PRESS RELEASE*

Friday, 7 June 2019

Monetary Policy Meeting

At its Monetary Policy Meeting, the Board of the Central Bank of Chile decided to reduce the monetary policy interest rate by 50 basis points, to 2.5%. The decision was adopted by the unanimous vote of the Board members.

Regarding the evolution of the external macroeconomic scenario, the main developments of the last month have revolved around the trade conflict, which has permeated other areas of the US-China relationship, plus other US trading partners. Fears that this may lead to a deterioration of the world economy have affected asset valuation, with falls in stock markets and long-term interest rates. Besides, the dollar has appreciated globally and commodity prices have dropped, copper included. In recent days, global financial markets have shown some improvement, hand in hand with signals coming from the central banks of developed countries about their will to boost the monetary impulse. Partial second-quarter inflation and activity data have been below market expectations. It is worth noting the situation of the labor market, manufacturing production and prospects. This coincides with a significant slowdown in global trade, that even posted annual contractions in some months.

With respect to local financial markets, external developments have been transmitted through the exchange rate, stock prices and the fixed-income market. Local risk indicators have also shown some increase, but remain contained. Market prices have factored in a lower MPR. Meanwhile, lending rates have declined recently, and a number of them are at their all-time lows.

The publication of first-quarter National Accounts confirmed lower-than-forecast activity growth, because of a poor performance of some more volatile lines related to natural resources, and mining. As for demand, the deceleration of machinery and equipment investment and exports stood out, both falling short of expectations, coinciding with the worsened external scenario during recent quarters and inventory build-up that failed to reverse as expected. Consumption brought no surprises, with a strengthened habitual component. April's Imacec revealed an improvement of the mining sector and non-mining growth that remained above 2% annually.

Annual CPI inflation —measured using the 2018=100 benchmark base— rose to 2.3% in May (2% in April). As expected, the month's inflation rate (0.6%) was largely the result of the increase in electricity rates. The CPIEFE stayed near 2% annually. Private inflation expectations available at the time of the Meeting show no big change. For the end of this year and one year ahead they stand somewhat below 3% annually, and remain in the neighborhood two years ahead.

On this occasion, the Board also considered the updating of the structural parameters that are used to evaluate the state of the economy, its outlook, and the calibration of monetary policy, the details of which will be included in the June Monetary Policy Report to be released next Monday at 8:30 hours. Most importantly, this allowed to quantify the effects of the massive immigration of recent years on trend and potential growth. The Board estimates the former in the 3.25% to 3.75% for the period 2019-2028, and the latter, around 3.4% for 2019-2021. In both cases this means an increase of 25 basis points with respect to earlier estimates. This, combined with the lower growth of the first quarter, results in a widening of the activity gap. Meanwhile, the neutral MPR has been revised downward by 25 basis points, partly reflecting the drop in neutral rates around the world.

Forecasts included in the Report suggest that in 2019 GDP growth will be between 2.75% and 3.5%, and between 3% and 4% in 2020 and 2021, in line with a recovery of growth in the second half of this year and increased potential growth. These projections consider the monetary policy decision of this Meeting.

The Board estimates that, in light of the updating of the structural parameters, the economy has not recovered enough to close the activity gap and boost inflation. Accordingly, the Board has deemed necessary to recalibrate the monetary impulse. The Board estimates that, if the baseline scenario materializes, this change in the MPR will suffice to ensure the convergence of inflation to the target in the policy horizon. Going forward, the onset of the MPR normalization process will depend on inflation clearly advancing to 3%. For this evaluation it will be particularly important the way the labor market will absorb the strong migratory inflow, the response of investment and the external developments. With this, the Board reiterates its will to conduct monetary policy with flexibility, so that projected inflation stands at 3% over the two-year horizon.

The minutes of this Monetary Policy Meeting will be published at 8:30 hours of Monday 24 June 2019. The next monetary Policy Meeting is scheduled to take place on 17–18 July 2019 and the statement thereof will be released at 18:00 hours this latter day.

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* The Spanish original prevails.