, savings products, mutual funds and insurance brokerage.

The Institutional segment is comprised of:

Institutional corporations such as universities, government agencies, municipalities and regional governments. As of June 30, 2006, these clients represented 1.9% of our total loans outstanding and offer customers a range of products, including commercial loans, leasing, factoring, foreign trade, credit cards, mortgage loans, checking accounts, cash management, savings products, mutual funds and insurance brokerage.

The Treasury Division provides sophisticated financial products mainly to companies in the wholesale banking and the middle market segments. This includes products such as short-term financing and funding, securities brokerage, interest rate and foreign currency derivatives, securitization services and other tailor made financial products. The Treasury division also manages the Bank's trading positions as well as the non-trading investment portfolio.

Our leasing subsidiary (Santiago Leasing S.A.) has been segmented into the above categories. The subsidiary Santander S.A. Agente de Valores is included in the Treasury Division and the mutual fund and insurance brokerage subsidiaries are included in the various sub-segments (other than in the Treasury Division).



The table below sets forth our lines of business and certain statistical information relating to each of them for the six-month period ended June 30, 2006. Please see *Note 26(y) to our Unaudited Consolidated Financial Statements*.

**At and for the six-month period ended June 30, 2006**  
(millions of constant Ch\$ as of June 30, 2006)

<b>Segment</b>	<b>Loans</b>	<b>Net interest revenue</b>	<b>Fees, net</b>	<b>Net loan loss provisions (1)</b>	<b>Financial transactions, net(2)</b>	<b>Net segment contribution (3)</b>
<b>Individuals</b>	4,621,147	150,838	51,130	(42,660)	-	159,308
Santander Banefe	542,011	47,069	10,705	(21,105)	-	36,669
Middle-upper income	4,078,738	103,728	40,425	(21,614)	-	122,539
Santiago Leasing S.A.	398	41	-	59	-	100
<b>SMEs</b>	1,684,315	57,202	13,179	(7,689)	-	62,692
<b>Total Retail</b>	6,305,462	208,040	64,309	(50,349)	-	222,000
<b>Middle-market</b>	2,614,278	29,531	6,578	1,183	-	37,292
Mid-sized companies	899,882	14,462	3,226	(1,007)	-	16,681
Real estate	552,241	3,706	717	2,191	-	6,614
Large companies	1,160,247	11,166	2,635	(284)	-	13,517
Santiago Leasing S.A.	1,908	197	-	283	-	480
<b>Wholesale</b>	1,873,121	17,015	3,770	1,021	-	21,806
<b>Institutional</b>	213,483	4,444	588	473	-	5,505
<b>Treasury (4)</b>	2	39,693	683	-	32,852	73,228
<b>Others (5)</b>	<b>146,725</b>	<b>415</b>	<b>2,169</b>	<b>441</b>	-	<b>3,025</b>
<b>Total</b>	<b>11,153,071</b>	<b>299,138</b>	<b>78,097</b>	<b>(47,231)</b>	<b>32,852</b>	<b>362,856</b>
<b>Other operating income (6)</b>						(16,903)
<b>Other income and expenses</b>						(18,973)
<b>Operating expenses</b>						(145,544)
<b>Price level restatement</b>						(7,466)
<b>Net income before taxes</b>						173,970

(1) Includes gross provisions for loan losses, net of releases on recoveries.

(2) Includes the net gains from trading, net mark-to-market gains and net foreign exchange transactions.

(3) Equal to the sum of net interest revenue, net fee income minus net provision for loan losses and net financial transactions.

(4) Includes Santander S.A. Agente de Valores.

- (5) Includes contribution of other Bank subsidiaries and other non-segmented items.
- (6) Includes other operating income net of other operating expenses.

***Operations through Subsidiaries***

The General Banking Law was amended on November 4, 1997, to extend the scope of a bank's permissible activities, which permitted us to provide directly the leasing and financial advisory services we could formerly offer only through our subsidiaries, to offer investment advisory services outside of Chile and to undertake activities we could not formerly offer directly or through subsidiaries, such as factoring, securitization, foreign investment funds, custody and transport of securities and insurance brokerage services.

For the six-months ended June 30, 2006, our subsidiaries collectively accounted for approximately 13% of our consolidated net income. The assets and operating income of these subsidiaries at and for the six-months ended June 30, 2006 represented 6% and 14% of our total assets and operating income, respectively. The following table sets forth a list of our subsidiaries and our ownership interest in each subsidiary at the dates indicated.

Subsidiary	Percentage Owned								
	June 30, 2005			December 31, 2005			June 30, 2006		
	Direct	Indirect	Total	Direct	Indirect	Total	Direct	Indirect	Total
%	%	%	%	%	%	%	%	%	
Santiago Leasing S.A.	99.50	□	99.50	99.50	□	99.50	99.50	□	99.50
Santiago Corredores de Bolsa Ltda.	99.19	0.81	100.00	99.19	0.81	100.00	99.19	0.81	100.00
Santander Santiago S.A. Administradora General de Fondos	99.96	0.02	99.98	99.96	0.02	99.98	99.96	0.02	99.98
Santander S.A. Agente de Valores	99.03	□	99.03	99.03	□	99.03	99.03	□	99.03
Santander Santiago S.A. Sociedad Securitizadora	99.64	□	99.64	99.64	□	99.64	99.64	□	99.64
Santander Santiago Corredora de Seguros Ltda.	99.99	□	99.99	99.99	□	94.99	99.99	□	99.99

In September 2006 we created a new subsidiary, Santander Servicios de Recaudación y Pagos Ltda, whose main function will be to open and operate special payment centers where non-clients can deposit to client accounts, checks and cashier checks and pay all types of services. These payment centers will operate seven days a week. We own 99.9% of this subsidiary, and the remaining 0.1% is owned by Santiago Leasing S.A. The Board of Directors has approved the merger between Santiago Corredores de Bolsa Ltda, a subsidiary of the Bank, and Santander Investment S.A. Corredores de Bolsa. Santiago Corredores de Bolsa will absorb Santander Investment S.A. Corredores de Bolsa by the end of 2006.

## Competition

### Overview

The Chilean financial services market consists of a variety of largely distinct sectors. The most important sector, commercial banking, includes a number of privately-owned banks and one public-sector bank, Banco del Estado (which operates within the same legal and regulatory framework as the private sector banks). The private-sector banks include local banks and a number of foreign-owned banks which are operating in Chile. The Chilean banking system is comprised of 25 private-sector banks and one public-sector bank. Five private-sector banks along with the state-owned bank together accounted for 80.4% of all outstanding loans by Chilean financial institutions at June 30, 2006.

The Chilean banking system has experienced increased competition in recent years largely due to consolidation in the industry and new legislation. For example, the merger of Banco de Chile with Banco de A. Edwards, effective January 2, 2002, resulted in the creation at that moment of the largest bank in Chile. Shortly after that merger was consummated, Santander Central Hispano announced the merger of the two banks it owned in Chile, Banco Santander-Chile and Banco Santiago, creating the largest bank in Chile. We also face competition from non-bank and non-finance competitors (principally department stores) with respect to some of our credit products, such as credit cards, consumer loans and insurance brokerage. In addition, we face competition from non-bank finance competitors, such as leasing, factoring and automobile finance companies,

with respect to credit products, and mutual funds, pension funds and insurance companies, with respect to savings products. Currently, banks continue to be the main suppliers of leasing, factoring and mutual funds, and the insurance sales business has grown rapidly.

As shown in the following table, we are the market leader in practically every banking service in Chile:

	Market Share at June 30, 2005	Market Share at December 31, 2005	Market Share at June 30, 2006	Rank as of June 30, 2006
Commercial loans	20.3%	19.8%	20.2%	1
Consumer loans	25.6	25.6	26.3	1
Mortgage loans (residential and general purpose)	23.5	23.5	23.9	1
Residential mortgage loans	24.6	24.9	25.5	2
Foreign trade loans (loans for export, import and contingent)	23.9	22.0	22.0	1
Total loans	23.0	22.6	22.8	1
Deposits	21.6	21.5	22.1(1)	1
Mutual funds (assets managed)	20.3	21.6	21.9	2
Credit card accounts	36.4	37.3	36.9	1
Checking Accounts (2)	26.2	25.7	24.3	1
Branches (3)	19.7	20.3	20.9	1
ATM locations	28.1%	28.1%	28.5%(4)	1

Source: Superintendency of Banks.

- (1) As of July 31, 2006 as reliable data at June 30, 2006 was not available.
- (2) Checking account market shares as of May 2005, November 2005 and May 2006.
- (3) Excluding special-service payment centers.
- (4) As of March 2006.

The following tables set out certain statistics comparing our market position to that of our peer group, defined as the five largest banks in Chile in terms of shareholders' equity at June 30, 2006.

### Loans

At June 30, 2006, our loan portfolio was the largest among Chilean banks. Our loan portfolio on a stand-alone basis represented 22.8% of the market for loans in the Chilean financial system at such date. The following table sets forth our and our peer group's market shares in terms of loans as at the dates indicated:

Loans	At June 30, 2006			At December 31, 2005	At June 30, 2005
	Ch\$ million	In million of US\$	Market Share	Market Share	Market Share
<b>Santander-Chile</b>	11,156,529	20,384	22.8%	22.6%	23.0%
Banco de Chile	8,657,793	15,819	17.7	18.1	17.8
Banco del Estado	6,609,765	12,077	13.5	13.3	13.1
Banco de Crédito e Inversiones	6,017,856	10,995	12.3	12.3	11.9
BBVA, Chile	3,795,691	6,935	7.8	8.0	7.7
Corpbanca	3,041,873	5,558	6.2	6.4	6.6
Others	9,594,345	17,530	19.7	19.3	19.9

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Chilean financial system	48,873,852	89,298	100.0%	100.0%	100.0%
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Source: Superintendency of Banks

**Deposits**

On a stand alone basis, we had a 22.3% market share in deposits, ranking the first place among banks in Chile, at July 31, 2006 (reliable data at June 30, 2006 is not available to us). Deposit market share is based on total time deposits at July 31, 2006 and June 30 and December 31, 2005, respectively, plus average monthly checking and demand deposit accounts at July 31, 2006 and June 30 and December 31, 2005, respectively, net of clearance. The following table sets forth our and our peer group's market shares in terms of deposits at the dates indicated:

Deposits(1)	At July 31, 2006			At December 31, 2005	At June 30, 2005
	Ch\$ million	In million of US\$	Market Share	Market Share	Market Share
<b>Santander-Chile</b>	8,722,832	16,171	22.3%	21.5%	21.6%
Banco de Chile	6,896,524	12,785	17.6%	16.4	16.2
Banco del Estado	6,174,775	11,447	15.8%	17.2	15.5
Banco de Crédito e Inversiones	4,564,950	8,463	11.7%	12.0	11.6
BBVA, Chile	3,110,027	5,766	7.9%	8.0	7.6
Corpbanca	1,722,104	3,193	4.4%	5.2	5.8
Others	7,988,289	14,809	20.3%	19.7	21.7
Chilean financial system	39,179,501	72,634	100.0%	100.0%	100.0%

- (1) The balances of checking and demand deposit accounts are the average monthly balances instead of period-end balances, as we believe that period-end balances are not always reflective of a bank's position in checking and demand deposit accounts. The source for the average balances is the Superintendency of Banks.

**Shareholders' equity**

With Ch\$1,084,985 million (US\$1,982 million) in shareholders' equity, at June 30, 2006, we were the largest commercial bank in Chile in terms of shareholders' equity. The following table sets forth our and our peer group's shareholders' equity at June 30, 2005 and 2006:

Equity	At June 30, 2006			At December 31, 2005 Market Share	At June 30, 2005
	Ch\$ millions	In million of US\$	%(1)	%(1)	%(1)
<b>Santander-Chile</b>	1,084,985	1,982	20.9%	21.1%	20.6%
Banco de Chile	734,228	1,342	14.1	15.1	13.3
Banco del Estado	469,925	859	9.0	8.7	9.2
Banco de Crédito e Inversiones	514,414	940	9.9	9.8	9.5

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BBVA, Chile	282,968	517	5.4	5.6	5.8
Corpbanca	407,406	744	7.8	7.9	8.1
Others	1,706,704	3,118	32.9	31.8	33.5
	<hr/>	<hr/>	<hr/>	<hr/>	<hr/>
Chilean financial system	5,200,630	9,502	100.0%	100.0%	100.00%
	<hr/>	<hr/>	<hr/>	<hr/>	<hr/>

Source: Superintendency of Banks.

(1) Percentage of total shareholders' equity of all Chilean banks.

31



**Efficiency**

At June 30, 2006, on a stand alone basis, we were the most efficient bank in our peer group. The following table sets forth our and our peer group's efficiency ratios (defined as operating expenses as a percentage of operating revenue, which is the aggregate of net interest revenue, fees and income from services (net ) and other operating income (net)) for the periods indicated:

Efficiency ratio	For the six-months ended June 30, 2006	For the year ended December 31, 2005	For the six-months ended June 30, 2005
	%	%	%
<b>Santander-Chile</b>	38.6%	44.0%	43.6%
Banco de Chile	50.0	50.4	51.7
Banco del Estado	57.2	60.7	62.0
Banco de Crédito e Inversiones	55.8	52.7	54.2
BBVA, Chile	61.5	68.6	65.0
Corpbanca	50.5	40.7	41.6
Chilean Financial System	51.0%	54.1%	53.8%

Source: Superintendency of Banks

**Return on average equity**

At June 30, 2006, we were the second most profitable bank in our peer group (as measured by return on equity) and the second most capitalized bank as measured by the BIS ratio. The following table sets forth our and our peer group's average return on equity for the six-months ended June 30, 2005 and 2006 and BIS ratios at the dates indicated:

	Return on average equity			BIS Ratio		
	For the six- months ended June 30, 2006	For the year ended December 31, 2005	For the six months ended June 30, 2005	at June 30, 2006	at December 31, 2005	at June 30, 2005
	%	%	%	%	%	%
<b>Santander-Chile</b>	26.1%	23.6%	23.1%	12.2%	12.9%	13.4%
Banco de Chile	27.2	26.7	29.5	11.7	11.2	11.3
Banco del Estado	11.3	9.2	10.3	11.0	10.7	11.7
Banco de Crédito e Inversiones	21.8	23.4	24.5	10.8	10.3	10.7
BBVA, Chile	13.2	10.7	13.1	10.9	10.8	11.0
Corpbanca	8.9	13.8	13.4	14.4	13.5	13.9
Chilean Financial System	17.7%	16.3%	17.6%	12.9%	13.0%	13.5%

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Source: Superintendency of Banks, except Santander-Chile. Calculated by annualizing net income recorded for the six-month period ended June 30, 2005 and 2006, and dividing the annualized net income by monthly average equity. For Santander-Chile, the average equity is calculated on a daily basis by the Bank (*See Item 3: Selected Statistical Information*  *Average Balance Sheet and Interest Rate Data*).

**Asset Quality**

At June 30, 2006, on a stand alone basis, we had the second lowest loan loss allowance to total loans ratio in our peer group. The following table sets forth our and our peer group's loan loss allowance to total loans ratio as defined by the Superintendency of Banks at the dates indicated.

	<b>Loan Loss allowances/total loans</b>		
	<b>At June 30, 2006</b>	<b>At December 31, 2005</b>	<b>At June 30, 2005</b>
	%	%	%
<b>Santander-Chile</b>	1.30%	1.42%	1.78%
Banco de Chile	1.61	1.70	1.84
Banco del Estado	1.65	1.64	1.71
Banco de Crédito e Inversiones	1.36	1.54	1.62
BBVA, Chile	1.26	1.35	1.81
Corpbanca	1.52	1.56	1.62
Chilean Financial System	1.52%	1.61%	1.79%

Source: Superintendency of Banks

**D. Regulation and Supervision****General**

In Chile, only banks may maintain checking accounts for their customers, conduct foreign trade operations, and together with non-banking financial institutions, accept time deposits. The principal authorities that regulate financial institutions in Chile are the Superintendency of Banks and the Central Bank. Chilean banks are primarily subject to the General Banking Law and secondarily, to the extent not inconsistent with this statute, the provisions of the Chilean Companies Law governing public corporations, except for certain provisions which are expressly excluded.

The modern Chilean banking system dates from 1925 and has been characterized by periods of substantial regulation and state intervention, as well as periods of deregulation. The most recent period of deregulation commenced in 1975 and culminated in the adoption of a series of amendments to General Banking Law. That law, amended most recently in 2001, granted additional powers to banks, including general underwriting powers for new issues of certain debt and equity securities and the power to create subsidiaries to engage in activities related to banking, such as brokerage, investment advisory and mutual fund services, administration of investment funds, factoring, securitization products and financial leasing services.

**The Central Bank**

The Central Bank is an autonomous legal entity created by the Chilean Constitution. It is subject to the Chilean Constitution and its own *ley orgánica constitucional*, or organic constitutional law. To the extent not inconsistent with the Chilean Constitution or the Central Bank's organic constitutional law, the Central Bank is also subject to private sector laws (but in no event is it subject to the laws applicable to the public sector). It is directed and administered by a board of directors composed of five members designated by the President of Chile, subject to the approval of the Senate.

The legal purpose of the Central Bank is to maintain the stability of the Chilean peso and the orderly functioning of Chile's internal and external payment system. The Central Bank's powers include setting reserve requirements, regulating the amount of money and credit in circulation, establishing regulations and guidelines regarding finance companies, foreign exchange (including the Formal Exchange Market) and banks' receipt-of-deposit activities.

### **The Superintendency of Banks**

Banks are supervised and controlled by the Superintendency of Banks, an independent Chilean governmental agency. The Superintendency of Banks authorizes the creation of new banks and has broad powers to interpret and enforce legal and regulatory requirements applicable to banks and financial companies. Furthermore, in case of noncompliance with such legal and regulatory requirements, the Superintendency of Banks has the ability to impose sanctions. In extreme cases, it can appoint, with the prior approval of the board of directors of the Central Bank, a provisional administrator to manage a bank. It must also approve any amendment to a bank's bylaws or any increase in its capital.

The Superintendency of Banks examines all banks from time to time, generally at least once a year. Banks are also required to submit their financial statements monthly to the Superintendency of Banks, and a bank's financial statements are published at least four times a year in a newspaper with countrywide coverage. In addition, banks are required to provide

extensive information regarding their operations at various periodic intervals to the Superintendency of Banks. A bank's annual financial statements and the opinion of its independent auditors must also be submitted to the Superintendency of Banks.

Any person wishing to acquire, directly or indirectly, 10.0% or more of the share capital of a bank must obtain the prior approval of the Superintendency of Banks. Absent such approval, the acquiror of shares so acquired will not have the right to vote them. The Superintendency of Banks may only refuse to grant its approval, based on specific grounds set forth in the General Banking Law.

According to Article 35 bis of the General Banking Law, the prior authorization of the Superintendency of Banks is required for:

- the merger of two or more banks;
- the acquisition of all or a substantial portion of a bank's assets and liabilities by another bank;
- the control by the same person, or controlling group, of two or more banks; or
- a substantial increase in the existing control of a bank by a controlling shareholder of that bank.

Such prior authorization is required solely when the acquiring bank or the resulting group of banks would own a significant market share in loans, defined by the Superintendency of Banks to be more than 15.0% of all loans in the Chilean banking system. The intended purchase, merger or expansion may be denied by the Superintendency of Banks; or, if the acquiring bank or resulting group would own a market share in loans determined to be more than 20.0% of all loans in the Chilean banking system, the purchase, merger, or expansion may be conditioned on one or more of the following:

- that the bank or banks maintain regulatory capital higher than 8.0% and up to 14.0% of their risk-weighted assets;
- that the technical reserve established in article 65 of the General Banking Law be applicable when deposits exceed one and a half times the resulting bank's paid-in capital and reserves; or
- that the margin for interbank loans be reduced to 20.0% of the resulting bank's regulatory capital.

If the acquiring bank or resulting group would own a market share in loans determined by the Superintendency of Banks to be more than 15% but less than 20%, the authorization will be conditioned on the bank or banks maintaining a regulatory capital not lower than 10% of their risks-weighted assets for the period specified by the Superintendency of Banks, which may not be less than one year. The calculation of the risk-weighted assets is based on a five-category risk classification system applied to a bank's assets that is based on the Basel Committee recommendations.

Pursuant to the regulations of the Superintendency of Banks, the following ownership disclosures are required:

- a bank is required to inform the Superintendency of Banks of the identity of any person owning, directly or indirectly, 5.0% or more of such bank's shares;
- holders of ADSs must disclose to the depositary the identity of beneficial owners of ADSs registered under such holders' names;
- the depositary is required to notify the bank as to the identity of beneficial owners of ADSs which such depositary has registered and the bank, in turn, is required to notify the Superintendency of Banks as to

the identity of the beneficial owners of the ADSs representing 5.0% or more of such banks' shares; and

- bank shareholders who individually hold 10.0% or more of a bank's capital stock and who are controlling shareholders must periodically inform the Superintendency of Banks of their financial condition.

**Limitations on Types of Activities**

Chilean banks can only conduct those activities allowed by the General Banking Law: making loans, accepting deposits and, subject to limitations, making investments and performing financial services. Investments are restricted to real estate for the bank's own use, gold, foreign exchange and debt securities. Through subsidiaries, banks may also engage in other specific financial service activities such as securities brokerage services, equity investments, securities, mutual fund management, investment fund management, financial advisory and leasing activities. Subject to specific limitations and the prior approval of the Superintendency of Banks and the Central Bank, Chilean banks may own majority or minority interests in foreign banks.

On March 2, 2002, the Central Bank authorized banks to pay interest on checking accounts. On March 20, 2002, the Superintendency of Banks published guidelines establishing that beginning on June 1, 2002, banks could offer a new checking account product that pays interest. The Superintendency of Banks also stated that these accounts may be subject to minimum balance limits and different interest rates depending on average balances held in the account and that banks may also charge fees for the use of this new product. For banks with a solvency score of less than A (See [Item 2D: Regulation and Supervision] Management and Capitalization Evaluation]) the Central Bank has also imposed additional caps to the interest rate that can be paid.

### **Deposit Insurance**

The Chilean government guarantees up to 90.0% of the principal amount of certain time and demand deposits and savings accounts held by natural persons with a maximum value of UF120 per person (Ch\$1,960,351 or U.S.\$3,582 at June 30, 2006) per calendar year in the entire financial system.

### **Reserve Requirements**

Deposits are subject to a reserve requirement of 9.0% for peso and foreign currency-denominated demand deposits and 3.6% for UF, peso and foreign currency-denominated time deposits (with terms of less than one year). For purposes of calculating the reserve obligation, banks are authorized to deduct daily from their foreign currency denominated liabilities, the balance in foreign currency of certain loans and financial investments held outside of Chile, the most relevant of which include:

- cash clearance account, which should be deducted from demand deposit for calculating reserve requirement;
- certain payment orders issued by pension providers;
- the amount set aside for [technical reserve] (as described below), which can be deducted from reserve requirement.

The Central Bank has statutory authority to require banks to maintain reserves of up to an average of 40.0% for demand deposits and up to 20.0% for time deposits (irrespective, in each case, of the currency in which they are denominated) to implement monetary policy. In addition, to the extent that the aggregate amount of the following types of liabilities exceeds 2.5 times the amount of a bank's paid-in capital and reserves, a bank must maintain a 100% [technical reserve] against them: demand deposits, deposits in checking accounts, or obligations payable on sight incurred in the ordinary course of business, other deposits unconditionally payable immediately or within a term of less than 30 days and time deposits payable within 10 days prior to maturity.

The Chilean Congress is currently reviewing legislation that will reform various laws regulating Chilean capital markets (*Reforma al Mercado de Capitales II*). Among other things, the [technical reserve] will be modified, permitting banks to use regulatory capital to determine the amount of the reserve.

### **Minimum Capital**

Under the General Banking Law, a bank is required to have a minimum of UF800,000 (approximately Ch\$14,521 million and US\$26.5 million at June 30, 2006) of paid-in capital and reserves, a regulatory capital of at least 8% of its risk weighted assets, net of required allowances, and paid-in capital and reserves of at least 3% of its total assets, net of required allowances.

However, a bank may begin its operations with 50.0% of such amount, provided that it has a regulatory capital of not less than 12.0% of its risk-weighted assets. Regulatory capital is defined as the aggregate of:

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- a bank's paid-in capital and reserves, excluding capital attributable to subsidiaries and foreign branches or *capital básico*;
- its subordinated bonds, valued at their placement price (but decreasing by 20.0% for each year during the period commencing six years prior to maturity), for an amount up to 50.0% of its basic capital; and
- its voluntary allowances for loan losses for an amount of up to 1.25% of its risk weighted-assets.

In 2002, the General Banking Law was modified, allowing banks to begin operations with a minimum capital of UF400,000 (approximately US\$13.3 million at June 30, 2006) of paid-in capital and reserves with the obligation to increase it to UF800,000 (approximately US\$26.5 million at June 30, 2006) in an undetermined period of time. If a bank maintains a minimum capital of UF 400,000 (approximately US\$13.3 million at June 30, 2006), it is required to maintain a minimum BIS



ratio of 12.0% . When such a bank's paid-in capital reaches UF600,000 (approximately US\$19.9 million at June 30, 2006), the total capital ratio required is reduced to 10.0% .

### **Capital Adequacy Requirements**

According to the General Banking Law, each bank should have a regulatory capital of at least 8.0% of its risk-weighted assets, net of required allowances. The calculation of risk weighted assets is based on a five-category risk classification system for bank assets that is based on the Basle Committee recommendations. In 2007, the third pillar of Basel II in Chile will include the implementation of capital limits with market risk and operational risk-weighted assets.

Banks should also have *capital básico*, or basic capital, of at least 3.0% of their total assets, net of allowances. Basic capital is defined as a bank's paid-in capital and reserves and is similar to Tier 1 capital except that it does not include net income for the period.

### **Lending Limits**

Under the General Banking Law, Chilean banks are subject to certain lending limits, including the following material limits:

- A bank may not extend to any entity or individual (or any one group of related entities), except for banks, directly or indirectly, unsecured credit in an amount that exceeds 5.0% of the bank's regulatory capital, or in an amount that exceeds 25.0% of its regulatory capital if the excess over 5.0% is secured by certain assets with a value equal to or higher than such excess. In the case of foreign export trade financing, the 5.0% ceiling for unsecured credits is raised to 10.0% and the 25.0% ceiling for secured credits to 30.0%. In the case of financing infrastructure projects built by government concession the 5.0% ceiling for unsecured credits is raised to 15.0% if secured by a pledge over the concession, or if granted by two or more banks or finance companies which have executed a credit agreement with the builder or holder of the concession;
- a bank may not extend loans to another financial institution subject to the General Banking Law in an aggregate amount exceeding 30.0% of its regulatory capital;
- a bank may not directly or indirectly grant a loan whose purpose is to allow an individual or entity to acquire shares of the lender bank;
- a bank may not lend, directly or indirectly, to a director or any other person who has the power to act on behalf of the bank; and
- a bank may not grant loans to related parties (including holders of more than 1.0% of its shares) on more favorable terms than those generally offered to non-related parties. Loans granted to related parties are subject to the limitations described in the first bullet point above. In addition, the aggregate amount of loans to related parties may not exceed a bank's regulatory capital.

In addition, the General Banking Law limits the aggregate amount of loans that a bank may grant to its employees to 1.5% of its regulatory capital, and provides that no individual employee may receive loans in excess of 10.0% of this 1.5% limit. Notwithstanding these limitations, a bank may grant to each of its employees a single residential mortgage loan for personal use once during such employee's term of employment.

Certain aspects of Chilean legislation governing capital markets is currently being reviewed by the Chilean Congress. MK2 is expected to, among other things, modify some of the provisions concerning lending limits. The 5% limit affecting unsecured credit referred above is expected to be raised to 10% and the ceiling for secured

credits is expected to be raised to 30%. Such limits are expected to be maintained in 5% and 25% for unsecured and secured credits, respectively, granted to individuals or entities directly or indirectly related to the property or management of the bank. See *Risk Factors--Risks Relating to Chile-- Chile's banking regulatory and capital markets environment is continually evolving and may change.*

**Allowance for Loan Losses**

Chilean banks are required to provide to the Superintendency of Banks detailed information regarding their loan portfolio on a monthly basis. The Superintendency of Banks examines and evaluates each financial institution's credit management process, including its compliance with the loan classification guidelines. Banks are classified into four categories: 1, 2, 3 and 4. Each bank's category depends on the models and methods used by the bank to classify its loan portfolio, as determined by the

Superintendency of Banks. Category 1 banks are those banks whose methods and models are satisfactory to the Superintendency of Banks. Category 1 banks will be entitled to continue using the same methods and models they currently have in place. A bank classified as a Category 2 bank will have to maintain the minimum levels of reserves established by the Superintendency of Banks while its board of directors will be made aware of the problems detected by the Superintendency of Banks and required to take steps to correct them. Banks classified as Categories 3 and 4 will have to maintain the minimum levels of reserves established by the Superintendency of Banks until they are authorized by the Superintendency of Banks to do otherwise. We are classified in Category 1.

Under the classifications effective January 1, 2004, loans are divided into: (i) consumer loans (including loans granted to individuals for the purpose of financing the acquisition of consumer goods or payment of services); (ii) residential mortgage loans (including loans granted to individuals for the acquisition, construction or repair of residential real estate, in which the value of the property covers at least 100% of the amount of the loan); and (iii) commercial loans (includes all loans other than consumer loans and residential mortgage loans).

In accordance with the regulations, which became effective as of January 1, 2004, the models and methods used to classify our loan portfolio must follow the following guiding principles, which have been established by the Superintendency of Banks and approved by our Board of Directors. In 2006, these models have been improved and various changes were and are being introduced. Group rating are being phased out and replaced by statistical scoring systems. A detailed description of this accounting policy is discussed below under *Item 3E Assets and Liabilities Management Loan Portfolio Classification of Loan Portfolio* and in Note 1 of our Unaudited Consolidated Financial Statements. The following describes the calculation of the allowance for loan losses.

*Allowances for individual evaluations on commercial loans*

- The Bank assigns a risk category level to each borrower and his respective loans.
- The Bank considers the following risk factors within the analysis: industry or sector of the borrower, owners or managers of the borrower, their financial situation, their payment capacity and payment behavior.
- Accordingly, the Bank assigns one of the following risk categories to each loan and borrower upon finishing the analysis:
  - ◆ Classifications A1, A2 and A3, correspond to borrowers with no apparent credit risk.
  - ◆ Classifications B, correspond to borrowers with some credit risk but no apparent deterioration of payment capacity.
  - ◆ Classifications C1, C2, C3, C4, D1 and D2 correspond to borrowers whose loans have deteriorated.

For loans classified as A1, A2, A3 and B, the Board of Directors of the Bank is authorized to determine the levels of required reserves. For loans classified in Categories C1, C2, C3, C4, D1 and D2, the bank must have the following levels of reserves:

Classification	Estimated range of loss	Reserve(1)
C1	Up to 3%	2%
C2	More than 3% up to 19%	10%
C3	More than 19% up to 29%	25%
C4	More than 29% up to 49%	40%
D1	More than 49% up to 79%	65%

D2 More than 79% 90%  
(1) Represents percentages of the required reserve amount to the aggregate amount of principal plus accrued unpaid interest of the loan.

*Allowances for group evaluations (commercial loans)*

- Allowances for group evaluations are permitted for a large number of borrowers whose individual loan amounts are relatively small. These models are intended to be used primarily to analyze commercial loans to individuals and small companies.
- Levels of required reserves are to be determined by the Bank, according to the estimated loss that may result from the loans, by classifying the loan portfolio using one or both of the following models:
  - ◆ A model based on the characteristics of the borrowers and their outstanding loans. Borrowers and their loans with similar characteristics will be placed into groups and each group will be assigned a risk level.

- ◆ A model based on the behavior of a group of loans. Loans with analogous past payment histories and similar characteristics will be placed into groups and each group will be assigned a risk level.

Commencing in the fourth quarter of 2006 the Bank will no longer analyze commercial loans on a group basis. All commercial loans will be rated on an individual basis and the performing smaller loans will be scored in an automated system that has been approved by the Superintendency of Banks and our Board of Directors. See *Item 3E Assets and Liabilities Management Loan Portfolio Classification of Loan Portfolio Allowance for Group Evaluations (Commercial Loans)*.

*Allowances for consumer and mortgage loan*

The allowances for consumer and mortgage loan are directly related to the aging of the loan or installment. The rating of a consumer and mortgage loans depends on its overdue status as shown in the table below.

Category	Consumer loans overdue status		Residential mortgage loans overdue status	
	From	To	From	To
	(Days)		(Days)	
A	□	□	□	□
B	1	30	1	180
B-	31	60	181	>181
C	61	120	□	□
D	121	>121	□	□

Commencing in 2006, the Bank has improved and modified the methodology for analyzing consumer and mortgage loans. All consumer and mortgage loans are now assigned a provisioning level on an individual borrower basis utilizing a more automated and sophisticated statistical model and considering borrower's credit history, including any defaults on obligations to other creditors, as well as the overdue periods in the Bank. Once the rating of the client is determined, the provisioning of consumer and mortgage loans is calculated using a risk category and related % which is directly related to the overdue periods.

Loan type	Reserve % (1)	Overdue days						
		1-30	31-60	61-120	121-180	181-360	361-720	>720
Consumer	Profile 1	5.2%	16.5%	29.7%	90.5%	Charged-off	-	-
	Profile 2	8.8%	20.0%	48.4%	90.5%	Charged-off	-	-
	Profile 3	13.5%	24.7%	48.4%	90.5%	Charged-off	-	-
Mortgage	Profile 1	0.3%	0.5%	1.2%	2.4%	6.8%	14.1%	28.3%
	Profile 2	1.5%	1.6%	2.5%	4.4%	6.8%	14.1%	28.3%

(1) Represents the percentage of required reserve amounts to the aggregate amount of the principal and accrued but unpaid interest on the loan. These percentages may vary as the model is improved.

*Additional reserves*

Under the regulations, banks are permitted to establish reserves above the limits described above only to cover specific risks that have been authorized by their Board of Directors.

*Write-offs*

In accordance with the regulations of the Superintendency of Banks, the Bank must write-off loans or portions thereof when collection efforts have been exhausted. Under the rules and regulations established by the Superintendency of Banks, write-offs must be made within the following maximum prescribed limits: 24 months after a loan is past due (3 months for consumer loans) for loans without collateral; 36 months after a loan is past due for loans with collateral. The Bank will also write-off commercial loans prior to the meeting of these criteria when the Bank no longer considers such loans or portions thereof to be collectible.

**Capital Markets**

Under the General Banking Law, banks in Chile may purchase, sell, place, underwrite and act as paying agents with respect to certain debt securities. Likewise, banks in Chile may place and underwrite certain equity securities. Bank subsidiaries may also engage in debt placement and dealing, equity issuance advice and securities brokerage, as well as in financial leasing, mutual fund and investment fund administration, investment advisory services and merger and acquisition

services. These subsidiaries are regulated by the Superintendency of Banks and, in some cases, also by the Superintendency of Securities and Insurance, the regulator of the Chilean securities market, open-stock corporations and insurance companies.

### **Legal Provisions Regarding Banking Institutions with Economic Difficulties**

The General Banking Law provides that if specified adverse circumstances exist at any bank, its board of directors must correct the situation within 30 days from the date of receipt of the relevant financial statements. If the board of directors is unable to do so, it must call a special shareholders' meeting to increase the capital of the bank by the amount necessary to return the bank to financial stability. If the shareholders reject the capital increase, or if it is not effected within the term and in the manner agreed to at the meeting, or if the Superintendency of Banks does not approve the board of directors' proposal, the bank will be barred from increasing its loan portfolio beyond that stated in the financial statements presented to the board of directors and from making any further investments in any instrument other than in instruments issued by the Central Bank. In such a case, or in the event that a bank is unable to make timely payment in respect of its obligations, or if a bank is under provisional administration of the Superintendency of Banks, the General Banking Law provides that the bank may receive a two-year term loan from another bank. The terms and conditions of such a loan must be approved by the directors of both banks, as well as by the Superintendency of Banks, but need not be submitted to the borrowing bank's shareholders for their approval. In any event, a creditor bank cannot grant interbank loans to an insolvent bank in an amount exceeding 25.0% of the creditor bank's regulatory capital. The board of directors of a bank that is unable to make timely payment of its obligations must present a reorganization plan to its creditors in order to capitalize the credits, extend their respective terms, condone debts or take other measures for the payment of the debts. If the board of directors of a bank submits a reorganization plan to its creditors and such arrangement is approved, all subordinated debt issued by the bank, whether or not matured, will be converted by operation of law into common stock in the amount required for the ratio of regulatory capital to risk-weighted assets not to be lower than 12.0%. If a bank fails to pay an obligation, it must notify the Superintendency of Banks, which shall determine if the bank is solvent.

### **Dissolution and Liquidation of Banks**

The Superintendency of Banks may establish that a bank should be liquidated for the benefit of its depositors or other creditors when such bank does not have the necessary solvency to continue its operations. In such case, the Superintendency of Banks must revoke a bank's authorization to exist and order its mandatory liquidation, subject to agreement by the Central Bank. The Superintendency of Banks must also revoke a bank's authorization if the reorganization plan of such bank has been rejected twice. The resolution by the Superintendency of Banks must state the reason for ordering the liquidation and must name a liquidator, unless the Chilean Superintendent of Banks assumes this responsibility. When a liquidation is declared, all checking accounts, other demand deposits received in the ordinary course of business, other deposits unconditionally payable immediately or that have a maturity of no more than 30 days, and any other deposits and receipts payable within 10 days, are required to be paid by using existing funds of the bank, its deposits with the Central Bank or its investments in instruments that represent its reserves. If these funds are insufficient to pay these obligations, the liquidator may seize the rest of the bank's assets, as needed. If necessary and in specified circumstances, the Central Bank will lend the bank the funds necessary to pay these obligations. Any such loans are preferential to any claims of other creditors of the liquidated bank.

### **Obligations Denominated in Foreign Currencies**

Foreign currency denominated obligations of Chilean banks are subject to various limits and obligations. The regulations of the Central Bank do not permit the difference, whether positive or negative, between a bank's assets and liabilities denominated in any foreign currency (including assets and liabilities denominated in U.S. dollars but payable in pesos, as well as those denominated in pesos and indexed to the U.S. dollar exchange rate) to exceed 20% of the bank's paid-in capital and reserves; except in the case where the balance of such assets exceeds the balance of such liabilities and the excess difference does not exceed the bank's allowances and reserves denominated in such foreign currency (excluding profits to be remitted abroad). Santander-Chile must also comply with various regulatory and internal limits regarding exposure to movements in foreign exchange rates (*See [Item 8: Quantitative and Qualitative Disclosures About Market Risks]*).

**Investments in Foreign Securities**

Under current Chilean banking regulations, banks in Chile may grant loans to foreign individuals and entities and invest in certain securities of foreign issuers. Chilean banks may only invest in equity securities of foreign banks and certain other foreign companies which may be affiliates of the bank or which would be complimentary to the bank's business if such companies were incorporated in Chile. Banks in Chile may also invest in debt securities traded in formal secondary markets. Such debt securities must be (1) securities issued or guaranteed by foreign sovereign states or their central banks or other foreign or international financial entities, and (2) bonds issued by foreign companies. A Bank may invest up to 5% of its regulatory capital in securities of foreign issuers. Such securities must have a minimum rating as follows:



Table 1

Rating Agency	Short Term	Long Term
Moody[s]	P2	Baa3
Standard and Poor[s]	A3	BBB-
Fitch IBCA	F2	BBB-
Duff & Phelps	D2	BBB-
Thomson Bank Watch	TBW2	BBB

In the event that the sum of the investments in foreign securities which have a: (i) rating below that indicated in Table 1 above, and equal or exceeds the ratings mentioned in the Table 2 below; and (ii) loans granted to other entities resident abroad exceed 20% (and 30% for banks with a BIS ratio equal or exceeding 10%), of the regulatory capital of such bank, the excess is subject to a mandatory reserve of 100%.

Table 2

Rating Agency	Short Term	Long Term
Moody[s]	P2	Baa3
Standard and Poor[s]	A3	BB-
Fitch IBCA	F2	BB-
Duff & Phelps	D2	BB-
Thomson Bank Watch	TBW2	BB

In addition, banks may invest in foreign securities for an additional amount equal to a 70% of their effective equities which ratings are equal or exceeds those mentioned in the following Table 3. This limit constitutes an additional margin and it is not subject to the 100% mandatory reserve.

Additionally, a Chilean Bank may invest in foreign securities whose rating is equal or exceeds those mentioned in the following Table 3 in: (i) term deposits with foreign banks; and (ii) securities issued or guaranteed by sovereign states or their central banks or those securities issued or guaranteed by foreign entities within the Chilean State; such investment will be subject to the limits by issuer up to 30% and 50%, respectively, of the regulatory capital of the Chilean bank that make the investment.

Table 3

<b>Rating Agency</b>	<b>Short Term</b>	<b>Long Term</b>
Moody's	P1	Aa3
Standard and Poor's	A1+	AA-
Fitch IBCA	F1+	AA-
Duff & Phelps	D1+	AA-
Thomson Bank Watch	TBW1	BB

Chilean banks may invest in securities without ratings issued or guaranteed by sovereign states or their central banks and structured notes issued by investment banks with a rating equal or above that in the immediately preceding Table 3, which return is linked with a corporate or sovereign note with a rating equal or above that in Table 2.

Subject to specific conditions, a bank may grant loans in U.S. dollars to subsidiaries or branches of Chilean companies located abroad, to companies listed on foreign stock exchanges authorized by the Central Bank and, in general, to individuals and entities domiciled abroad, as long as the Central Bank is kept informed of such activities.

#### **New Regulations Regarding Market Risk**

In 2005, the Superintendency of Banks introduced new market risk limits and measures for Chilean banks. On an unconsolidated basis the Bank must separate its balance sheet into two separate categories: trading portfolio (*Libro de Negociación*) and non-trading, or permanent, portfolio (*Libro de Banca*). The trading portfolio as defined by the Superintendency of Banks includes all instruments that are valued for accounting purposes at market prices, free of any restrictions or immediate sale and frequently bought and sold by the Bank or maintained with the intention of selling them in the short-term in order to profit from short-term price variations. The non-trading portfolio is defined as all instruments in the balance sheet not considered in the trading portfolio (*See Item 8-Market Risk*).

**E. Property, Plants and Equipment**

We are domiciled in Chile and own our principal executive offices located at Bandera 140, Santiago, Chile. We also own fifteen other buildings in the vicinity of our headquarters and we rent four other buildings. At June 30, 2006, we owned the premises at which 47% of our branches were located. The remaining branches operate at rented locations.

Main properties as of June 30, 2006	Number
Central Offices	
Own	13
Rented	4
Total	17
Branches (1)	
Own	164
Rented	166
Total	332
Other property (2)	
Own	71
Rented	45
Total	126

(1) Some branches are located inside central office buildings and other properties. Including these branches, the total number of branches is 367.

(2) Consists mainly of parking lots, mini-branches and property owned by our subsidiaries.

The following table sets forth a summary of the main computer hardware and other systems-equipment that we own. We believe that our existing physical facilities are adequate for our needs.

Category	Brand	Application
Mainframe	IBM	Back-end, Core-System Altamira.
Midrange	IBM	Interconnections between Mainframe and mid-range
Midrange	Stratus	Tellers
	SUN/Unix	Interconnections applications Credit & debit cards
	SUN/UNIX	Treasury, MIS, Work Flow, Accounting
Midrange	IBM	WEB
Desktop	IBM	Platform applications
Call Center	Avaya	Telephone system
	Genesys	Integration Voice/data
	Nice	Voice recorder
	Periphonics	IVR

The main software systems used by us are:

Category	Brand	Application
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Core-System	ALTAMIRA	Accenture
Data base	DB2	IBM
Data base	Oracle	Oracle
Data base	SQL Server	Microsoft
WEB Service	Internet Information Server	Microsoft
Message Service	MQSeries	IBM
Transformation	MQIntegrator	IBM

**Item 3. Operating and Financial Review and Prospects****A. New Accounting Standards for Financial Investments and Derivatives**

In accordance with Circular N°3345 issued by the Superintendency of Banks, which became effective on June 30, 2006, the accounting standards for valuing financial instruments acquired for trading or investment purposes, including derivative instruments, was amended. The new accounting standards require that these instruments be carried at their market or fair value, and the historical differences in valuation of such instruments recognized with respect to any dates prior to 2006 be adjusted directly against the Bank's equity. Banks are required to adopt the new accounting standards set forth in Circular No. 3345 in preparing their financial statements at and for the six-months ended June 30, 2006 and going forward.

The following table summarizes the primary changes to the accounting standards as a result of our implementation of Circular No. 3345.

	<b>Before changes to accounting principles</b>	<b>After changes to accounting principles</b>	
<b>Derivatives</b>	Foreign exchange forward contracts	Valued at closing spot exchange rate, initial discount/premium amortized over the life of contract	recognized at fair value; trading contracts: revaluation gains or losses recorded as gains or losses from trading activities
	Forward contracts between U.S. dollars and Ch\$/UF	Valued at closing spot exchange rate, initial discount/premium amortized over the life of contract	hedge contracts: Fair value hedges: hedged assets and liabilities are also recognized at
	Interest rate swaps	<p>difference between interest income/expense recorded in net income in the period when agreement is settled in cash;</p> <p>Fair value and revaluation gains or losses are not recognized</p>	<p>fair value; revaluation gains or losses on both derivatives and hedged items are recognized in the same line of the income statement</p> <p>Cash flow hedges: effective portion of revaluation gains or losses on hedged risk recognized in shareholders' equity (such amount is recognized in income statement when the offsetting changes hedged affect income statement); ineffective portion of revaluation gains or losses recognized in income statement</p>
<b>Other financial investments</b>	Non- Permanent (Trading instruments)	Recognized at fair value on balance sheet; revaluation gains or losses and realized gains or losses are	No changes

recognized in income statements under "gains/losses from trading activities"; interest income and indexation adjustments are reported as "interest revenue"

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Permanent Investment (Available-for-Sale investment instruments)

recognized at fair value on balance sheet; unrealized gains or losses are reported under shareholders' equity, and recognized in income statement under "gains/losses from trading activities" when sold or impaired

Title of "available-for- sale portfolio changed from "permanent"

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Held-to-maturity investment instruments

N/A

New category; recorded at cost plus accrued interest and adjustments, less allowance for impairment

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In order to implement these new accounting standards, we have created a new line item "derivatives" under both "assets" and "liabilities" in our consolidated balance sheet, and reclassified certain other items within other assets, other liabilities, financial instruments, interest income, interest expenses and other operating income, net in our consolidated balance sheet and income statement at and for the six-months ended June 30, 2006.

The net effect of the accounting changes on our net income for the six-month period ended June 30, 2006 was a gain of Ch\$7,089 million. For comparison purposes, we have also retrospectively reclassified these items at and for the six-months ended June 30, 2005, but did not retrospectively apply the new accounting standards to these items. If we had applied the valuation of derivatives to market prices in the six-month period ended June 30, 2005, the net effect on our net income would have been a loss of Ch\$7,264 million.

We started to apply these new accounting standards to our financial statements at and for the six-months ended June 30, 2006. Amounts at December 31, 2005 or any prior dates or for any periods ended December 31, 2005 or for any prior periods have not been retroactively adjusted or reclassified to reflect these changes. As a result, our results of operations and financial condition at and for the six-months ended June 30, 2006 are not entirely comparable to those previously reported by us at any dates or for any periods prior to January 1, 2006.

In connection with our implementation of the new accounting standards, for the six-months ended June 30, 2006, interest revenue and interest expense no longer include the translation gain or loss of financial assets and liabilities denominated in foreign currencies. Such gain or loss is now reclassified as results of foreign exchange transactions. Reported amounts for the six-months ended June 30, 2005 have been reclassified on a comparable basis. Gains or losses on investments in mutual funds have also been reclassified from net interest income to other operating income for the six-months ended June 30, 2005 and 2006.

For the six-months ended June 30, 2006, gains and losses on forward transactions have been reclassified to net gains (losses) on trading activities. In prior periods, such transactions were not marked to market and the difference between the interest paid or received on a specified notional amount was recorded under "foreign exchange transactions, net". Such amounts for the six-months ended June 30, 2005 have been reclassified to net gains (losses) on trading activities in order to be more comparable to the results for the six-months ended June 30, 2006, but have not been retroactively adjusted to reflect fair value.

## **B. Critical Accounting Policies**

We prepare our financial statements in accordance with Chilean GAAP, which requires management to make estimates and assumptions with respect to certain matters that are inherently uncertain. We also reconcile our financial statements to U.S. GAAP (*See Note 27 to our Audited Consolidated Financial Statements and Note 26 to our Unaudited Consolidated Financial Statements*) and are required to make estimates and assumptions in this reconciliation process. Certain critical accounting policies, in particular those relating to goodwill and intangible assets, are only applicable for U.S. GAAP purposes. Our consolidated financial statements include various estimates and assumptions, including but not limited to the adequacy of the allowance for loan losses, estimates of the fair value of certain financial instruments, the selection of useful lives of certain assets and the valuation and recoverability of goodwill. We evaluate these estimates and assumptions on an ongoing basis. Management bases its estimates and assumptions on historical experience and on various other factors that are believed to be reasonable under the circumstances. Actual results in future periods could differ from those estimates and assumptions, and if these differences were significant enough, our reported results of operations would be affected materially.

We believe that the following are the more critical judgment areas or involve a higher degree of complexity in the application of the accounting policies that currently affect our financial condition and results of operations:

### *Derivative activities*

At June 30, 2006, derivatives are valued at market price and the net unrealized gain (loss) on derivatives is classified as a separate line item in the balance sheet. In prior periods, the notional amounts were carried off the balance sheet. Our derivative holdings at June 30, 2005 have been reclassified from "other assets" and "other

liabilities to derivatives, but have not been marked to market as would be required under currently applicable accounting principles. Our annual financial statements incorporated by reference do not reflect such reclassification. For the six-months ended June 30, 2005 and for all prior periods, presented or incorporated by reference, the unrealized gains, losses, premiums and discounts arising from derivatives contracts were recorded on a net basis under other assets and other liabilities, and these derivatives contracts were not marked to market on the balance sheet.



Pursuant to the new accounting standards, banks must mark-to-market derivatives. A derivative held for trading purposes must be marked-to-market and the unrealized gain or loss recognized in income. New accounting standards have also been adopted for derivatives held for hedging purposes with effect for the six-months ended June 30, 2006, changes in book value of hedged items are included in the mark-to-market and trading line items, except to the extent set forth below.

The SBIF recognizes three kinds of hedge accounting: (i) cash flow hedges, (ii) fair value hedges and (iii) hedging of foreign investments.

- When a cash flow hedge exists, the fair value movements on the part of the hedging instrument that is effective are recognized in equity. Any ineffective portion of the fair value movement on the hedging instrument is recognized in the income statement.
- When a fair value hedge exists, the fair value movements on the hedging instrument and the corresponding fair value movements on the hedged item are recognized in the income statement. Hedged items in the balance sheet are presented at their market value in 2006.
- When a hedge of foreign investment exposure exists (i.e. investment in a foreign branch), the fair value movements on the part of the hedging instrument that is effective are recognized in equity. Any ineffective portion of the fair value movement on the hedging instrument is recognized in the income statement.

We enter into forward contracts for our own account and for the accounts of our customers. The values of the forward contracts are marked-to-market on monthly basis and the revaluation gain or loss is recognized in the line item mark-to-market and trading activities. Previously, they were classified as foreign exchange transactions, except gains or losses on UF-Ch\$ forwards, which used to be classified as net interest income.

#### *Allowance for loan losses*

Chilean banks are required to maintain loan loss allowances in amounts determined in accordance with the regulations issued by the Superintendency of Banks. Under these regulations, we must classify our portfolio into various categories of payment capability. The minimum amount of required loan loss allowances is determined based on fixed percentages of estimated loan losses assigned to each category. As of January 1, 2004, the new loan loss allowance regulations set by the Superintendency of Banks came into effect. Loans are divided into: (i) consumer loans (including loans granted to individuals for the purpose of financing the acquisition of consumer goods or payment of services); (ii) residential mortgage loans (including loans granted to individuals for the acquisition, construction or repair of residential real estate, in which the value of the property covers at least 100% of the amount of the loan); and (iii) commercial loans (includes all loans other than consumer loans and residential mortgage loans).

Commencing in December 2006, we will no longer assess commercial loans for impairment losses on a group basis. All commercial loans are assessed on an individual basis in an automated system that has been approved by the Superintendency of Banks and our Board of Directors. A detailed description of this provisioning policy is discussed below under [Selected Statistical Information](#) [Loan loss allowances](#) and in Note 1 to our Consolidated Financial Statements. For a description of the regulations relating to loan loss allowances to which we were previously subject to and the new regulations, see [Item 2: Information on the Company](#) [Regulation and Supervision](#) [Allowance for Loan Losses](#).

#### *Goodwill and Intangible Assets with Indefinite Useful Lives*

Under U.S. GAAP, we have significant intangible assets consisting of goodwill and trademarks with indefinite useful lives. We record all assets and liabilities acquired in purchase acquisitions, including goodwill and other acquired intangibles, at fair value. These include amounts pushed down from Banco Santander Central Hispano.

Goodwill and indefinite-lived assets are no longer amortized over their estimated useful lives using straight-line and accelerated methods, and are subject to at least an annual impairment review. The initial goodwill and intangibles recorded and subsequent impairment analysis requires management to make subjective judgments concerning estimates of how the acquired asset will perform in the future using a discounted cash flow analysis. Additionally, estimated cash flows may extend beyond ten years and, by their nature, are difficult to determine. Events and factors that may significantly affect the estimates include, among others, competitive forces, customer behavior and attrition, changes in revenue growth trends, cost structures and technology and changes in interest rates and specific industry or market sector conditions. For a further discussion of accounting practices for goodwill and intangible assets with indefinite useful lives under U.S. GAAP, see *Note 26 to our Unaudited Consolidated Financial Statements*.

## **Differences between Chilean and United States Generally Accepted Accounting Principles**

Accounting principles generally accepted in Chile vary in certain important respects from the accounting principles generally accepted in the United States. Such differences involve certain methods for measuring the amounts shown in the consolidated financial statements, as well as additional disclosures required by accounting principles generally accepted in the United States and the accounting treatment of the merger.

Note 26 to our Unaudited Consolidated Financial Statements presents a description of the significant differences between Chilean GAAP and U.S. GAAP.

## **C. Operating Results**

### **Chilean Economy**

All of our operations and substantially all of our customers are located in Chile. Accordingly, our financial condition and results of operations are substantially dependent upon economic conditions prevailing in Chile. The Chilean economy grew by 6.4% in 2005 following growth of 6.1% in 2004 and 3.7% in 2003. In the first half of 2006 the Chilean economy grew 4.9%. The strength of the emerging Asian economies and the stable economic environment in the rest of the developed world has continued to benefit Chile's economy despite the rise in international oil prices. This positive external scenario has also led to strong growth of internal consumption and investment demand that grew 8.3% in the first half of 2006 on a year-on-year basis.

These positive growth figures can be attributed, in part, to the rising prices of Chile's main exports, most importantly copper. The export sector in Chile increased 4.7% in the same period. The price of copper increased 60.2% in six-month period ended June 30, 2006, 45.4% in 2005 and 42.7% in 2004. Exports of copper totaled US\$17.4 billion, or 44%, of total Chilean exports in 2005. In the first half of 2006, copper exports totaled US\$15.1 billion, an increase of 83.2% compared to the first half of 2005. This was partially offset by lower mining output. Despite record prices of Chile's main mineral exports, production fell in the third quarter of 2006 due to strikes and other stoppage events. The average unemployment rate remained stable at 8.7% in the first half of 2006 compared the same period of 2005.

Inflation in 2005 reached 3.7%, the highest level since 1998, mainly driven by rising oil prices and strong internal demand. The annual consumer product index, or the yearly CPI inflation rate reached 3.9% as of June 2006, which was also affected by international oil prices. The Central Bank continued to tighten monetary policy in the first half of 2006, albeit at a slower pace than in 2005. The overnight interbank rate set by the Central Bank increased 225 basis points in 2005 to 4.5% in December 2005. Since January 1, 2006, the Central Bank has raised its reference rate three times to 5.25%.

Long-term rates, on the other hand, did not increase at the same pace. After surging in the last quarter of 2005, long-term rates have been declining in most periods of 2006. Even though the economy is growing at healthy pace, the slowdown of the U.S. economy has dampened the trend of rising interest rates both locally and internationally. The yield on the Chilean Central Bank's 10 year note in real terms was 2.43% and 3.29%, respectively at September 30 and December 31, 2005. At September 30, 2006, the yield was 3.07%.

Despite these developments at the macroeconomic level, economic activities in Chile may slow down given the volatility of international markets and the possible slow-down of the world economic growth.

### **Impact of Inflation**

Inflation impacts our results of operations. Although Chilean inflation has been moderate in recent years, Chile has experienced high levels of inflation in the past. High levels of inflation in Chile could adversely affect the Chilean economy and have an adverse effect on our business, financial condition and results of operations. In 2005, inflation rate reached 3.7% compared to 2.4% in 2004. The annualized CPI inflation rate reached 3.9% as of June 2006 compared to 2.7% as of June 2005. There can be no assurance that Chilean inflation will not change

significantly from the current level. Although we currently benefit from moderate levels of inflation in Chile, due to the current structure of our assets and liabilities (i.e., a significant portion of our loans are indexed to the inflation rate, but there are no corresponding features in deposits, or other funding sources that would increase the size of our funding base), there can be no assurance that our business, financial condition and result of operations in the future will not be adversely affected by changing levels of inflation. In summary:

*UF-denominated assets and liabilities.* Our assets and liabilities are denominated in Chilean pesos, UF and foreign currencies. The UF is revalued in monthly cycles. On each day in the period beginning the tenth day of the current month through the ninth day of the succeeding month, the nominal peso value of the UF is indexed up (or down in the event of deflation) in order to reflect a proportional amount of the change in the Chilean Consumer Price Index during the prior calendar

month. One UF equaled to Ch\$17,489.25 and Ch\$18,151.40 at June 30, 2005 and 2006, respectively. The effect of any changes in the nominal peso value of our UF-denominated assets and liabilities is reflected in our results of operations as an increase (or decrease, in the event of deflation) in interest revenue and expense, respectively. Our net interest revenue will be positively affected by an inflationary environment to the extent that our average UF-denominated assets exceed our average UF-denominated liabilities. Our net interest revenue will be negatively affected by inflation in any period in which our average UF-denominated liabilities exceed our average UF-denominated assets. Our average UF-denominated assets exceeded our average UF-denominated liabilities by Ch\$1,108,952 million and Ch\$2,140,729 million for the six-months ended June 30, 2005 and 2006, respectively. See *Item 3E: Asset and Liability Management* Selected Statistical Information Average Balance Sheets and Interest Rate Data. The Bank generally has more UF-denominated financial assets than UF-denominated financial liabilities. In the first half of 2006, the interest gained on interest-earning assets denominated in UF increased 12.5% as a result of the inflation and the larger amount of assets than liabilities denominated in UFs. The interest paid on these liabilities decreased, by 5.7% during this period, despite higher inflation rates, as the average balance of liabilities denominated in UFs decreased and thus the UF-asset gap increased. A change in real rates also affected the amount of interest earned and paid this period.

<b>Inflation sensitive income</b>	<b>At June 30,</b>		
	<b>2005</b>	<b>2006</b>	<b>% Change</b>
	<b>(In million of constant Chilean pesos at June 30, 2006)</b>		
Interest gained on UF assets	188,767	212,441	12.5%
Interest paid on UF liabilities	(90,846)	(85,637)	(5.7%)
<b>Net Gain</b>	<b>97,921</b>	<b>126,804</b>	<b>29.5%</b>

- Peso-denominated assets and liabilities.** Interest rates prevailing in Chile during any period primarily reflect the inflation rate during the period and expectations of future inflation. The responsiveness to such prevailing rates on our peso-denominated interest-earning assets and interest-bearing liabilities varies. See *Item 3C: Operating Results* Interest Rates. We maintain a substantial amount of non-interest-bearing peso-denominated demand deposits. Because such deposits are not sensitive to inflation, any decline in the rate of inflation would adversely affect our net interest margin on inflation-indexed assets funded with such deposits, and any increase in the rate of inflation would increase the net interest margin on such assets. The ratio of such demand deposits to average interest-earning assets was 17.1% and 14.1% at June 30, 2005 and 2006, respectively.
- Price level restatement.** Chilean GAAP requires that financial statements be restated to reflect the full effects of loss in the purchasing power of the Chilean peso on the financial position and results of operations of reporting entities. The Bank must adjust its capital, fixed assets and other non-financial assets for variations in price levels. Since the Bank's capital is generally larger than the sum of fixed and other non-financial assets, when inflation is positive, the Bank would record a loss from price level restatement. For the six-months ended June 30, 2006, the loss from price level restatement totaled Ch\$7,466 million compared to a loss of Ch\$4,956 million in the same period of 2005. The inflation rate used for calculating price level restatement was similar in these periods (0.98% in the first half of 2006 and 0.99% in the first half of 2005), but as the Bank lowered its payout ratio, the gap between equity and other assets widened, which resulted in an increase in the loss from price level restatement. This is partially offset by the positive impact on the funding mix and margins due to a higher proportion of earnings that do not have to be substituted with more expensive deposits.

## Interest Rates

Interest rates earned and paid on our assets and liabilities reflect, to a certain degree, inflation, expectations regarding inflation, changes in short-term interest rates set by the Central Bank and movements in long-term real rates. The Central Bank manages short-term interest rates based on its objectives of balancing low inflation and economic growth. Because our liabilities generally reprice sooner than our assets, changes in the rate of inflation or short-term rates in the economy are reflected in the rates of interest paid by us on our liabilities before such changes are reflected in the rates of interest earned by us on our assets. Therefore, when short-term interest rates fall, our net interest margin is positively impacted, but when short-term rates increase, our interest margin is negatively affected. At the same time, our net interest margin tends to be adversely affected in the short term by a decrease in inflation rates since generally our UF-denominated assets exceed our UF-denominated liabilities.

*See [Item 3C: Operating Results][Impact of Inflation][Peso ] denominated Assets and Liabilities.] An increase in long-term rates also has a positive effect on our net interest margin, because our interest-earning assets generally have longer tenors than our interest-bearing liabilities. In addition, because our peso-denominated liabilities have relatively short repricing periods, they are generally more responsive to changes in inflation or short-term rates than our UF-denominated liabilities. As a result, during periods when current inflation or expected inflation exceeds the previous period's inflation, customers often switch funds from UF-denominated deposits to peso-denominated deposits, which generally bear higher interest rates, thereby adversely affecting our net interest margin.*

## Foreign Exchange Fluctuations

The Chilean government's economic policies and any future changes in the value of the Chilean peso against the U.S. dollar could adversely affect our financial condition and results of operations. The Chilean peso has been subject to significant devaluation in the past, including a decrease of 14.7% in 2001 and 8.6% in 2002, and may be subject to significant fluctuations in the future. In 2004 and 2005, the Chilean peso appreciated 6.6% and 8.1% against the dollar, respectively. In the first six-months of 2006, the Chilean peso depreciated 6.4% against the U.S. dollar. See *Item 1A: Selected Financial Data* Exchange Rates. A significant portion of our assets and liabilities are denominated in foreign currencies, principally the U.S. dollar, and we historically have maintained and may continue to maintain material gaps between the balances of such assets and liabilities. Because such assets and liabilities, as well as interest-earned or paid on such assets and liabilities, and gains and losses realized upon the sale of such assets, are translated to Chilean pesos in preparing our financial statements, our reported income is affected by changes in the value of the Chilean peso relative to foreign currencies (principally the U.S. dollar).

Foreign currency denominated obligations of Chilean banks are subject to various limits and obligations. The regulations of the Central Bank do not permit the difference, whether positive or negative, between a bank's assets and liabilities denominated in any foreign currency (including assets and liabilities denominated in U.S. dollars but payable in pesos, as well as those denominated in pesos and indexed to the U.S. dollar exchange rate) to exceed 20% of the bank's paid in capital and reserves; except in the case where the balance of such assets exceeds the balance of such liabilities and the excess does not exceed the bank's allowances and reserves denominated in such foreign currency (excluding profits to be remitted abroad). At June 30, 2005 and 2006, the net foreign currency position was Ch\$57,962 million and Ch\$95,458 million, respectively. The Bank also uses a sensitivity analysis to limit the potential loss in fluctuations of U.S. interest rates on interest income and a VaR model to limit foreign currency trading risk (See *Item 8: Quantitative and Qualitative Disclosures About Market Risk*). The net loss on foreign exchange transactions was Ch\$(7,893) million and Ch\$(49,747) million for the six-months ended June 30, 2005 and 2006. These results include the change in value of the Bank's spot position in foreign currencies and the change in book value of assets and liabilities denominated in foreign currencies. It does not include the mark-to-market gains or losses on the Bank's forward contracts that primarily hedge the spot position in foreign currencies. That result is reflected in net gains on trading activities.

## Results of Operations for the Six-month Period Ended June 30, 2005 and 2006

The following discussion is based upon and should be read in conjunction with the Interim Unaudited Consolidated Financial Statements. The Interim Unaudited Consolidated Financial Statements have been prepared in accordance with Chilean GAAP (including the rules of the Superintendency of Banks relating thereto), which differ in certain significant respects from U.S. GAAP. *Note 26 to the Unaudited Consolidated Financial Statements* describes the principal differences between Chilean GAAP and U.S. GAAP and includes reconciliations to U.S. GAAP of our net income for the six-months ended June 30, 2005 and 2006 and of our shareholders' equity at June 30, 2005 and 2006. The Unaudited Consolidated Financial Statements have been restated in constant Chilean pesos of June 30, 2006. See *Note 1(c) to the Unaudited Consolidated Financial Statements*.

## Introduction

The following table sets forth the principal components of our net income for the six-month period ended June 30, 2005 and 2006.

At June,		% Change	
2005	2006	2006	2005/2006
(in millions of constant Ch\$ of June 30, 2006)		(in thousands of US\$(1))	

**CONSOLIDATED INCOME  
STATEMENT****DATA****Chilean GAAP:****Interest income and expense**

Interest revenue	445,155	558,785	1,020,967	25.5%
Interest expense	(185,095)	(259,647)	(474,406)	40.3%
	<hr/>	<hr/>	<hr/>	<hr/>
Net interest revenue	260,060	299,138	546,561	15.0%
<b>Provision for loan losses</b>	(30,192)	(47,231)	(86,296)	56.4%
<b>Fees and income from services</b>				
Fees and other services income	79,819	95,958	175,326	20.2%
Other services expense	(14,719)	(17,861)	(32,633)	21.3%
	<hr/>	<hr/>	<hr/>	<hr/>
Total fees and income from services, net	65,100	78,097	142,693	20.0%



	At June,			% Change
	2005	2006	2006	2005/2006
	(in millions of constant Ch\$ of June 30, 2006)		(in thousands of US\$)(1)	
<b>Other operating income, net</b>				
Net gain (loss) from trading and brokerage	30,947	82,599	150,918	166.9%
Foreign exchange transactions, net	(7,893)	(49,747)	(90,894)	530.3%
Others, net	(10,018)	(16,903)	(30,884)	68.7%
Total other operating income, net	13,036	15,949	29,140	22.3%
<b>Other income and expenses</b>				
Non-operating income, net	(20,721)	(19,538)	(35,698)	(5.7%)
Income attributable to investments in other companies	528	649	1,186	22.9%
Losses attributable to minority interest	(125)	(84)	(153)	(32.8%)
Total other income and expenses	(20,318)	(18,973)	(34,665)	(6.6%)
<b>Operating expenses</b>				
Personnel salaries and expenses	(70,287)	(73,137)	(133,630)	4.1%
Administrative and other expenses	(47,969)	(53,443)	(97,646)	11.4%
Depreciation and amortization	(18,312)	(18,964)	(34,649)	3.6%
Total operating expenses	(136,568)	(145,544)	(265,925)	6.6%
<b>Loss from price-level restatement</b>	(4,956)	(7,466)	(13,643)	50.6%
<b>Income before income taxes</b>	146,162	173,970	317,865	19.0%
<b>Income taxes</b>	(25,760)	(29,191)	(53,335)	13.3%
<b>Net income</b>	120,402	144,779	264,530	20.2%

(1) Amounts stated in U.S. dollars at and for the six-month period ended June 30, 2005 and 2006 have been translated from Chilean pesos at the exchange rate of Ch\$547.31 = US\$1.00 at June 30, 2006. See *Item 1A: Selected Financial Data* Exchange Rates for more information on the observed exchange rate.

Net income for the six-month period ended June 30, 2006 increased 20.2% to Ch\$144,779 million compared to Ch\$120,402 million for the six-months ended of June 30, 2005, primarily as a result of the strength of the Chilean economy, which continued to fuel loan growth and banking activities, especially in the higher-yielding retail banking segments, which in turn has fueled growth of net interest revenue and fee income. Net interest revenue increased 15.0%, totaling Ch\$299,138 million and fee income grew 20.0% and reached Ch\$78,097 million in the first half of 2006 compared to the first half of 2005. Our net interest margin in the first half of 2006 reached 4.7% compared to 4.5% in the first half of 2005.

The increase in net interest revenue was partially offset by a 56.4%, or Ch\$17,039 million, increase in provisions for loan losses. Provisions for loan losses increased by Ch\$15,702 million, or 30.0%, primarily as a result of the growth of the Bank's consumer loan portfolio as a proportion of its total portfolio, for which provisions are required to be made in a shorter period of time than provisions for the rest of the loan portfolio. In addition, recoveries on loans previously charged off increased at a lower rate than charge-offs. They increased by 15.7%, or Ch\$3,055 million.

Overall asset quality indicators continued to improve in the first half of 2006. The consolidated risk index, which is a ratio of total loan loss allowance, calculated according to the guidelines established by us (and approved by the Superintendency of Banks), divided by total loans, decreased from 1.82% at June 30, 2005 to 1.32% at June 30, 2006. Past due loans at June 30, 2006 decreased by 29.9% compared to June 30, 2005. Past due loans as a percentage of total loans decreased from 1.29% at June 30, 2005 to 0.79% at June 30, 2006. The improvement in asset quality was mainly due to the positive economic environment and the increase in charge-offs.

Operating expenses for the first half of 2006 increased by 6.6% compared to the first half of 2005, primarily as a result of an increase in administrative and other expenses and personnel salaries and related expenses. The 4.1% rise in personnel expenses reflected a 3.3% increase in average headcount and an increase in bonuses paid to business teams for reaching business targets. Administrative expenses increased by 11.4% for the first half of 2006 compared to the same period in 2005, which reflected an increase in expenses as a result of the expansion of our distribution network. Our efficiency ratio, despite higher costs, continued to improve, reaching a record low of 37.0% for the first half of 2006 compared to 40.4% for the first half of 2005, which was partly attributable to increases in our net interest income and net fee income.

Results in the first half of 2006 also included a gain of Ch\$7,089 million following the adoption of new accounting criteria for valuing financial instruments, which resulted in a gain from trading activities. If we had applied the new accounting standards for the six-month period ended June 30, 2005, the net effect on our results would have been a loss of Ch\$7,264 million.

**Net interest revenue**

	For the six-month period ended		% Change
	June 30,		
	2005	2006	2005/2006
	<b>(In millions of constant Ch\$ of June 30, 2006, except percentages)</b>		
Interest revenue	445,155	558,785	25.5%
Interest expense	(185,095)	(259,647)	40.3%
<b>Net interest revenue</b>	<b>260,060</b>	<b>299,138</b>	<b>15.0%</b>
Average interest-earning assets	11,557,831	12,870,029	11.4%
Average loans	9,137,886	10,349,942	13.3%
Average non-interest-bearing demand deposits	1,975,515	1,814,094	(8.2%)
Average interest-bearing liabilities	8,282,998	9,501,568	14.7%
<b>Net interest margin(1)</b>	<b>4.5%</b>	<b>4.7%</b>	
<b>Average nominal rate earned(2)</b>	<b>7.7%</b>	<b>8.7%</b>	
<b>Average nominal rate paid(3)</b>	<b>4.5%</b>	<b>5.5%</b>	
Average shareholders' equity and average demand deposits to total average interest-earning assets	26.1%	25.3%	
Average loans / Average assets	68.5%	69.2%	
<b>Economic indicators:</b>			
Inflation rate (Variation of UF)	0.99%	0.98%	
90 day nominal rate	2.80%	4.64%	
10 year Central Bank real rate	2.69%	3.09%	

(1) Net interest margin is net interest revenue divided by average interest-earning assets, on an annualized basis (multiplied by 2).

(2) Interest income divided by average interest-earning assets, on an annualized basis (multiplied by 2).

(3) Interest expense divided by average interest-bearing liabilities, on an annualized basis (multiplied by 2).

Net interest revenue for the six-month period ended June 30, 2006 increased by 15.0% compared to the corresponding period in 2005, mainly reflecting a 11.4% increase in average interest-earning assets, coupled with an increase in our net interest margin from 4.5% for the first half of 2005 to 4.7% for the first half of 2006.

Average interest earning asset growth was led by a 13.3% increase in average loans. This growth in average lending was driven by the stable economic environment and gain in market share in retail lending. Total loan market share decreased 20 basis points from 23.0% in June 30, 2005 to 22.8% as of June 30, 2006. Market share in lending to individuals increased from 25.1% as of June 30, 2005 to 25.9% as of June 30, 2006 led by a 90 basis point rise in residential mortgage lending and a 60 basis point rise in consumer lending market share.

The principal factor positively affecting our net interest margin was the change in asset mix. Total average loans for the first half of 2006 increased by 12.5%. High yielding average consumer loans increased 26.8% in the first half of 2006 compared to the same 2005 period. The average nominal rate paid on loans was 9.4% for the first half of 2006 compared to 8.4% for the same period of 2005. The average annualized rate earned on consumer loans increased from 20.4% for the six-month period ended June 30, 2005 to 21.6% for the six-month period ended June 30, 2006. At the same time, higher interest rates also helped to increase margins. The average real yield on Central Bank 10 year bonds, a benchmark for long-term loan rates, reached 3.09% in the first half of

2006 compared to 2.69% in the same period of 2005.

Net interest margin was also positively affected by the larger UF gap. Our average UF-denominated assets exceeded our average UF-denominated liabilities by Ch\$2,140,729 million for the six-month period ended in June 30, 2006 compared to Ch\$1,108,952 million for the same period of 2005. This 93.0% rise in the average UF gap was created in the second quarter of 2006 when inflation increased as a result of increasing oil prices. Even though inflation in both periods was similar, the larger gap created in a high inflation environment positively impacted our net interest income. See [Item 3C: Operating ResultsImpact of Inflation] for a quantitative disclosure of the impact of inflation on our net interest income.

The principal factors negatively affecting the net interest margin were the rise in short-term interest rates and the lower ratio of the average balances of non-interest-bearing demand deposits and shareholders' equity to interest-earning assets. As interest-bearing liabilities generally have shorter terms than interest-earning assets, a rise in short-term rates has a negative effect on our net interest margin. The average annualized nominal rate paid on interest-bearing liabilities increased from 4.5% for the first half of 2005 to 5.5% for the first half of 2006. The average 90-day Central Bank rate, a benchmark rate for deposits, increased in nominal terms from 2.80% for the first half of 2005 to 4.60% in the first half of 2006.

As short-term interest rates increased, so did the attractiveness of time deposits, thereby increasing the costs of our time deposits. Average time deposits increased by 25.4% in the first half of 2006 compared to the first half of 2005. Non-interest bearing demand deposits decreased by 8.2% in the same period. Average time deposits represented 42.2% of average liabilities

for the first half of 2006 compared to 37.8% for the same period of 2005. Average free funds (non-interest bearing demand deposits and shareholders' equity), as a percentage of interest earning assets, also decreased, as a result of the rise in short-term rates, from 26.1% for the first half of 2005 to 22.7% for the first half of 2006. This was partially offset by the rise in spread earned over free funds as a result of the higher interest rate environment.

### **Provision for loan losses**

As of January 1, 2006, we have improved our credit scoring systems for consumer and mortgage loans. The new credit scoring system considers both the length of time by which the loan is overdue and the borrower's risk profile, which includes the borrower's overall indebtedness and credit behavior under the obligations to third parties. See *Item 3E: Asset and Liability Management* [Loan Portfolio] Classification of Loan Portfolio Allowances for consumer and mortgage loans.

Through June 30, 2006, we maintained a model for calculating loan loss allowance based on group analysis of those commercial loans that were not assessed on an individual basis (approximately 25% of total commercial loans). Commencing in December 2006, we expect to no longer analyze commercial loans on a group basis. All commercial loans will be rated on an individual basis and loans in small amounts will be scored in an automated system utilizing various factors to calculate an expected loss ratio, which is equivalent to the allowance for loan loss set aside for the loan. These changes to our provisioning policies in respect of commercial loans were approved by the Superintendency of Banks and our Board of Directors. See *Item 3E: Asset and Liability Management* [Loan Portfolio] Classification of Loan Portfolio Allowances for group evaluations on commercial loans.

For statistical information with respect to our substandard loans and reserves for probable loan losses, see [Item 3E: Asset and Liability Management] Loan Loss Provisions Analysis of Substandard Loans and Amounts Past Due and [Item 3E: Asset and Liability Management] Loan Loss Provisions Analysis of Loan Loss Provisions, as well as Note 7 to the Unaudited Consolidated Financial Statements for the six-month periods ended June 30, 2005 and 2006. The amount of provision charged to income in any period consists of net provisions established for possible loan losses, net of recoveries on loans previously charged off.

	For the six-month period ended		% Change
	June 30,	June 30,	
	2005	2006	2005/2006
<b>(In millions of constant Ch\$ of June 30, 2006, except percentages)</b>			
Provision expenses	4,242	150	(96.5%)
Charge-offs	(53,935)	(69,937)	29.7%
Recoveries for loans previously charged off	19,501	22,556	15.7%
<b>Provisions expense, net</b>	<b>(30,192)</b>	<b>(47,231)</b>	<b>56.4%</b>
Period-end loans	9,783,992	11,153,071	14.0%
Substandard loans	314,354	336,973	7.2%
Past-due loans	126,353	88,559	(29.9%)
Loan loss allowance	177,987	147,583	(17.1%)
Substandard loans / Period-end loans (1)	3.21%	3.02%	
Past due loans / Period-end loans (2)	1.29%	0.79%	
Consolidated risk index (3)	1.82%	1.32%	

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Coverage ratio (4)	140.9%	166.6%
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- (1) Substandard loans (all mortgage and consumer loans rated B- or worse and all commercial loans rated C2 or worse) divided by period- end loans.
  - (2) Past due loans divided by period-end loans.
  - (3) Loan loss allowance divided by period-end loans.
  - (4) Loan loss allowance divided by past due loans.

Net provision expenses for loan losses totaled Ch\$47,231 million for the six-month period ended June 30, 2006, an increase of 56.4% compared to the same period of 2005, primarily due to an increase in charge-offs. Charge-offs increased by 30.0%, or Ch\$15,702 million, in the six-months ended June 30, 2006 compared to the corresponding period of 2005, primarily as a result of the growth of our consumer loan portfolio, for which credit risk is higher and provisions are required to be made within much shorter periods than the rest of the loan portfolio. In addition, recoveries on loans previously charged off increased at a lower rate than charge-offs. These recoveries increased by 15.7%, or Ch\$3,055 million, in the six-months ended June 30, 2006 compared to the corresponding period of 2005. Our recovery department is currently being reorganized in order to keep up with the growth in our retail lending business. We recorded a net decrease of Ch\$150 million from loan loss allowance,

compared to a net decrease of Ch\$4,242 million in the corresponding period of 2005, primarily due to the increase in retail loans, which require increased gross provisions.

Overall asset quality indicators continued to improve in the first half of 2006. The consolidated risk index, which is a ratio of total loan loss allowances, calculated according to the guidelines established by the Superintendency of Banks and the Bank, divided by total loans, decreased from 1.82% at June 30, 2005 to 1.32% at June 30, 2006. Past due loans at June 30, 2006 decreased by 29.9% compared to June 30, 2005. Past due loans as a percentage of total loans decreased from 1.29% at June 30, 2005 to 0.79% at June 30, 2006. The improvement in asset quality was primarily due to the positive economic environment and the increase in charge-offs.

We expect provisions for loan losses to increase in future periods in line with the overall growth of our loan portfolio and our increased lending to small companies and individuals which poses a higher risk of default than lending to traditional corporate and commercial customers. See *□Risk Factors□Risks Associated with our Business□Our exposure to individuals and small businesses could lead to higher levels of loan losses and charge-offs□* and *□Risk Factors□Risks Associated with our Business□The growth of our loan portfolio may expose us to increased loan losses.□*

### **Fee income**

The following table sets forth certain components of our income from services (net of fees paid to third parties directly connected to providing those services, principally fees relating to credit card processing and ATM network administration) for the six-month period ended June 30, 2005 and 2006.

	<b>For the six-months ended</b>		
	<b>June 30,</b>		
	<b>(In million of constant Ch\$</b>		
	<b>of</b>		
	<b>June 30, 2006)</b>	<b>% Change</b>	
	<b>2005</b>	<b>2006</b>	<b>2005/2006</b>
Checking account and lines of credit (1)	18,826	25,646	36.2%
Agreements to administer and to collect insurance policies	8,604	11,844	37.7%
Mutual fund services	8,895	9,356	5.2%
Credit cards	5,987	8,931	49.2%
Automatic teller cards	6,981	7,275	4.2%
Insurance brokerage	4,877	4,446	(8.8%)
Sales and purchases of foreign currencies	2,685	2,415	(10.1%)
Contingent loans	1,505	1,544	2.6%
Payment Agency services	1,592	1,317	(17.3%)
Underwriting	1,532	888	(42.0%)
Stock brokerage	590	628	6.4%
Custody and trust services	383	213	(44.4%)
Bank drafts and fund transfers	126	124	(1.6%)
Saving accounts	128	122	(4.7%)
Others	2,389	3,348	40.1%
<b>Total</b>	<b>65,100</b>	<b>78,097</b>	<b>20.0%</b>

(1) See *Item 3H Reconciliation of Non-GAAP Measures*

Total net fee income increased by 20.0% to Ch\$78,097 million for the first half of 2006 compared to the corresponding period in 2005. The positive economic environment led to a rise in the usage and penetration of bank products in the first six-months of 2006. The number of middle-upper income individual clients who are

cross-sold (a client with a checking account who also uses at least four other banking products) increased by 33.3% at June 30, 2006 compared to June 30, 2005. The number of small and mid-sized enterprises that are cross-sold increased by 78.0% in the same period. In Santander Banefe, the number of cross-sold clients (clients who also use at least two other products) rose by 22.0% at June 30, 2006 compared June 30, 2005.

Fees from checking accounts and lines of credit increased by 36.2%, primarily as a result of a rise in the fee charged for lines of credit and the growth of our checking account and credit line base. These products are offered together and, therefore, are being analyzed as a single product (*See Item 3H. Reconciliation of Non-GAAP Measures*). Our market share in checking accounts at May 2006, the last figure available, was 26.2% compared to 24.3% at May 2005. In this same period, our checking



account base increased by 18.2%, compared to 9.4% for the market as a whole. This indicates that of all new accounts opened in this twelve month period, 47% were opened with us.

Credit card fees increased by 49.2% for the six-month-period ended June 30, 2006 compared to the same period of 2005. We were the market leader in bank credit card with 37.3% market share as of June 30, 2006. Usage of credit cards issued by us measured in monetary terms increased by 18.3% for the June 30, 2006 compared to June 30, 2005. The number of our credit card customer accounts increased by 25.3% to 890,365 at June 30, 2006 compared to June 30, 2005. The rise in credit card fees is partially offset by the other credit card expenses reflected in "Other operating losses, net."

The collection and administration of insurance policies increased by 37.7% for the six-months ended June 30, 2006 compared to the same period of 2005. These fees are directly related to the growth of our mortgage loan book and lower-than-estimated claim rates, which results in higher administration fees paid by insurers to us.

The 6.4% rise in ATM fees was mainly driven by the increase in the number of ATMs installed by the Bank. As of June 30, 2006, Bank had 1,443 ATMs compared to 1,225 as of June 30, 2005. The rise in ATMs was offset by increased competition in order to obtain ATM locations with large retailers.

Other fees increased by 40.1% in the first six-months of 2006 mainly due to a rise in fees paid to us in connection with financial advisory services provided to companies and internet banking services for corporate clients. Payment agency service charges decreased by 17.3% in the period being analyzed. Payment agency service charges are mainly related to collection services we perform on behalf of corporate customers. These services are increasingly being performed through our internet banking services. Underwriting fees decreased by 42.0% in the same period. This decrease was partially offset by financial advisory fees being charged to corporate clients.

Fees from our mutual fund asset management subsidiary increased by 5.2%. Total assets under management increased by 18.5% to Ch\$1,813,195 million (US\$3.3 billion) at June 30, 2006 compared to June 30, 2005.

Insurance brokerage fees decreased by 8.8% for the six-months ended June 30, 2006 compared to the first half of 2005. Increased competition during the period lowered premiums, which negatively affected the growth rate of insurance brokerage.

***Other operating income (expenses), net***

The following table sets forth information regarding our other operating income (expenses), net, for the six-month period ended June 30, 2005 and 2006.

	<b>For the six-months ended June</b>		<b>% Change</b>
	<b>30,</b>		
	<b>2005</b>	<b>2006</b>	<b>2005/2006</b>
	<b>(In millions of constant Ch\$ of June 30, 2006, except percentages)</b>		
Net gains from trading activities	30,947	82,599	166.9%
Foreign exchange transactions, net	(7,893)	(49,747)	530.3%
Total net gains from financial transactions	23,054	32,852	42.5%
Other operating losses, net	(10,018)	(16,903)	68.7%
Total other operating income	13,036	15,949	22.3%

Total other operating income, net, totaled a gain of Ch\$15,949 million for the six-month period ended June 30, 2006 compared to a gain of Ch\$13,036 million for the same period of 2005.

In accordance with Circular No. 3345 issued by the Superintendency of Banks, effective January 1, 2006, the accounting criteria for valuing financial instruments acquired for trading or investment purposes, including derivative instruments, was amended. In summary, we must record our derivatives portfolio at fair value and hedge accounting was introduced. *See Item 3.A.- New Accounting Standards for Financial investments and Derivatives.*

Net gains from trading activities totaled Ch\$82,599 million in the first half of 2006. This line item in the first six-months of 2006 mainly included: (i) unrealized gains of Ch\$77,448 million on financial instruments (including derivatives), which includes a gain of Ch\$7,089 million resulting from the change in accounting standards, (ii) gains of Ch\$5,580 million from mark-to-market adjustments made on securities in the fixed income trading portfolio, and (iii) losses of Ch\$42 million from sales of fixed income instruments.

The net result from foreign exchange transactions totaled a loss of Ch\$49,747 million for the six-months ended June 30, 2006. These results mainly included the translation gain or loss of assets and liabilities denominated in foreign currencies (excluding derivatives) that is the counterpart to hedged positions with derivatives. The net gain from trading of foreign currencies in the first half of 2006 was Ch\$2,930 million.

For analysis purposes only, we have presented in the table above □Total net gains from financial transactions□ the net gain on trading activities and foreign exchange transactions (*See Item 3H. Reconciliation of Non-GAAP Measures*). As the Bank hedges its foreign exchange exposure by entering into foreign currency forwards (*See Item 8: Quantitative and Qualitative Disclosures About Market Risk*), the effects recorded in foreign exchange transactions are largely offset by mark-to-market adjustments on foreign currency forwards.

The net gain from financial transactions increased by 42.5% to Ch\$32,852 million for the six months ended June 30, 2006 compared to the corresponding period of 2005 due to a Ch\$7,089 million gain generated by the change in accounting principles described in Item 3.A. and total gains from financial transactions of Ch\$25,763 million, an increase of 11.8% compared to the gains from financial transactions recorded for the first half of 2005. The figures for the six-months ended June 20, 2006 and the corresponding period of 2005 are therefore not strictly comparable. Gains from financial transactions for the first half of 2006 included gains of Ch\$10,666 million generated by our proprietary trading desk. Gains from financial transactions for the first half of 2006 also included gains of Ch\$18,002 million from transactions conducted on customer request.

For the six-month period ended June 30, 2006, other operating losses, net, increased by 68.7% to Ch\$16,903 million compared to Ch\$10,018 million for the first half of 2005, primarily due to our increased business activities, which resulted in increases in sales force expenses, credit card related expenses and other customer related expenses. Other operating expenses consisted primarily of expenses relating to the Bank's outsourced sales force, results from the sale of repossessed assets, expenses relating to the maintenance of repossessed assets, expenses relating to credit card services and other client services.

Total sales force expenses increased by 8.6% to Ch\$8,163 million for the six-month period ended June 30, 2006 compared to the corresponding period in 2005, primarily due to our increased retail banking business activities, which resulted in an increase in commissions paid to our sales force. Expenses relating to our credit card business increased by 353.2% to Ch\$2,429 million for the six-months ended June 30, 2006 compared to the corresponding period in 2005, primarily as a result of relatively higher premium rates on fraud insurance covering some of our new cards and an increase in the membership fees paid to Transbank, the company collectively owned by major banks in Chile which runs credit card payment networks in Chile. These higher costs were offset by higher fees and usage of our credit card business, strong growth of lending and savings products (in part sold by the sales force).

Customer service expenses, which consist primarily of expenses paid to third parties for transporting funds for corporate customer, as part of cash management agreements, increased by 83.7% to Ch\$5,209 million for the six-months ended June 30, 2006 compared to the corresponding period in 2005. This reflects higher business activity in general and was offset by positive performance of our cash management business. We generate fees for collection and corporate e-banking services and generates net interest income off of floating balances of these clients.

The results from the sale of repossessed assets decreased by 48.0% to Ch\$1,560 million for the first half of 2006 compared to the first half of 2005. In the first half of 2005, we recognized a gain of Ch\$1,100 million from the leasing of a large repossessed asset, which explains the decline in income in this line item in the first half of 2006.

#### ***Other income and expenses, net***

The following table sets forth information regarding our operating expenses for the six-month period ended June 30, 2005 and 2006.

	<b>For the six-months ended June 30,</b>		<b>% Change</b>
	<b>2005</b>	<b>2006</b>	<b>2005/2006</b>
	<b>(In millions of constant Ch\$ of June 30, 2006, except percentages)</b>		
Non-operating income (expense), net	(20,721)	(19,538)	(5.7%)
Income attributable to investments in other companies	528	649	22.9%
Losses attributable to minority interest	(125)	(84)	(32.8%)
<b>Total</b>	<b>(20,318)</b>	<b>(18,973)</b>	<b>(6.6%)</b>

The net loss recorded in other income and expenses, net, decreased by 6.6% for the first half of 2006 compared to the first half of 2005, primarily due to provisions for repossessed assets, which totaled Ch\$9,549 million for the six-months ended June 30, 2006, a decrease of 30.6% compared to the first half of 2005. This was partially offset by the 41.4% decrease in the gains from the sale of repossessed assets previously charged-off, which totaled Ch\$4,598 million for the first half of 2006. Non-operating results also include provisions for other contingencies. These contingencies are mainly relating to non-credit risks, including non-specific contingencies, tax contingencies and other non-credit contingencies or impairments. For the first half of 2006, these provisions totaled Ch\$11,848 million, including Ch\$15,029 million in non-specific contingencies (a decrease of 3.0% from the 2005 period), which remained effectively stable compared to the amount of non-credit provisions recognized in the first half of 2005 (See Note 18 to our Unaudited Consolidated Financial Statements).

### **Operating expenses**

The following table sets forth information regarding our operating expenses for the six-month period ended June 30, 2005 and 2006.

	<b>For the six-months ended June 30,</b>		<b>% Change</b>
	<b>2005</b>	<b>2006</b>	<b>2005/2006</b>
	<b>(In millions of constant Ch\$ of June 30, 2006, except percentages)</b>		
Personnel salaries and expenses	(70,287)	(73,137)	4.1%
Administrative expenses	(47,969)	(53,443)	11.4%
Depreciation and amortization	(18,312)	(18,964)	3.6%
<b>Total</b>	<b>(136,568)</b>	<b>(145,544)</b>	<b>6.6%</b>
<b>Efficiency ratio(1)</b>	<b>40.4%</b>	<b>37.0%</b>	

(1) The efficiency ratio is the ratio of total operating expenses to total operating revenue. Total operating revenue consists of net interest revenue, fees and income from services, net, and other operating income, net.

Operating expenses for the first half of 2006 increased by 6.6% compared to the first half of 2005. The 4.1% rise in personnel expenses reflects a 3.1% increase in average headcount and an increase in bonuses paid to business teams for reaching business targets. Administrative expenses increased by 11.4% for the same periods, reflecting an increase in expenses as a result of the expansion our distribution network. The branch network totaled 367 branches as of June 30, 2006, an increase of 12.2% since June 2005. Out ATM network totaled 1,443 machines, an increase of 17.8% since June 2005. We expect personnel and administrative expenses to grow at a higher pace in future periods as a result of our strategy to expand our retail banking business.

Depreciation and amortization expenses increased 3.6% for the first half of 2006 compared to the first half of 2005, which is also mainly attributable to the investments in the distribution network and other fixed assets.

The expansion of our branch and ATM network helped us increase our retail business. The relatively larger expenses incurred as a result of the expansion of the branch and ATM network partially offset by increases in productivity as operating income increased 16.3%. As a result, our efficiency ratio, representing operating expenses divided by operating income, improved from 40.4% for the first half of 2005 to a record low of 37.0% for the first half of 2006. The rate of expansion of our branch and ATM network in the medium-term may vary with fluctuations in the outlook of the Chilean economy.

### **Loss from price level restatement**

The loss from price level restatement totaled Ch\$7,466 million for the first half of 2006, an increase of 50.6% compared to the same period of 2005. We must adjust our capital, fixed assets and other assets for the variations in price levels. Because our capital is larger than the sum of our fixed and other assets, price level restatement usually results in a loss and fluctuates with the inflation rate. The inflation rate used for calculating price level restatement was similar in the periods being analyzed (0.98% for the first half of 2006 and 0.99% for the first half of 2005), but, we lowered our payout ratio (dividends over net income), the gap between equity and other assets widened, which resulted in an increase in the loss from price level restatement. This is partially offset by the positive impact on margins caused by retaining a higher proportion of earnings that do not have to be substituted for more expensive deposits.

***Income tax***

Our income tax expense increased by 13.3% to Ch\$29,191 million for the first half of 2006, primarily due to the 19.0% growth of income before taxes. The effective tax rate for the first half of 2006 was 16.8%, compared to 17.6% for the first half

of 2005. The statutory corporate tax rate was 17% (See Note 20 of our *Unaudited Consolidated Financial Statements at June 30, 2006 and 2005*).

## D. Liquidity and Capital Resources

### Sources of Liquidity

Santander-Chile's liquidity depends upon its (1) capital, (2) reserves and (3) financial investments, including investments in government securities. To cover any liquidity shortfalls and to augment its liquidity position, Santander-Chile has established lines of credit with foreign and domestic banks and also has access to Central Bank borrowings.

The following table sets forth our on-balance sheet contractual obligations and commercial commitments by remaining maturity. In addition, we have certain off-balance sheet commitments, which are mainly commitments to extend credit not otherwise accounted for as contingent loans, overdraft protection and credit card lines of credit. See "Other Off-Balance Sheet Arrangements and Commitments." The following table does not reflect our payment obligations under derivative contracts.

At June 30, 2006, the scheduled maturities of our contractual obligations and of other commercial commitments, including accrued interest, were as follows:

Contractual Obligations	Due within 1 year	Due after 1 year but within 3 years	Due after 3 years but within 6 years	Due after 6 years	Total
	<b>(in millions of constant Ch\$ of June 30, 2006)</b>				
Deposit and other obligations(1)	5,335,395	1,260,363	38,289	11,117	6,645,164
Mortgage finance bonds	99,861	112,344	142,892	237,740	592,837
Subordinated bonds	2,285	43,444	17,690	327,565	390,984
Bonds	120,912	81	382,825	58,960	562,778
Chilean Central Bank borrowings:					
Credit lines for renegotiations of Loans	5,752	-	-	-	5,752
Other Central Bank borrowings	166,067	-	-	-	166,067
Borrowings from domestic financial institutions	3,590	-	-	-	3,590
Investments sold under agreements to Repurchase	149,641	-	-	-	149,641
Foreign borrowings	1,308,406	325,865	2,980	-	1,637,251
Other obligations	44,327	3,661	3,784	1,566	53,338
Total cash obligations (2)	7,236,236	1,745,758	588,460	636,948	10,207,402

(1) Excludes demand deposit accounts and saving accounts, which totaled Ch\$ 2,367,553 million at June 30, 2006.

(2) The Bank as of the date of the filing of this document has no significant purchase obligations.

### Operational leases

Certain bank premises and equipment are leased under various operating leases. Future minimum rental commitments at June 30, 2006 under non-cancelable leases are as follows:

**At June 30,  
2006**



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	<b>(in millions of constant Ch\$ of June 30, 2006)</b>
Due within 1 year	7,965
Due after 1 year but within 2 years	7,233
Due after 2 years but within 3 years	6,254
Due after 3 years but within 4 years	3,096
Due after 4 years but within 5 years	1,511
Due after 5 years	528
<hr/>	
Total	<b>26,587</b>
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At June 30, 2006, the scheduled maturities of other commercial commitments, including accrued interest, were as follows:

Other Commercial Commitments	Due within 1 year	Due after 1 year but within 3 years	Due after 3 years but within 6 years	Due after 6 years	Total
<b>(in millions of constant Ch\$ of June 30, 2006)</b>					
Letters of credit	119,280	89,490	33,818	-	242,588
Guarantees	476,150	28,027	850	-	505,027
Other commercial commitments	283,676	474	1	-	284,151
Total other commercial commitments	879,106	117,991	34,669	-	1,031,766

**(i) Capital and Reserves**

We currently have regulatory capital in excess of the minimum requirement under the current Chilean regulations. According to the General Banking Law, a bank should have regulatory capital of at least 8% of its risk-weighted assets, net of required loan loss allowances, and paid-in capital and reserves (□basic capital□) of at least 3% of its total assets, net of required loan loss allowances. For these purposes, the regulatory capital of a bank is the sum of (1) the bank□s basic capital, (2) subordinated bonds issued by the bank valued at their placement price for an amount up to 50% of its basic capital; *provided* that the value of the bonds shall decrease by 20% for each year that elapses during the period commencing six years prior to their maturity, and (3) its voluntary allowances for loan losses, for an amount of up to 1.25% of its risk weighted assets. The merger of Old Santander-Chile and Santiago required a special regulatory preapproval of the Superintendency of Banks, which was granted on May 16, 2002. The resolution granting this preapproval imposed a regulatory capital to risk-weighted assets ratio of 12% for the merged bank. This indicator was reduced to 11% by the Superintendency of Banks effective January 1, 2005. For purposes of weighing the risk of a bank□s assets, the General Banking Law considers five different categories of assets, based on the nature of the issuer, the availability of funds, the nature of the assets and the existence of collateral securing such assets.

The following table sets forth our minimum capital requirements set by the Superintendency of Banks at the dates indicated. See Note 13 to our Unaudited financial statements for a description of the minimum capital requirements.

	At June 30, 2005(1)	At December 31, 2005(2)	At June 30, 2006(1)
Net capital base	871,804	842,122	940,206
3% of total assets net of loan loss allowance	(421,264)	(394,078)	(465,452)
Excess over minimum required equity	450,540	448,044	474,754
Basic capital as a percentage of the total assets, net of provisions	6.2%	6.4%	6.1%
Regulatory capital	1,294,920	1,206,421	1,313,205
11% of risk-weighted assets, net of loan loss allowance	(1,061,387)	(1,029,863)	(1,184,655)
Excess over minimum regulatory capital	233,533	176,558	128,550
Regulatory equity as a percentage of risk-weighted assets	13.4%	12.9%	12.2%

(1) In millions of constant Chilean pesos as of June 30, 2006.

(2) In millions of constant Chilean pesos as of December 31, 2005.

**(iii) Financial Investments**

The following table sets forth our investment in Chilean government and corporate securities and certain other financial investments at the dates indicated. Financial investments that have a secondary market are carried at market value. All other financial investments are carried at acquisition cost, plus accrued interest and indexation readjustments, as applicable.

	Trading		Available For Sale(3)		
	At	At	At	At	At
	June 30, 2005(1)	December 31, 2005(2)	June 30, 2006(1)	June 30, 2005(1)	June 30, 2006(1)
<b>Central Bank and Government Securities</b>					
Marketable debt securities (4)	273,363	460,181	293,871	141,144	149,527
Investment collateral under agreements to repurchase (5)	174,907	56,967	1,318	42,094	38,123
Investment purchased under agreements to resell	56,758	23,120	181,925	-	-
Subtotal	505,028	540,268	477,114	183,238	187,650
<b>Corporate securities</b>					
Marketable securities (4)	404,744	617,010	401,201	282,041	355,486
Investment collateral under agreements to repurchase (5)	55,158	34,251	117,488	-	-

	Trading			Available For Sale(3)	
	At	At	At	At	At
	June 30, 2005(1)	December 31, 2005(2)	June 30, 2006(1)	June 30, 2005(1)	June 30, 2006(1)
Investment purchased under agreements to resell	-	-	-	-	-
Subtotal	459,902	651,261	518,689	282,041	355,486
Time deposits in Chilean institutions	52,987	57,966	26,095	-	-
Total	1,017,917	1,249,495	1,021,898	465,279	543,136

(1) In millions of constant Chilean pesos as of June 30, 2006.

(2) In millions of constant Chilean pesos as of December 31, 2005.

(3) Pursuant to the new accounting standards effective June 2006, financial investments are required to be classified into one of the following categories: trading, available-for-sale and held-to-maturity. Financial investments at June 30, 2005 have been reclassified into the new categories. Amounts at December 31, 2005 have not been reclassified.

(4) Including market value adjustment.

(5) Under Chilean GAAP, investment securities that are sold subject to repurchase agreements are reclassified from their investment category to "investments under agreements to repurchase." Under U.S. GAAP, no such reclassification would be made since, in substance, the investment securities serve only as collateral for the borrowing.

Under Chilean GAAP, investments held for trading must be marked-to-market.

The following table sets forth an analysis of our investments at June 30, 2006, by remaining maturity and the weighted average nominal rates of such investments:

**TRADING****Remaining Maturity(1)**

	<b>Within one year</b>	<b>Weighted Average Nominal Rate</b>	<b>One to five years</b>	<b>Weighted Average Nominal Rate</b>	<b>Five to ten years</b>	<b>Weighted Average Nominal Rate</b>	<b>More than ten years</b>	<b>Weighted Average Nominal Rate</b>	<b>Total</b>	<b>Weighted Average Nominal Rate</b>
<b>(in millions of constant Ch\$ of June 30, 2006, except percentages)</b>										
<b>Government securities</b>										
Central Bank securities	106,759	4.2%	184,235	3.5%	35,474	3.3%	14,562	3.3%	341,030	
Government pension bonds	209	3.0	122	3.4	66	3.9	24	4.3	421	
<b>Total</b>	<b>106,968</b>		<b>184,357</b>		<b>35,540</b>		<b>14,586</b>		<b>341,451</b>	
<b>Investments purchased under resale agreements</b>	<b>25,301</b>	<b>5.3</b>	<b>109,124</b>	<b>6.3</b>	<b>-</b>		<b>-</b>		<b>134,425</b>	
<b>Time deposits in</b>										
Chilean Financial Institutions	15,105	6.0	10,990	4.0	-		-	-	26,095	
Other Marketable Securities	278,734	4.4	28,665	5.0	57,886	5.3	35,907	5.3	401,192	
<b>Total</b>	<b>293,839</b>		<b>39,655</b>		<b>57,886</b>		<b>35,907</b>		<b>427,287</b>	
<b>Investment Collateral under Agreements to Repurchase</b>	<b>11,131</b>	<b>4.0%</b>	<b>72,736</b>	<b>4.0%</b>	<b>10,376</b>	<b>4.5%</b>	<b>24,492</b>	<b>5.2%</b>	<b>118,735</b>	

**Total  
Financial**

<b>Investment</b>	<u>437,239</u>	<u>405,872</u>	<u>103,802</u>	<u>74,985</u>	<u>1,021,898</u>
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(1) Represents the remaining contractual maturities of these financial assets, and does not necessarily represent our intentions with respect to such assets.

**AVAILABLE FOR SALE****Remaining Maturity(1)**

	<b>Within one year</b>	<b>Weighted Average Nominal Rate</b>	<b>One to five years</b>	<b>Weighted Average Nominal Rate</b>	<b>Five to ten years</b>	<b>Weighted Average Nominal Rate</b>	<b>More than ten years</b>	<b>Weighted Average Nominal Rate</b>	<b>Total</b>	<b>Weighted Average Nominal Rate</b>
<b>(in millions of constant Ch\$ of June 30, 2006, except percentages)</b>										
<b>Government securities</b>										
Central Bank securities	15,871	3.1%	66,626	5.6%	69,309	5.7%	4,610	3.6%	156,415	4.1%
Government pension bonds	9,534	3.3	7,536	3.6	12,801	4.0	1,364	4.3	31,235	3.8
<b>Total</b>	<b>25,405</b>		<b>74,162</b>		<b>82,110</b>		<b>5,974</b>		<b>187,650</b>	
<b>Investments Purchased under Resale</b>										
<b>Agreements Other Financial</b>	-	-	-	-	-	-	-	-	-	-
<b>Investments</b>										
Time deposits in										
Chilean Financial Institutions	-	-	-	-	-	-	-	-	-	-
Other Marketable Securities	738	4.6%	3,303	4.5%	31,107	4.4%	320,338	4.5%	355,486	4.4%
<b>Total</b>	<b>738</b>		<b>3,303</b>		<b>31,107</b>		<b>320,338</b>		<b>355,486</b>	
<b>Investment Collateral under Agreements to Repurchase</b>	-	-	-	-	-	-	-	-	-	-

<b>Total Financial Investment</b>	26,143	77,465	113,217	326,312	543,136
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(1) Represents the remaining contractual maturities of these financial assets, and does not necessarily represent our intentions with respect to such assets.

**Unused sources of liquidity**

The Bank also has credit ratings from three international agencies. Our ratings are equivalent to the Chilean sovereign ratings, but our bond ratings from Moody's Investor Services are higher than the maximum given to Chilean government instruments. We believe our credit ratings, as presented below, are a positive factor when obtaining financing. In 2006, Moody's improved its rating for the Republic of Chile and for the Bank.

<b>Moody's</b>	<b>Rating</b>
Long-term Bank Deposits	A2
Senior bonds	A1
Subordinated Debt	A2
Bank Financial Strength	B-
Short-term	P-1
Outlook	Stable
<b>Standard &amp; Poor's</b>	<b>Rating</b>
LT Foreign Issuer Credit	A
LT Local Issuer Credit	A
ST Foreign Issuer Credit	A-1
ST Local Issuer Credit	A-1
Outlook	Stable



<b>Fitch</b>	<b>Rating</b>
Foreign Currency LT Debt	A
Local Currency LT Debt	A+
Foreign Currency ST Debt	F1
Local Currency ST Debt	F1
Outlook	Stable

### Working capital

As a bank, we satisfy our working capital needs through general funding, the majority of which derives from deposits and other borrowings from the public. *See [Item 3D: Liquidity and Capital Resources - Deposits and Other Borrowings].* In our opinion, our working capital is sufficient for our present needs.

### Liquidity Management

Liquidity management seeks to ensure that, even under adverse conditions, we have access to the funds necessary to cover client needs, maturing liabilities and capital requirements. Liquidity risk arises in the general funding for our financing, trading and investment activities. It includes the risk of unexpected increases in the cost of funding the portfolio of assets at appropriate maturities and rates, the risk of being unable to liquidate a position in a timely manner at a reasonable price and the risk that we will be required to repay liabilities earlier than anticipated.

Our general policy is to maintain liquidity adequate to ensure our ability to honor withdrawals of deposits, make repayments of other liabilities at maturity, extend loans and meet our own working capital needs. Our minimum amount of liquidity is determined by the statutory reserve requirements of the Central Bank. Deposits are subject to a statutory reserve requirement of 9% for demand deposits and 3.6% for peso, UF-denominated and foreign currency denominated time deposits with a term of less than a year. *See [Item 2C: Business Overview]Regulation and Supervision.* The Central Bank has statutory authority to increase these percentages to up to 40% for demand deposits and up to 20% for time deposits. In addition, a 100% special reserve (*reserva técnica*) applies to demand deposits, deposits in checking accounts, other demand deposits received or obligations payable on sight and incurred in the ordinary course of business, other than deposits unconditionally payable immediately or within a term of less than 30 days and other time deposits payable within 10 days. This special reserve requirement applies to the amount by which the total of such deposits exceeds 2.5 times the amount of a bank's paid-in capital and reserves. Interbank loans are deemed to have a maturity of more than 30 days, even if payable within the following 10 days.

The Central Bank also requires us to comply with the following liquidity limits:

- Our total liabilities with maturities of less than 30 days cannot exceed our total assets with maturities of less than 30 days by an amount greater than our capital. This limit must be calculated in local currency and foreign currencies together as one gap.
- Our total liabilities with maturities of less than 90 days cannot exceed our total assets with maturities of less than 90 days by more than twice of our capital. This limit must be calculated in local currency and foreign currencies together as one gap.

We believe we are in compliance with these limits.

We have set other liquidity limits and ratios that minimize liquidity risk and that conform with Central Bank regulations. *See [Item 8: Quantitative and Qualitative Disclosures About Market Risk].*

**Cash Flow**

The tables below set forth our main sources of cash. The subsidiaries are not an important source of cash flow for us and therefore have no impact on our ability to meet our cash obligations. No legal or economic restrictions exist on the ability of subsidiaries to transfer funds to us in the form of loans or cash dividends as long as these subsidiaries abide by the regulations of the *Ley de Sociedad Anónimas* regarding loans to related parties and minimum dividend payments.

	<b>Six-month period ended June 30,</b>	
	<b>2005</b>	<b>2006</b>
	<b>(in millions of constant Ch\$ of June 30, 2006)</b>	
Net cash provided by operating activities	(73,384)	122,450

The Ch\$195,834 million increase in cash provided by operating activities in the six month period ended June 30, 2006 compared to the six month period ended June 30, 2005 was mainly due to (i) a Ch\$108,382 million variation in net changes in other assets and liabilities, (ii) a Ch\$37,016 million variation in the net change in interest accruals and (iii) higher commercial activity reflected in an increase in net interest revenue and net fee income.

	<b>Six-month period ended June 30,</b>	
	<b>2005</b>	<b>2006</b>
	<b>(in millions of constant Ch\$ of June 30, 2006)</b>	
Net cash provided by (used in) investing activities	169,908	(890,349)

Net cash used in investing activities in the first half of 2006 totaled Ch\$890,349 million mainly as a result of the growth of the Bank's loan and financial investment portfolios. In the same period of 2005 the increase in loans was offset by the fall in financial investments.

	<b>Six-month period ended June 30,</b>	
	<b>2005</b>	<b>2006</b>
	<b>(in millions of constant Ch\$ of June 30, 2006)</b>	
Net cash provided by (used in) financing activities	316,726	1,118,173

In the first half of 2006, the Bank financed its lending activities with increases in current accounts, time deposits, short-term funds borrowed and senior bonds. The rise in financing activities compared to the first half of 2005 was mainly due to greater amounts of bonds issued and short-term funds borrowed.

### **Deposits and Other Borrowings**

The following table sets forth our average daily balance of liabilities for the six-months ended June 30, 2005 and 2006, in each case together with the related average nominal interest rates paid thereon.



## For the six-months ended June 30,

	2005			2006		
	Average Balance	% of Total Average Liabilities and shareholders' equity	Average Nominal Rate	Average Balance	% of total average liabilities and shareholders' equity	Average Nominal Rate
<b>(In million of constant Ch\$ at June 30, 2006, except percentages)</b>						
Savings accounts	122,872	0.9%	1.1%	107,116	0.7%	0.1%
Time deposits	5,038,345	37.8%	1.7%	6,318,311	42.2%	2.4%
Central Bank borrowings	205,224	1.5%	1.6%	95,724	0.6%	2.6%
Repurchase agreements	103,308	0.8%	12.3%	117,646	0.8%	12.3%
Mortgage finance bonds	969,448	7.3%	3.8%	621,133	4.2%	3.6%
Other interest-bearing liabilities	1,843,801	13.8%	2.5%	2,241,638	15.0%	3.0%
Subtotal interest-bearing liabilities	8,282,998	62.1%	2.2%	9,501,568	63.5%	2.7%
<b>Non-interest-bearing liabilities</b>						
Non-interest-bearing deposits	1,975,515	14.8%		1,814,094	12.1%	
Contingent liabilities	896,822	6.7%		924,490	6.2%	
Other non-interest-bearing liabilities	1,130,302	8.5%		1,618,600	10.8%	
Shareholders' equity	1,043,298	7.8%		1,107,461	7.4%	
Subtotal non-interest-bearing liabilities and shareholders' equity	5,045,937	37.9%		5,464,645	36.5%	
<b>Total liabilities and shareholders' equity</b>	13,328,935	100.0%		14,966,213	100.0%	

Our most important source of funding is our time deposits. Average time deposits represented 42.2% of our average total liabilities and shareholders' equity in the six-month period ended June 30, 2006. Our current funding strategy is to continue to utilize all sources of funding in accordance with their costs, their availability

and our general asset and liability management strategy. Special emphasis is being placed on lengthening the maturities of time deposits with institutional investors and increasing in general our deposits from retail customers. We also intend to continue to broaden our customer deposit base, to emphasize core deposit funding and to lengthen the maturities of time deposits received from institutional investors. Management believes that broadening our deposit base by increasing the number of account holders has created a more stable funding source.

**Composition of Deposits and Other Commitments**

The following table sets forth the composition of our deposits and similar commitments at the dates indicated.

	<u>At June 30, 2005(1)</u>	<u>At December 31, 2005(2)</u>	<u>At June 30, 2006(1)</u>
Checking accounts	1,429,197	1,455,924	1,572,712
Other demand liabilities	1,162,196	668,325	744,576
Savings accounts	117,350	109,423	106,046
Time deposits	5,351,563	5,797,288	6,539,118
Other commitments (3)	40,816	44,561	50,265
<b>Total</b>	<b>8,101,122</b>	<b>8,075,521</b>	<b>9,012,717</b>

(1) In millions of constant Chilean pesos as of June 30, 2006.

(2) In millions of constant Chilean pesos as of December 31, 2005.

(3) Includes primarily leasing accounts payable relating to purchases of equipment.

**Maturity of Deposits**

The following table sets forth information regarding the currency and maturity of our deposits at June 30, 2006, expressed in percentages. UF-denominated deposits are similar to peso-denominated deposits in all respects, except that the principal is readjusted periodically based on variations in the Chilean consumer price index.

	<b>Ch\$</b>	<b>UF</b>	<b>Foreign Currency</b>	<b>Total</b>
Demand deposits	1.5%	-	-	0.8%
Savings accounts	-	4.7%	-	1.6%
Time deposits:				
Maturing within 3 months	62.9%	28.8%	92.9%	56.3%
Maturing after 3 but within 6 months	11.5%	5.8%	6.3%	8.8%
Maturing after 6 but within 12 months	11.4%	21.4%	0.7%	13.0%
Maturing after 12 months	12.7%	39.3%	0.1%	19.6%
Total time deposits	98.5%	95.3%	100.0%	97.7%
<b>Total deposits</b>	<b>100.0%</b>	<b>100.0%</b>	<b>100.0%</b>	<b>100.0%</b>

The following table sets forth information regarding the maturities of the outstanding time deposits in excess of U.S.\$100,000 issued by us at June 30, 2006.

	<b>Ch\$</b>	<b>UF</b>	<b>Foreign Currency</b>	<b>Total</b>
<b>(in millions of constant Ch\$ of June 30, 2006)</b>				
Time deposits:				
Maturing within 3 months	1,745,479	591,644	824,502	3,161,625
Maturing after 3 but within 6 months	383,790	119,069	63,651	566,510

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Maturing after 6 but within 12 months	401,832	509,036	6,227	917,095
Maturing after 12 months	384,139	794,585	321	1,179,045
	<u>2,915,240</u>	<u>2,014,334</u>	<u>894,701</u>	<u>5,824,275</u>
Total time deposits				



**Short-term Borrowings**

The principal categories of our short-term borrowings are amounts borrowed under foreign trade lines of credit, domestic interbank loans, Central Bank borrowings and repurchase agreements. The table below presents the amounts outstanding at each period end indicated and the weighted-average nominal interest rate thereon by type of short-term borrowing.

	At June 30,			
	2005		2006	
	Weighted Average Nominal Interest Rate		Weighted Average Nominal Interest Rate	
	Balance	Rate	Balance	Rate
(In millions of constant Ch\$ of June 30, 2006, except percentages)				
Investments under repurchase agreements	149,641	1.3%	280,039	1.2%
Central Bank borrowings	166,067	1.4%	25,525	11.6%
Domestic interbank loans	3,590	36.7%	4,216	11.2%
Borrowings under foreign trade credit lines	1,637,251	2.1%	977,506	1.3%
Total short-term borrowings	1,956,549		1,287,286	

The following table shows the average balance and the average nominal rate for each short-term borrowing category during the periods indicated:

	At June 30,			
	2005		2006	
	Average Nominal Interest Rate		Average Nominal Interest Rate	
	Balance	Rate	Balance	Rate
(In millions of constant Ch\$ of June 30, 2006)				
Investments under repurchase agreements	103,308	12.3%	177,646	12.3%
Central Bank borrowings	205,224	1.6%	95,724	2.6%
Domestic interbank loans	4,062	32.4%	3,589	13.2%
Borrowings under foreign trade credit lines	295,279	11.9%	19,819	65.1%

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Total short-term borrowings	<u>607,873</u>	<u>236,778</u>
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The following table presents the maximum month-end balances of our principal sources of short-term borrowings during the periods indicated:

	<b>Maximum 2005 Month-End Balance</b>	<b>Maximum 2006 Month-End Balance</b>
	<u>                    </u>	<u>                    </u>
Investments under agreements to repurchase	601,516	355,439
Central Bank borrowings	310,567	235,253
Domestic interbank loans	44,548	3,589
Borrowings under foreign trade credit lines	1,111,423	1,756,659
	<u>                    </u>	<u>                    </u>
Total short-term borrowings	<u>2,068,054</u>	<u>2,350,940</u>

**Total Borrowings**

Our long-term and short-term borrowings are summarized below. Borrowings are generally classified as short-term when they have original maturities of less than one year or are due on demand. All other borrowings are classified as long-term, including the amounts due within one year on such borrowings.

	<b>At June 30, 2006</b>		
	<b>Long-term</b>	<b>Short-term</b>	<b>Total</b>
	<b>(in millions of constant Ch\$ of June 30, 2006)</b>		
Central Bank borrowings	-	166,067	166,067
Credit lines for renegotiations of loans	-	5,752	5,752
Investments under agreements to repurchase	-	149,641	149,641
Mortgage finance bonds	492,976	99,861	592,837
Other borrowings: bonds	441,866	120,912	562,778
Subordinated bonds	388,699	2,285	390,984
Borrowings from domestic financial institutions	-	3,590	3,590
Foreign borrowings	328,845	1,308,406	1,637,251
Other obligations	9,011	44,327	53,338
<b>Total borrowings</b>	<b>1,661,397</b>	<b>1,900,841</b>	<b>3,562,238</b>

	<b>December 31, 2005</b>		
	<b>Long-term</b>	<b>Short-term</b>	<b>Total</b>
	<b>(in millions of constant Ch\$ as of Decemehr 31, 2005)</b>		
Central Bank borrowings	-	173,206	173,206
Credit lines for renegotiations of loans (a)	6,655	-	6,655
Investments under agreements to repurchase	-	49,779	49,779
Mortgage finance bonds (b)	551,772	117,189	668,961
Other borrowings: bonds (c)	413,525	1,718	415,243
Subordinated bonds (d)	385,751	-	385,751
Borrowings from domestic financial institutions	-	2,528	2,528
Foreign borrowings (e)	64,243	1,034,003	1,098,246
Other obligations (f)	11,751	30,341	42,092
<b>Total borrowings</b>	<b>1,433,697</b>	<b>1,408,764</b>	<b>2,842,461</b>

	<b>At June 30, 2005</b>		
	<b>Long-term</b>	<b>Short-term</b>	<b>Total</b>

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(in millions of constant Ch\$ of June 30,  
2006)

Central Bank borrowings	-	25,525	25,525
Credit lines for renegotiations of loans (a)	-	7,953	7,953
Investments under agreements to repurchase	-	280,039	280,039
Mortgage finance bonds (b)	736,137	155,637	891,774
Other borrowings: bonds (c)	344,556	-	344,556
Subordinated bonds (d)	564,300	202	564,502
Borrowings from domestic financial institutions	-	4,216	4,216
Foreign borrowings (e)	22,361	955,145	977,506
Other obligations (f)	9,356	33,108	42,464
		<u>          </u>	<u>          </u>
Total borrowings	1,676,710	1,461,825	3,138,535
		<u>          </u>	<u>          </u>

*a) Credit lines for renegotiations of loans*

Central Bank borrowings include credit lines for the renegotiations of loans and other Central Bank borrowings. These credit lines were provided by the Central Bank for the renegotiations of loans due to the need to refinance debts as a result of the economic recession and crisis of the banking system in the early 1980s. The credit lines for renegotiations are related to mortgage loans linked to the UF index and bear a real annual interest rate of 6.0% at June 30, 2005 and 2006.

*(b) Mortgage finance bonds*

These bonds are used to finance the granting of mortgage loans. The outstanding principal amounts of the bonds are amortized on a quarterly basis. The range of maturities of these bonds is between five and twenty years. The bonds are linked to the UF index and bear a real weighted-average annual interest rate of 3.6% .

	<b>At June 30, 2006</b>
	<b>(in millions of constant Ch\$ of June 30, 2006)</b>
Due within 1 year	99,861
Due after 1 year but within 2 years	58,066
Due after 2 years but within 3 years	54,278
Due after 3 years but within 4 years	51,435
Due after 4 years but within 5 years	48,682
Due after 5 years	280,515
	<b>592,837</b>
Total mortgage finance bonds	<b>592,837</b>

*(c) Bonds*

	<b>At June 30, 2005(1)</b>	<b>At December 31, 2005(2)</b>	<b>At June 30, 2006(1)</b>
Santiago bonds, series A, B, C, D and F	12,398	11,115	10,001
Santander bonds denominated in UF	93,040	161,694	334,058
Santander bonds denominated in US\$	239,118	242,434	218,719
	<b>344,556</b>	<b>415,243</b>	<b>562,778</b>
Total	<b>344,556</b>	<b>415,243</b>	<b>562,778</b>

(1) In millions of constant Chilean pesos as of June 30, 2006.

(2) In millions of constant Chilean pesos as of December 31, 2006.

Santiago bonds include series A, B, C and F issued by the former Santiago S.A. and series B and D issued by the former Banco O'Higgins, prior to its merger with the Bank in 1997. These bonds are intended to finance loans that have a maturity of greater than one year, are linked to the UF index and bear a weighted average annual interest rate of 7.0% with interest and principal payments due semi-annually.

On December 17, 2004, Santiago Leasing S.A.. assigned through public deed a total of UF3,041,102 (Ch\$52,663 million at December 31, 2004) in bonds to Banco Santander Chile. These bonds are linked to the UF index and bear an annual interest rate of 5.6% . At June 30, 2005 and 2006, the balance is included in Santander bonds linked to the UF.

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On October 5, 2005, the Bank issued bonds denominated in UF for a total of UF8 million and bear an average annual interest rate of 3.0% .

On May 25, 2006, the Bank issued bonds denominated in UF for a total of UF6 million and bear an average annual interest rate of 4.6% .

Our bonds linked to the UF also includes bonds issued by the former Banco Santander-Chile. These bonds are intended to finance loans that have a maturity of greater than one year, are linked to the UF index and bear a weighted average annual interest rate of 6.5% .

On December 9, 2004, the Bank issued senior bonds, denominated in U.S. dollars, for a total of US\$400 million. These bonds carry a nominal interest rate of LIBOR plus 0.35% per annum (5.28% and 3.37% at June 30, 2005 and 2006, respectively), interest payable quarterly and principal payable with a 5 year maturity.

The remaining maturities of these bonds at June 30, 2006 are as follows:

	<b>At June 30,</b>
	<b>2006</b>
	<b>(in millions of constant Ch\$ of June 30, 2006)</b>
Due within 1 Year	120,912
Due after 1 year but within 2 years	81
Due after 2 years but within 3 years	-
Due after 3 years but within 4 years	347,498
Due after 4 years but within 5 years	17,903
Due after 5 years	76,384
<b>Total bonds</b>	<b>562,778</b>

*d) Subordinated bonds*

	<b>At June 30, 2005(1)</b>	<b>At December 31, 2005(2)</b>	<b>At June 30, 2006(1)</b>
Santiago bonds denominated in US\$ (3)	48,018	43,131	43,443
Santander bonds denominated in US\$ (4) (8)	252,672	259,872	267,513
Old Santander bonds denominated in US\$ (5)	176,952	-	--
Santiago Bonds linked to the UF (6)	53,312	53,354	31,802
Santander Bonds linked to the UF (7)	33,548	29,394	48,225
<b>Total subordinated bonds</b>	<b>564,502</b>	<b>385,751</b>	<b>390,984</b>

(1) In millions of constant Chilean pesos as of June 30, 2006.

(2) In millions of constant Chilean pesos as of December 31, 2005.

(3) On July 17, 1997, the former Banco Santiago issued subordinated bonds, denominated in U.S. dollars, for a total of US\$300 million. The bonds carry a nominal interest rate of 7.0% per annum, with semi-annual interest payments and one repayment of principal after a term of 10 years.

(4) On January 16, 2003, the Bank completed a voluntary exchange for new subordinated bonds, which will mature in 2012. A total of US\$ 221,961,000 in principal of the Santiago bonds were offered and redeemed by the Bank. The bonds carry a nominal interest rate of 7.375% per annum, with semi-annual interest payments and one repayment of principal at maturity after a term of 10 years.

(5) On October 30, 1998, the former Banco Santander-Chile issued subordinated bonds, denominated in U.S. dollars, for a total of US\$200 million. The bonds carry a nominal interest rate of 6.5% per annum, with semi-annual interest payments and one repayment of principal at maturity after a term of 7 years. These bonds matured and were paid off in November 2005.

(6) The Series C and E Bonds outstanding at June 30, 2005 and 2006 are intended for the financing of loans with a maturity of greater than one year. They are linked to the UF index and carry an annual interest rate of 7.5% and 6.0%, respectively, with interest and principal payments due semi-annually.

(7)

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The Series C, D and E Bonds outstanding at June 30, 2005 and 2006 are intended for the financing of loans with a maturity of greater than one year. They are linked to the UF index and carry an annual interest rate of 7.0% with interest and principal payments due semi-annually.

- (8) On December 9, 2004, the Bank issued subordinated bonds, denominated in U.S. dollars, for a total of US\$ 300 million. These bonds carry a nominal interest rate of 5.375% per annum, semi-annual interest payments and one repayment of principal after a term of 10 years.



The remaining maturities of these bonds which are considered long-term at June 30, 2006, are as follows:

	<b>At June 30,</b>
	<b>2006</b>
	<b>(in millions of constant Ch\$ of June 2006)</b>
Due within 1 Year	2,285
Due after 1 year but within 2 years	43,444
Due after 2 years but within 3 years	-
Due after 3 years but within 4 years	17,690
Due after 4 years but within 5 years	-
Due after 5 years	327,565
	<hr/>
Total subordinated bonds	390,984
	<hr/>

*e) Foreign borrowings*

These are short-term and long-term borrowings from foreign banks. The remaining maturities of these borrowings at June 30, 2006 are as follows:

	<b>At June 30,</b>
	<b>2006</b>
	<b>(in millions of constant Ch\$ of June 30, 2006)</b>
Due within 1 Year	1,308,406
Due after 1 year but within 2 years	320,039
Due after 2 years but within 3 years	5,826
Due after 3 years but within 4 years	-
Due after 4 years but within 5 years	2,980
Due after 5 years	-
	<hr/>
Total foreign borrowings	1,637,251
	<hr/>

Our foreign borrowings are denominated principally in U.S. dollars, and are principally used to fund the Bank's foreign trade loans and bear an annual average interest rate of 2.5% and 2.7% at June 30, 2005 and 2006. Our foreign borrowings increased at June 30, 2006 compared to June 30, 2005, primarily because foreign trade loans were increasingly funded by foreign borrowings as a result of the increased cost for currency forward transactions between Chilean pesos and foreign currencies.

*f) Other obligations*

Other obligations are summarized as follows:

	<b>At June 30,</b>
	<b>2006</b>
	<b>(in millions of constant</b>
	<b>Ch\$ of June 30,</b>
	<b>2006)</b>
Due within 1 Year	9,649
Due after 1 year but within 2 years	2,051
Due after 2 years but within 3 years	1,610
Due after 3 years but within 4 years	1,701
Due after 4 years but within 5 years	1,203
Due after 5 years	2,446
	<hr/>
Total long term obligations	18,660
	<hr/>
Short-term obligations:	
Amounts due to credit card operators	19,102
Acceptance of letters of credit	15,576
	<hr/>
<b>Total short term obligations</b>	<b>34,678</b>
	<hr/>
<b>Total other obligations</b>	<b>53,338</b>
	<hr/>

***Other Off-Balance Sheet Arrangements and Commitments***

We are party to transactions with off-balance-sheet risk in the normal course of our business. These transactions expose us to credit risk in addition to amounts recognized in the consolidated financial statements.

These transactions include commitments to extend credit not otherwise accounted for as contingent loans, such as overdraft protection and credit card lines of credit. Such commitments are agreements to lend to a customer at a future date, subject to the customer compliance with the contractual terms. The aggregate amount of these commitments was Ch\$2,780,898 million at June 30, 2006, which will be financed with our deposit base. Since a substantial portion of these commitments is expected to expire without being drawn upon, the total amount of commitments does not necessarily represent our actual future cash requirements. We use the same credit policies in making commitments to extend credit as we do for granting loans. In the opinion of our management, our outstanding commitments do not represent an unusual credit risk.

From time to time, the Bank enters into agreements to securitize certain assets by selling those assets to unconsolidated and unaffiliated entities, which then sell debt securities secured by those assets. These sales are non-recourse to the Bank. However, in the past, the Bank has occasionally purchased a subordinated bond issued by the unconsolidated entity. At June 30, 2006, we did not hold any of these subordinated bonds in our investment portfolio.

The Bank and its brokerage subsidiary enter into derivative transactions as part of their asset and liability management and in acting as dealers to satisfy their clients' needs. The notional amounts of these contracts are carried off-balance-sheet. *See Note 12 to the Unaudited Consolidated Financial Statements.*

Foreign exchange forward contracts involve an agreement to exchange the currency of one country for the currency of another country at an agreed-upon price and settlement date. These contracts are generally standardized contracts, normally for periods between 1 and 180 days and are not traded in a secondary market; however, in the normal course of business and with the agreement of the original counterparty, they may be terminated or assigned.

When we enter into a forward exchange contract, we analyze the credit risk (the risk that the counterparty might default on its obligations) before approving such transactions. Subsequently, on an ongoing basis, we monitor the possible losses involved in each contract. To manage the level of credit risk, we deal with counterparties of good credit standing, enter into master netting agreements whenever possible and, when appropriate, obtain collateral.

The Central Bank requires that foreign exchange forward contracts be made only in U.S. dollars and other major foreign currencies. Most of our forward contracts are made in U.S. dollars against the Chilean peso or the UF. Occasionally, forward contracts are also made in other currencies, but only when the Bank acts as an intermediary.

Unrealized gains, losses, premiums and discounts arising from foreign exchange forward contracts are shown on a net basis under other assets and other liabilities (see *Note 10 to our Unaudited Interim Consolidated Financial Statements*).

We enter into interest rate and cross currency swap agreements to manage exposure to fluctuation in currencies and interest rates. At June 30, 2006, these swaps are marked-to-market. For the six-month period ended June 30, 2006, the difference between the interest paid or received on a specified notional amount (interest as the instrument or the associated "hedge") is recognized under "foreign exchange transactions, net". The fair value of the swap agreement and changes in the fair value as a result of changes in market interest rates are not recognized in the consolidated financial statement at and for the six-month period ended June 30, 2005, therefore the figures at June 30, 2005 in the table presented below are not entirely comparable to the corresponding figures at June 30, 2006.

In 2005, banks were authorized to operate in the currency and interest rate options market. The notional amounts of these options are carried off-balance-sheet. These contracts are valued at fair value and the changes in fair value are recognized in the consolidated financial statements.

Our foreign currency futures, forward operations, options and other derivative products outstanding at June 30, 2005 and 2006 are summarized below:

**(a) Foreign currency and interest rate contracts:**

	Number of contracts		Notional amounts						
			Up to 3 months			Over 3 months			
	At June 30, 2005	At December 31, 2005	At June 30, 2006	At June 30, 2005	At December 31, 2005	At June 30, 2006(1)	At June 30, 2005	At December 31, 2005	At June 30, 2006(1)
(in thousands of US dollars)									
Chilean market:									
Future purchase of foreign currency with Chilean pesos	1,244	956	1,233	3,892,790	5,198,228	5,556,019	5,119,346	3,418,092	3,270,192
Future sale of foreign currency with Chilean pesos	1,242	2,146	1,851	2,566,289	3,077,468	3,206,981	2,395,935	3,490,314	5,986,992
Futures or other interest rate contracts	24	340	52	232,255	6,119,545	134,317	92,526	1,273,247	13,148

Foreign currency forwards	246	253	301	2,334,689	289,972	2,115,448	1,947,300	226,011	2,021,299
Foreign markets: Foreign currency swaps	293	129	872	2,469,693	573,982	9,823,948	2,387,849	199,397	7,362,383
Interest rate swaps	45	107	20	402,023	1,305,457	762,838	745,938	2,558,182	3,000

(1) The figures for June 30, 2006 are not presented at fair value in order to make them comparable to prior periods. The figures presented in our balance sheet are presented at fair value.

The notional amounts refer to the U.S. dollars bought or sold or to the U.S. dollar equivalent of foreign currencies bought or sold for future settlement. The contract terms correspond to the duration of the contracts as from the date of the transaction to the date of the settlement.

**(b) Contracts expressed in the UF index:**

	Number of contracts		Notional amounts						
			Up to 3 months			Over 3 months			
	At June 30, 2005	At December 31, 2005	At June 30, 2006	At June 30, 2005	At December 31, 2005	At June 30, 2006(1)	At June 30, 2005	At December 31, 2005	At June 30, 2006(1)
				UF	UF	UF	UF	UF	UF
Forwards in UF/Ch\$ sold	36	19	5	3,100,000	2,100,000	900,000	5,800,000	3,300,000	430,887
Forwards in UF/Ch\$ purchased	59	36	14	5,700,000	3,600,000	2,900,000	8,300,000	5,400,000	2,100,000

**(c) Options:**

			At June 30, 2006			
			30 days	31 to 60 days	61 to 90 days	> 90 days
(in thousands of U.S. dollars)						
Call	Bought	Currency	-	19,343	-	4,303
		Interest rate	-	-	-	-
	Sold	Currency	-	-	100	4,303
		Interest rate	-	-	-	183
Put	Bought	Currency	-	-	100	20,000
		Interest rate	-	-	-	-
	Sold	Currency	-	19,343	-	10,000
		Interest rate	-	-	-	-

**E. Asset and Liability Management**

Please refer to *Item 8: Asset and Liability Management* regarding our policies with respect to asset and liability management.

**Capital Expenditures**

The following table reflects capital expenditures for the six-month periods ended June 30, 2005 and 2006:

		For the six-months June 30,	
		2005	2006
(in millions of constant Ch\$ at June 30, 2006)			
	Land and Buildings	1,113	1,873
	Machinery and Equipment	6,037	2,520
	Furniture and Fixtures	1,767	769
	Vehicles	310	182
	Other	928	537
	Total	10,155	5,881

## Selected Statistical Information

The following information is included for analytical purposes and should be read in conjunction with our financial statements as well as the discussion in *Item 3: Operating and Financial Review and Prospects*. Pursuant to Chilean GAAP, the financial data in the following tables at all dates prior to and for all periods through as of June 30, 2005 have been restated in constant Chilean pesos at June 30, 2006. The UF is linked to, and is adjusted daily to, reflect changes in the previous month's Chilean consumer price index. See *Note 1(c) to our financial statements*.

### Average Balance Sheets, Income Earned from Interest-Earning Assets and Interest Paid on Interest-Bearing Liabilities

The average balances for interest-earning assets and interest-bearing liabilities, including interest and readjustments received and paid, have been calculated on the basis of daily balances for us on an unconsolidated basis. Such average balances are presented in Chilean pesos, in UF and in foreign currencies (principally U.S.\$). Figures from our subsidiaries have been calculated on the basis of monthly balances. The average balances of our subsidiaries, except Santander S.A. Agente de Valores have not been categorized by currency. Therefore, it is not possible to calculate average balances by currency for such subsidiaries on the basis of daily, weekly or monthly balances.

The nominal interest rate has been calculated by dividing the amount of interest and principal readjustment due to changes in the UF index (gain or loss) during the period by the related average balance, both amounts expressed in constant pesos. For presentation purposes, the nominal rates obtained from this formula are also presented on an annualized basis which was calculated by multiplying the six-month average nominal rate by 2. The real rates calculated for each period have been converted into real rates using the following formulas:

Where:

Rp= real average rate for peso-denominated assets and liabilities (in Ch\$ and UF) for the period;

Rd= real average rate for foreign currency-denominated assets and liabilities for the period;

Np= nominal average rate for peso-denominated assets and liabilities for the period;

Nd= nominal average rate for foreign currency-denominated assets and liabilities for the period;

D= devaluation rate of the Chilean peso to the U.S. dollar for the period; and

I= inflation rate in Chile for the period (based on the variation of the Chilean Consumer Price Index).

The real interest rate can be negative for a portfolio of peso-denominated loans when the inflation rate for the period is higher than the average nominal rate of the loan portfolio for the same period. A similar effect could occur for a portfolio of foreign currency denominated loans when the inflation rate for the period is higher than the sum of the devaluation rate for the period and the corresponding average nominal rate of the portfolio.

The formula for the average real rate for foreign currency denominated assets and liabilities (Rd) reflects a gain or loss in purchasing power caused by the difference between the devaluation rate of the Chilean peso and the inflation rate in Chile during the period.

The following example illustrates the calculation of the real interest rate for a dollar-denominated asset bearing a nominal annual interest rate of 10.0% (Nd = 0.10), assuming a 5.0% annual devaluation rate (D = 0.05) and a 12.0% annual inflation rate (I = 0.12):

In the example, since the inflation rate was higher than the devaluation rate, the real rate is lower than the nominal rate in dollars. If, for example, the annual devaluation rate were 15.0%, using the same numbers, the real rate in Chilean pesos would be 12.9%, which is higher than the nominal rate in U.S. dollars. Using the same numbers, if the annual inflation rate were greater than 15.5%, the real rate would be negative.

Contingent loans (consisting of guarantees and open and unused letters of credit) have been treated as interest-earning assets. Although the nature of the income derived from such assets is similar to a fee, Chilean banking regulations require that



such income be accounted for as interest revenue. As a result of this treatment, the comparatively low rates of interest earned on these assets have a distorting effect on the average interest rate earned on total interest-earning assets.

The real rate for contingent loans has been stated as the nominal rate, since we do not have an effective funding obligation for these loans. The foreign exchange gains or losses on foreign currency-denominated assets and liabilities have not been included in interest revenue or expense. Similarly, interest on financial investments does not include trading gains or losses on these investments. Interest is not recognized during periods in which loans are past due. However, interest received on past due loans includes interest on such loans from the original maturity date.

Non-performing loans that are overdue for 90 days or less have been included in each of the various categories of loans, and therefore affect the various averages. Non-performing loans consist of loans as to which either principal or interest is overdue (i.e., non-accrual loans) and restructured loans earning no interest. Non-performing loans that are overdue for 90 days or more are shown as a separate category of loans (past due loans). Interest and/or indexation readjustments received on all non-performing dollar-denominated loans during the periods are included as interest revenue. However, all peso-denominated loans that are classified as non-performing do not accrue interest or indexation adjustments as interest revenue.

Included in interbank deposits are checking accounts maintained in the Central Bank and foreign banks. Such assets have a distorting effect on the average interest rate earned on total interest-earning assets because currently balances maintained in Chilean peso amounts do not earn interest, and the only balances held in a foreign currency that earn interest are those maintained in U.S. dollars, but those only earn interest on the amounts that are legally required to be held for liquidity purposes. Additionally, this account includes interest earned by overnight investments. Consequently, the average interest earned on such assets is comparatively low. We maintain these deposits in these accounts to comply with statutory reserves requirements and to facilitate international business, rather than to earn income.

The monetary gain or loss on interest-earning assets and interest-bearing liabilities is not included as a component of interest revenue or interest expense because inflation effects are taken into account in the calculation of real interest rates.

The following tables show, by currency of denomination, average balances and, where applicable, interest amounts and real rates for our assets and liabilities for the six-month period ended June 30, 2005 and 2006:

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	<u>Average Balance(1)</u>	<u>Interest Earned</u>	<u>Real Rate</u>	<u>Nominal Rate</u>	<u>Nominal Rate Annualized(2)</u>	<u>Average Balance(1)</u>	<u>Interest Earned</u>
<b>ASSETS</b>							
<b>Interest-earning assets</b>	<b>For the six-months ended June 30, 2005</b>						
Interbank deposits							
Ch\$	41,886	729	0.6%	1.7%	3.5%	34,964	906
UF	10,483	275	1.5%	2.6%	5.2%	10,405	289
Foreign currencies	493,634	6,270	-4.9%	1.3%	2.5%	848,444	19,627
<b>Subtotal</b>	<b>546,003</b>	<b>7,274</b>	<b>-4.3%</b>	<b>1.3%</b>	<b>2.7%</b>	<b>893,813</b>	<b>20,822</b>
Financial investments							
Ch\$	592,934	12,915	1.0%	2.2%	4.4%	499,814	19,572
UF	382,806	21,020	4.3%	5.5%	11.0%	581,168	23,860
Foreign currencies	898,202	20,102	-3.9%	2.2%	4.5%	545,292	10,514
<b>Subtotal</b>	<b>1,873,942</b>	<b>54,037</b>	<b>-0.7%</b>	<b>2.9%</b>	<b>5.8%</b>	<b>1,626,274</b>	<b>53,946</b>
Commercial loans							
Ch\$	1,792,492	91,057	3.9%	5.1%	10.2%	2,142,587	126,525
UF	3,129,377	105,326	2.2%	3.4%	6.7%	3,930,993	136,268
Foreign currencies	123,684	2,400	-4.2%	1.9%	3.9%	81,510	2,199
<b>Subtotal</b>	<b>5,045,553</b>	<b>198,783</b>	<b>2.7%</b>	<b>3.9%</b>	<b>7.9%</b>	<b>6,155,090</b>	<b>264,992</b>
Consumer loans							
Ch\$	988,406	101,914	9.1%	10.3%	20.6%	1,247,300	136,439
UF	7,077	393	4.4%	5.6%	11.1%	15,898	865
Foreign currencies	5,442	0	-6.1%	0.0%	0.0%	5,525	0
<b>Subtotal</b>	<b>1,000,925</b>	<b>102,307</b>	<b>9.0%</b>	<b>10.2%</b>	<b>20.4%</b>	<b>1,268,723</b>	<b>137,304</b>
Mortgage loans							
Ch\$	544	17	2.0%	3.1%	6.3%	494	18
UF	837,898	40,247	3.6%	4.8%	9.6%	581,675	25,366
Foreign currencies	0	0	0.0%	0.0%	0.0%	0	0
<b>Subtotal</b>	<b>838,442</b>	<b>40,264</b>	<b>3.6%</b>	<b>4.8%</b>	<b>9.6%</b>	<b>582,169</b>	<b>25,384</b>
Foreign trade loans							