



# Development of Chilean Markets

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# Market Conditions: Monetary Policy

- Countries that have voluntarily adopted a free-floating exchange rate regime have reduced inflation and have experienced lower growth volatility\*.
- Since 1999 the Central Bank of Chile (CBC) has adopted a free-floating regime. Despite the FX flexibility, the CBC can intervene in the market under exceptional circumstances.
- In August 2001 the CBC adopted an inflation target regime: 3% with a range  $\pm 1\%$  in an horizon of 24 months. This change reinforced the credibility of monetary policy as it has One objective → One instrument
- Since 1999 we have intervened only four times, selling or buying IR.

(\*) IMF (2004b), World Economic Outlook, Washington, DC.



# Market Conditions: Monetary Policy

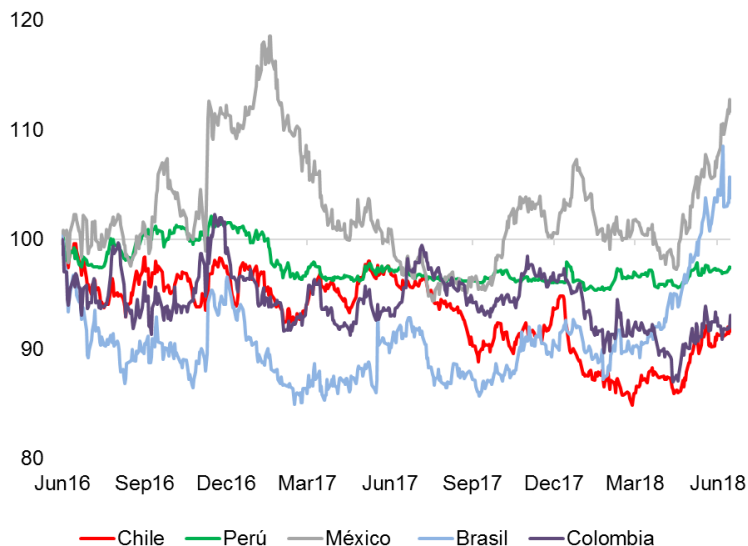
- The free floating exchange regime usually adds more volatility to the CLP, especially during scenarios of international shocks, and of course when there are commodities shocks (we are a commodity exporting country). But at the same time, with inflation anchored, it reduces volatility in the interest rate (yield curve).
- Due to our condition as a commodity exporting country, combined with our Monetary Policy framework, our currency is more volatile than others, particularly during periods of financial stress. But, this doesn't impact the credibility of the CBC in its ability to conduct Monetary Policy.
- It is also relevant that long term rate volatility is lower compared to other rates in the region.



During last two years we have observed that the Chilean peso (CLP) has had a similar trend to its peers. Nevertheless, the local rate responds like others during some events, and in general has a more stable trend.

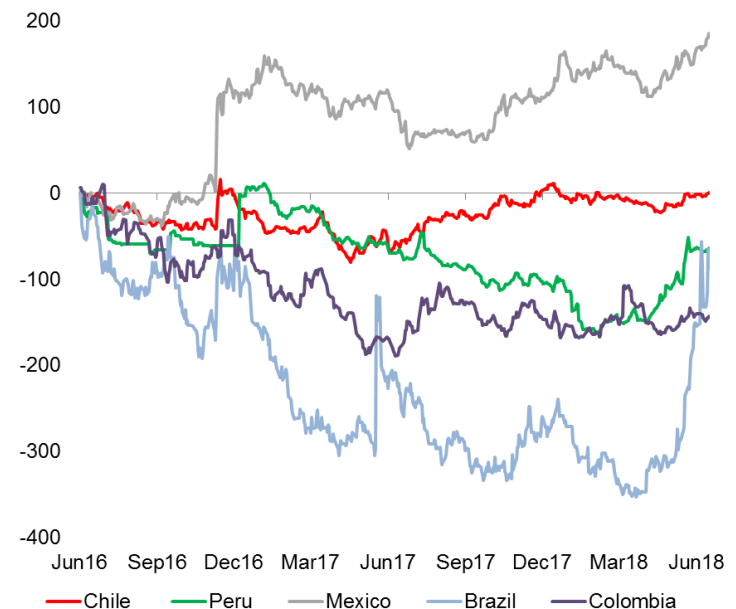
### Latam Currencies

(basis point, 100=June2016)



### 10 year rates Latam

(basis point, 100=June2016)



Source: Bloomberg.

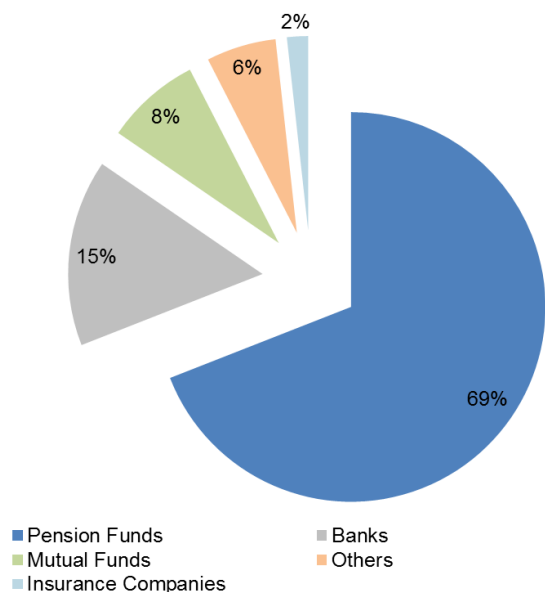


# Demand and Liquidity of Fixing Markets

Pension funds are the main investors in benchmark bonds. Since their strategy is to “buy and hold”, this affects the supply and liquidity of these instruments. Despite the fact that trade volume has increased in last years, it is still lower than the volumes in others markets of the region.

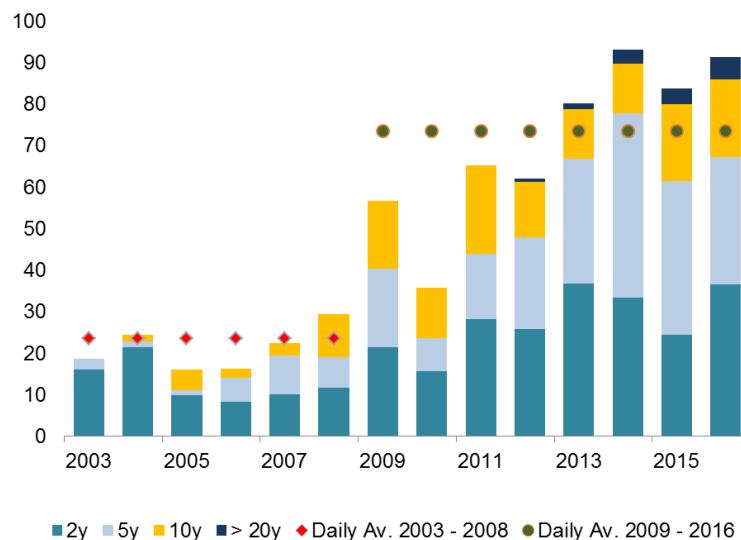
## Demand for Benchmark Bond Market (\*)

(December 2016)



## Daily Average of Trade Volume of Nominal Bonds

(Mill. US\$)



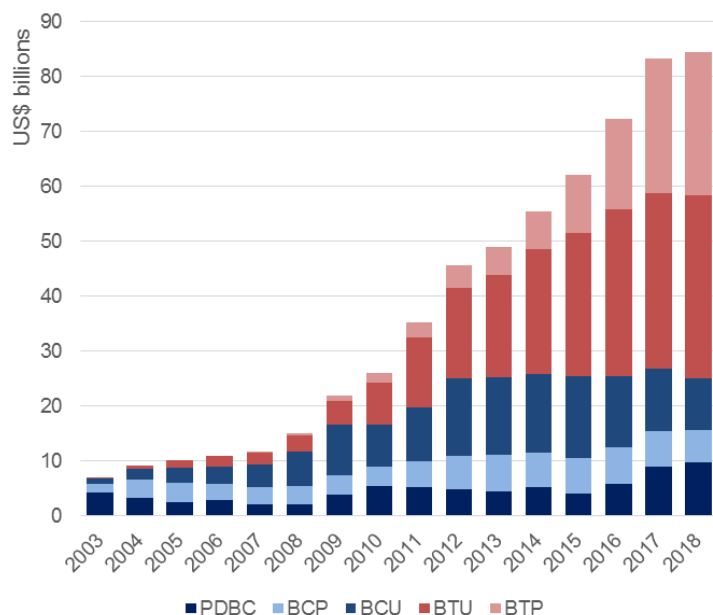
(\*) Include Government and Central Bank bonds.

Source: Central Bank of Chile, Bolsa Comercio Stgo, Central Securities Depository.

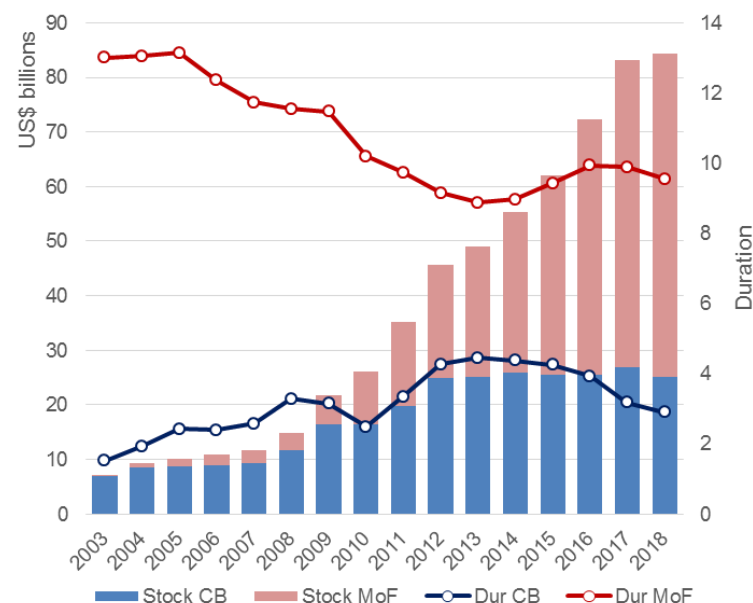


# Benchmark Bonds in the Chilean market

## CB/MoF instruments stocks



## CB/MoF stock-duration



BCP: Central Bank Bond in CLP. BCU: Central Bank Bond in UF (inflation linked bond). PDBC: Central Bank Bill in CLP. BTP: Ministry of Finance Bond in CLP. BTU: Ministry of Finance Bond in UF (inflation linked bond).



# The MoF and CB agenda

The MoF and CBC as Fiscal Agent have implemented an agenda focused on improving the competition and liquidity of the domestic fixed income market since 2014. This includes the following:

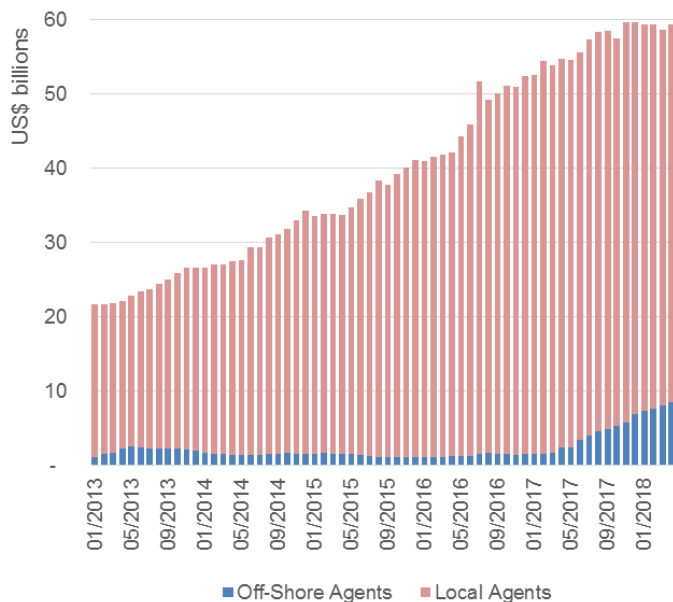
- An increase in the initial issue amount of the benchmark in the primary markets.
- Tax simplification for interest payments (capital gains tax exemptions).
- Adjustment to the MoF bonds program in order to switch out the out of market bonds and to increase the stocks of current benchmark bonds (CLP/UF in 5, 10, 20 and 30 years).
- Incorporation of the local bonds in Euroclear.
- Book building by issuing simultaneously with local and international investors.
- MoF local bonds incorporated as eligible collateral in OMOs by CBC.



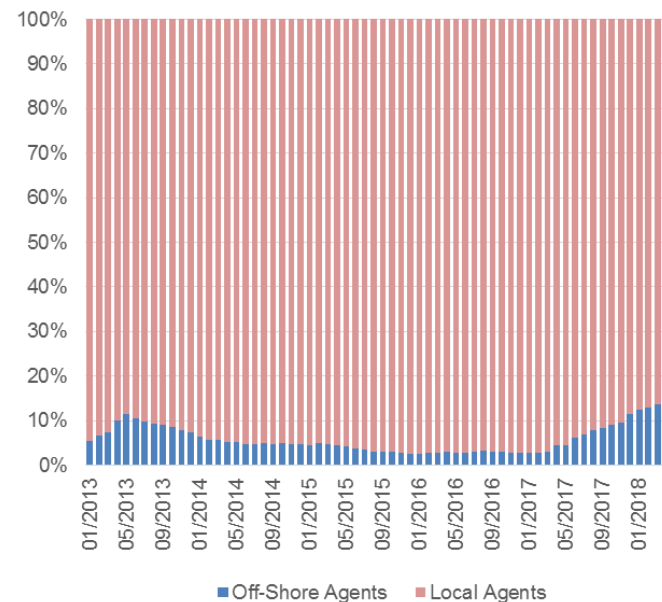
# Chilean bonds (MoF) participation in international index (GBI)

In February 2017 the bond issued through Euroclear was included in GBI Emerging Market Bond Index. The participation of Chile (MoF) in the index increased from 0.10% to 2.58% as a result.

## MoF stock



## MoF market share

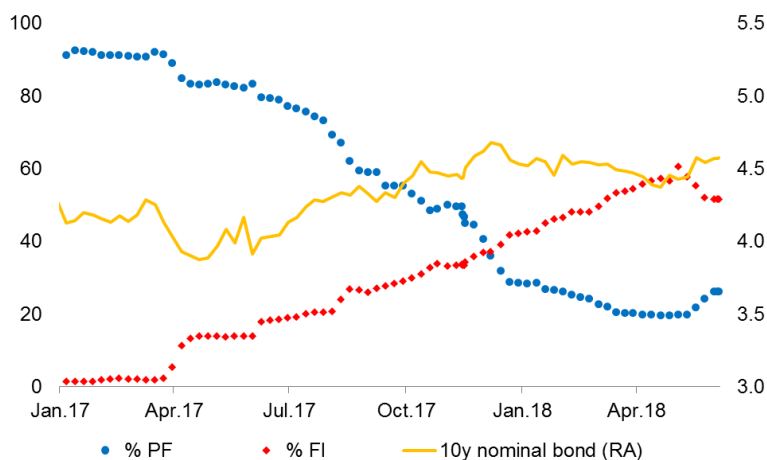


# Recent Developments

We have observed that since June 2017 foreign investors have been rapidly increasing their demand for the 10 year bond. Foreign investors currently hold 45% of the Jan'18 bond (diminishing the proportion held by Pension Funds), and 11% of the total stock of the benchmark bond. These trades have been carried out with normality, without affecting the rate's volatility.

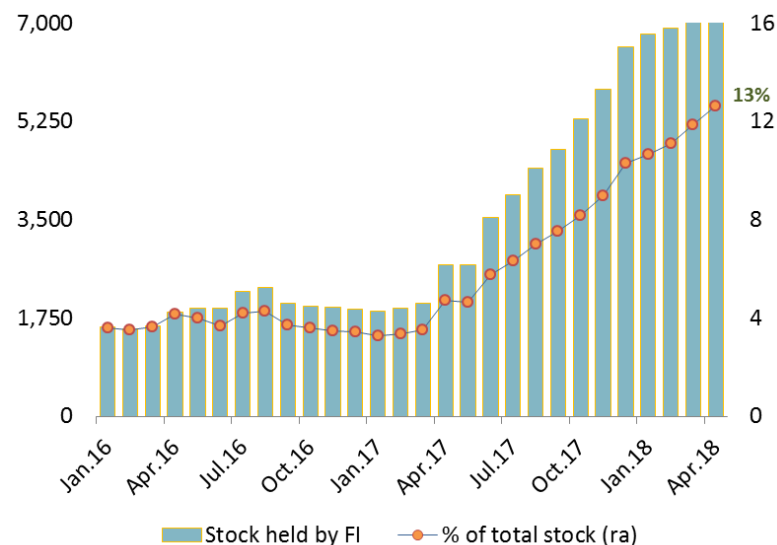
## 10 years nominal bond, Pension Fund (PF) and Foreign Investors (FI) share

(percentage)



## Stock of local bonds held by Foreign Investors

(US\$ mil.; percentage)

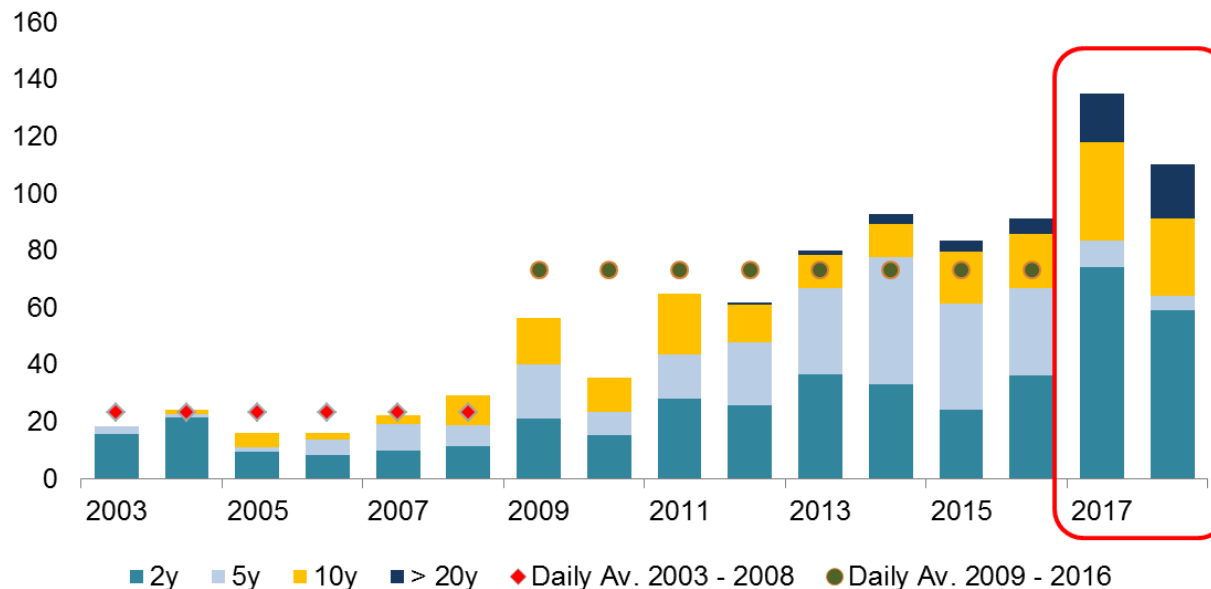


Source: Central Bank of Chile, Bolsa Comercio Stgo, Bloomberg.



**Additionally, because of the greater participation of Foreign Investors, the trade volume has increased by nearly 50%. The daily average trade volume is currently US\$ 110 million, helping to improve the liquidity of the market.**

**Daily Average of Trade Volume of Nominal Bonds**  
(mil. US\$)



Source: Central Bank of Chile, Bolsa Comercio Stgo.





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