



Monetary Policy in Chile

2nd BBVA Latin American local Markets Conference

Sebastián Claro
Deputy Governor
Central Bank of Chile
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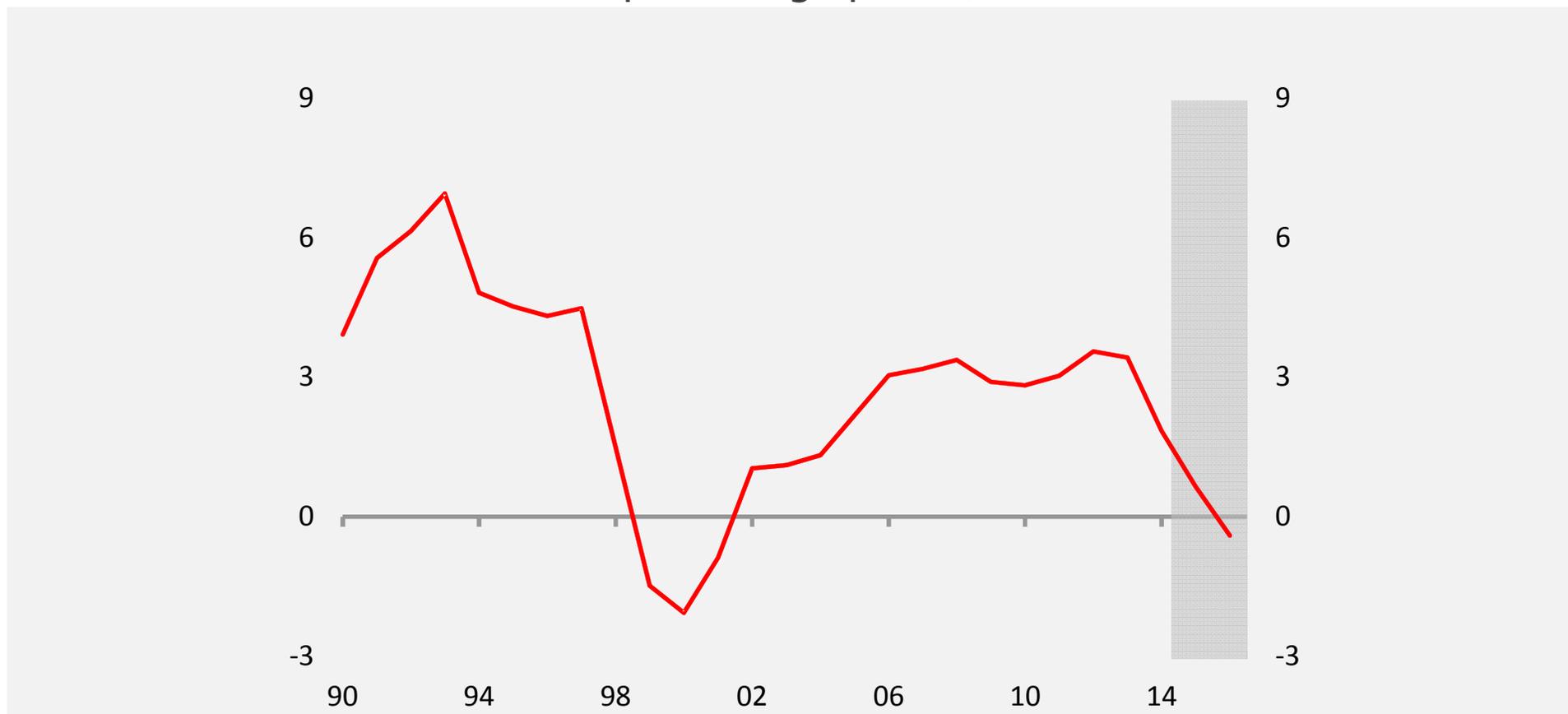


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1. Growth and inflation dynamics in Chile
 2. Monetary Policy perspectives
 3. Following the Fed?
 4. Some highlights from the Financial Stability Report



Chile has had two significant growth cycles since the mid 1980s.

Chile: Growth differential vs. USA (1) (2)
(percentage points)



(1) 3-year moving averages.

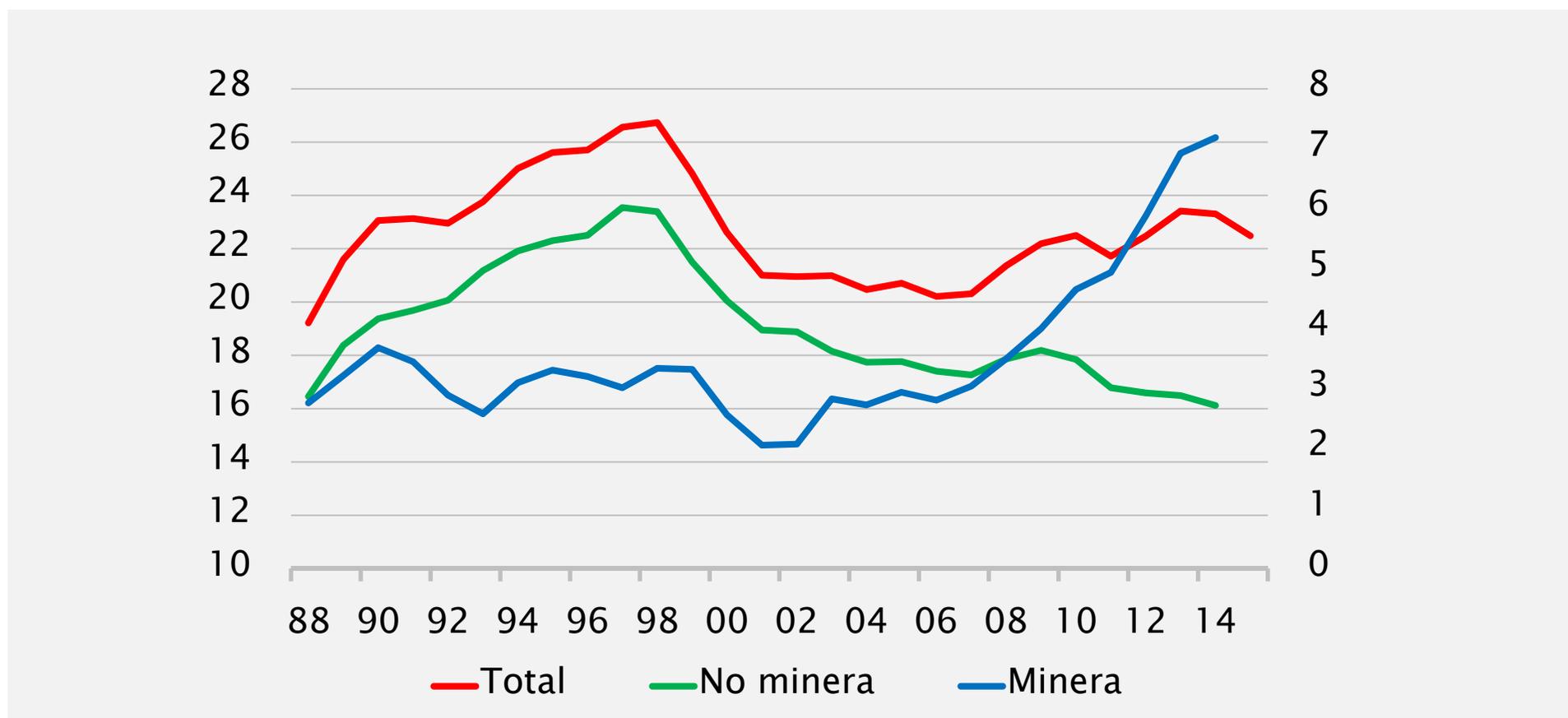
(2) Projections for 2015–2016.

Source. Central Bank of Chile and WEO, IMF.



The evolution of mining and non-mining investment reveals the nature of these cycles.

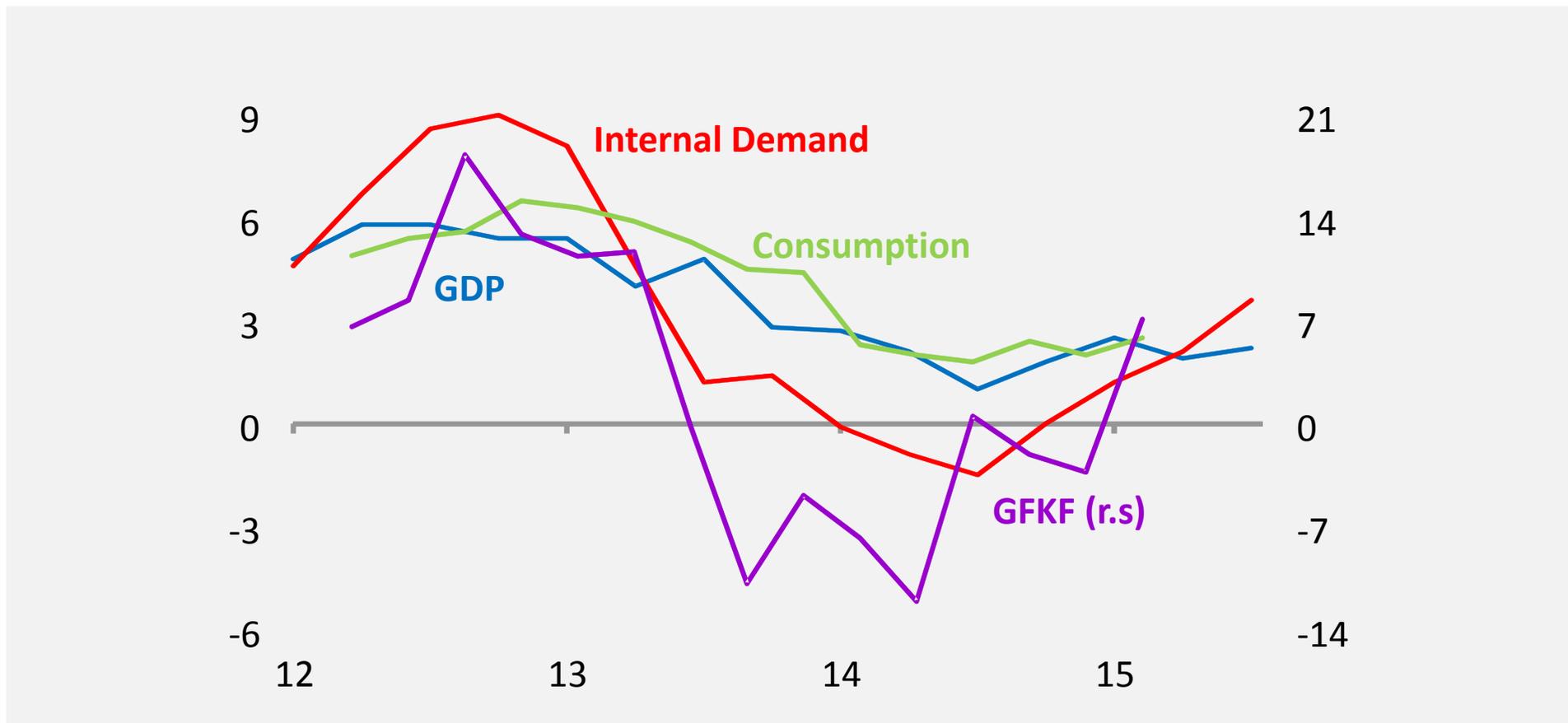
Investment Rate (1986–2015e)
(percentage of GDP)





The growth rate has decreased in the last couple of years to levels around 2%, and the outlook points towards weak growth in the near future.

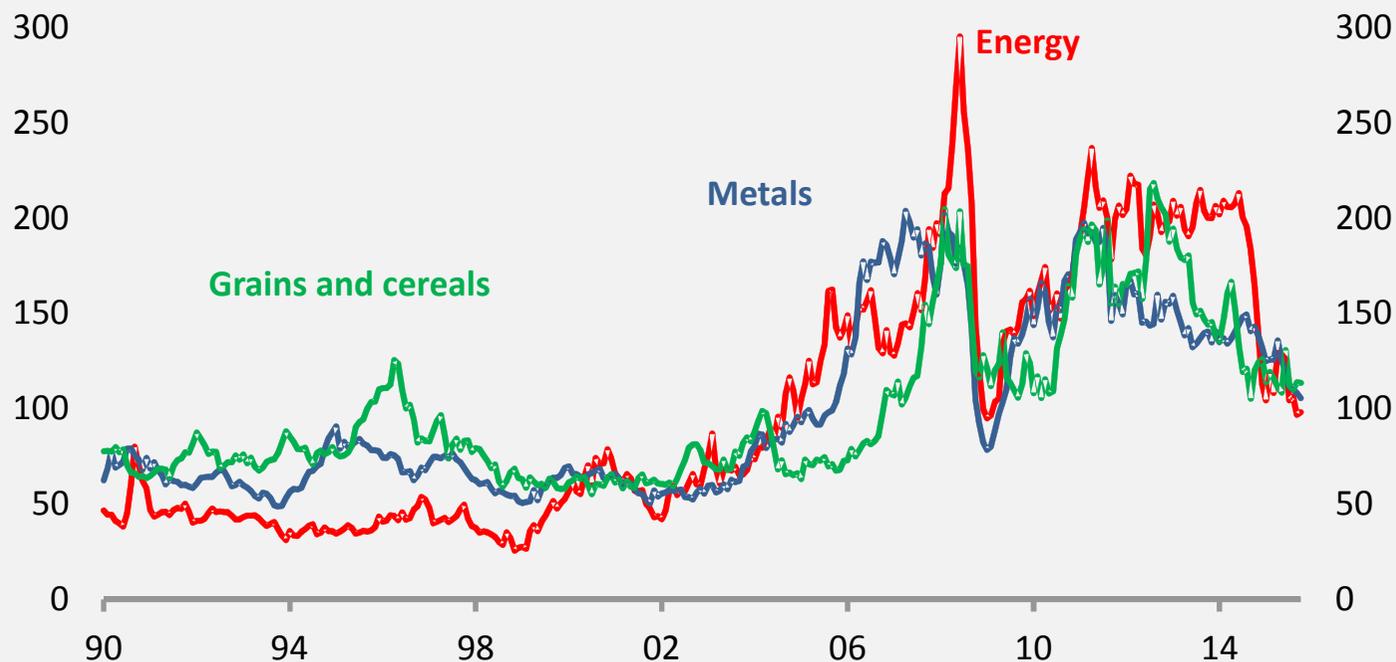
Quarterly GDP and Internal demand growth
(annual rate)





There are many reasons for this slowdown. Commodities is one. Global liquidity and risk appetite is another.

Commodity prices by group (1)
(fixed-base index: 1990-2015=100)



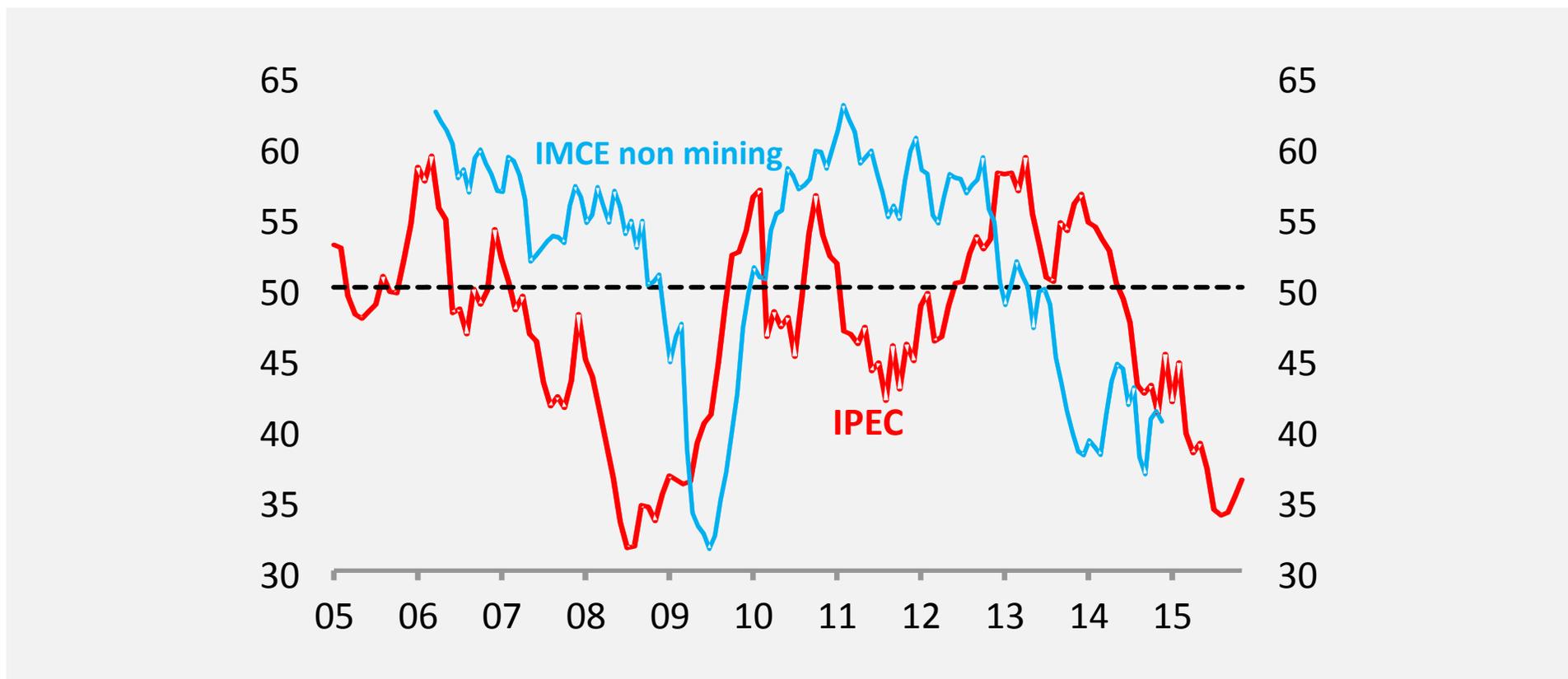
(1) Goldman Sachs Index.
Source: Bloomberg.





Also, idiosyncratic factors – partly reflected in the sharp fall of confidence indicators – are affecting investment and consumption.

Consumer and producer confidence indices (1)
(Index)



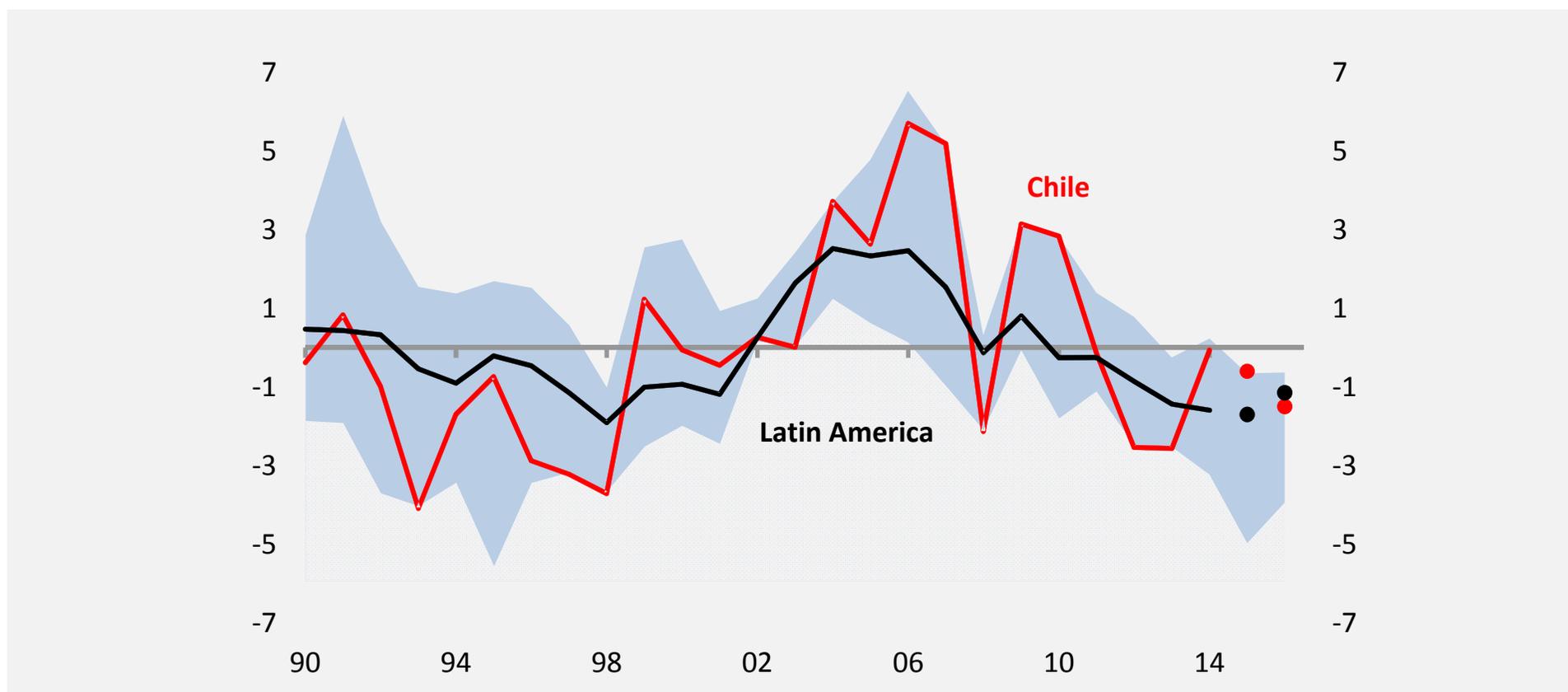
(1) Values over (under) 50 reveal optimism (pesimism).
Sources: Adimark e Icare/Universidad Adolfo Ibáñez..





The adjustment in the current account in Chile has been quite significant.

Latin America: Current account (1) (2) (3)
(percent of GDP, deviation from the mean)



(1) The area corresponds to the maximum–minimum range among economies.

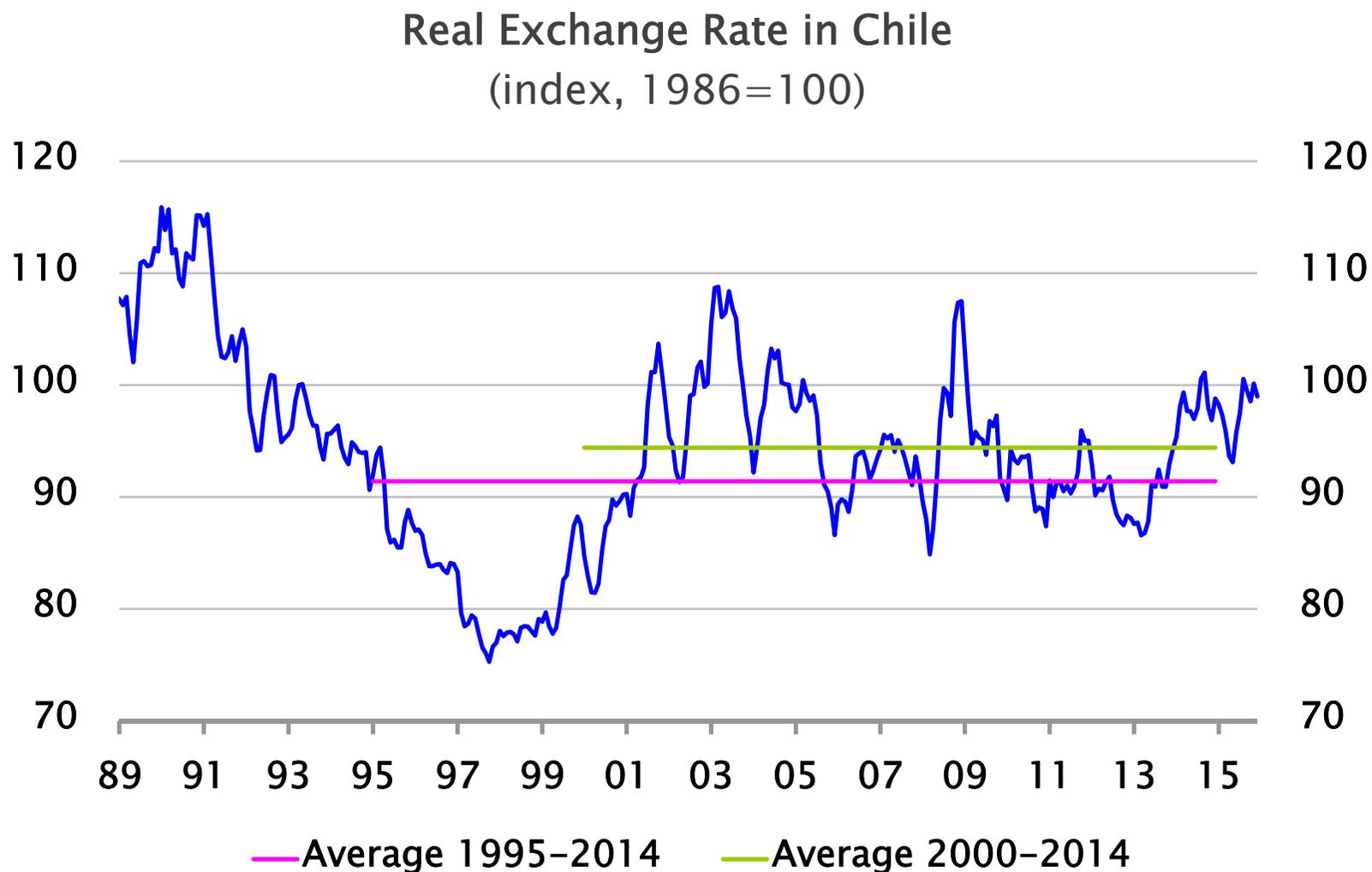
(2) Latin America considers Brazil, Chile, Colombia, Mexico and Peru.

(3) The two dots are 2015–2016 forecasts.

Sources: Central Bank of Chile, Consensus Forecasts and International Monetary Fund.



This adjustment has required a significant depreciation of the Real Exchange Rate

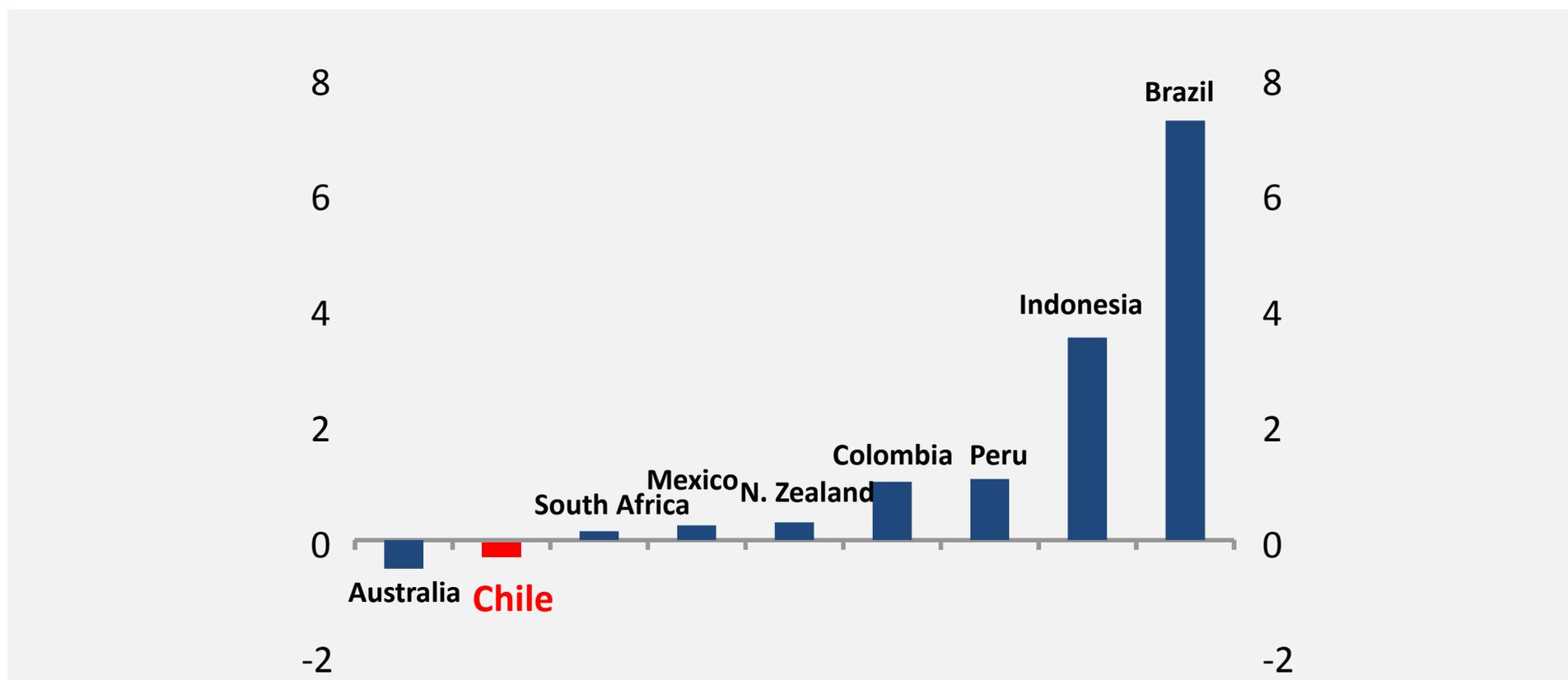


Source: Central Bank of Chile.



Monetary policy has been accomodative, allowing the exchange rate to adjust while keeping domestic financial conditions favorable.

Real Monetary Policy Rate (1)
(percentage)



(1) Computed as the difference between the nominal monetary policy rate and one-year ahead inflation expectations.

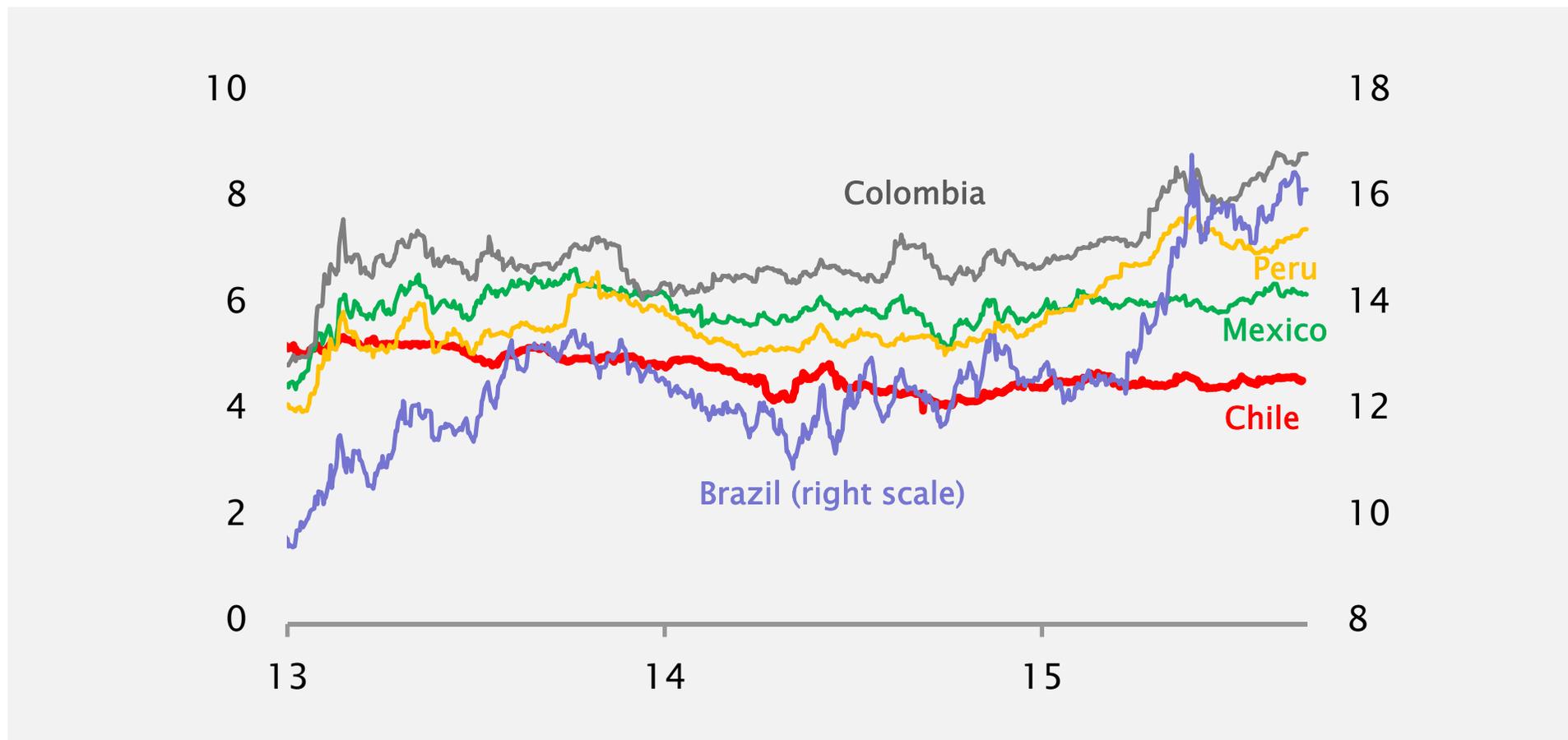
Source: Central Bank of Chile and Consensus Forecast.





Long-term interest rates in Chile remain low and stable.

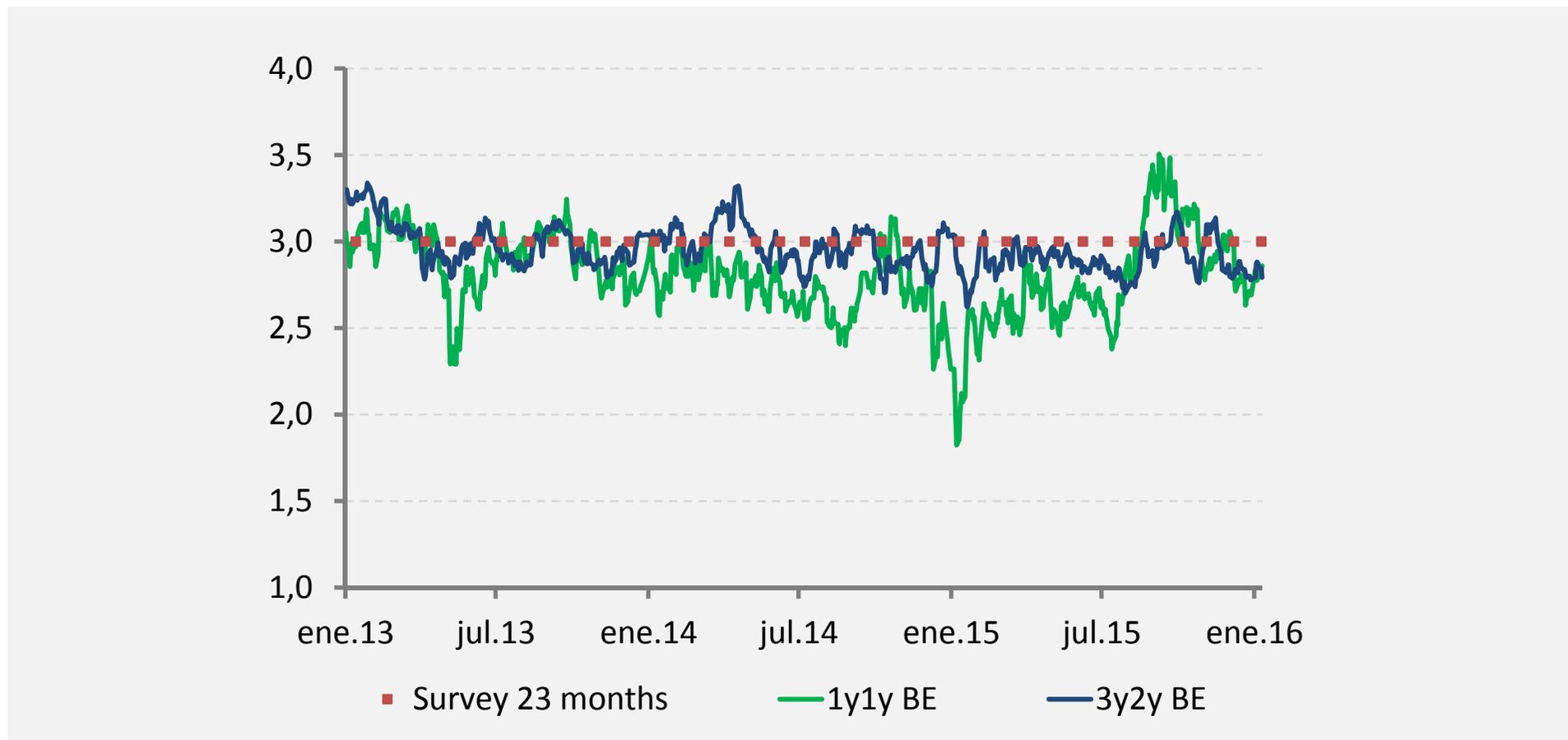
10-year government bond rates in Latin America
(percent)





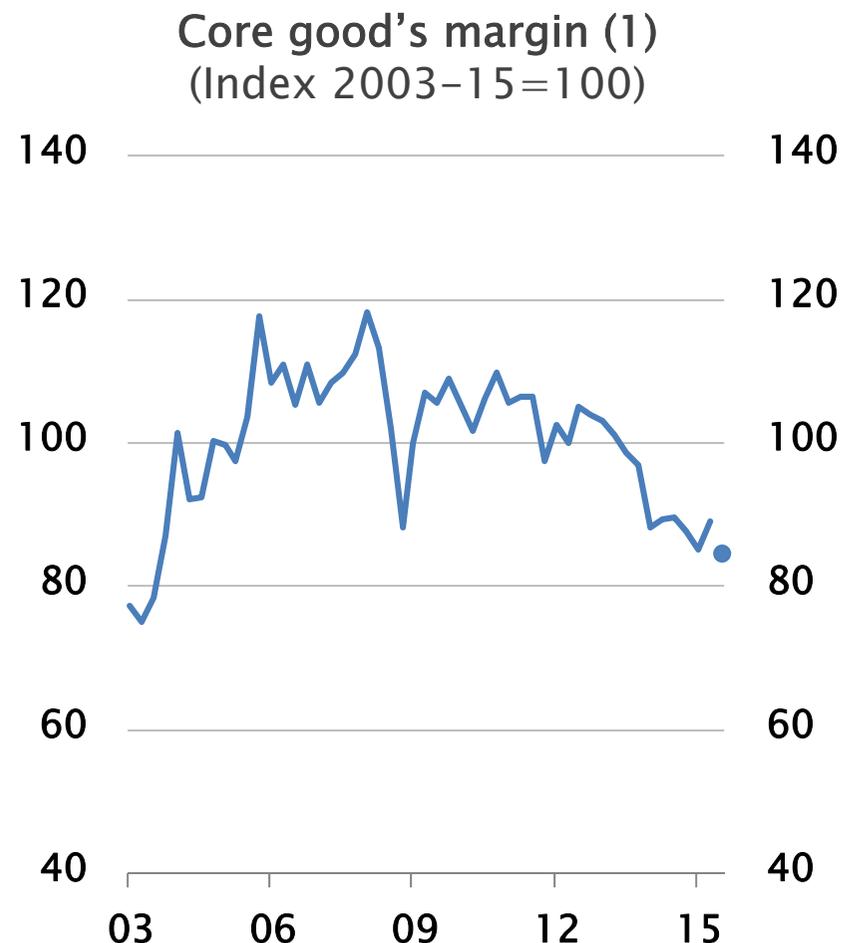
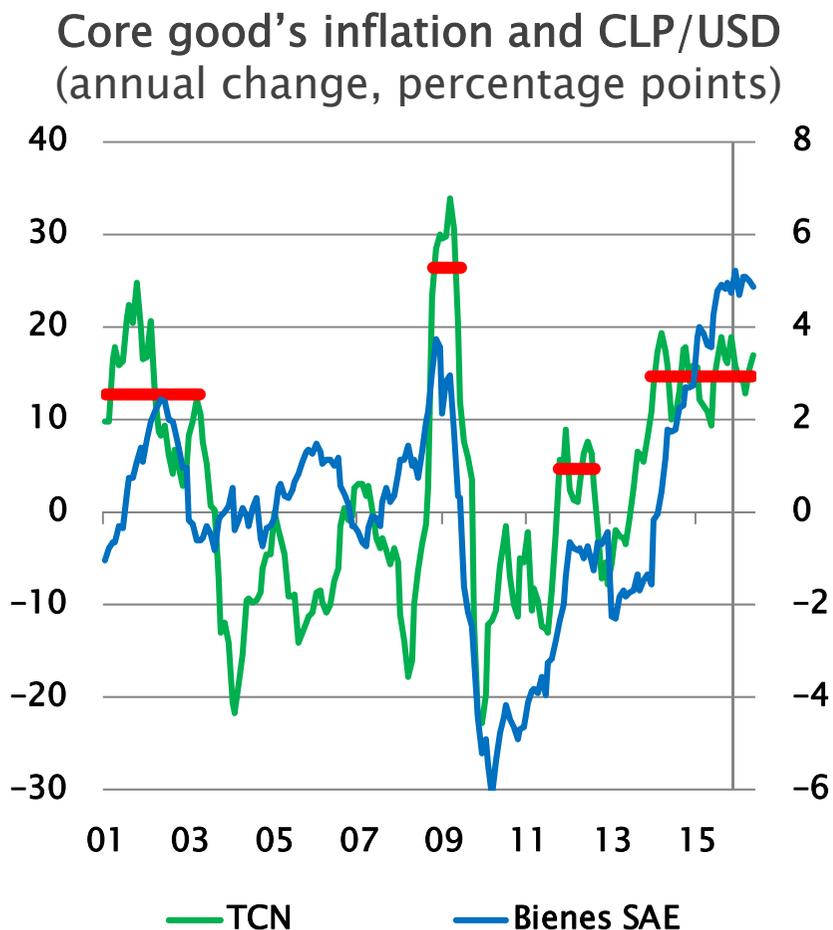
And medium-term inflation expectations have been solidly anchored around the inflation target.

Inflation Expectations (percent)





The depreciation of the peso has had a material effect on good's inflation.



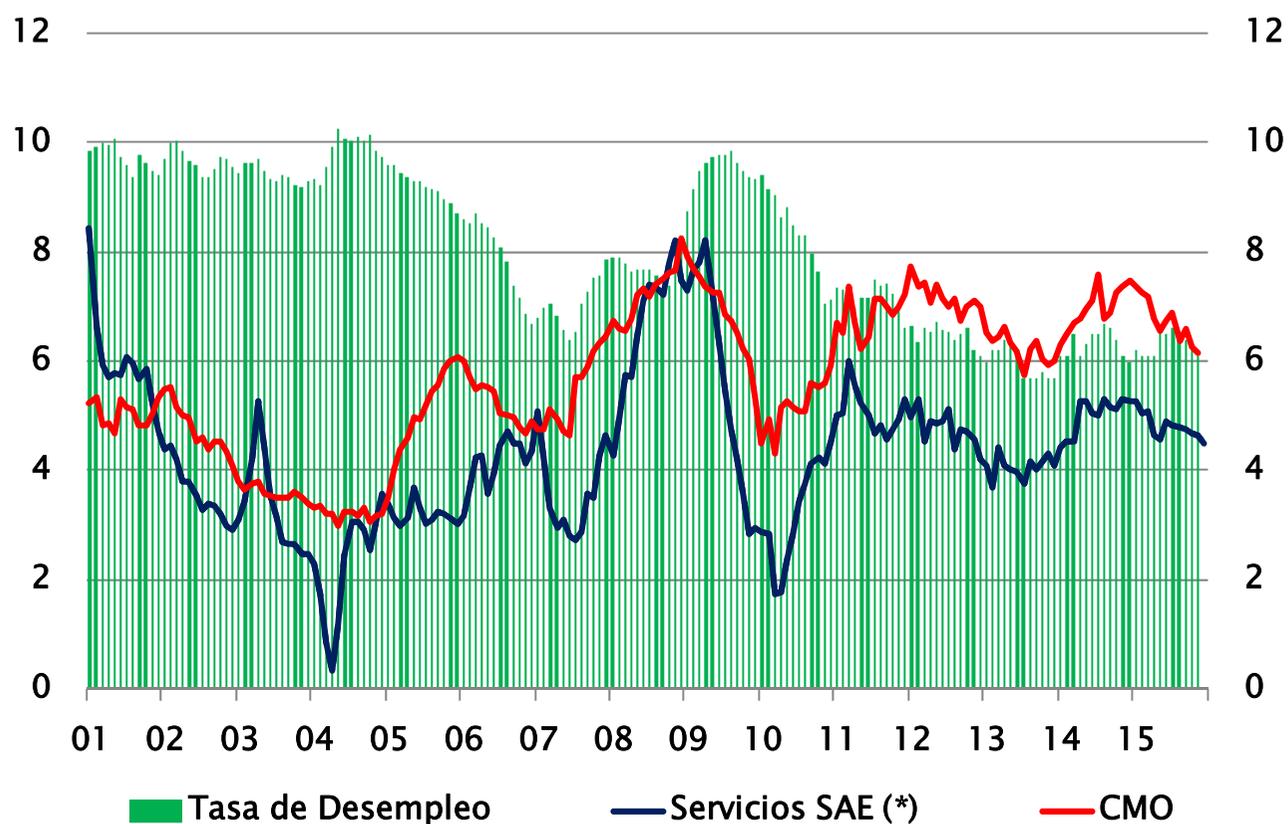
(1) (1) Computed as the difference between good's core inflation and consumption good's IVUM.

(2) Source: Central Bank of Chile and INE.



The slowdown in activity has not translated in an easing of wage and service inflation pressures.

Core Service Inflation , wages and unemployment (1) (annual change, percentage points)

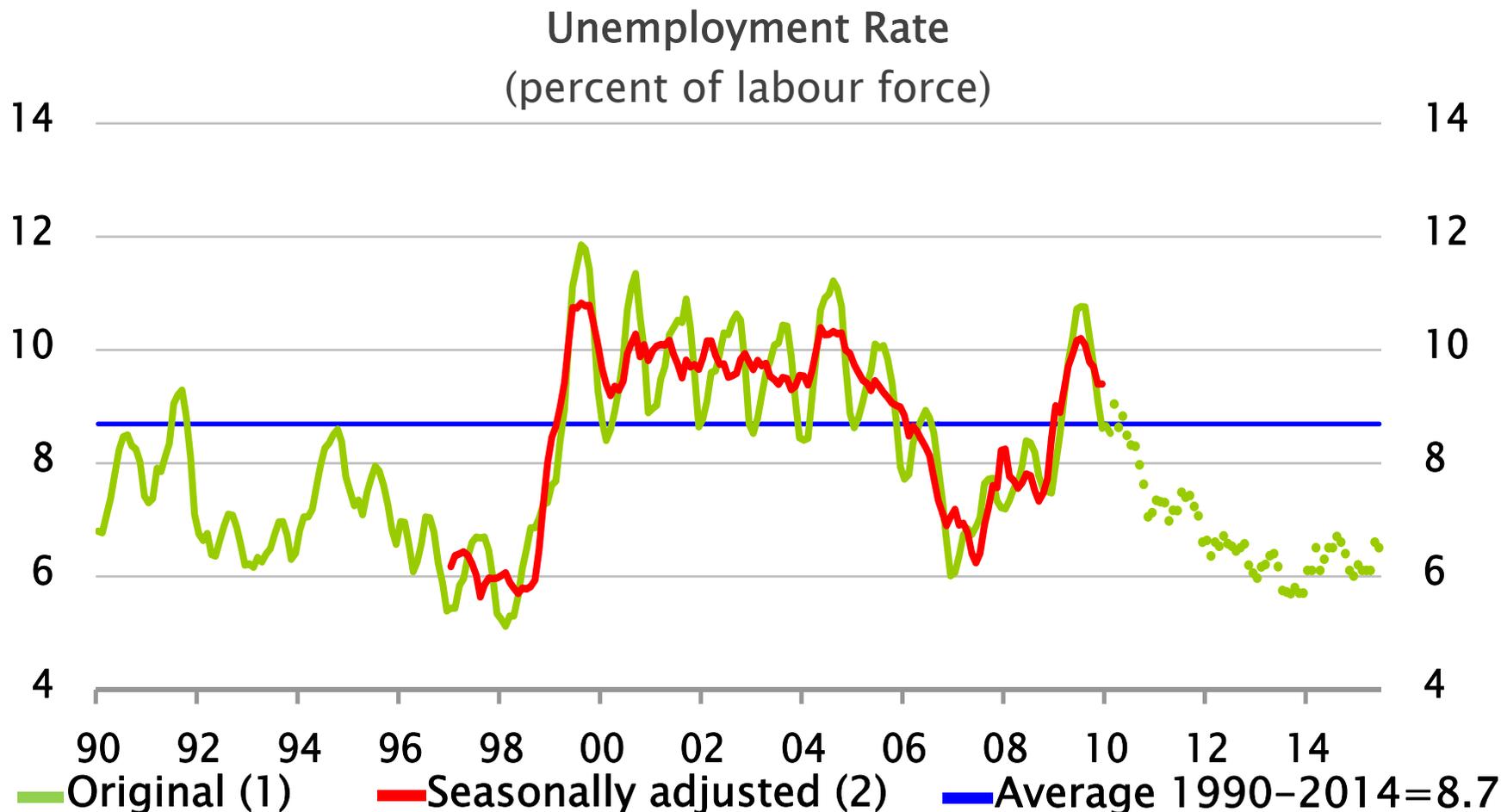


(1): Core service inflation excludes financial services (2.4%).

Sources: Central Bank of Chile and INE.



The labor market has been quite resilient to the slowdown of output.



(1) Dots correspond to the New National Survey on Employment (NENE).

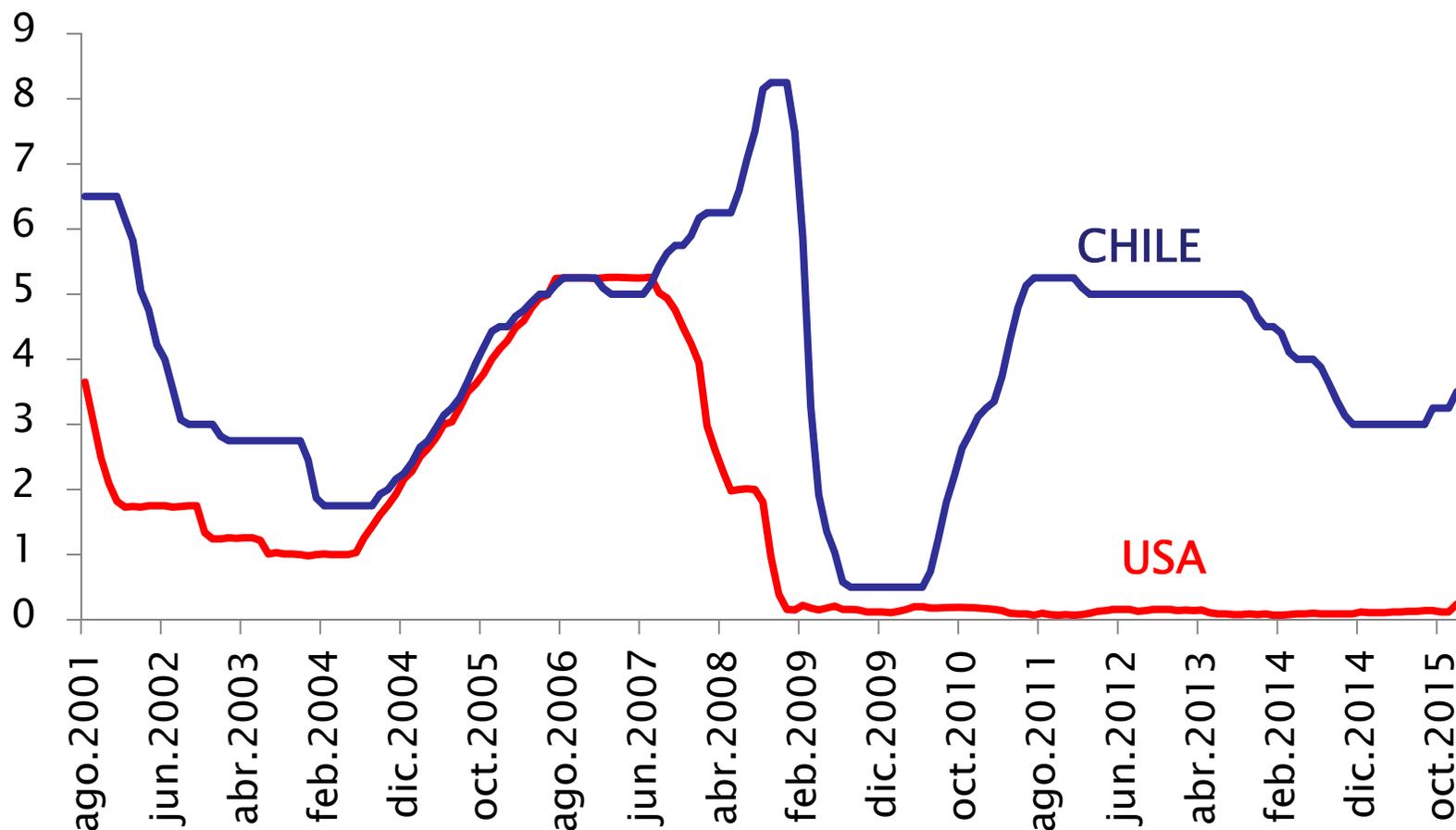
(2) Seasonally adjusted by the Central Bank of Chile.

Sources: Central Bank of Chile and National Bureau of Statistics.



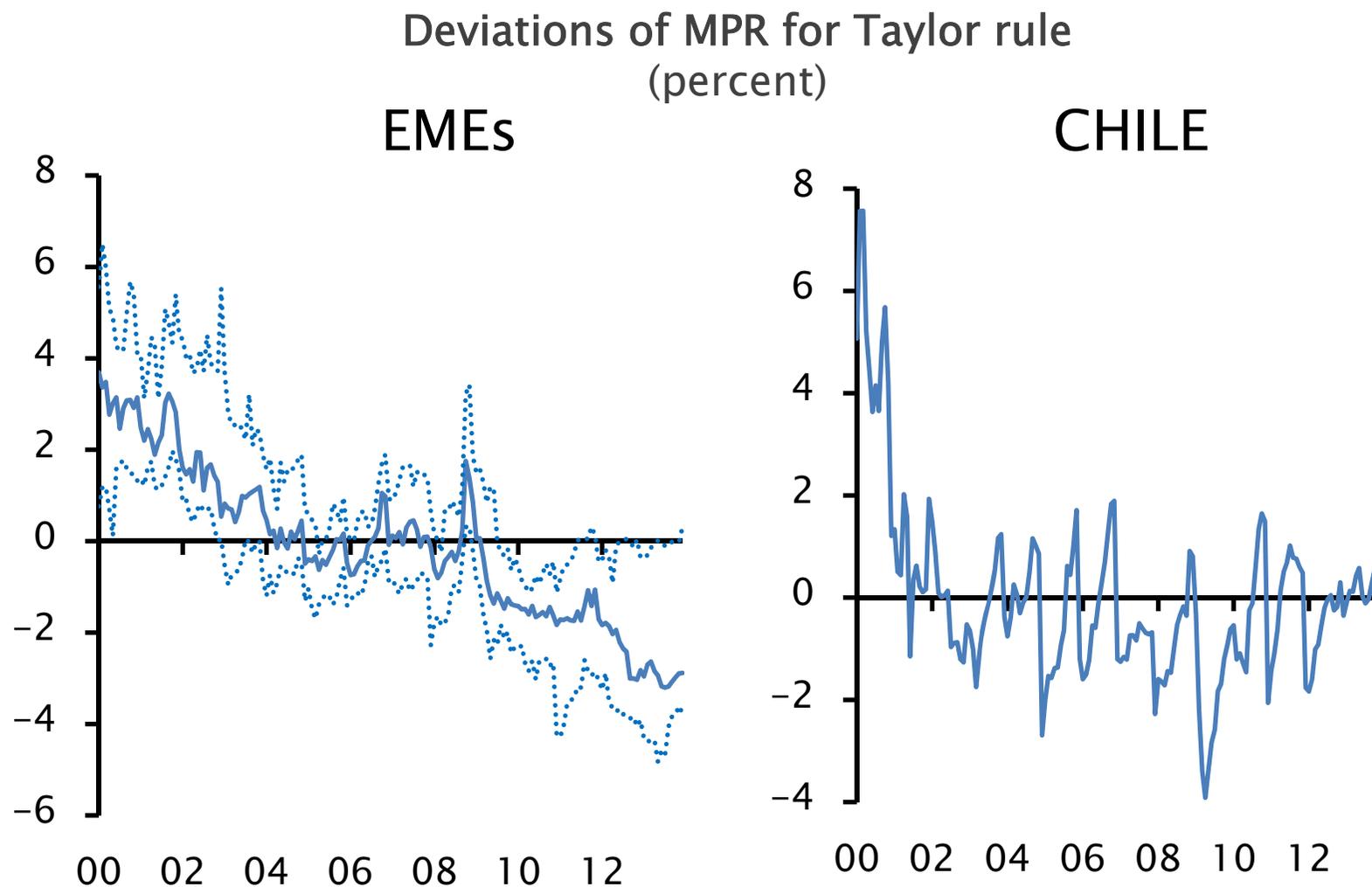
The gradual path of MP normalization in Chile responds to domestic inflation considerations.

Monetary Policy Rates in Chile and the U.S
(percent)





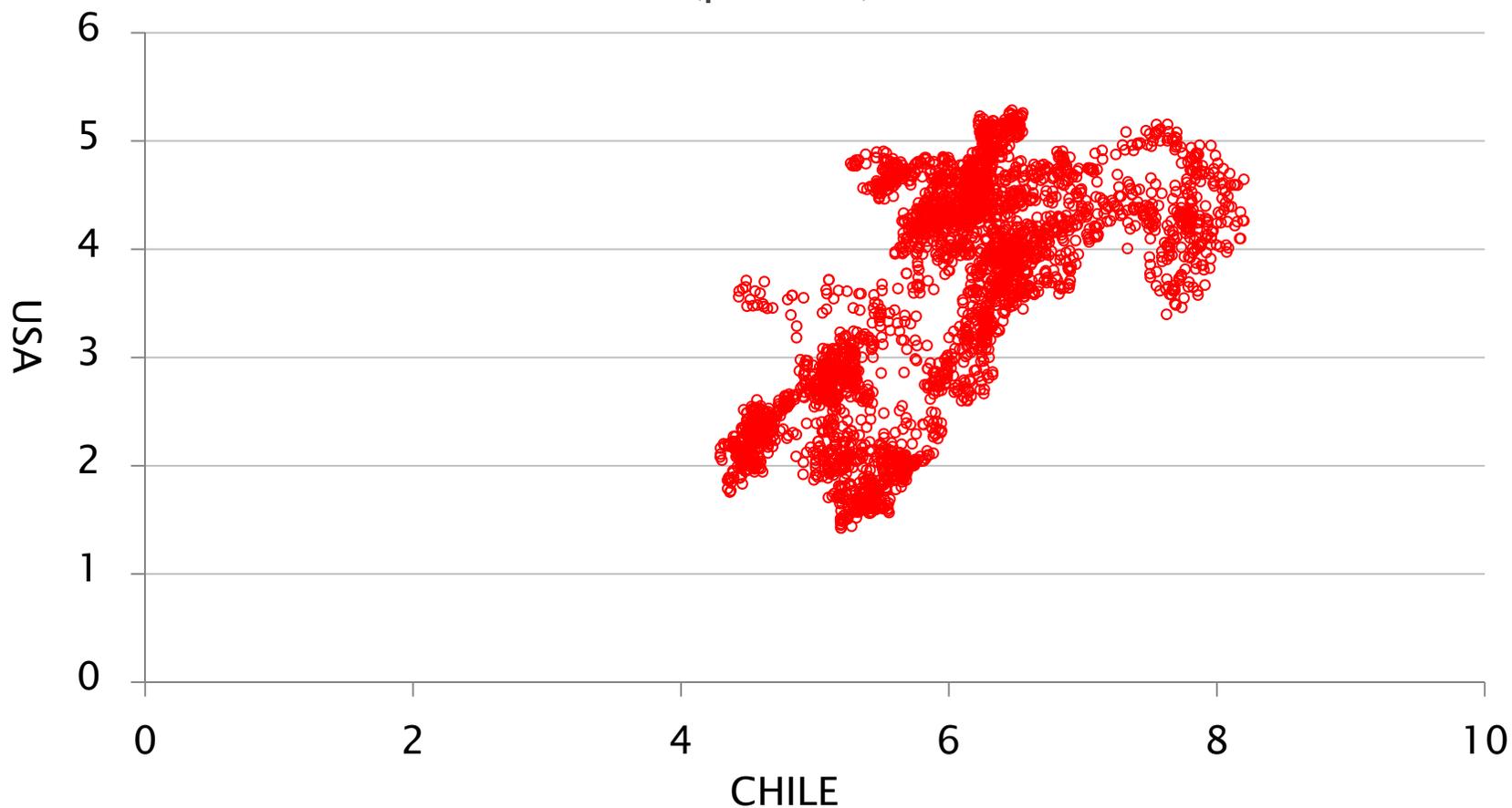
Relative to a Taylor–rule benchmark, Chile has had an independent MP in the last 15 years.





In any case, long term rates are highly correlated across countries.

10-year government Bond Rates in Chile and the U.S (1)
(percent)

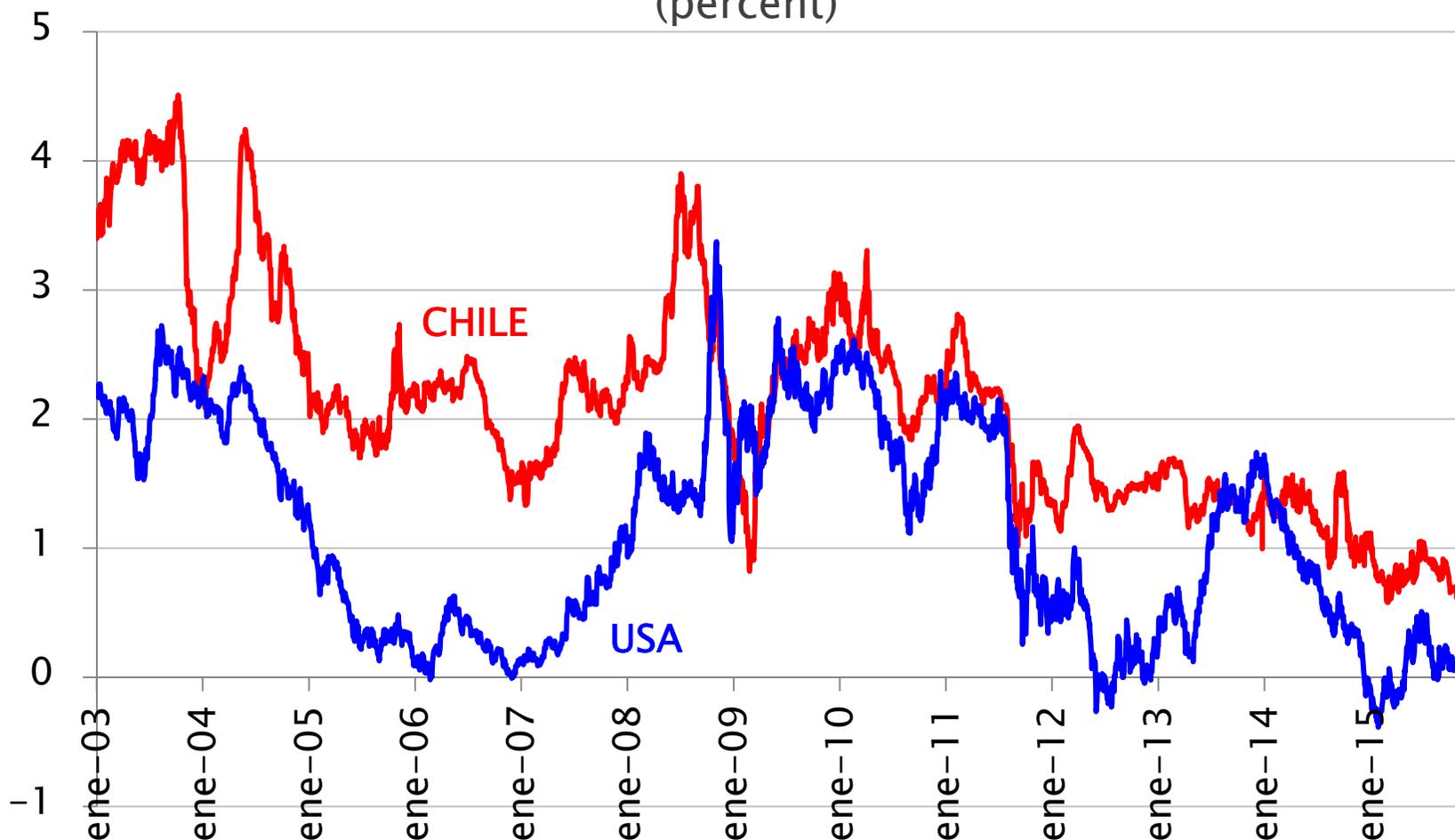


Source: Central Bank of Chile and Federal Reserve Bank.



This co-movement is specially strong in the term-premium component of longer term yields.

10y government bond term premium in Chile and the U.S (1)
(percent)

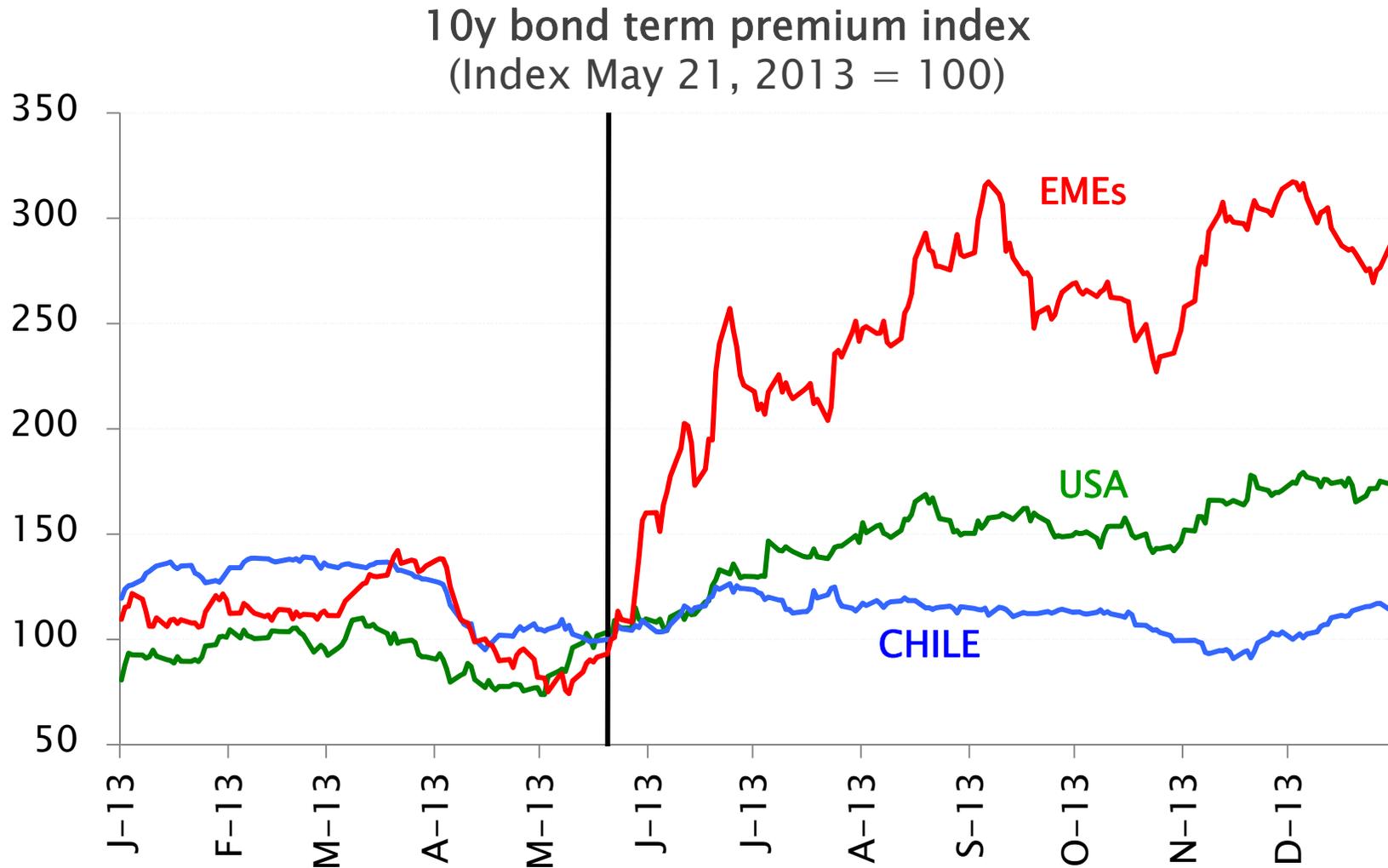


(1) Decomposition based upon the Adrian et al, (2013) methodology.

Source: Albagli, Ceballos, Claro and Romero, 2015, Channels of US Monetary Policy Spillovers of International Bond Markets, working paper 771, Central Bank of Chile



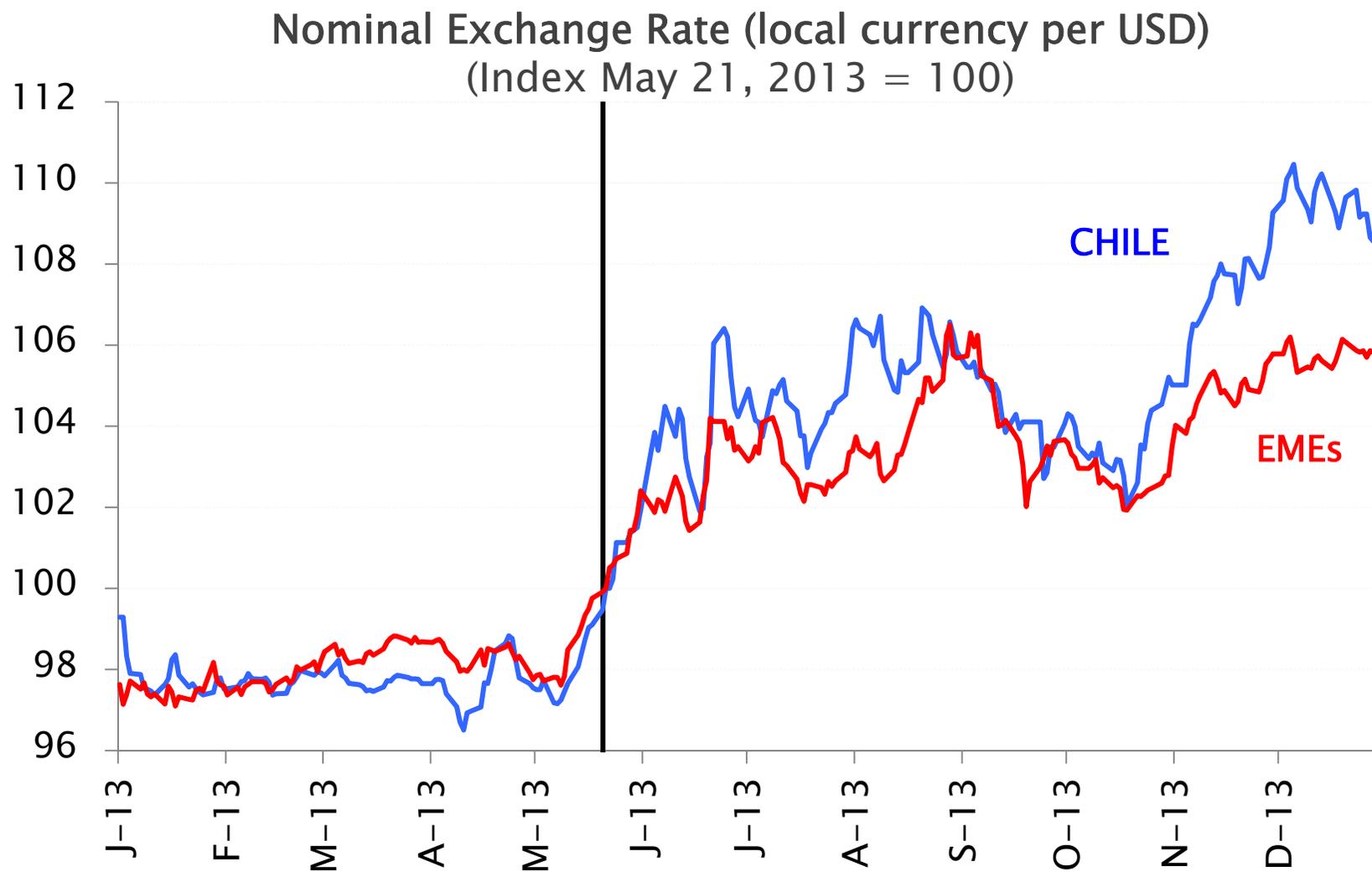
However, there are exceptions. Bernanke's taper talk in may 2013 is one of those.



Source: Albagli et al, (2015)



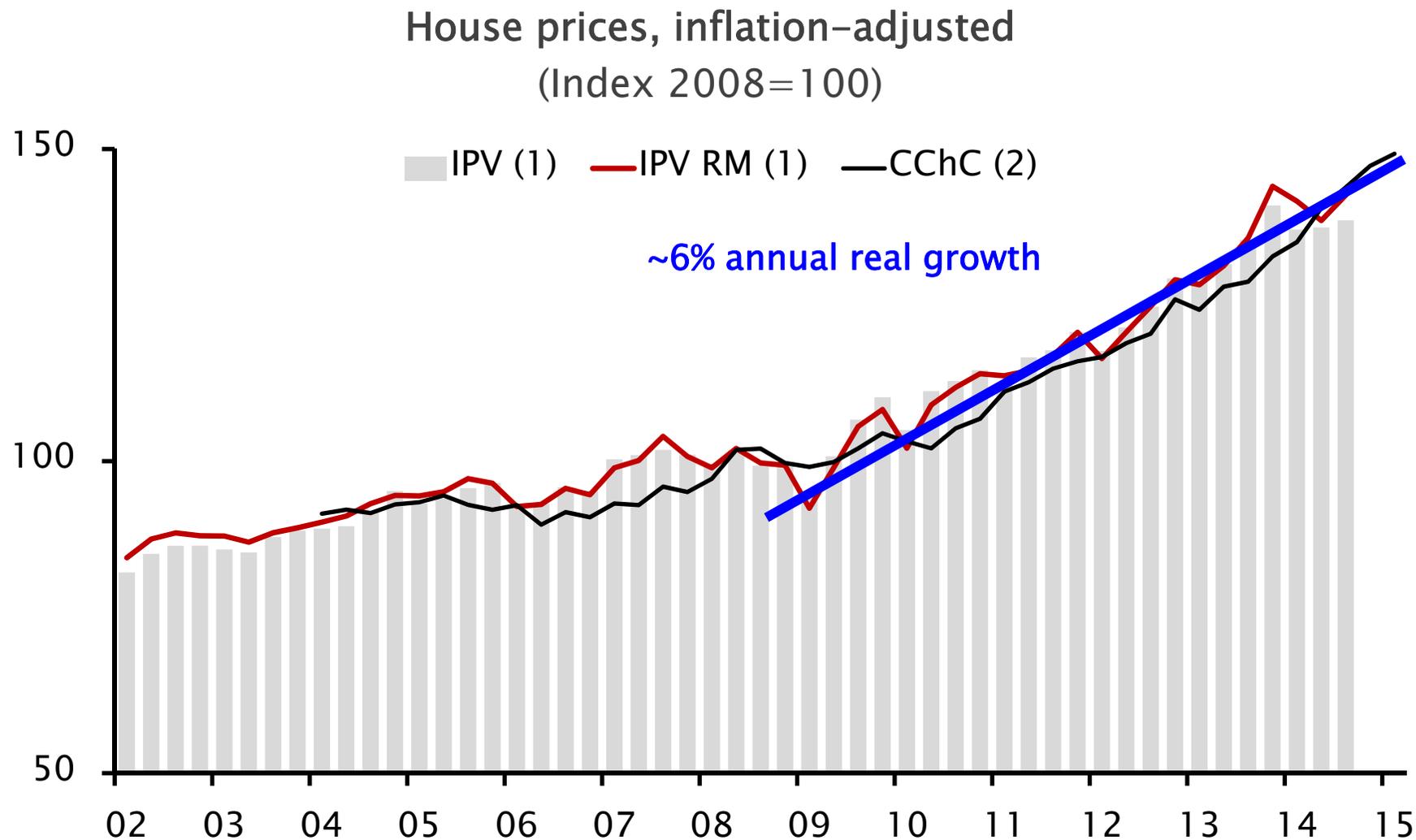
Naturally, the depreciation of CLP was more intense.



Source: Central Bank of Chile



High correlation of long rates poses important challenges for monetary policy in EMEs. For instance, in housing.

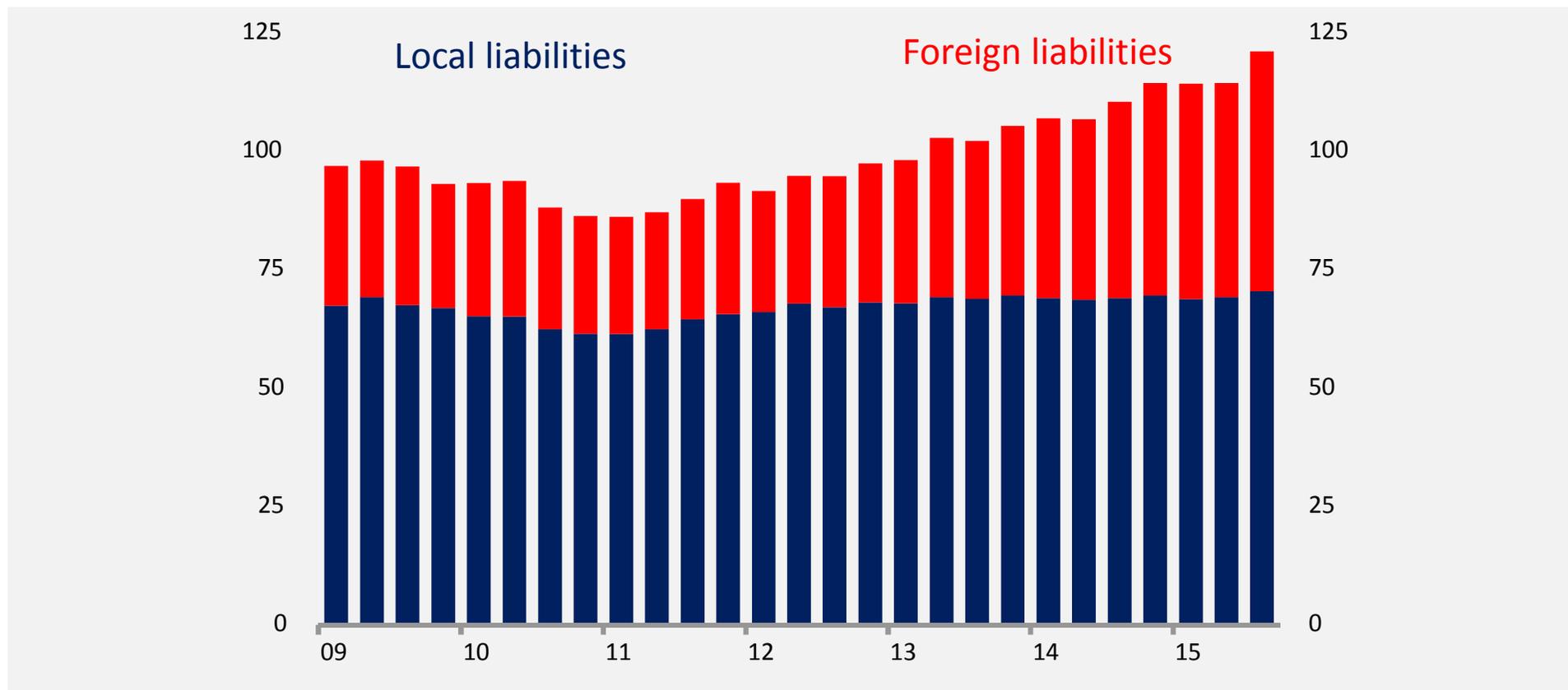


Source: Central Bank of Chile, SII and CChC



Corporate debt as a share of GDP has increased in the last few years, specially its foreign component.

Total Corporate Debt (1)
(share of GDP)



(1) Excludes banks.

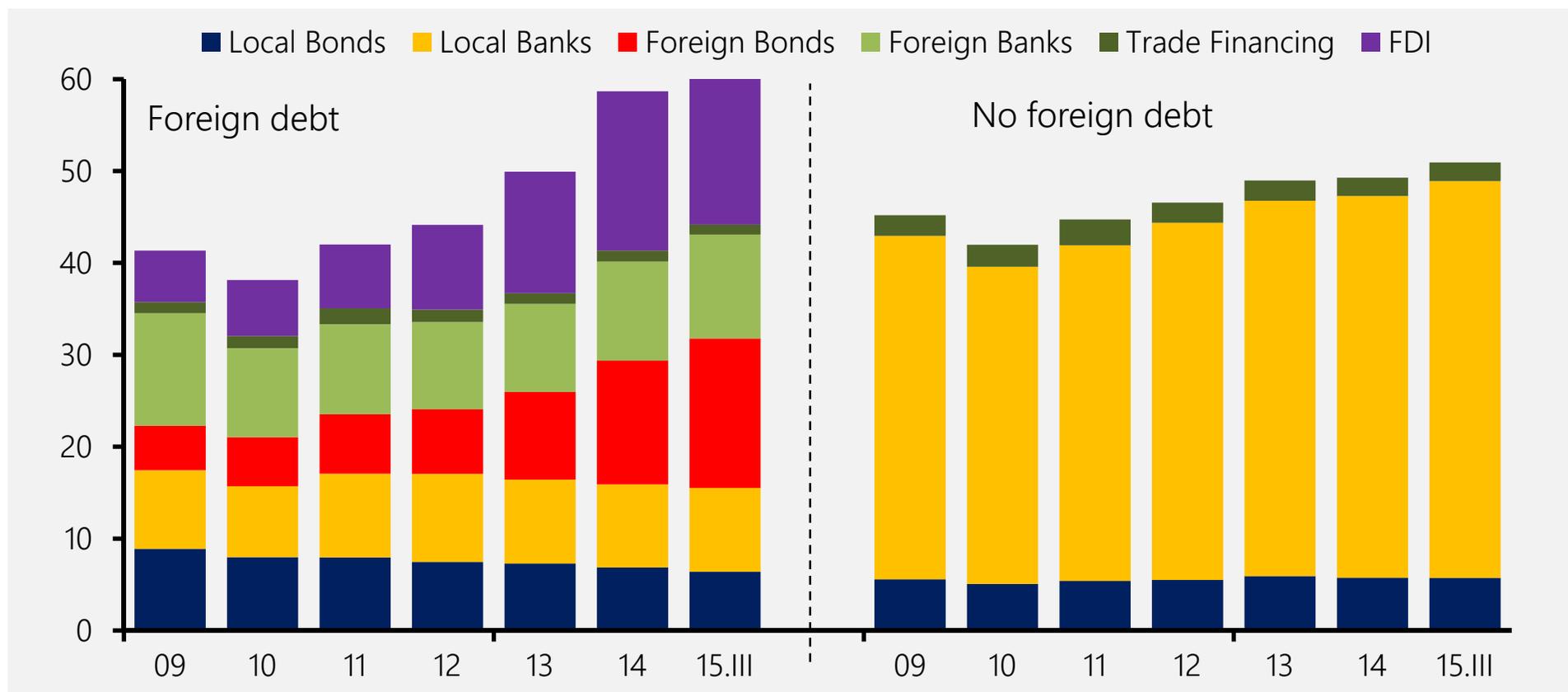
Source: FSR 2015.II, Central Bank of Chile.





Firms with foreign liabilities have little debt with domestic banks, which are mostly exposed to domestic firms with little financing beyond banks.

Total Corporate Debt by type of firm (1)
(share of GDP)



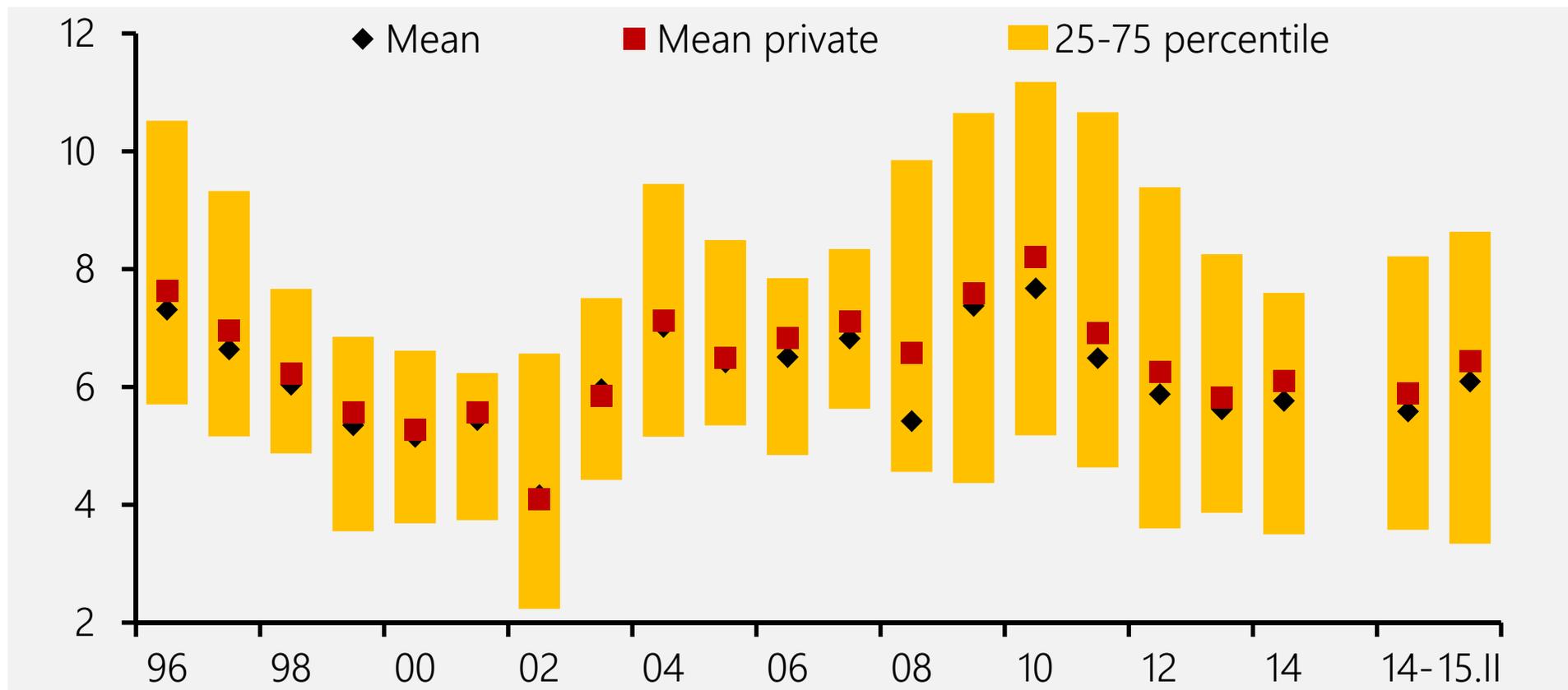
(1) Left hand panel includes all firms with any foreign debt (loans, bond and FDI) between 2009 and 2015.





Profitability has been quite estable in the last few years, at relatively low levels.

Return on Assets (1)
(percentage)



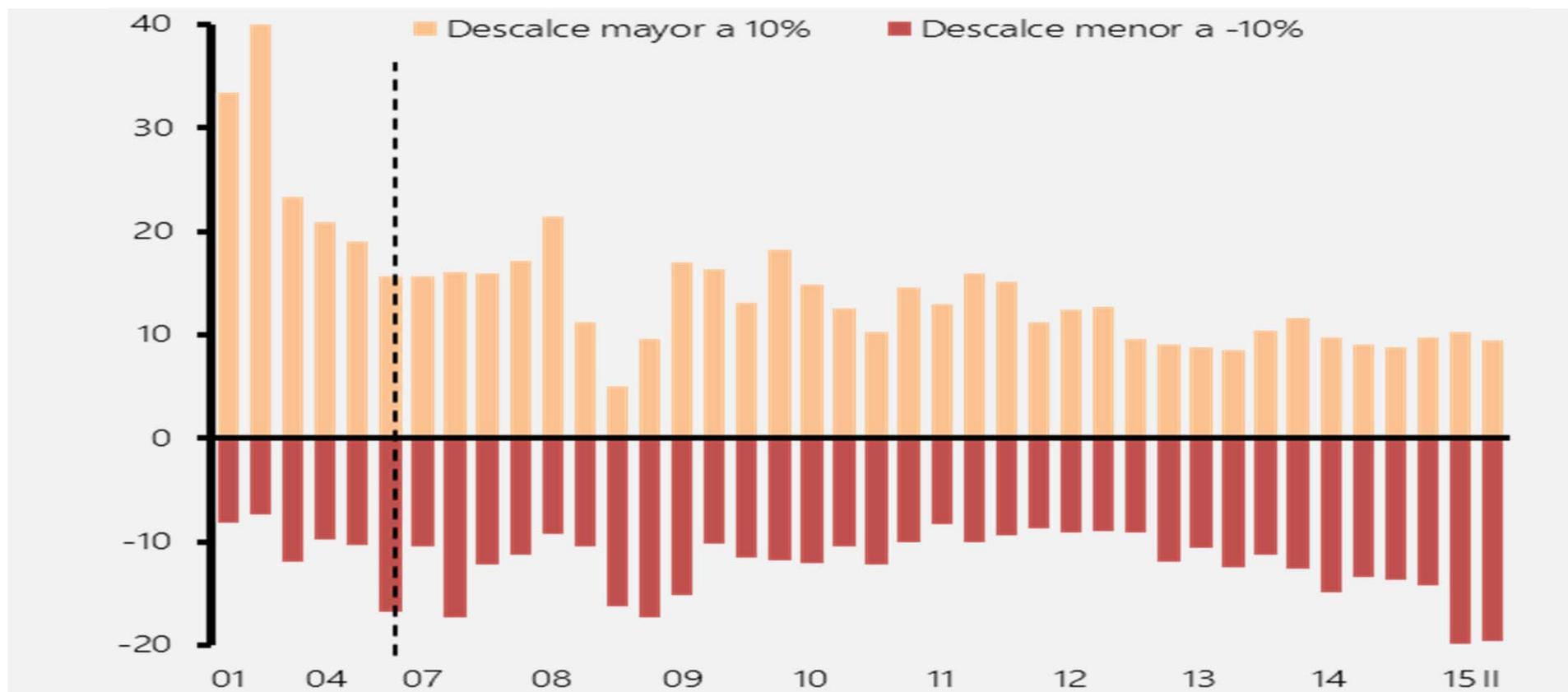
(1) Earnings before financial expenditures and taxes as a share of total assets.
Source: FSR 2015.II, Central Bank of Chile.





Available information shows no relevant currency mismatch in the corporate sector. A credible flexible FX regime is crucial for this.

Currency mismatch in the corporate sector (1)
(share of total assets)



(1) Based upon a sample of firms reporting financial statements in CLP. Net USD liabilities as a share of total assets.

Source: FSR 2015.II, Central Bank of Chile.

