

THE MACROECONOMY AND MONETARY POLICY IN CHILE

9th BBVA LATAM Conference, London, January 16th 2023

Pablo García, Vice Governor



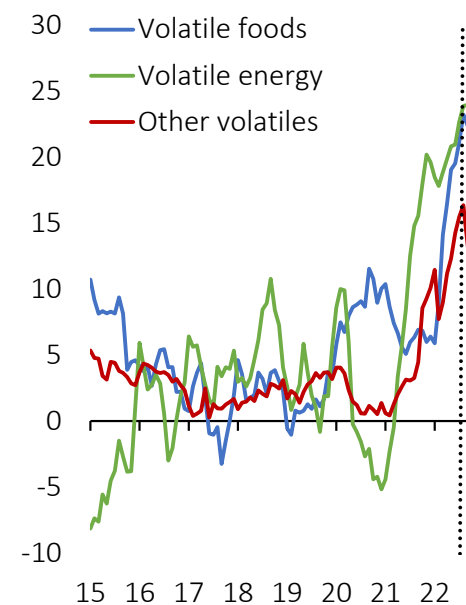
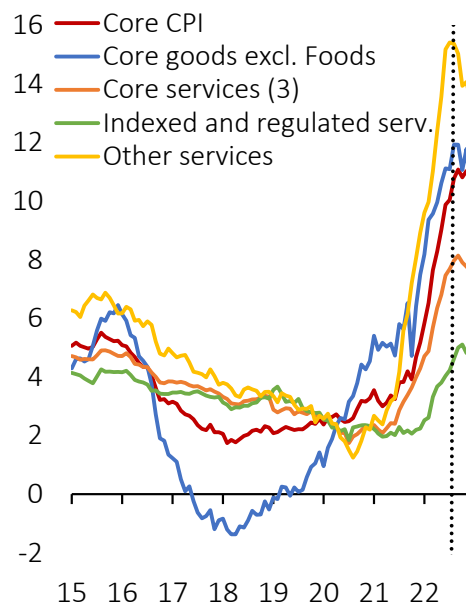
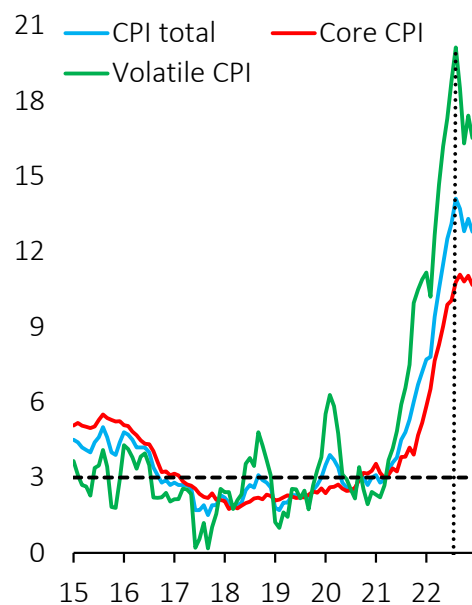
SALAR DE TARA
Región de Antofagasta

Headline and core inflation remains at very high levels.



Inflation indicators (1) (2)

(annual change, percent)

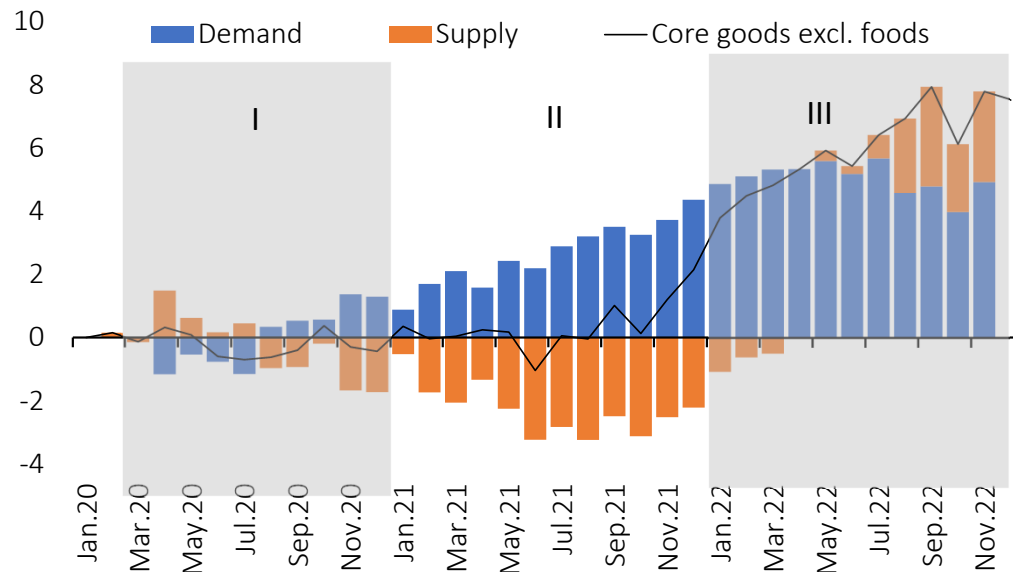


(1) Dotted vertical line marks statistical cutoff of September 2022 MP Report. (2) For details on the different groupings and their share in total CPI basket, see box IV.1 in December 2019 MP Report, [Carlomagno & Sansone \(2019\)](#), and [Economic Glossary](#). (3) Core services consider the sum of indexed, regulated and other services. Sources: Central Bank of Chile and National Statistics Institute (INE).

Both demand and supply-side factors have kept inflation high.



Structural decomposition of goods CPI w/o volátiles and excluding foods (*)
(cumulative change since January 2020, percentage points)



- The excessive increase in spending from 2021 onwards is the main cause behind the high inflation the Chilean economy faces today.
- Since the end of 2021 and in 2022 there were also problems in global supply chains, the effects of the war in Ukraine, and the stronger dollar.
- In the past few months, the adjustment of consumption and the overall economy **has begun easing demand pressures on prices.**
- Also, lower commodity prices and logistic problems resolution **have stabilized the supply pressures on prices.**

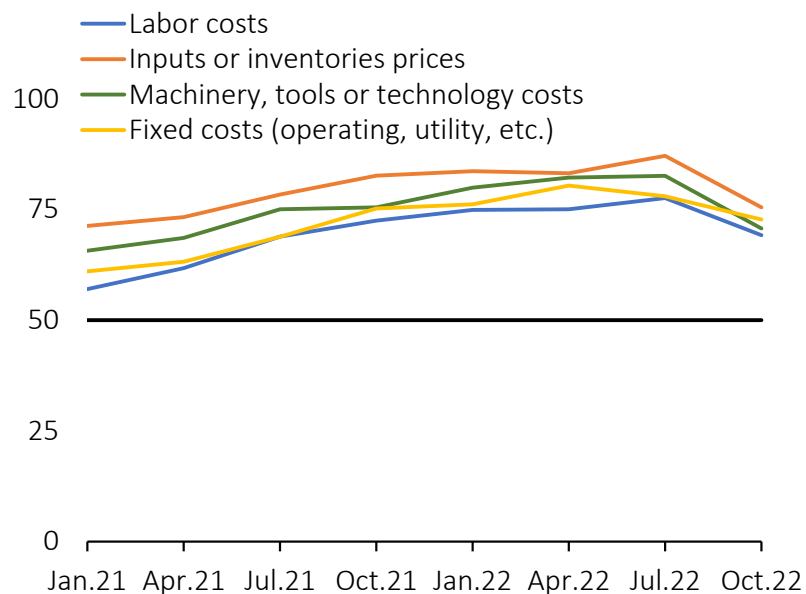
(*) For methodological details, see [Box I.1, MP Report December 2022](#). The black line shows the cumulative evolution from March 2020 to December 2022. Shaded areas denote the following periods: (I) March-December 2020, (II) January-December 2021, and (III) January-December 2022
Source: [Carlomagno et al. \(2022\)](#) based on INE, SII, and Central Bank of Chile data.

Looking forward, local firms have perceived lower cost pressures and the exchange has appreciated somewhat while remaining weak in historical terms.



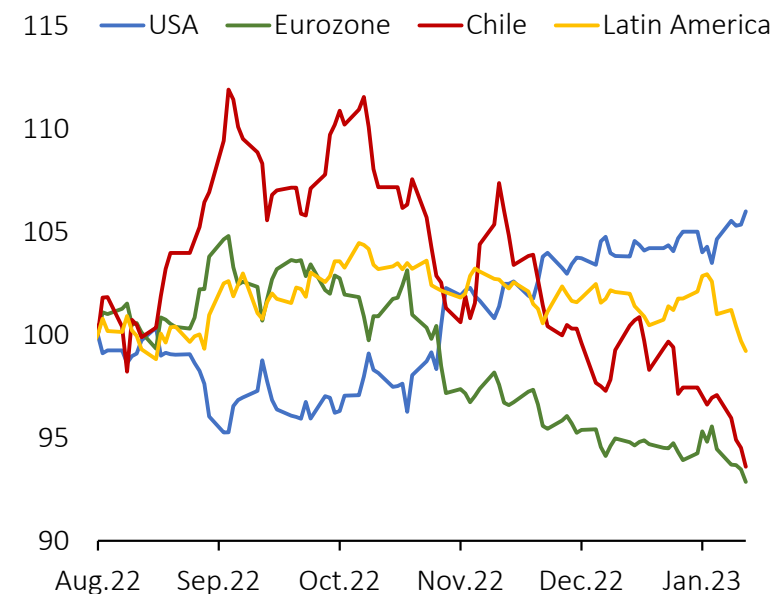
EPN: Firm's perception on evolution of costs in the past three months (1)

(diffusion index)



Currencies (2) (3)

(index, 31.Aug.22=100)



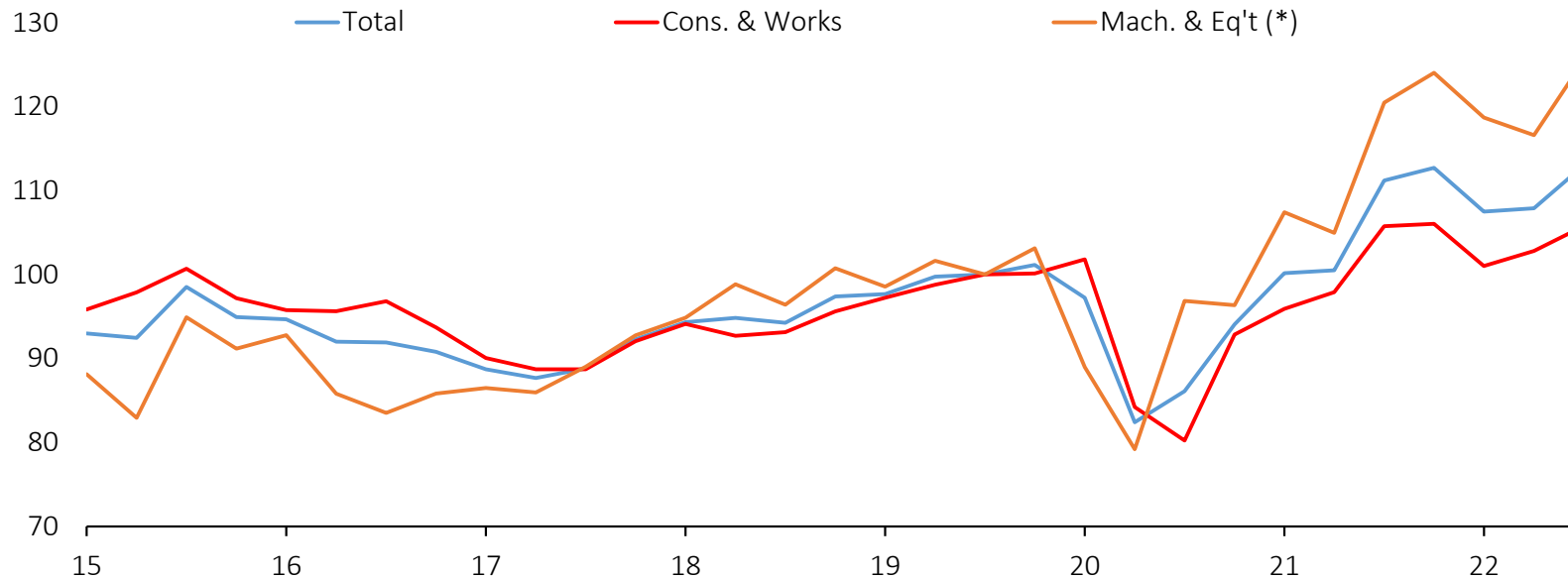
(1) Value above (below) 50 indicates a higher share of costs increasing (decreasing) responses. Responses weighted by firm size. Weighting by size incorporates the economic importance of the firms in the index, giving greater weight to the responses of firms with greater participation in value added. (2) Considers movements since the statistical closure of the September MP Report (31 August). (3) For Latin America, the simple exchange rate average of Brazil, Mexico, Colombia, and Peru. Sources: Central Bank of Chile and Bloomberg.

Investment exceeded expectations in the third quarter, although it was concentrated in some specific sectors.



Investment

(index, 2019Q3 = 100, seasonally-adjusted)



(*) Includes the following categories: Other transportation vehicles, Engines and turbines, Pumps and compressors, Steam boilers, Electronic communication devices, Computer equipment, and Medical devices.

In 2021, it accounted for almost 23% of nominal imports of capital goods.

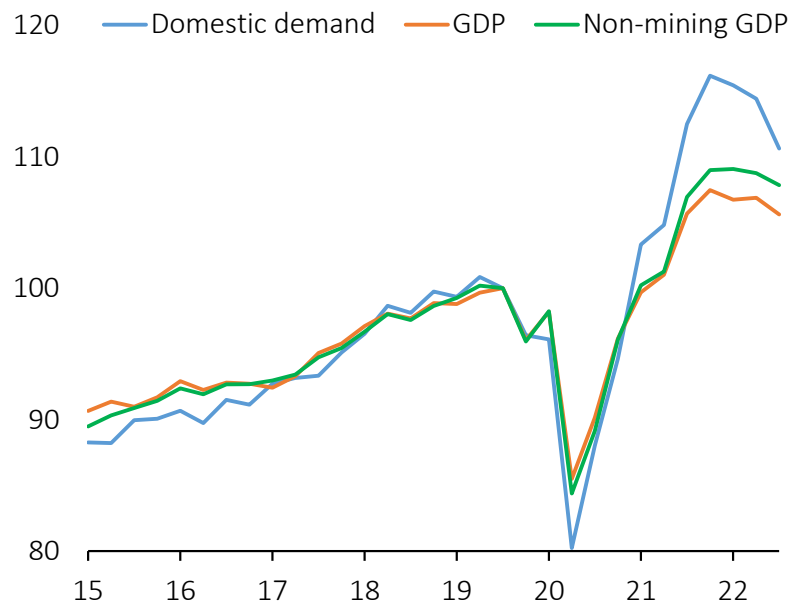
Source: Central Bank of Chile.

Demand-side pressures have also moderated.



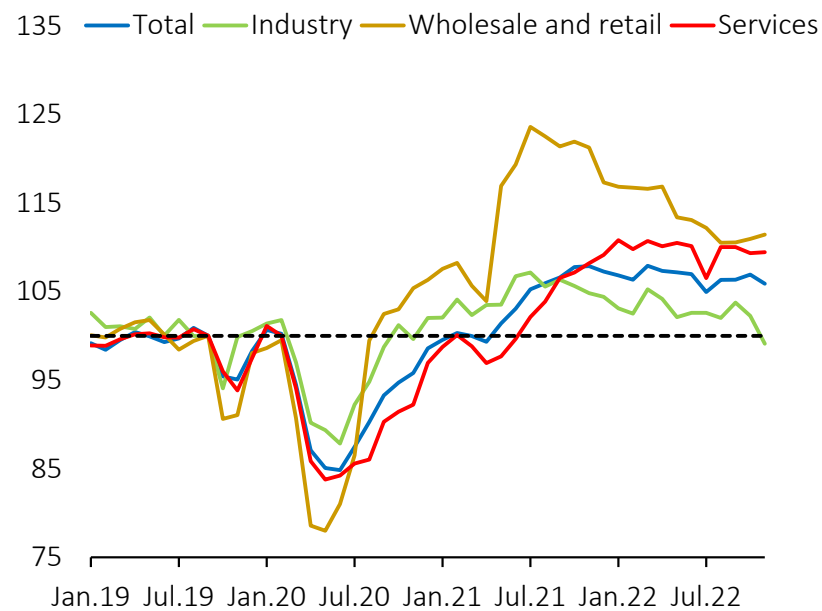
Activity indicators

(index, 2019Q3 = 100, seasonally-adjusted)



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(index, September 2019 = 100, seasonally-adjusted)



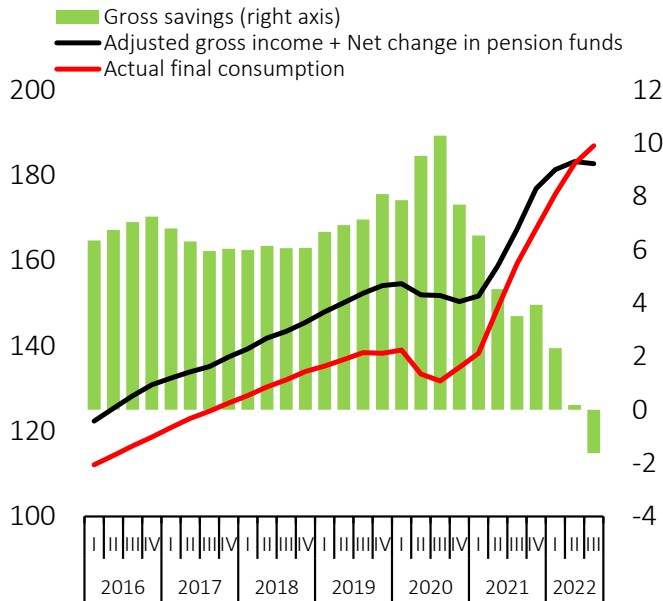
Source: Central Bank of Chile.

Consumption has remained above disposable income, generating negative savings that have gradually depleted household's liquid assets.



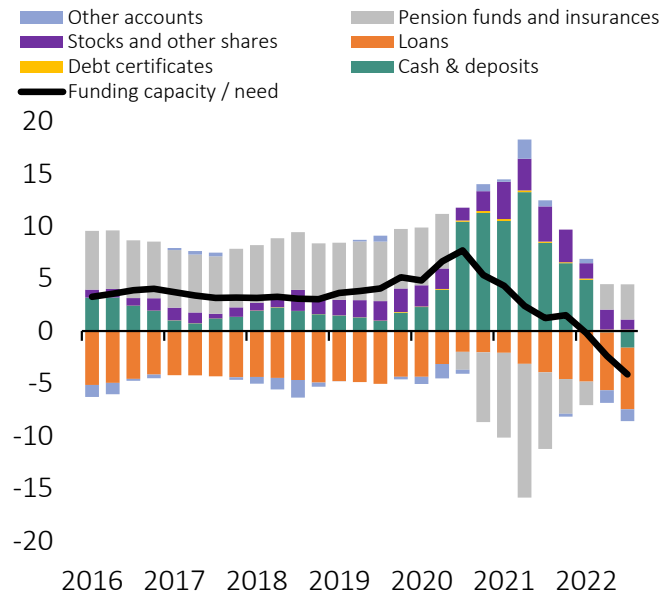
Savings, consumption, and disposable income (1)

(moving annual sum, trillions of CLP; percent of GDP)



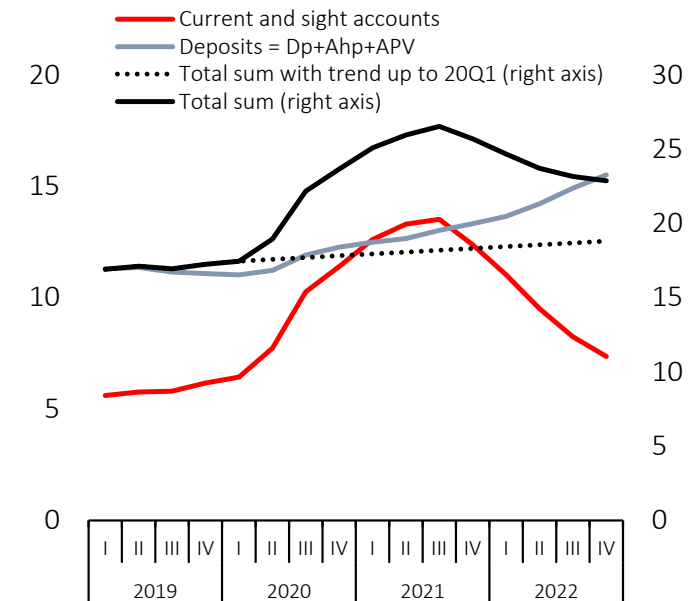
Funding needs (Curr. Acc. – households)

(percent of GDP, moving annual sum)



Personal balances (2)

(12-month percent of GDP, quarterly)

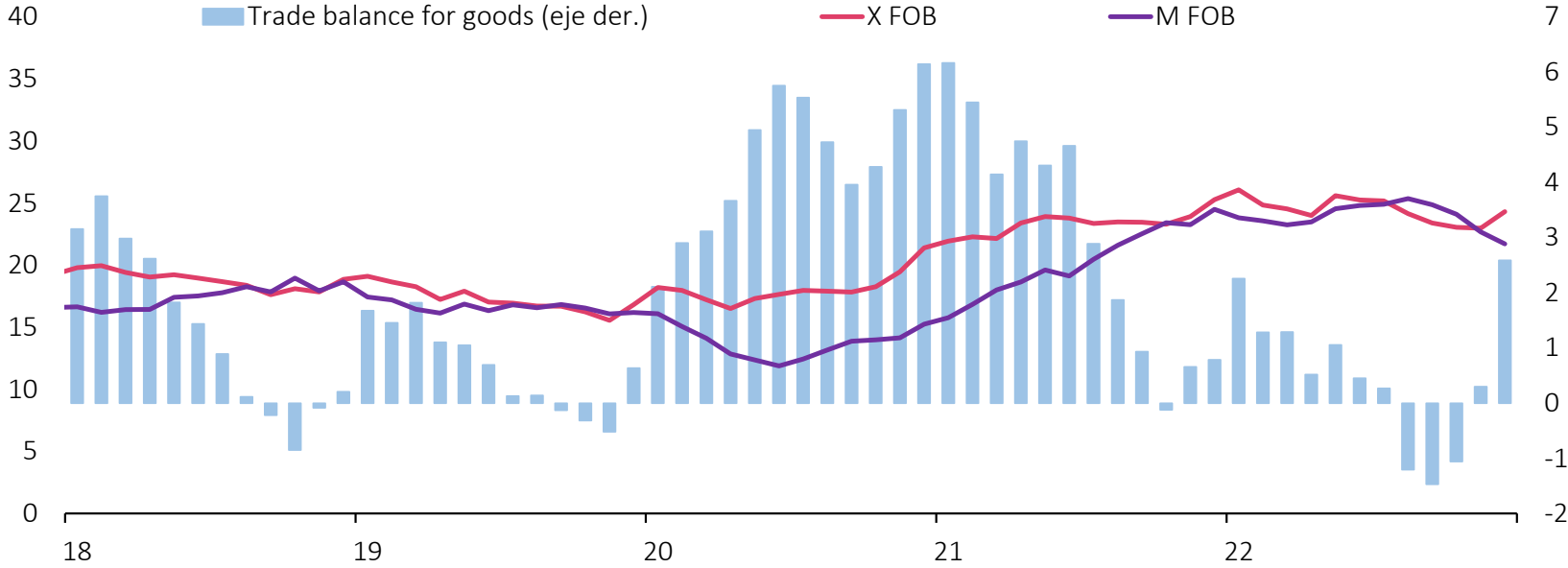


(1) Adjusted Gross Income: Gross income plus accounting adjustment, represents the maximum amount that households can afford to consume, and it will always be greater than their gross disposable income. Gross savings = Adjusted gross income + change in pension funds – actual final consumption. (2) Components of monetary aggregates. Dp: Term deposits; Ahp: Term Savings Deposits; APV: AFP voluntary savings quotas. Data as of Q4: December MP Report GDP projection. Current accounts and sight accounts, and term deposits corresponding to individuals. Breakdown data for people available from 2019. Source: Central Bank of Chile.

Trade balance for Q4 improves substantially through lower consumption imports, suggesting an undergoing current account (and savings/investment) rebalancing.



Trade balance for goods
(billions of dollars, moving quarters)

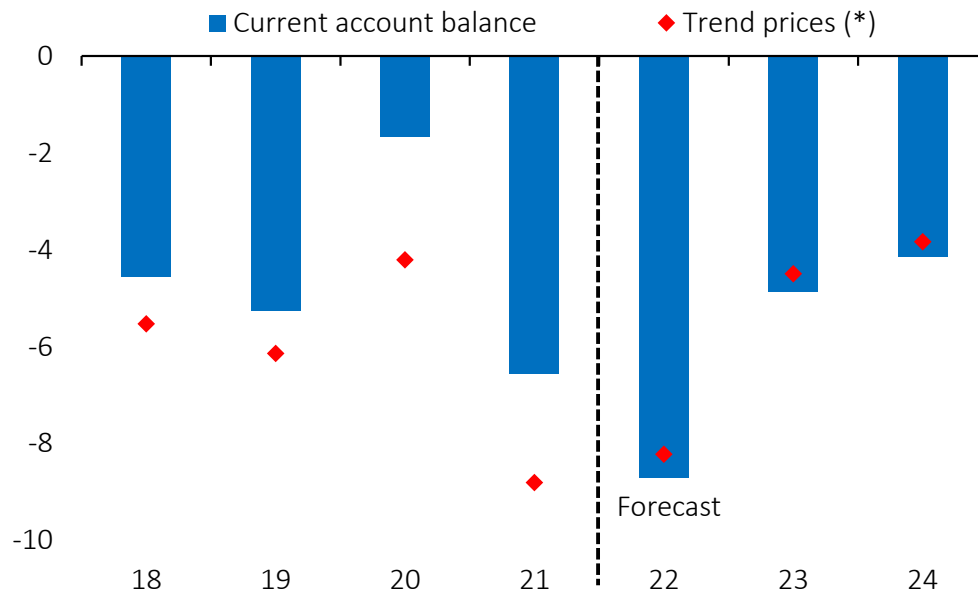


Source: Central Bank of Chile.

The medium term forecast considers a narrowing of the current-account deficit.



Current account of the balance of payments
(percent of GDP, last twelve months)



The current-account deficit will narrow in the coming quarters:

- ➔ As the economy gradually restores balance between savings and investment.
- ➔ Lower transportation costs will also play a part.

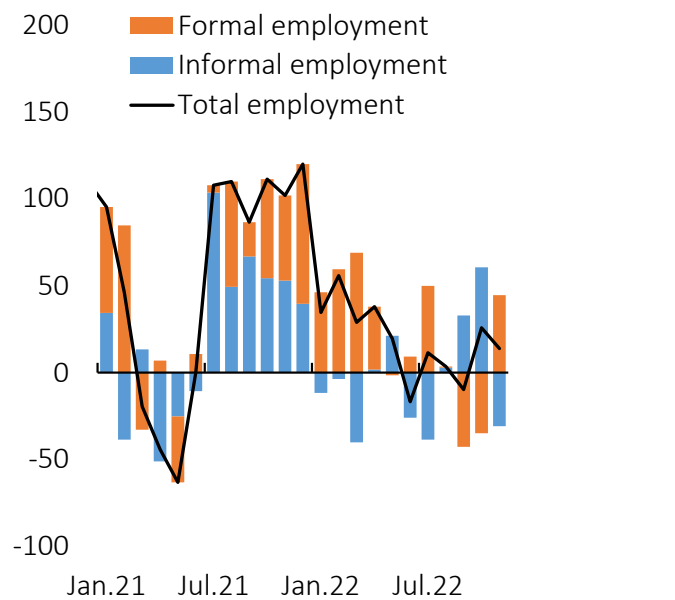
(*) For details, [see Economic Glossary](#).

Source: Central Bank of Chile.

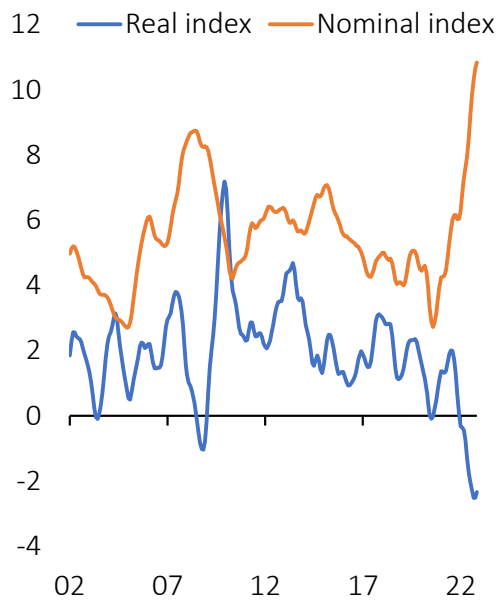
Several indicators point to a cooling labor market. Job creation has softened, and real wages are declining.



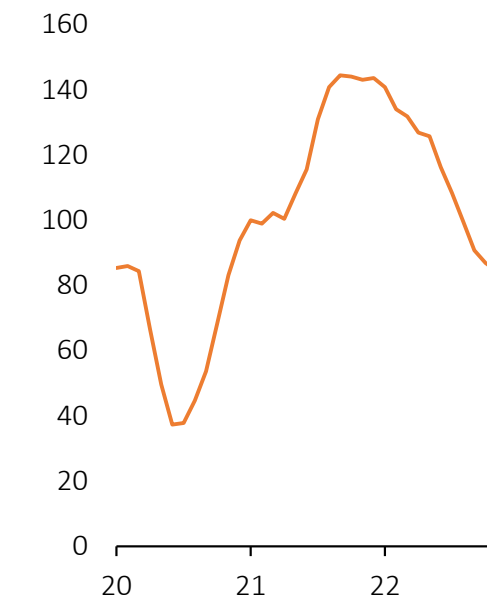
Formal and informal employment
(moving quarter/moving quarter change, thousands)



Wage index
(percent, annualized quarterly velocity, moving annual average)



Job Openings (IALI)
(index, January 2021 = 100; moving 3-month average)

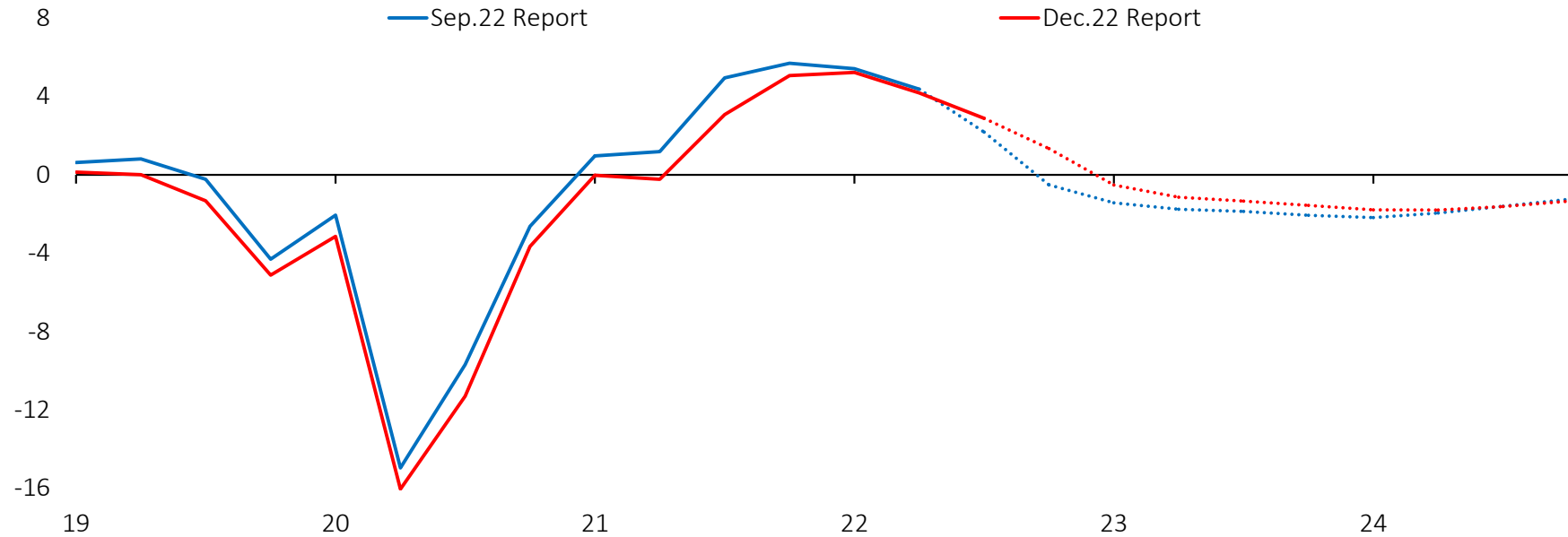


Sources: National Statistics Institute and Central Bank of Chile.

This is consistent with the expected normalization of the output gap.



Activity gap (1) (2)
(level, percentage points)



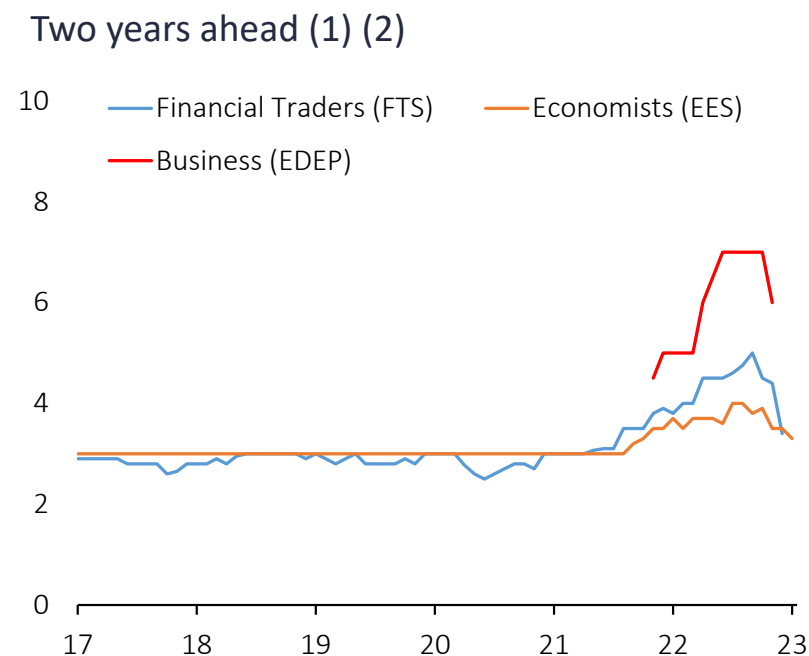
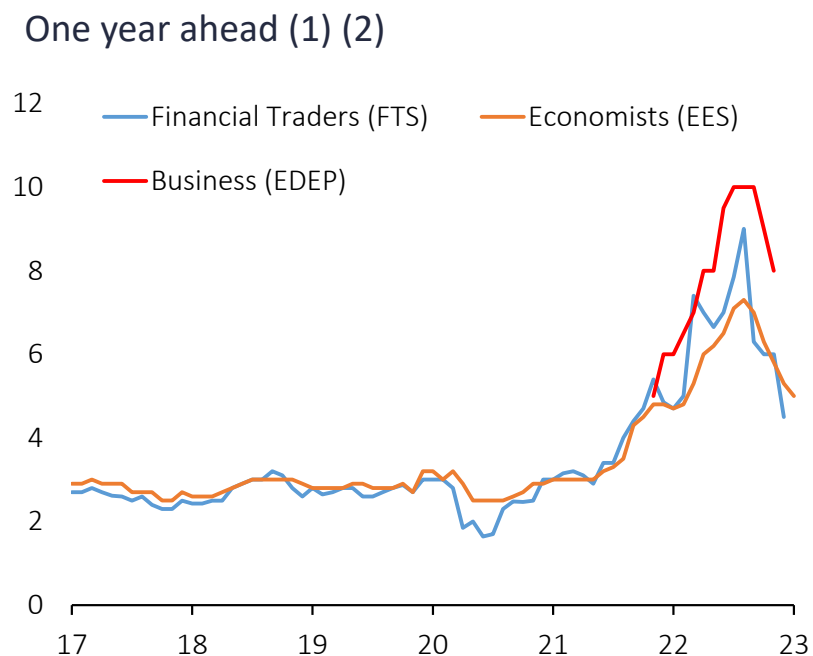
(1) Dotted lines show projections. (2) Projection uses structural parameters updated in the MP Report of December 2022 (trend) with methodological revision of potential GDP.

Source: Central Bank of Chile.

Although inflation expectations remain high, there has been some moderation alongside the observed macroeconomic adjustment.



Inflation expectations (annual change, percent)



(1) Median responses are shown. (2) Financial Traders Survey uses the survey for the first two weeks of each month through January 2018. From February 2018 onwards, it considers the last survey published in the month. In the months with no survey published, the latest available survey is used.

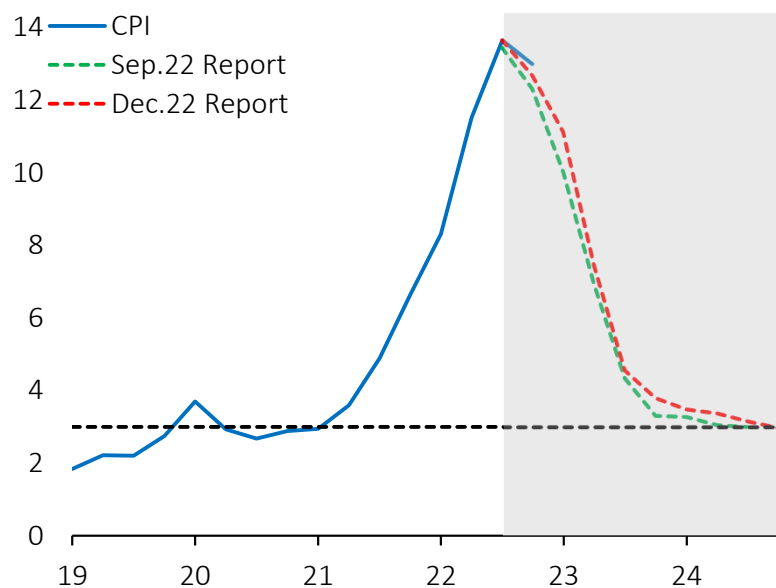
Source: Central Bank of Chile.

The central scenario considers that headline inflation will continue to decline and will return to the 3% target by the second half of 2024. Core inflation will decline more slowly and will reach the target by the end of the same year.



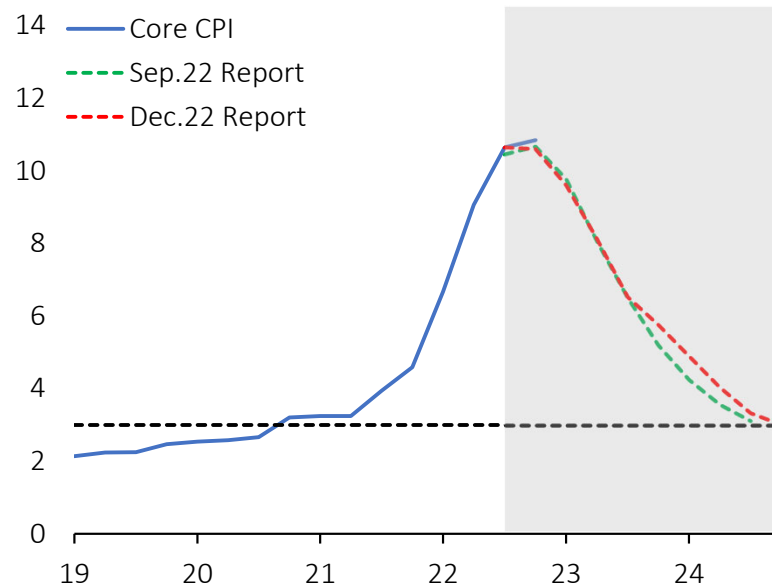
Headline CPI inflation forecast (*)

(annual change, percent)



Core CPI inflation forecast (excludes volatiles) (*)

(annual change, percent)



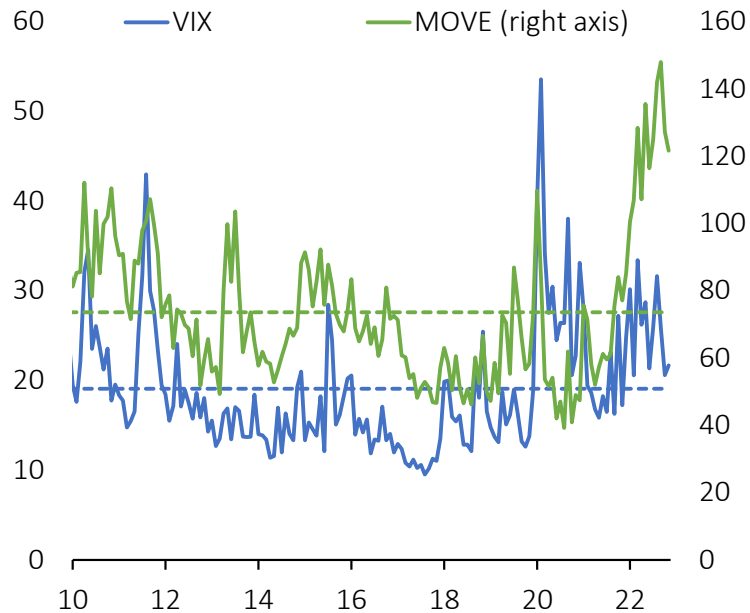
(*) As from the fourth quarter of 2022, indicators correspond to forecasts (dashed lines).

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

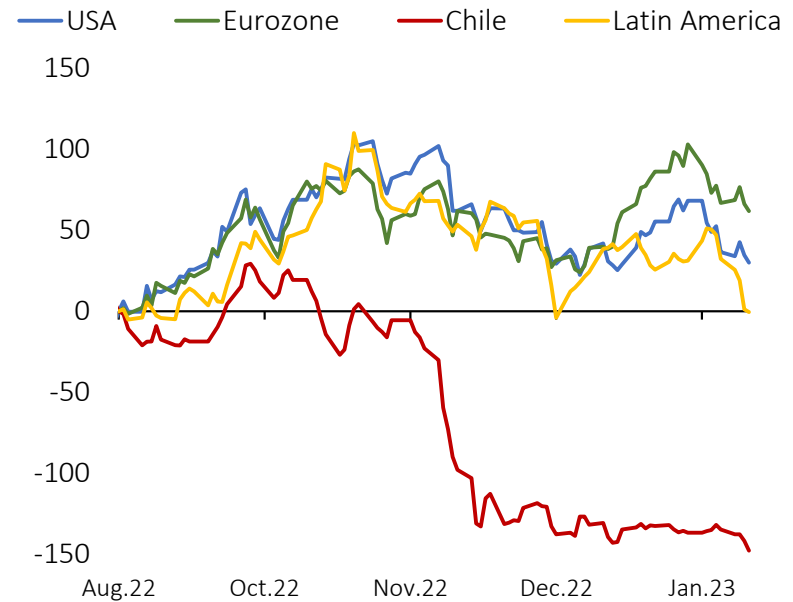
The fixed income market in Chile has remained resilient in spite of sustained global financial volatility.



Global Volatility (1) (2)
(indexes)



Yields on 10-year local currency bonds (3) (4)
(difference with respect to 31.Aug.22, basis points)



(1) Dashed horizontal lines show historical averages of each index between 2010 and 2022. (2) The VIX index measures implicit volatility in one-month U.S. S&P500 options. The MOVE index measures implicit volatility in options on the U.S. Treasury bond with different durations at one month. (3) Considers movements with respect to statistical cutoff of September MP Report (31 August). (4) For Latin America, the simple average of Brazil, Mexico, Colombia, and Peru is used.

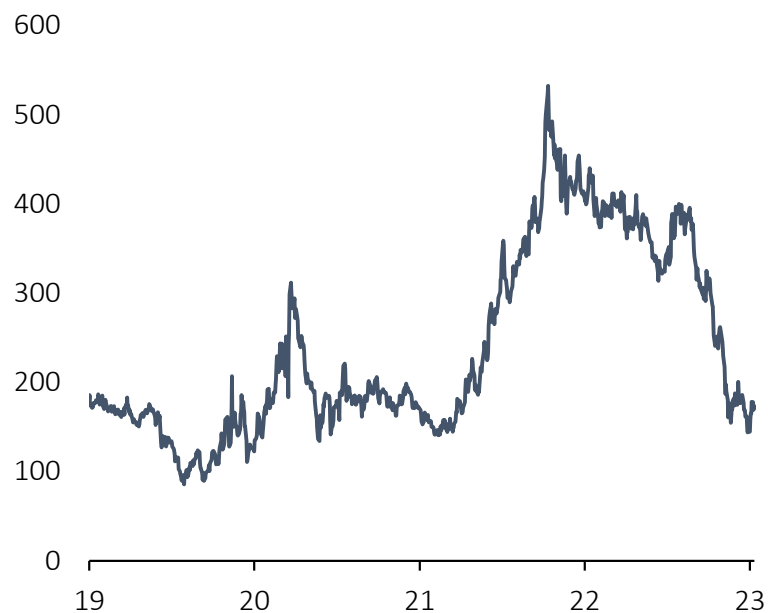
Sources: Central Bank of Chile and Bloomberg.

Domestic risk premia have abated in local fixed income markets.



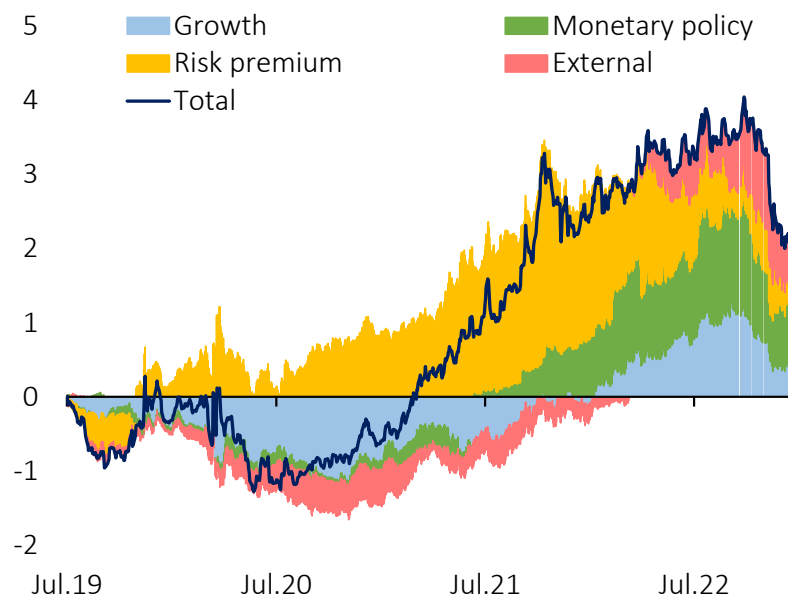
Ten-year BTP-UST spreads

(basis points)



Structural decomposition of 10-year zero rate (*)

(percentage points, accumulated since 1 July 2019)

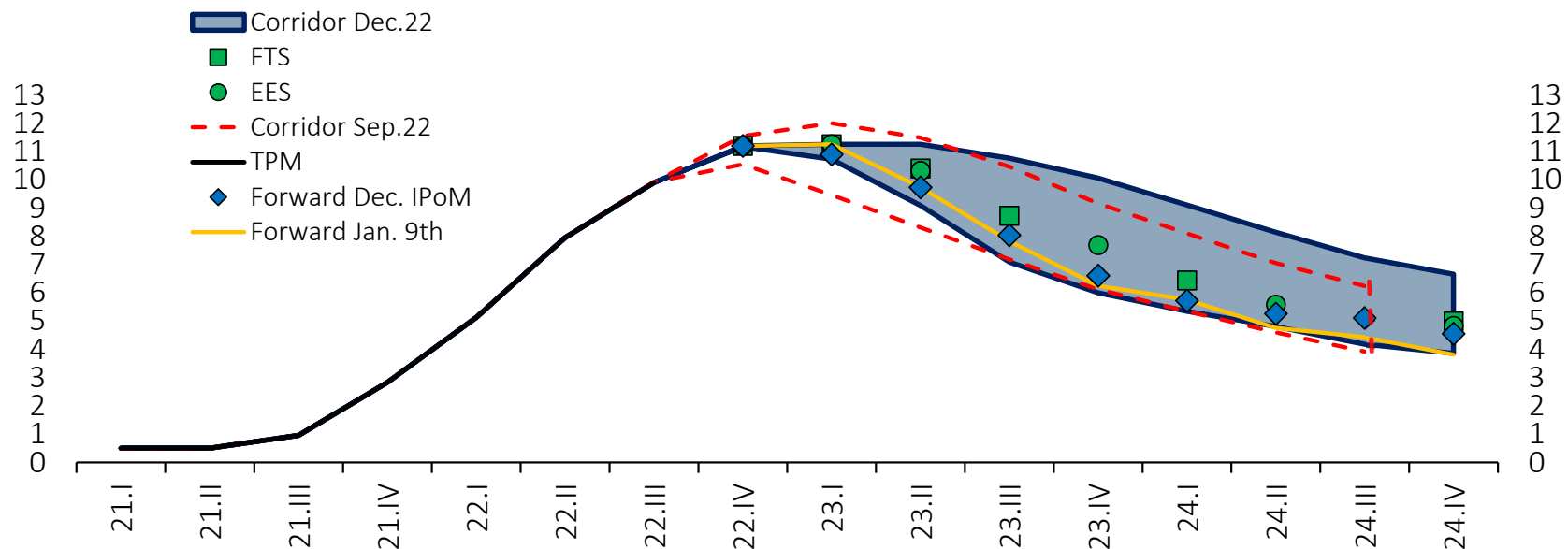


(*) Historical decomposition of the long rate from a BVAR based on the identification strategy proposed by [Eterovic and Eterovic \(2022\)](#), incorporating an external block. The exogenous block encompasses all US shocks (monetary policy, growth, risk aversion and pure risk), which have been added for simplicity. Source: Central Bank of Chile based on RiskAmerica.

The outlook for inflation will determine the timing and speed of a potential monetary policy shift.



MPR corridor (*)
(quarterly average, percent)



(*) The corridor is constructed by following the methodology of [Box V.1 of the March 2020 MP Report](#) and [Box V.3 of the March 2022 MP Report](#). For further details, see methodological note ([figure II.1, chapter II, IPoM December 2022](#)).

Source: Central Bank of Chile.



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