# MONETARY POLICY PROSPECTS

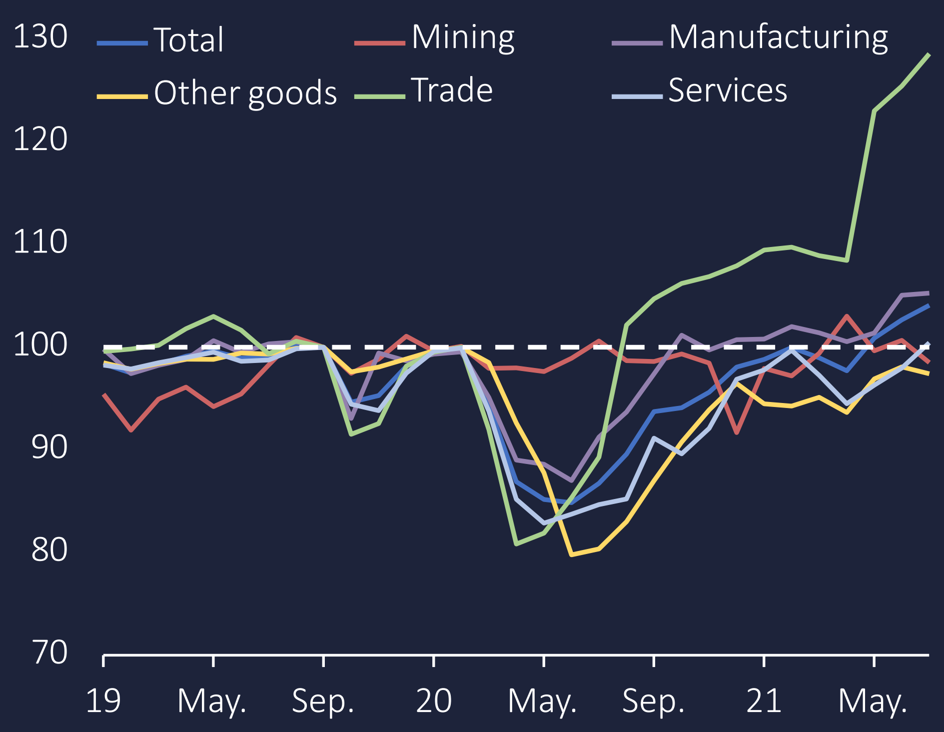
OCTOBER 2021

PABLO GARCIA – MEMBER OF THE BOARD

# The Chilean economy has recovered its level prior to the outbreak of the social crisis and the pandemic, with an unprecedented speed compared to past recessions.

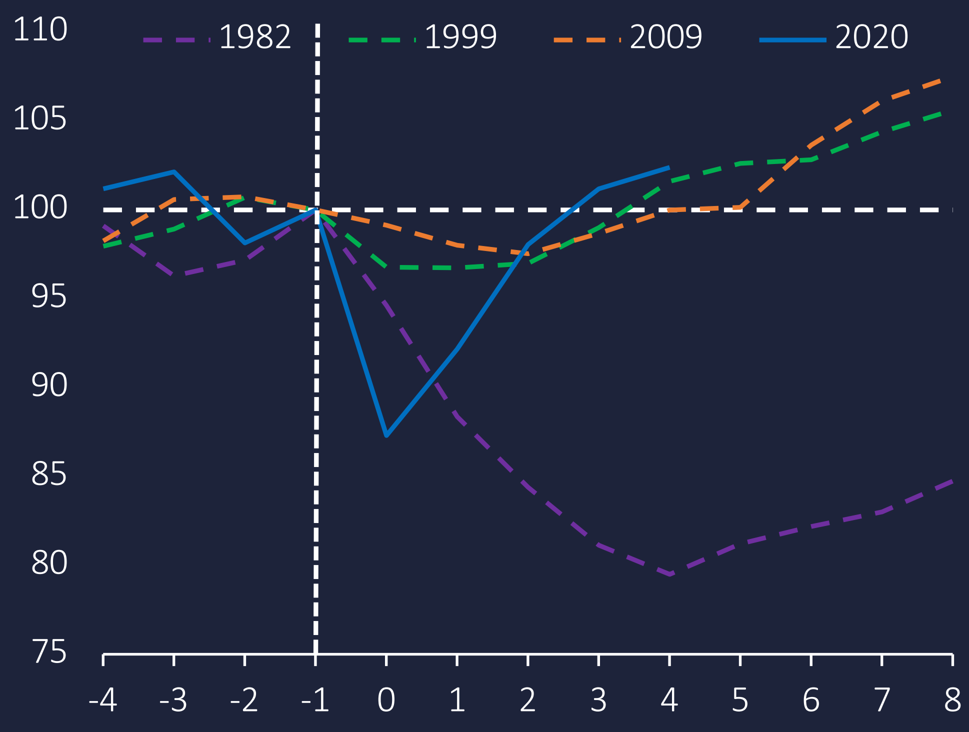
Imacec by sectors

(seasonally-adjusted levels, Sept. 2019=100)




Total GDP in crisis episodes (*)

(seasonally-adjusted series, index período -1=100)



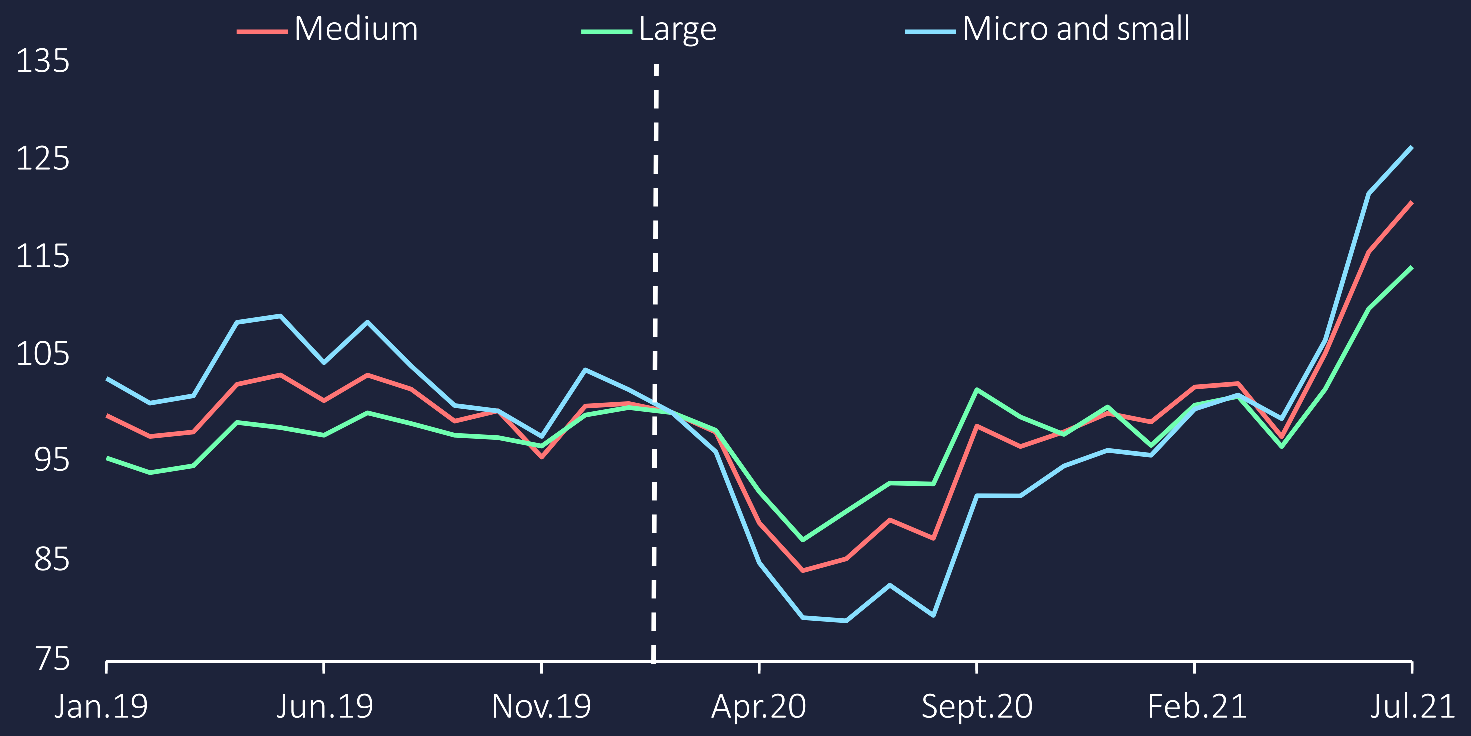

(*) Respective zero periods: 1981.4, 1998.4, 2008.4, 2020.2.

Source: Central Bank of Chile.

# It is a broad based recovery across all firm sizes.

Sales by firm size (*)

(index, February 2020=100)




(*) Dashed vertical line shows February 2020 sales. For details, see Chapter V in September 2021 Monetary Policy Report.

Sources: Central Bank of Chile and Internal Revenue Service (SII).

Sales of smaller firms have recovered the most, illustrating the effectiveness of credit support policies and the opening of the economy in recent months.

# Policy support to aggregate demand has been unprecedented.

Effects on GDP of measures adopted during the Covid-19 crisis

(percent change with respect to same period, previous year)

| | **2020** | **2021 H1** |
|---|---|---|
| Conventional monetary policy (1) | [0.2 - 0.8] | [0.6 - 2,1] |
| Unconventional credit policies (2) | [2.2 - 4.8] | [2.7 - 4.4] |
| Fiscal policy | 0.8 | 1.7 |
| **Total fiscal and monetary policy** | **[3.2 - 6.4]** | **[5.0 - 8.2]** |
| Pension fund withdrawals | 1.2 | 2.9 |
| **Total** | **[4.4 - 7.6]** | **[7.9 - 11,1]** |
| Actual GDP | -5.8 | 8.7 |
| Counterfactual GDP | [-10.2 ; -13.4] | [0.8 ; -2.4] |

(1) Conventional monetary policy is MPR related.

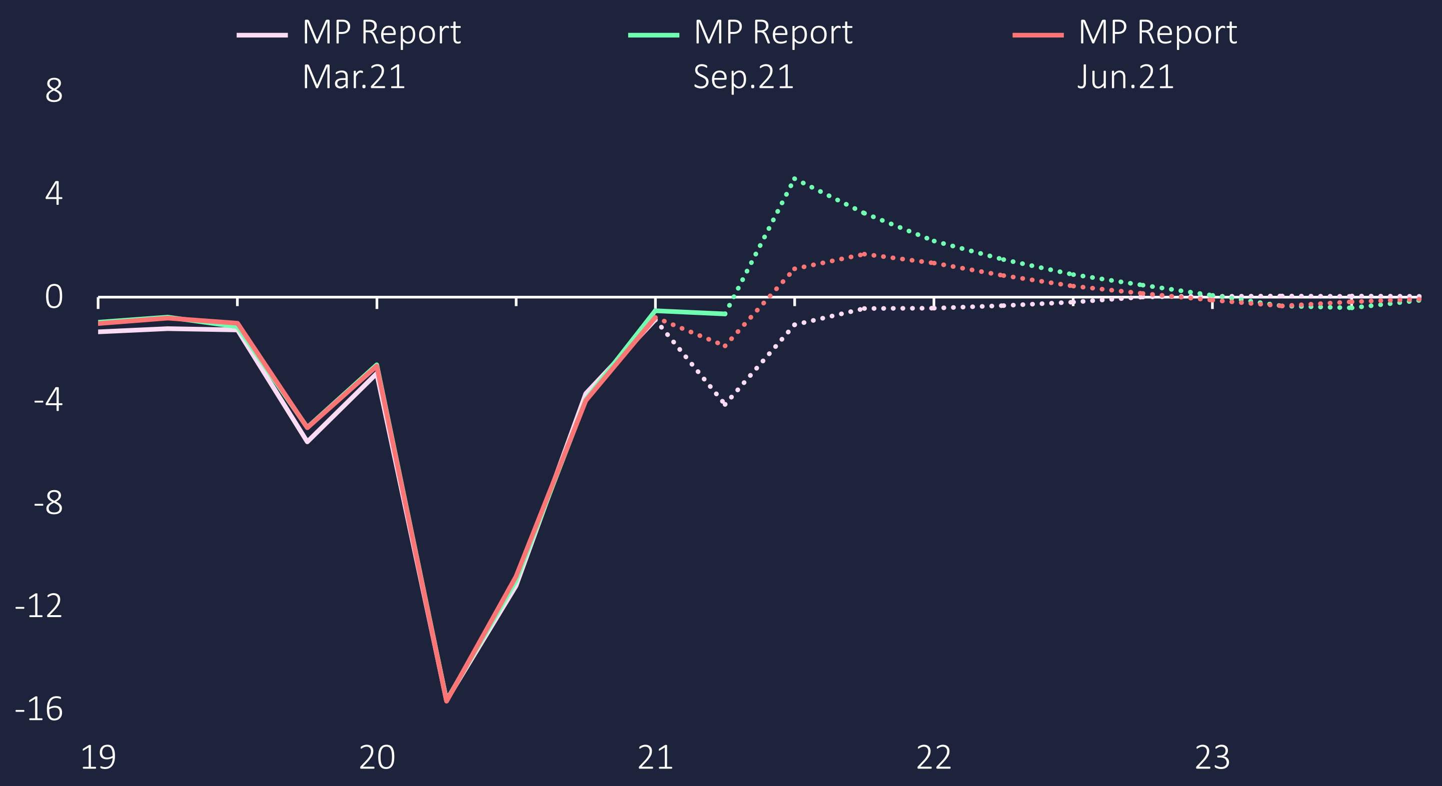
(2) Figures encompass monetary and sovereign guarantee policies that sought to stabilize financial markets, including the FCIC-Fogape program, bond purchases, and domestic- and foreign-currency liquidity programs.

Source: Central Bank of Chile.

# The output gap closed during the second quarter of this year and has moved into positive territory.

## Output gap (*)

(level, percentage points)

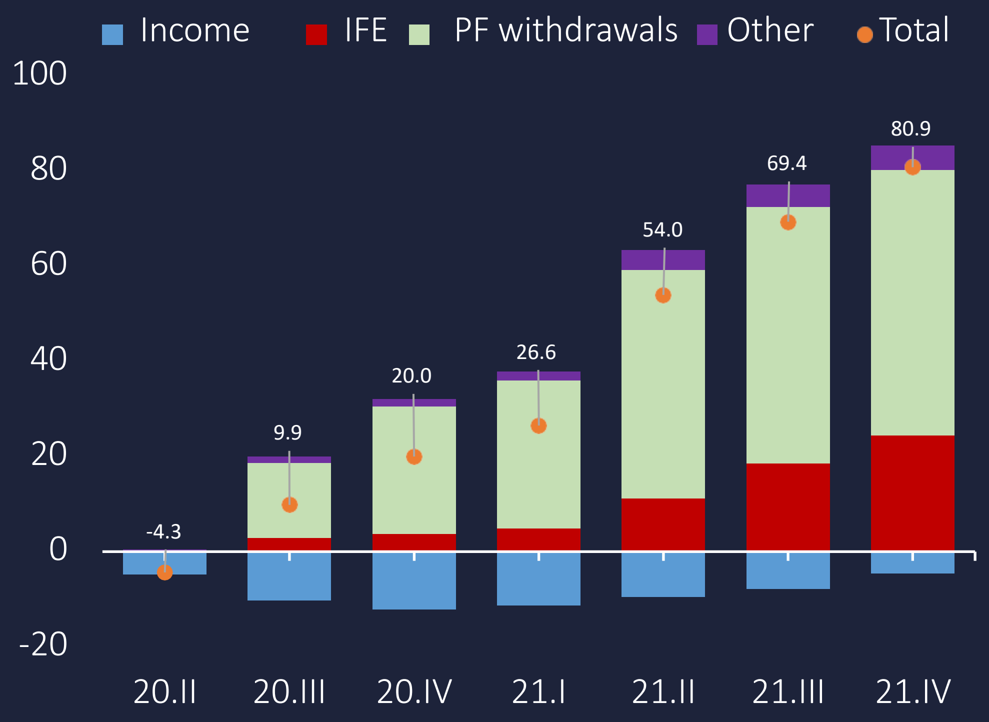



Going forward, it will turn positive and then will begin to decline as spending momentum subside

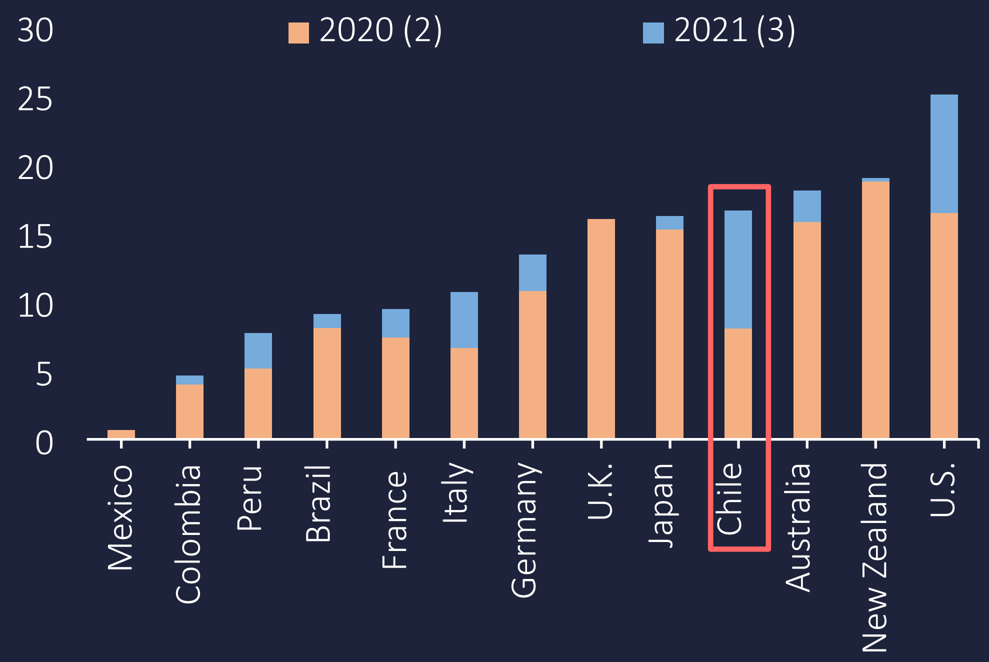
(*) Dotted lines show projections of each MP Report. The June and September projections use the structural parameters updated in the June 2021 MP Report.
Source: Central Bank of Chile.

# The accumulation of massive pension savings withdrawals and fiscal transfers have significantly increased household liquidity.

Households' umulative income and liquidity injections (1)
**(billions of dollars)**




Expenditures or foregone tax revenue by governments in response to Covid-19
(percent of 2020 GDP)

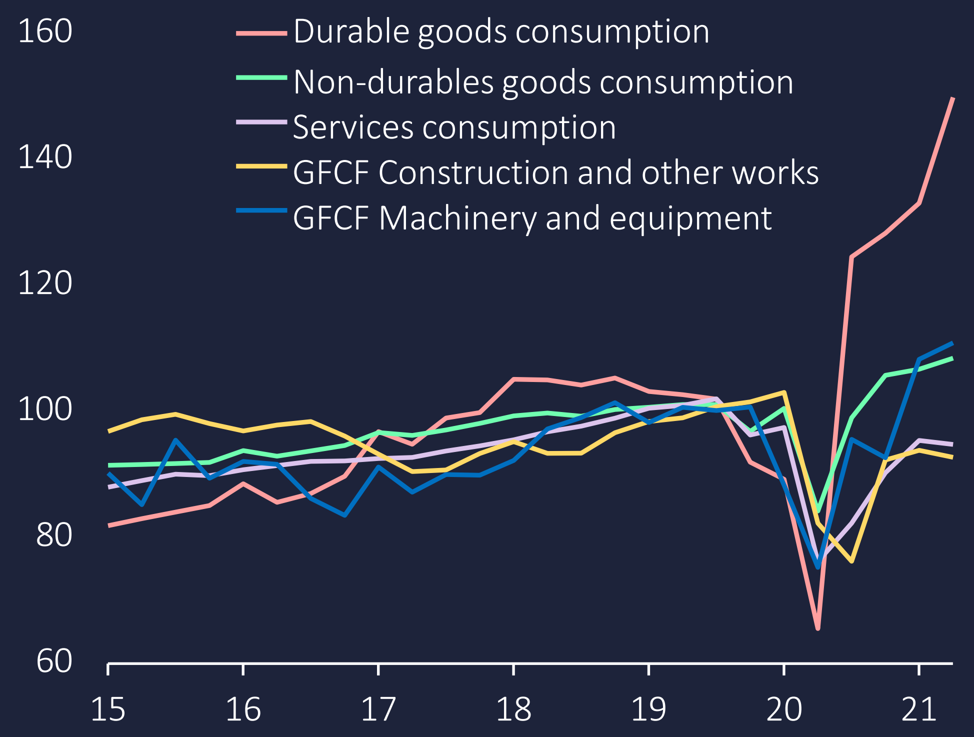



(1) For details on the methodology, see chapter III in MP Report of September 2021. (2) Corresponds to Fiscal Monitor data for January 2021. (3) Difference between July and January 2021 delivery. Chile considers an additional 2.8% for IFE.
Sources: International Monetary Fund, Ministry of Finance, Superintendence of Pensions and Central Bank of Chile.

# The various stimulus measures have strongly boosted demand, which has resulted in higher-than-expected growth in private consumption.

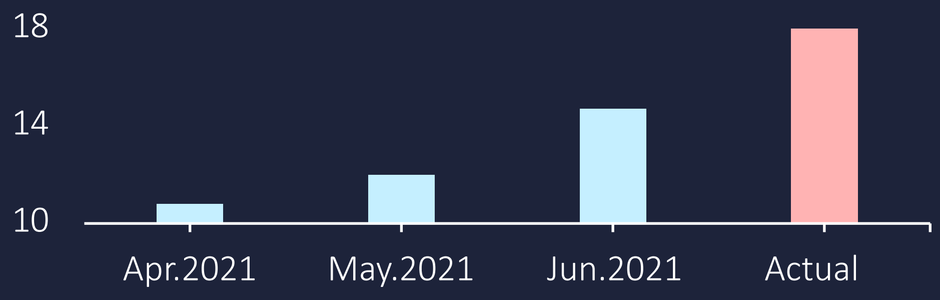
## Domestic demand

(seasonally-adjusted series; index, 2019 average=100)



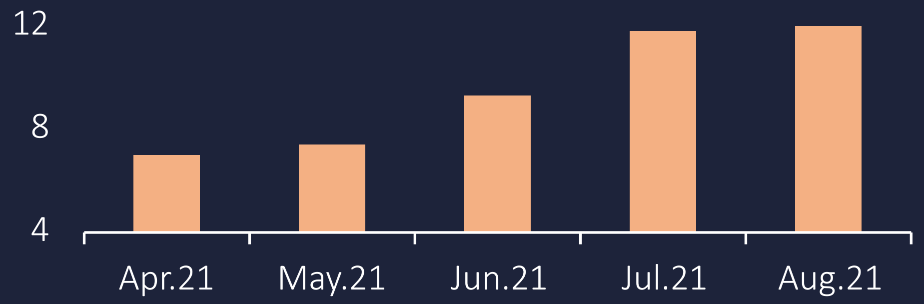

## GDP second quarter 2021: actual vs market projection (*)

(annual change, percent)




## Private consumption 2021: market projection (*)

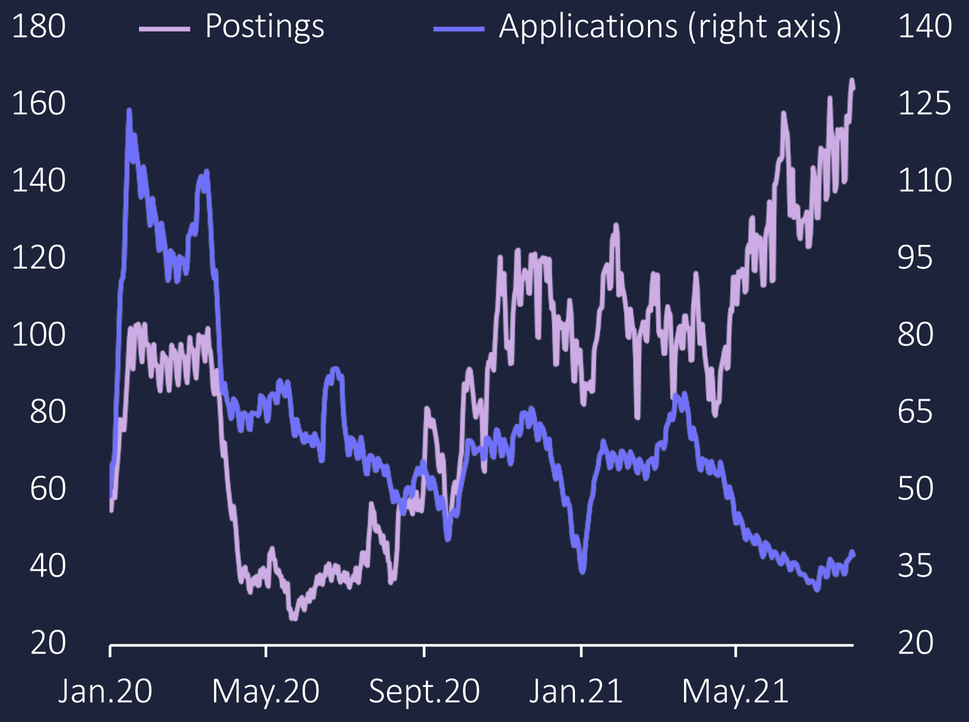
(annual change, percent)



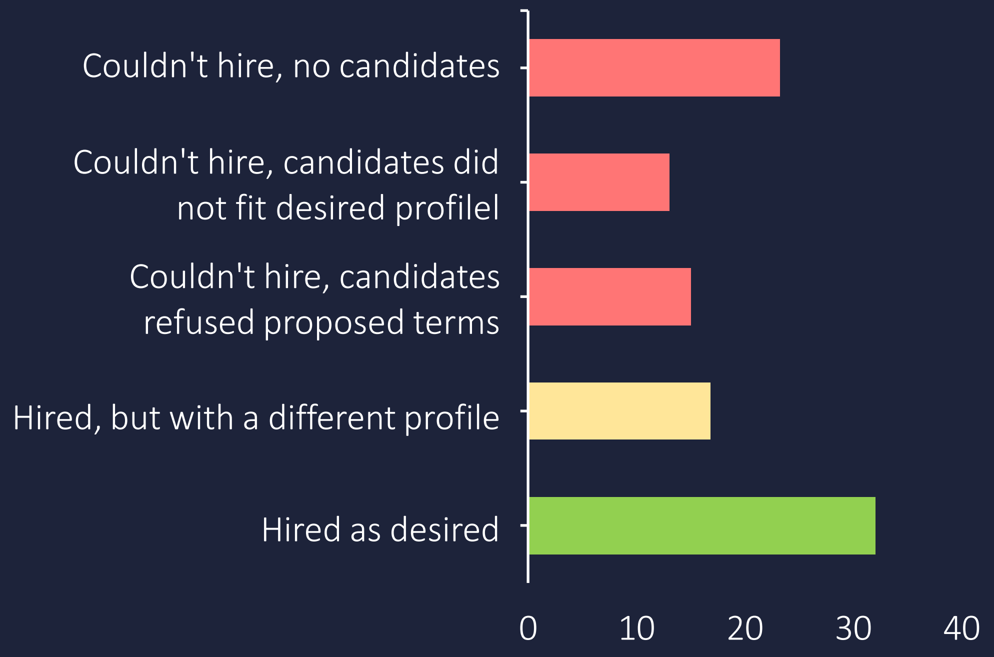

(*) Projections contained in Economic Expectations Survey.
Source: Central Bank of Chile.

# Labor market tightness is apparent, coupled with likely skill mismatches.

Job postings and applications on the Internet
(index, base 100=3 March 2020, moving 15-day average)



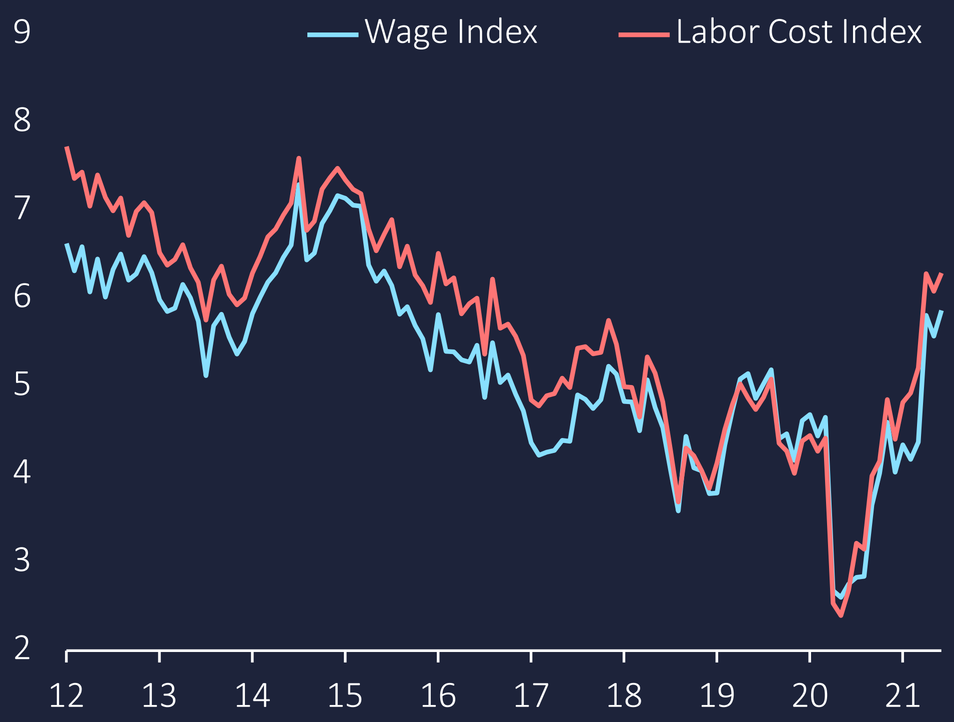

August BPR (*): Among firms wanting to hire, Generally, what happened with labor search?
(percent of total respondents saying they had searched for labor in 2021)



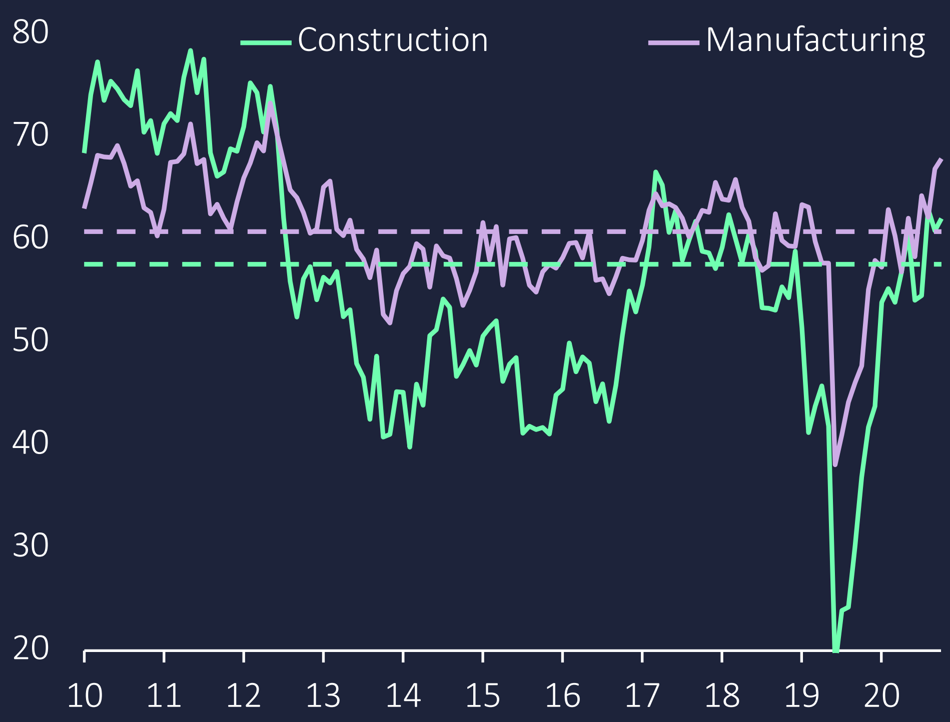

(*) Business Perceptions Report (BPR).
Sources: Central Bank of Chile and SABE Project of SENCE Labor Observatory and ISCI-WIC, University of Chile, based on websites trabajando.com and laborum.com.

# The combination of higher labor demand and tight labor supply is consistent with the recent acceleration of annual nominal wage growth.

Nominal wages (1)
(annual change, percent)




IMCE: Wage expectations (2) (3)
(diffusion index)

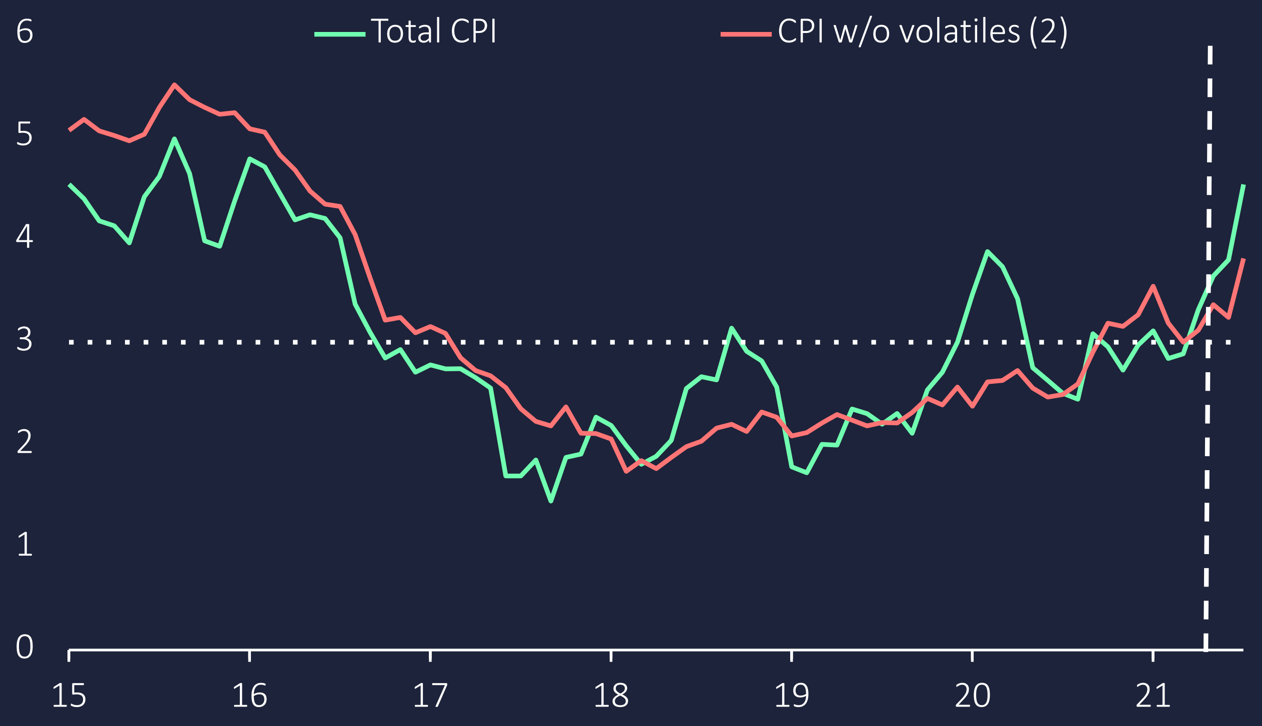



(1) Wage Index (IR) and Labor Cost index (ICMO). (2) Value above (below) 50 indicates an expansion (contraction) outlook. (2) Dashed horizontal lines show historical averages from January 2004 through May 2021 for each series. (3) Expectations for wages are six months ahead.
Sources: National Statistics Institute (INE) and Icare/Universidad Adolfo Ibáñez.

# Inflation has been picking up.

Headline and core inflation (1)

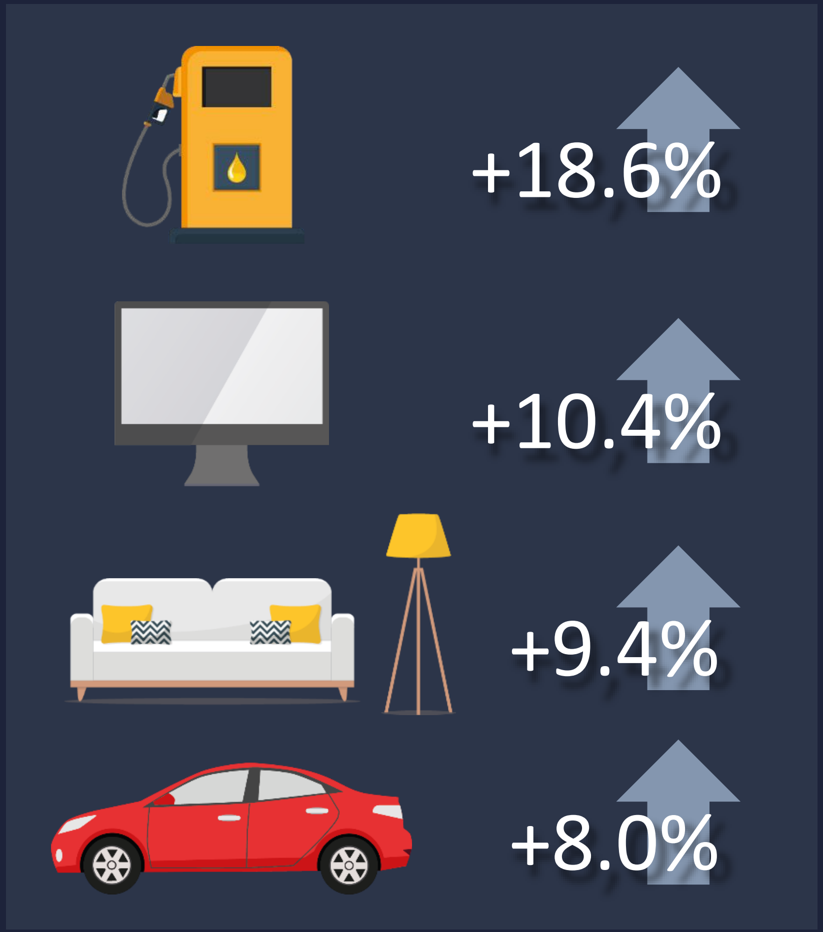
(annual change, percent)



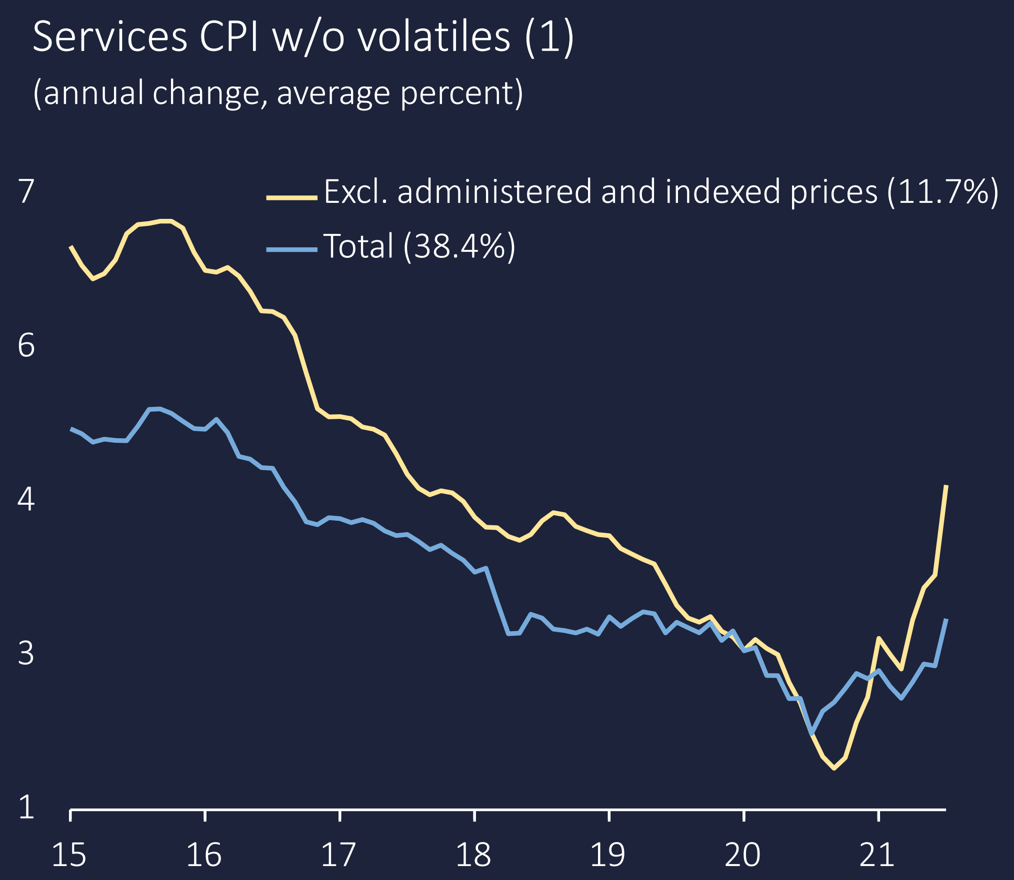

(1) Dashed vertical line indicates statistical cut-off of June 2021 Report. (2) CPI without volatility has 65.1% share in total CPI basket. For more details, see box IV.1 in December 2019 MP Report and Carlomagno and Sansone (2019).

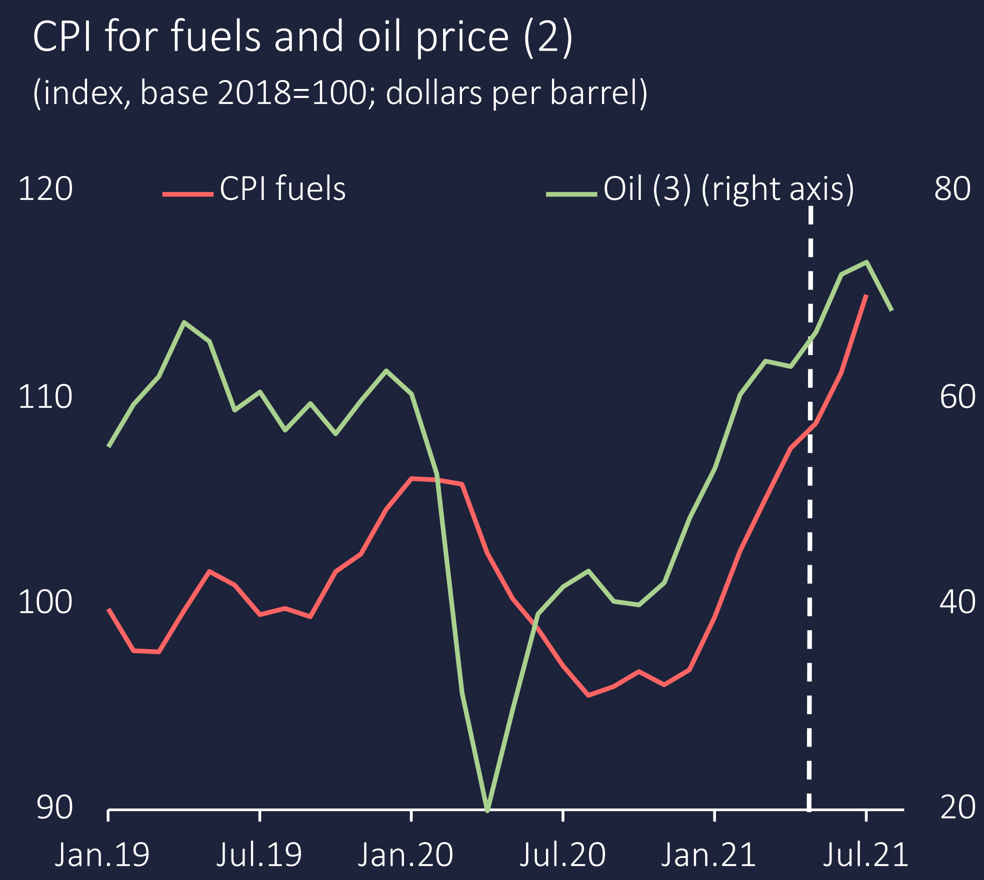
Price hikes at July 2021

(annual change, percent)



# Core services inflation has also risen, especially when excluding administered and indexed items. Among volatile items, the new rise in fuel prices stands out.



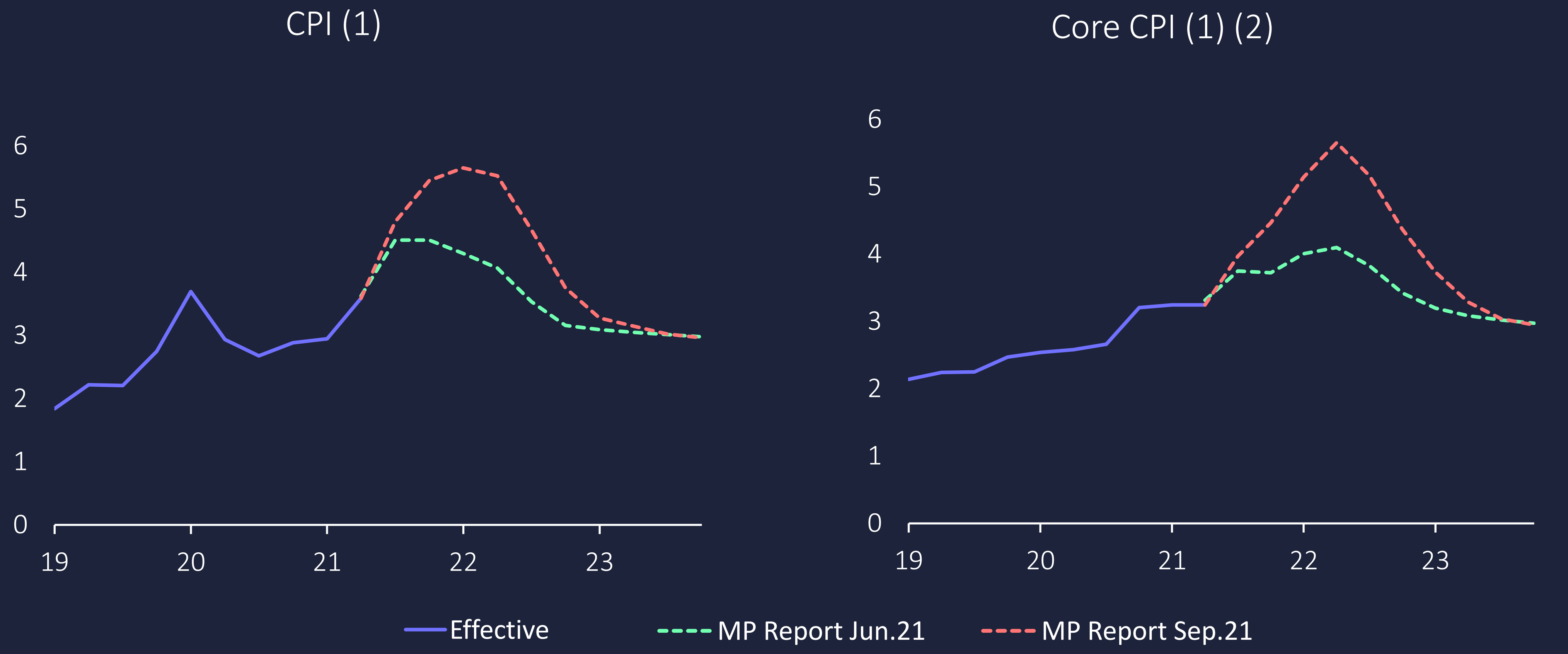




(1) In parentheses, share in total CPI basket. (2) Dashed vertical line indicates statistical cut-off of June 2021 MP Report. (3) Average price between Brent and WTI oil barrels.
Sources: Central Bank of Chile, Bloomberg, and National Statistics Institute (INE).

# Annual inflation will end this year at 5.7%, and will be above 5% during the first half of 2022. Core CPI will peak around mid-2022.

Inflation forecasts

(annual change, percent)

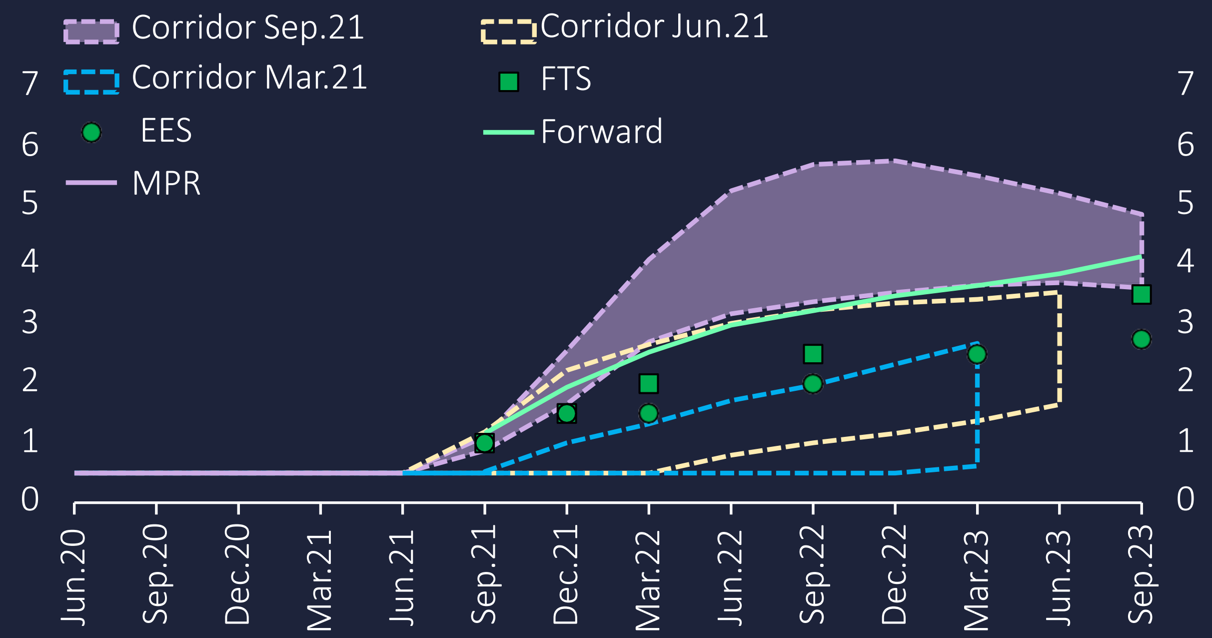



(1) Dashed lines indicate forecast in respective MP Report. (2) Measured by CPI w/o volatiles.

Sources: Central Bank of Chile and National Statistics Institute (INE).

# The Board raised the MPR to 1.5% in August (+75bp), after raising it by 25bp in July, and anticipates that it will continue to withdraw the monetary impulse, bringing the MPR at levels similar to its neutral towards the middle of the first semester of 2022.

MPR corridor (*)
(percent)




(*) The corridor is built following the methodology of Box V.1 of the March 2020 Report. It includes the FTS of August 26, the EES of August 10 and the quarter's mean smoothed forward curve (statistical cutoff). The methodology corresponds to the extraction of the implicit MPR considering the forward curve on the interest rate swap curve up to 2 years, discounting the fixed rates for each term at the simple accrual of the ICP.
Source: Central Bank of Chile.

The Board decided to intensify the withdrawal of monetary stimulus to avoid the accumulation of macroeconomic imbalances that could jeopardize the convergence of inflation to the 3% target. This is so because a scenario has emerged in which the Board has less room for maneuver, as a result of:

- Rapid evolution of macroeconomic scenario
- Inflation expectations dynamics
- Sensitivity scenarios associated with higher pressures on prices

banco central Chile

MONETARY POLICY REPORT

SEPTEMBER 2021

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