Monetary Policy Meeting[1]

DECEMBER 2020

CENTRAL BANK OF CHILE

[1] This is a translation of a document written in Spanish. In case of discrepancy or difference in interpretation, the Spanish original prevails. Both versions are available at www.bcentral.cl

MINUTES OF THE MONETARY POLICY MEETING

Monetary policy meeting No. 278, held on 7 December 2020.

Present: Mario Marcel, Governor; Joaquín Vial, Vice-Governor; Pablo García, Board member; Alberto Naudon, Board member; Rosanna Costa, Board member.

Also present: Alejandro Zurbuchen, General Manager; Juan Pablo Araya, General Counsel and Attestor Elías Albagli, Monetary Policy Division Director; Beltrán de Ramón, Financial Markets Division Director; Solange Berstein, Financial Policy Division Director; Gloria Peña, Statistics Division Director; Michel Moure, Institutional Affairs Division Director; Markus Kirchner, Macroeconomic Analysis Manager; Enrique Orellana, Monetary Policy Strategy and Communications Manager; Miguel Fuentes, International Analysis Manager; Felipe Lozano, Communications Manager; Andrés Pérez, Advisor to the Finance Minister; Marlys Pabst, Secretary General.

1. Background

The local and international economic scenario continued to be determined by the evolution of the people' mobility and its relation to the pandemic. In Chile, although infections had declined and mobility had increased since mid-year, improvements in activity had been slower than expected in September. This had been especially true for the sectors most affected by social distancing, such as construction and a good proportion of services. The withdrawal of pension savings had resulted in temporary increases in consumption, especially of imported goods, which had had a positive impact on sectors such as trade but had also put pressure on the prices of the products most demanded. Investment, beyond the reactivation of public and private projects, was being affected by the financial situation of companies and the persistent uncertainty. The labor market had shown some recovery, with a rise in employment compared to mid-year.

The balance of these elements meant a downward revision of the forecasts contained in the December MP Report for this year's growth. The central scenario foresaw that the economy would keep improving, that mobility restrictions would not return to mid-2020 levels, and that the fiscal and monetary impulse would continue. Even so, dismay caused by the sharp drop in activity, plus the necessary use of public and private strenghts to overcome the emergency, heightened vulnerability to risk scenarios and posed significant challenges to recovering near-trend growth rates.

2. Background analysis and discussion

Regarding the external scenario, it was noted that, positive news exceeded the negative. Along with the news about a vaccine becoming available, there was good news about GDP in several countries during the third quarter —notably China—, the copper price hike and the elimination of some risks, such as those associated with the U.S. elections. Naturally there were also negative elements, mainly the increase of infections in several European countries and in the United States and the fact that the scars caused by this the crisis had become more evident. Both facts suggested that there was the risk of a slower recovery going forward, even with a readily available vaccine.

Locally, there was consensus that news was not as encouraging. Incoming data on activity had surprised on the downside, with both regular consumption and investment being weaker than expected. In addition, the data was difficult to interpret, particularly because of doubts about how much of it was due to the measures taken in association with the pandemic; how much was a reflection of something more persistent resulting from the scars of the crisis; and how much was simply statistical noise with no macroeconomic content. It was noted that something similar happened with inflation, which had been particularly volatile in recent months, making it difficult to read. Most importantly, however, the evolution of inflation was leaving behind the risk of persistently low inflation that could affect the evolution of inflation expectations.

It was also noted that another important factor in the macroeconomic scenario would be the evolution of uncertainty and its potential impact on investment. This was compounded with sanitary issues—e.g. possible new outbreaks or progress in vaccination—, the fear of new violence episodes as manifested in some surveys, together with financial difficulties in some companies. Their behavior would be decisive for investment to be reactivated beyond large-scale public and private projects. In any case, there were also favorable aspects, such as the performance of the stock market, the evolution of business expectations and the higher price of copper.

Beyond the immediate evolution of the macro scenario, it was remarked that the ugliest side of the Covid-19 crisis was dissipating, and a worst-case scenario had been averted. Since June, half of the sharp fall of the previous three months had been recovered and by 2021 a growth range between 5.5% and 6.5% was projected. These projections were largely based on a reduction in infections, the gradual phasing out of sanitary restrictions, the impulse of monetary and fiscal policy, and the capacity of many companies to adapt. Furthermore, private consumption was being boosted by two withdrawals of pension savings. Although the announcement of the Metropolitan Region's retreat to step 2 of the deconfinement plan could reduce somewhat the momentum at the margin, to the extent that it could help articulate a more orderly transition to the application of a vaccine, it would avoid having to resort to more drastic measures. There were also newly incorporated exemptions for construction and some services activities.

3. Analysis of monetary policy options

All the Board members agreed that, given the macroeconomic context caused by the pandemic, there was no other options than reinforcing the message that monetary policy would maintain a strong monetary impulse for an extended period of time, in order to ensure the consolidation of the economic recovery and achievement of the Bank's objectives. Accordingly, it was foreseen that the MPR would remain at its minimum level over a large part of the two-year monetary policy horizon, and the unconventional measures would remain in application.

The Board agreed on the necessity to assess the situation of commercial credit, in particular the limited use of Phase 2 of the FCIC facility by the financial system. In this respect, various doubts arose as to what it meant that it was not being used with the expected intensity and what the implications for the current monetary impulse were. They all agreed that it was imperative to address these questions in order to possibly make adjustments to these measures. Especially important was to determine whether more structural phenomena were occurring—as a result, for example, of the scars being left by the crisis—that could affect economic recovery in a more sustained way. They thought it also necessary to examine the coherence of a possible extension and redesign of the FCIC with other existing regulatory, credit and guarantee policies that could be operating.

4. Monetary policy decision

Governor Marcel, Vice-Governor Vial and Board members García, Naudon, and Costa voted for keeping the monetary policy rate at 0.5%. They also agreed to keep in place the unconventional measures to support liquidity and credit. In particular, they decided to maintain the total stock of bank bonds acquired under different programs—in the order of US$8 billion—for at least the next six months, reinvesting the coupons as they matured. This included the purchases under the CC-VP program. Regarding the FCIC, the Board decided not to introduce any changes to the total of resources available and conditions for utilization. Nonetheless, it agreed to assess a possible extension and changes in access parameters that would facilitate its use to respond to the needs of the economy at the present stage