banco central Chile

Press Release*

Wednesday, 13 October 2021

Monetary Policy Meeting – October 2021

At its Monetary Policy Meeting, the Board of the Central Bank of Chile decided to raise the monetary policy interest rate (MPR) by 125 basis points, to 2.75%. The decision was adopted by the unanimous vote of its members.

On the external front, the outlook for global activity has moderated at the margin, as a result of the constraints associated with new Covid-19 outbreaks in some economies and persistent bottlenecks around the world, which has held back growth in certain industries. This has occurred in a context of further rising global inflation. In recent days, there have been notorious increases in fuel prices, with oil rising above US$80 per barrel, that is, an increase of more than 15% since the latest Meeting. Copper has continued to trade at around $4.2 per pound. In this scenario, several central banks have adopted a less expansionary stance, as the Fed and the Bank of England have made changes in their communications and Norway, New Zealand and several emerging economies have raised their policy rates. The international financial markets show a reduced appetite for risk, considering both the aforementioned elements and the fear surrounding China's real-estate sector. This has led to interest rate increases across the board, a depreciation of a significant number of currencies against the dollar, and mixed movements in the stock markets.

In Chile, the financial markets have deteriorated much more strongly and systematically, standing at the extremes of international movements. This is explained by idiosyncratic factors, especially the change in the inflation outlook and uncertainty surrounding political and legislative issues, most importantly new withdrawals of pension funds. In the fixed-income market, interest rates rose in every category, especially in the medium and long tranches. The 10-year nominal interest rate exceeded 6.5%, a record high in over a decade. This, since early September to date, the difference with its U.S. counterpart went from around 370 basis points (bp) to near 500pb. Over the same period, the exchange rate continued to rise, accumulating a depreciation of more than 5% relative to the dollar, while the IPSA fell by around 8% and the country risk (CDS) increased by some 25pb.

Regarding activity, the August Imacec rose 19.1% annually and 1.1% monthly in seasonally adjusted terms. Trade continues to lead as the most dynamic sector, while several lagging sectors —especially service activities— have been returning to their pre-pandemic levels. This result, together with high demand, have responded to the easing of sanitary restrictions. Investment-related items have shown a significant rebound, reflecting a recovery that has become more transversal, beyond the fact that the tradable component continues to be the most dynamic. In the labor market, employment has increased in the main categories, accompanied by a fall in the rate of inactivity and unemployment, which stood at 8.5% in the June-August quarter. Still, there remains a clear mismatch between labor supply and demand, mainly among the less skilled, which has also reflected in wage increases. In this context, private expectations for this year's growth have risen further, up to 11% in the Economic Expectations Survey (EES) of October. For the years 2022 and 2023, the economic performance expectation is reduced considerably, to around 2% each. Business confidence (IMCE) is in optimistic territory, with increased hiring in the short term, although it also shows higher costs and inventory shortages. Among consumers, meanwhile, confidence shows a slight drop (IPEC), especially affected by the increase in inflation which, according to several qualitative indicators, ranks first as the economic issue of greatest concern for Chileans.

As for bank credit, consumer and commercial loans reduced their annual contraction rates in real terms, while the flow of mortgage loans has remained fairly stable. Interest rates posted new marginal increases in every portfolio. Meanwhile, the Bank Lending Survey of the third quarter shows stronger demand in most credit segments, while supply is more stable according to measured perceptions.

In September, the annual variation of the CPI rose to 5.3%, outweighing expectations, while its core part accumulated an annual increase of 4.2%, close to the forecast in the September Monetary Policy Report. The increase of recent months has affected every item in the CPI basket, reflecting inflationary pressures on both the demand and the cost side, as well as the sharp depreciation of the peso. In addition, in recent months the INE has been reinstating in its measurement the prices imputed during the pandemic. In this context, inflation expectations have risen in all horizons. In the immediate term, some measures exceed the forecasts in the September MP Report, going past 6% for the end of this year. Two years ahead, the median of the EES and of the Financial Traders Survey (FTS) has risen and remains above 3% annually.

The evolution of the macroeconomic scenario has increased the risks regarding the convergence of inflation to the 3% target within the policy horizon. Although core inflation has evolved in line with projections, the outlook for the coming months has been rising, in a context where inflation expectations two years ahead stand above the 3% target. The Board has decided to anticipate the withdrawal of the monetary stimulus, projecting that the policy rate will reach its neutral level sooner than foreseen in the September Report's central scenario. The MPR trajectory will be assessed in the next Monetary Policy Report, taking consideration of the need to prevent a more persistent increase in inflation that drives it to depart from the 3% target in the two-year horizon.

Additionally, the Board agreed to suspend the reserve accumulation program initiated last January, by virtue of the recent evolution of the financial market and the level of international reserves already reached.

The minutes of this Monetary Policy Meeting will be released at 8:30 hours of Thursday 28 October 2021. The next Monetary Policy Meeting will be held on 14 December 2021, and the statement thereof will be published at 18:00 hours the same day.

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* The Spanish original prevails.