Monday, 6 May 2024

Financial Policy Meeting – first half 2024

At today's Financial Policy Meeting, the Board of the Central Bank of Chile decided to maintain the Counter-cyclical Capital Buffer at 0.5% of risk-weighted assets, which will be enforceable as from the end of May 2024. The decision was adopted by the unanimous vote of the Board members.

On the external scenario, global financial conditions are still tight and important geopolitical risks persist. Markets reflect high sensitivity to incoming news, in a context of continued uncertainty about the start and velocity of the monetary policy normalization cycle in the United States. This has affected short-term market interest rates, which have risen in a significant number of economies. In turn, long-term rates remain high, and there are considerable risks regarding sovereign debt around the world.

In this context, the external scenario continues to be the main source of risks for local financial stability. Financial conditions for emerging economies could be significantly affected, in a scenario where external interest rates remain unchanged for a long time or increase. In such a case, an abrupt correction could occur in the prices of some financial assets, in addition to having severe effects on the most indebted agents. All this in an environment in which vulnerabilities remain in some segments of the credit markets. The non-residential real estate sector stands out, causing concern among regulators in the main economies.

The local economy has resolved the significant macroeconomic imbalances of recent years. The decline of inflation and short-term interest rates have helped normalize the financial indicators of households and firms. However, the delay in the recovery of some previously identified sectors (e.g., trade, construction, and real estate) has contributed to increase delinquency rates, which are high by historical standards, especially affecting the commercial portfolio. The cost of long-term funding has evolved in line with international macro-financial developments, affecting interest rates on mortgage loans and longer-term commercial loans. Meanwhile, the capital market depth remains at low levels.

Bank credit is performing in line with the business cycle. Commercial loans continue to contract in annual terms, mainly due to still weak demand. In the household segment, consumer lending has eased its twelve-month declines while housing loans are growing steadily in annual terms, albeit slowly from a historical perspective.

The banking system has administered the increase in credit risk by accumulating provisions and collaterals. Banking stress tests that are presented in our Financial Policy Report (IEF) of the first half, show that banks have a sufficient level of provisions and capital to withstand a scenario of severe tensions. Overall, the banking industry needs to continue to prepare to confront the challenges associated with convergence to Basel III, so it will have to further strengthen its capital base.

The Board has decided to maintain the CCyB at a level of 0.5% of risk-weighted assets, which will be enforceable as from the end of this month. This level is maintained as a precautionary measure in view of similar external uncertainty and risk balance as we depicted in our last IEF. This means that an extreme negative event is still possible, which could result in a significant drop in credit. Having a pre-established capital buffer that can be released upon the occurrence of an event of such nature, would help mitigate its impacts on the provision of credit to households and firms.

The minutes of this Financial Policy Meeting will be published at 8:30 hours of Wednesday 22 May. The next Meeting will be held on 18 and 19 November 2024 and the statement thereof will be released at 18:00 hours of the second day. For further details on the Counter-cyclical Capital Buffer (CCyB), log on to the following link.