banco central Chile

MONETARY POLICY REPORT

SEPTEMBER 2023

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The Central Bank of Chile's Monetary Policy

Money plays a fundamental role in the proper functioning of any economy. To preserve such role, the monetary policy of the Central Bank of Chile (CBCh) must protect the value of the national currency —the peso—, in its quest to keep inflation low and stable. Achieving this fosters the population's wellbeing by safeguarding their income's purchasing power and making the economy function better. When inflation is low and stable, monetary policy can also moderate fluctuations in employment and production.

The inflation target and the monetary policy interest rate (MPR)

The Bank conducts its monetary policy seeking that, irrespective of the current level of inflation, its forecast for a two-year horizon will be 3%. This is similar to the practice of other countries in the world that have, as does Chile, a floating exchange rate; this is the so-called inflation targeting scheme.

The MPR is the main instrument used by the Bank to achieve the inflation target. Its level is decided at the Monetary Policy Meeting, which is held eight times a year. In practice, the MPR is a reference interest rate to determine the cost of money and other financial prices, such as the exchange rate, and longer-term interest rates, among others. In turn, these variables affect the demand for goods and services and, thereby, prices and inflation. Monetary policy decisions take several quarters to be fully reflected in the economy, which warrants that monetary policy be made from a forward-looking point of view, having as its primary focus the inflation projection two years ahead, and not just today's inflation.

Communication, transparency and the Monetary Policy Report

Since the Central Bank makes its monetary policy decisions autonomously, it must constantly account for them and their results to the general public. This is so not only because it is a government agency within a democratic society, but also because a credible monetary policy, understood by the people, helps to keep inflation low and stable. Through the Monetary Policy Report (MP Report), the Bank communicates to the general public its view of the recent evolution of the economy, its projections for the coming years and the way in which, in this context, it will conduct monetary policy in order to meet the inflation target.

The MP Report is published four times a year (every March, June, September, and December) and is put together by a team of around 60 persons.

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*/ This Report incorporates the monetary policy decision of 5 September. For the central scenario construction purposes, the statistical cut-off date is 30 August. This document was originally written in Spanish. In case of discrepancy or difference in interpretation, the Spanish version prevails.

SUMMARY

Broadly speaking, the macroeconomic scenario has evolved in line with forecasts in the June Report. Inflation has continued to fall, although it is still high, in a context where activity and demand have continued to advance in their adjustment process, cost pressures have been reduced and two-year inflation expectations stand at 3%. This has allowed the Board to reduce the Monetary Policy Rate (MPR) by 175 basis points (bp) since July, to 9.5%. Although the decline in inflation is a global phenomenon, the outlook differs from one country to the next. Thus, while in some economies monetary policy is becoming less contractionary, in others a more prolonged tightening than anticipated is foreseen, particularly in the developed world. These divergences have been permeating global financial markets, with opposing movements in interest rates and depreciations in an important group of currencies, including the Chilean peso. The central scenario projections contain few changes with respect to our last Report. GDP will vary between -0.5 and 0% this year, to resume positive growth rates in the two subsequent years. Private consumption has stabilized and its projection is maintained, while investment is expected to contract somewhat less than expected this year. Headline inflation is expected to continue to decline, reaching 3% in the second half of 2024. Core inflation would do so in early 2025. If the central scenario projections of this Report materialize, in the short term the MPR will continue on the path outlined in the July Meeting. In any case, the magnitude and timing of the process of MPR reductions will take into account the evolution of the macroeconomic scenario and its implications for the inflation trajectory. Although the most extreme risk scenarios have been losing relevance, the process of inflationary convergence continues to pose significant challenges.

Inflation has continued to decline, but remains at high levels. In July, the annual variation of both headline and core CPI was 6.5% and 8.5%, respectively, below their peaks of 2022. In recent months, inflation has been falling somewhat faster than expected, which is due to the behavior of the core part of goods inflation. This is coupled with the decline in volatile components, especially energy. Services inflation has been slower to decline.

Inflation has declined in a context in which the cost pressures seen in previous quarters have been receding. Beyond its recent increase, the nominal exchange rate is well below its levels in the middle of last year, which has been reflected in the evolution of goods inflation. Other cost factors have also contributed. Transport fares have decreased, global value chains have been reinstated, and external prices have come down after the rises they recorded at the outbreak of the war in Ukraine.

One key factor behind the decline in inflation has been that macroeconomic imbalances have shown progress in their resolution. This process has continued as anticipated in previous reports. Discounting seasonality, non-mining GDP declined 0.5% in the second quarter with respect to the first. At the sector level, there was mixed performance. The dynamism of several service sectors contrasts with the poorer performance of wholesale and retail trade and construction, among others. This is in line with the outlook on the demand side, where goods consumption has declined the most, in contrast with the resilience of the services component. July's Imacec showed a more positive performance of activity, although partly associated with temporary factors that favored personal services and electric power generation, among others.

The fall in private consumption has been moderating throughout the year. After a sharp contraction early this year, the second quarter saw a much more stable performance, in line with projections in the June Report. Partial third-quarter indicators —such as retail sales and imports— confirm this trend. The durable goods component continues to accumulate the largest drop after its 2021 peak, although its level rebounded slightly in the second quarter.

Consumption behavior occurs at the same time as labor income has been stabilizing. Job creation remains constrained, with weak expectations about its future performance. Unemployment has oscillated between 8.5% and 8.8% for several months, amid the recovery shown by the labor force. Real wage growth has been increasing, influenced by the increase in the minimum wage and the impact of lower inflation.

At the margin, gross fixed capital formation (GFCF) showed an improvement in its tradable component, although its overall performance remains poor. In its seasonally adjusted series, investment in machinery and equipment grew 3.6% quarter-on-quarter, a result that came from several sectors, although with a higher incidence of mining and energy. At the same time, the construction and works component has been contracting since the end of 2022, in line with expectations.

Regarding bank credit conditions, the MPR cuts have begun to be transmitted to market interest rates. Interest rates on commercial loans show declines, although their levels differ depending on size and/or risk rating (Box I.3). Thus, the available data suggest that monetary policy transmission channels are operating as usual.

The external scenario continues to be marked by high uncertainty. On the one hand, financial risks continue to be present, amid expectations that monetary policy will remain contractionary in developed economies and the beginning of tightening cycles in several emerging economies. Inflation has continued to ease globally. However, the outlook varies across countries, which has influenced the actions of monetary policymakers (Box I.1). Thus, while the U.S. Federal Reserve has not ruled out the possibility of further rate hikes —the same as in Europe and the U.K.—, several central banks in emerging economies have already begun a process of cuts, Chile's included. This keeps the risks associated with the permanence of high interest rates in the main economies latent. In addition, there are those linked to the delicate situation of regional banks and the implications of the credit rating downgrade in the U.S., among others.

Meanwhile, doubts about the performance of the Chinese economy have been intensified in recent months. Second-quarter activity data showed a somewhat stronger-than-expected slowdown, following the temporary boost from the lifting of Covid-related sanitary restrictions. Several short-term fundamentals appear weak. Among them, its complex real-estate situation, the deterioration of household and business confidence and the restructuring of world consumption towards services at the expense of goods. These elements interact with more structural vulnerabilities that have escalated in recent years, such as the high level of indebtedness of local governments and firms. All this in a scenario where the space for expansionary macroeconomic policies is narrower than in the past.

In this context, interest rates have reacted with rises in developed markets and mixed movements in emerging ones, a global appreciation of the dollar and, in recent weeks, a reduction in risk appetite. The Chilean peso has depreciated significantly from June to date. This is explained both by changes in the interest rate differential and by the greater risk aversion associated with incoming news, such as the situation in China, the fiscal outlook in the U.S. and the uncertainty about the global disinflation process. Other local financial variables have performed more favorably, such as the stock market and risk premiums, amid lower internal uncertainty.

Projections

The central scenario projections are largely unchanged from the June Report. Headline inflation will continue to decline and is expected to close the year at 4.3% annually (4.2% in June), and to converge to 3% in the second half of 2024. This projection takes into account the somewhat-lower-than-expected figures of recent months —particularly in June—, the impact of the recent peso depreciation, and higher external fuel prices. These last two elements help explain a slightly higher average inflation during 2024. The central scenario assumes that the real exchange rate (RER) will remain around its current levels over the projection horizon.

Core inflation will end 2023 at 6.3% annually (6.5% in June), reaching 3% in early 2025. The decline in the services component will be slow, due to the impact of indexation of wages and prices. In the goods component, beyond the effect of the peso depreciation, its decline will continue to be determined by more moderate demand pressures and the easing of external and internal cost factors.

In activity, revisions are few and focus on the mining sector. Expected growth for this year is between -0.5% and 0.0% (-0.5%/0.25% in June). This projection takes into account the impact of the operating problems that have affected mining production in recent months, whose programmed increases throughout 2023 will become effective as of the fourth quarter of the year. Non-mining activity, meanwhile, will resume positive quarterly variations as of the end of this year, and will then gradually approach an expansion rate consistent with its potential level. Thus, for 2024 and 2025, total GDP expansion ranges of 1.25%-2.25% and 2.0%-3.0%, respectively, are expected.

This projection considers that the activity gap will continue to close in the remainder of the year, in line with the necessary conditions for the convergence of inflation. The evolution of the local economy has led to a narrowing of the activity gap, after several quarters of positive values. Towards 2024 and 2025, the gap is still projected to be negative, which will allow completing the inflationary convergence process within the policy horizon.

In the coming months, private consumption will remain near its current levels. For 2023, private consumption is expected to fall by 4.9% (same as in June), mostly due to the sharp decline of the first quarter. For 2024 and 2025, increases of 1.7% and 1.9% are projected, similar to previous projections.

For the medium term, the expected evolution of private consumption is consistent with a gradual recovery in real income and financial conditions becoming more favorable as the process of MPR cuts progresses. Real wages will continue to rise in the near future, in a context where the labor market will behave in line with the business cycle. In turn, the transmission of monetary easing to interest rates will gradually alleviate the financial burden on households.

Total GFCF will contract 1.2% this year and 0.6% next year. The weakness will be particularly visible in the construction and works component, as has been observed for the last few quarters. In any case, the difference in projections for 2023 compared to the estimate in June (-3%) stands out, mainly due to a better performance of machinery and equipment during the second quarter.

Towards 2025, GFCF is projected to resume positive growth rates. That year, growth of 2.4% is anticipated for this part of spending (2.2% in June). This will occur amid easing domestic financial conditions, which will support the positive impact of the reduction in local uncertainty that has been observed since the end of last year. The Capital Goods Corporation's Survey reported an increase in projected investment amounts for 2024 and 2025, especially in mining, although they are still lower than in the previous two years.

The current account deficit will decline further this year, in line with the gradual recovery of private savings. Cumulatively over twelve months, this deficit fell to 4.5% of GDP in the second quarter (6.6% in the first quarter). The successive restoration of the savings-investment balance will cause the current account deficit to reach 3.4% of GDP in 2023 and to stand at 4% in the next two years.

The Chilean economy will continue to receive a modest impulse from abroad. As in the June Report, trading partners' growth is forecast to average 2.8% between 2023 and 2025. This takes into account a different composition in performance among countries. On the one hand, because of a downgrade in the outlook for China this year and, on the other hand, because the U.S. is expected to have a more moderate and delayed recession. The terms of trade do not show significant changes either.

Monetary policy

The macroeconomic scenario has evolved as anticipated, with inflation projected to converge to the 3% target in the second half of 2024. If the central scenario projections of this Report materialize, in the short term the MPR will continue on the path outlined in the July Meeting. This means that, at the end of the year, the MPR would be between 7.75 and 8%. In any case, the magnitude and timing of the process of MPR reductions will take into account the evolution of the macroeconomic scenario and its implications for the inflation trajectory and the achievement of the 3% target within the policy horizon.

With respect to the sensitivity scenarios, the upper bound of the corridor reflects scenarios in which the inflationary convergence process is less favorable than expected. For example, this could occur in a situation where the world economy shows greater resilience, particularly in the U.S., and further increases in commodity prices are observed. This would generate greater inflationary pressures globally, which would be transmitted to local inflation. Its medium-term inflationary effects could be more persistent if there is a correction of inflation expectations.

The lower bound of the corridor reflects scenarios in which the inflationary convergence is faster than anticipated. This could be the case if the economy faces lower-than-expected pressures from the demand side. Such a situation would arise if activity is subject to shocks that reduce the external impulse; if there is a deterioration in business and household confidence that impairs the performance of investment and consumption; or if the impact of credit conditions is greater than initially estimated.

About the risks faced, they are still mostly associated with the global macro-financial situation. The same as in June, the possibility that a further deterioration of the economy could trigger episodes of high volatility, reduced liquidity and incentives for capital outflows from the emerging world continues to stand out. In addition to the sources of risk previously identified, there are also doubts about China, especially regarding the evolution of its economy and financial market. The implications of these scenarios for monetary policy will depend on how the combination and magnitude of these elements affect the outlook for medium-term inflation convergence.

TABLE 1: INFLATION (1)
(annual change, percent)

	2021	2022	2023 (f)		2024 (f)		2025 (f)	
			MP Rep. Jun.23	MP Rep. Sep.23	MP Rep. Jun.23	MP Rep. Sep.23	MP Rep. Jun.23	MP Rep. Sep.23
Average CPI	4.5	11.6	7.7	7.6	3.3	3.5	3.0	3.0
December CPI	7.2	12.8	4.2	4.3	2.9	3.0	3.0	3.0
CPI in around 2 years (2)							3.0	3.0
Average core CPI	3.8	9.3	9.1	8.7	4.0	3.8	3.0	3.0
December core CPI	5.2	10.7	6.5	6.3	3.0	3.1	3.0	3.0
Core CPI around 2 years (2)							3.0	3.0

(1) Core inflation is measured using the CPI without volatiles.
(2) For June 2023 MP Report corresponds to inflation forecast for the second quarter of 2025, for September 2023 MP Report to inflation forecast for the third quarter of 2025.
(f) Forecast.
Sources: Central Bank of Chile and National Statistics Institute (INE).

TABLE 2: INTERNATIONAL BASELINE SCENARIO ASSUMPTIONS

	2021	2022	2023 (f)		2024 (f)		2025 (f)	
			MP Rep. Jun.23	MP Rep. Sep.23	MP Rep. Jun.23	MP Rep. Sep.23	MP Rep. Jun.23	MP Rep. Sep.23
	(annual change, percent)							
Terms of trade	11.9	-7.7	1.7	1.9	-2.4	-2.9	-3.1	-1.6
Trading partners	6.7	2.8	3.0	3.1	2.3	2.3	3.0	2.9
World GDP at PPP	6.3	3.3	2.6	2.9	2.2	2.2	3.1	3.0
Developed GDP at PPP	5.4	2.7	0.5	1.3	0.3	0.1	2.2	1.7
Emerging GDP at PPP	7.5	3.7	3.8	3.8	3.4	3.5	3.7	3.7
	(levels)							
LME copper price (US$cent/pound)	423	400	385	385	365	370	350	355
Oil price, average WTI-Brent (US$/barrel)	69	97	75	79	71	78	68	73

(f) Forecast.
Source: Central Bank of Chile.

TABLE 3: INTERNAL SCENARIO
(annual change, percent)

	2021	2022	2023 (f)		2024 (f)		2025 (f)	
			MP Rep. Jun.23	MP Rep. Sep.23	MP Rep. Jun.23	MP Rep. Sep.23	MP Rep. Jun.23	MP Rep. Sep.23
GDP	11.7	2.4	-0.5 / 0.25	-0.5 / 0.0	1.25 - 2.25	1.25 - 2.25	2.0 - 3.0	2.0 - 3.0
Domestic demand	21.7	2.3	-4.2	-4.3	1.0	1.5	2.0	2.2
Domestic demand (w/o inventory	18.5	3.0	-3.3	-3.1	0.8	1.1	1.9	2.0
Gross fixed capital form	15.7	2.8	-3.0	-1.2	-1.0	-0.6	2.2	2.4
Total consumption	19.3	3.1	-3.4	-3.7	1.4	1.6	1.8	1.9
Private consumption	20.8	2.9	-4.9	-4.9	1.5	1.7	1.8	1.9
Goods and services exports	-1.4	1.4	2.4	0.9	4.4	4.0	2.5	2.4
Goods and services imports	31.8	0.9	-8.3	-9.8	2.2	3.1	0.6	1.2
Current account (% of GDP)	-7.5	-9.0	-3.7	-3.4	-4.0	-4.0	-3.9	-4.0
Gross national saving (% of GDP)	17.0	16.4	19.1	19.3	18.7	19.0	19.2	19.1
Gross fixed capital formation (% of nominal GDP)	23.1	24.8	23.0	23.3	23.0	23.1	23.2	23.1

(f) Forecast.
Source: Central Bank of Chile.

I. RECENT EVOLUTION OF THE MACROECONOMIC SCENARIO

Global activity has shown moderate performance and the outlook for the coming years remains weak. Inflation has continued to decline around the world, although some core indicators have shown a more persistent evolution, especially in the developed world. This has led these economies to expect monetary policy to remain contractionary for several months ahead. In contrast, in Latin America, monetary tightening is expected to ease soon, with some countries, such as Chile and Brazil, having already started the cycle of benchmark rate cuts. This divergence in monetary policies has affected the rates and currencies in a set of countries, including the Chilean peso. Local inflation has continued to decline, although it remains high. This reduction has been driven by the prices of core goods and some volatile items. The domestic economy continues to adjust in line with expectations, with consumption looking somewhat more stable and investment remaining sluggish, albeit with improvements at the margin. The labor market shows a path consistent with the cycle, while the current-account deficit continues to narrow. Inflation and growth expectations have not changed substantially, and expectations for the Monetary Policy Rate (MPR) point to new reductions in the coming quarters.

THE INTERNATIONAL SCENARIO

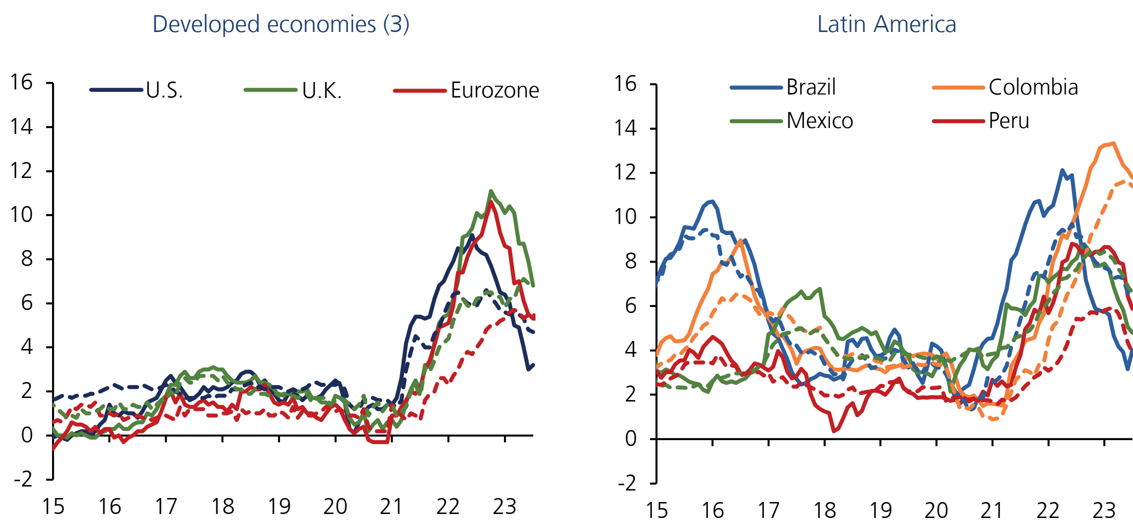
The world economy is still performing poorly, with a weak outlook for the next two years. On the one hand, the Chinese economy remains weak: second-quarter activity data reflected a somewhat more intense slowdown than expected, after the temporary boost provided by the lifting of the Covid-related sanitary restrictions. The fundamentals of foreign trade, domestic consumption and investment point to low dynamism. The latter continues to be strongly affected by the complex situation of its real-estate sector, which is also having an impact on consumer confidence. On top of this, fiscal and monetary policy have little room for maneuver. Meanwhile, the Eurozone is still showing signs of stagnation and its outlook continues to be affected by a contractionary monetary policy, the weakness of the external sector and the effects of the energy crisis. In Latin America, activity has slowed in several countries, with the exception of Mexico. Added to the tightening of financial conditions are low levels of consumer confidence and factors of local uncertainty in several countries.

On the contrary, the U.S. economy has been more resilient so far, but projections continue to point to an eventual recession. Second-quarter economic figures were better than expected, influenced by strong consumption —especially in the services sector—, as well as by an acceleration in non-residential investment and a greater fiscal impulse. All of this in a scenario in which the labor market seems to be slowly easing its tightness. Going forward, high interest rates and the continued decline in the levels of savings accumulated in the pandemic anticipate low consumption dynamism. At the same time, the tightening of bank credit conditions portends a poor investment performance.

Inflation has continued to decline globally, although its reduction has been heterogeneous among both components and economies (box I.1). The relative progress has been greater in Latin America, where the process of monetary tightening began earlier, which also explains the divergence of expected monetary policy paths with respect to developed economies (figures I.1 and I.2). Transversally, goods components led the decline in global inflation, along with the reestablishment of value chains, the decline in global transportation costs and the pass-through of exchange rate appreciation in various economies. In several Latin American countries, the earlier start of MPR hikes and the faster unwinding of fiscal stimulus (figure I.3), contributed significantly to normalizing activity and demand, which helps to explains the faster drop of inflation from last year's levels. In this context, expectations point to an easing of monetary tightening in the region. Some countries, such as Brazil and Chile, have already cut their rates.

In the developed world, despite the fall in headline inflation, the evolution of some core indicators, labor market pressures, together with the messages delivered by central banks suggest that they will maintain monetary tightening for an extended period of time (figures I.1 and I.2). Tight labor markets have continued to put pressure on wages, partly explaining the high services inflation in developed countries. In this context, the Federal Reserve (Fed) resumed rate hikes at its July meeting citing that inflation is still high. Its authorities have emphasized that the rate will remain high for several more months and that their upcoming decisions will continue to be conditioned by the new information available, without ruling out the possibility of new hikes. The Eurozone presents a similar situation, as the European Central Bank applied a new hike and has continued to communicate that it will assess its movements on a meeting-by-meeting basis. Meanwhile, the Bank of England accumulated an increase of 75 basis points (bp) in its last two meetings.

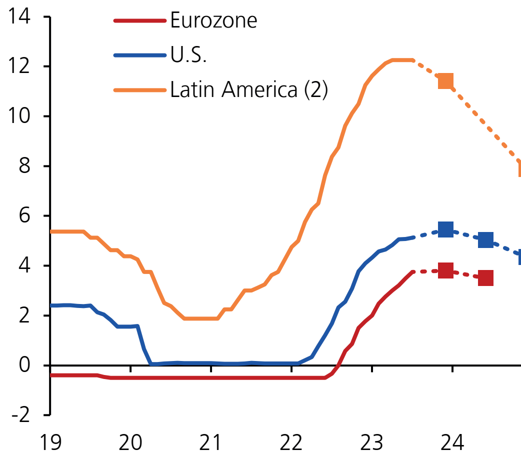
FIGURE I.1 WORLD INFLATION (1) (2)
(annual change, percent)



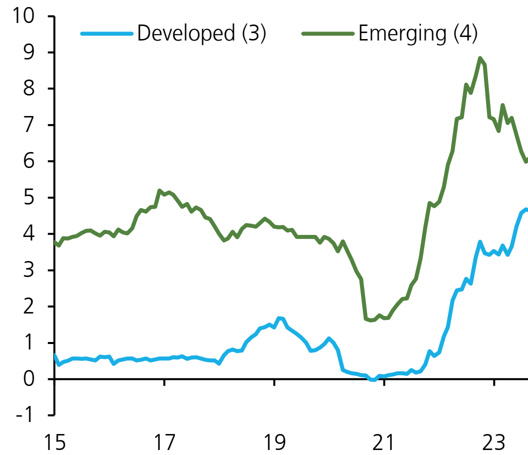
(1) Dashed lines show core inflation. (2) Core measures exclude foods and energy. (3) Eurozone's August data is preliminary.
Source: Bloomberg.

FIGURE I.2

World monetary policy rates and expectations (1)
(percentage points)

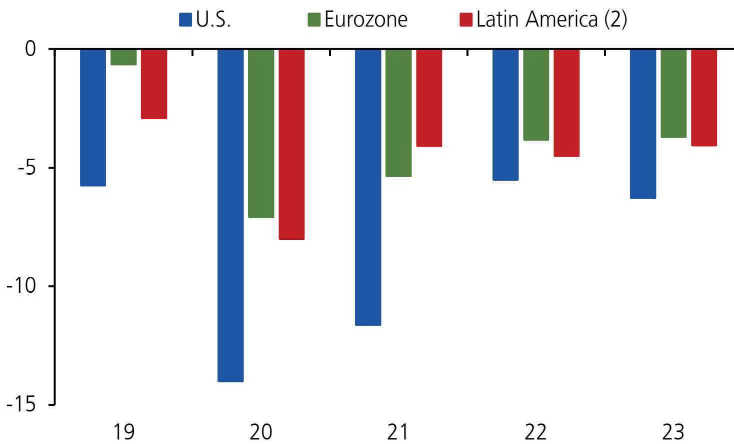


Two-year interest rates
(percent)



(1) Expectations for the U.S. and the Eurozone derived from asset prices. For the U.S., as of Dec.23, Jun.24 and Dec.24. For the Eurozone as of Dec.23 and Jun.24. (2) For Brazil, Mexico, Peru and Colombia, the median is used. Expectations as of Dec.23 and Dec.24 are obtained from respective central bank surveys, with the exception of Peru, which come from Bloomberg. (3) Median for U.S., Eurozone, Canada, Czech Republic, Australia, New Zealand, United Kingdom, Sweden and Norway. (4) Median for Chile, Brazil, Mexico, Colombia, Peru, Indonesia, Poland and Thailand.
Sources: Bloomberg and central banks' expectations surveys.

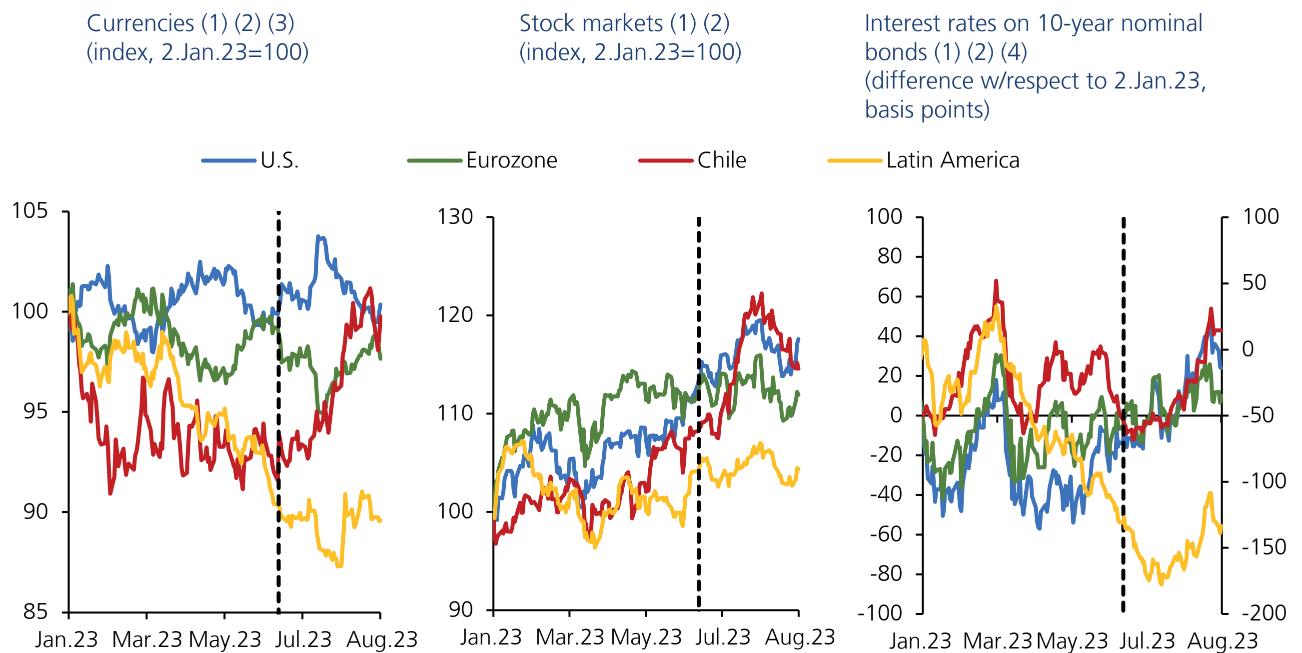
FIGURE I.3 FISCAL BALANCE BY ECONOMIES (1)
(percent of GDP)



(1) Projection for 2023 is based on IMF's WEO for April 2023. (2) Median for Brazil, Colombia, Mexico and Peru.
Source: World Economic Outlook, IMF.

Financial markets have responded to this scenario with differing trends in short-term interest rates —rises in the developed world and mixed movements in emerging markets— and the depreciation of a significant set of currencies, amid financial risks that remain in force (figures I.2 and I.4). The increase in short-term rates in developed economies contrasts with the falls in several emerging countries, consistent with the divergence of the expected trajectories of their monetary policies. This differential has influenced the strengthening of the dollar globally for several weeks, a trend that has been reinforced by a decrease in risk appetite in the last month, which also would have put upward pressure on the U.S. long-term rates. Several factors have contributed to the lower risk appetite, among them, the downgrade of the credit rating of the US sovereign debt and of some regional banks in that country, and the greater uncertainty about China's activity and real-estate sector. Meanwhile, stock markets show mixed movements and risk indicators have decreased in Latin America since the statistical closing of our latest Report, despite increases in recent weeks. All in all, the risks of a reversal in financial asset prices and capital outflows from emerging economies remain, in an environment in which interest rates remain high and global liquidity continues to shrink.

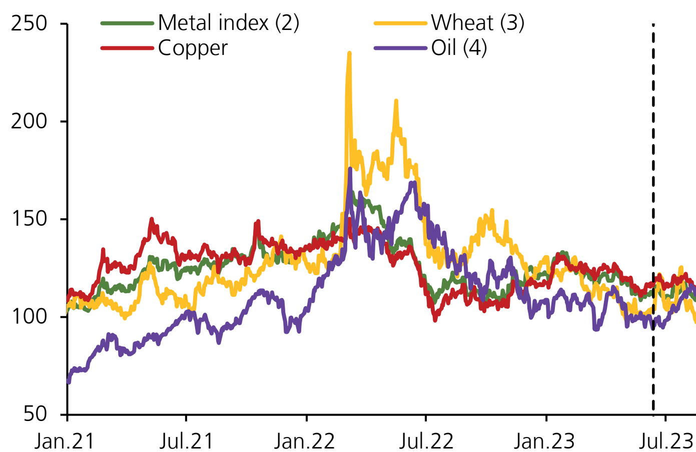
FIGURE I.4 FINANCIAL CONDITIONS



(1) For Latin America, the simple average of the indices for Brazil, Mexico, Colombia and Peru is used. (2) Dashed vertical line marks the statistical closing of the June 2023 Report. (3) An increase in the index denotes a currency depreciation, and vice versa. For the U.S., the multilateral exchange rate is used. (4) Latin America corresponds to the right axis.
Sources: Central Bank of Chile and Bloomberg.

Regarding commodities, it is worth noting the significant increase in the oil price since our last Report (figure I.5). Such increase was driven by Saudi Arabia's production cut announcements, amid global demand that has remained solid. At our statistical closing, the price of an average Brent-WTI barrel fluctuated around US$83 (+14% from the previous Report). The price of copper was around US$3.8 per pound, similar to the previous statistical closing. Its behavior has shown some volatility in recent months, which balances the poor performance of construction in China with optimistic expectations associated with the use of copper for the energy transition, in a context in which inventories remain tight. Food prices continued to fall, influenced by improved supply prospects and lower production costs. Russia's withdrawal from the Black Sea Grains Initiative temporarily affected grain prices. In July, the FAO index fell 12% annually, with monthly declines in most of its components.

FIGURE I.5 COMMODITY PRICES (1)
(index, 2010-2023 average=100)



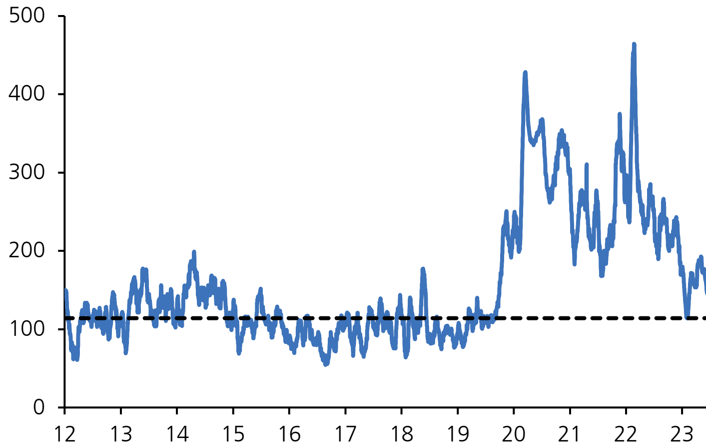
(1) Dashed vertical line marks statistical closing for the June 2023 Report. (2) S&P GSCI Industrial Metals. (3) One-month futures prices. (4) WTI-Brent average.
Source: Bloomberg.

THE DOMESTIC SCENARIO

In the local financial market, the beginning of the MPR reduction cycle and the expectation of future cuts have also affected the interest rate differential with foreign countries. This is one of the main factors behind the peso's depreciation in recent months (figure I.4). Considering the average of the 10 days prior to the closing of this Report, the peso/dollar parity was around $860 (+8% with respect to the closing of the June Report). This rise is also explained by the increase in global risk aversion, linked to different events, such as the situation in China, the fiscal outlook in the United States and the uncertainty about the global disinflation process.

Other local financial variables have performed better, such as the stock market and risk premiums, as local uncertainty has subsided. Since the June Report, the IPSA has increased by around 8%, accumulating gains close to 20% since the beginning of the year (figure I.4). The Economic and Political Uncertainty Index (DEPUC) has decreased and is close to the levels prior to the 2019 social crisis (figure I.6).

FIGURE I.6 ECONOMIC UNCERTAINTY INDEX (DEPUC) (*)
(index)

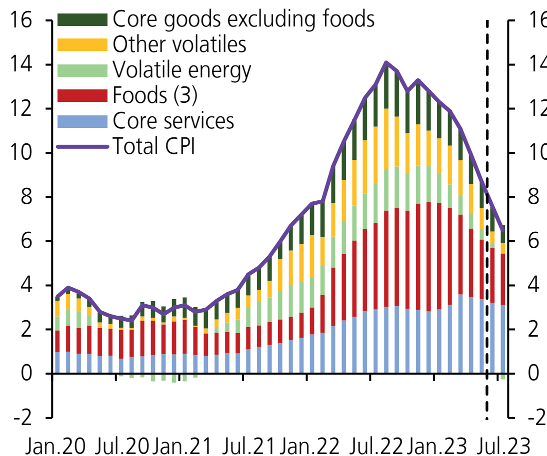


(*) Dashed horizontal line denotes average index between 2012 and 2019.
Source: Central Bank of Chile.

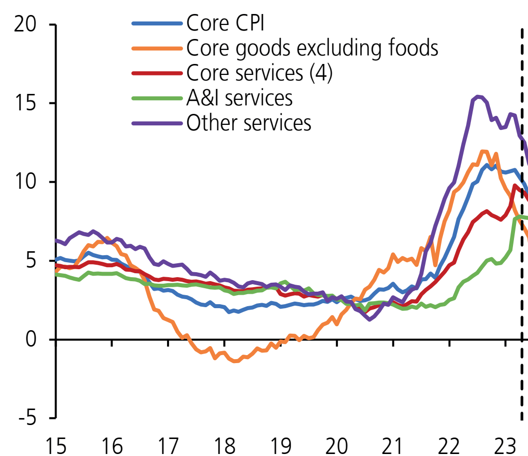
Inflation has continued to decline, although it remains at high levels. Headline and core inflation (CPI without volatile items) dropped to 6.5% and 8.5% annually in July, respectively (figure I.7). Since our last Report, the significant reduction in core inflation of goods and volatile components, especially energy, stands out. This again contrasts with the slower decline in services inflation. Although the latter has moderated since the beginning of the year, the administered and indexed (A&I) services component continues to show significant annual variations, items that in many cases are still subject to adjustments related to high past inflation rates.

FIGURE I.7

Inflation indicators (1) (2)
(contributions to annual change, percentage points)



Core inflation (1)
(annual change, percent)

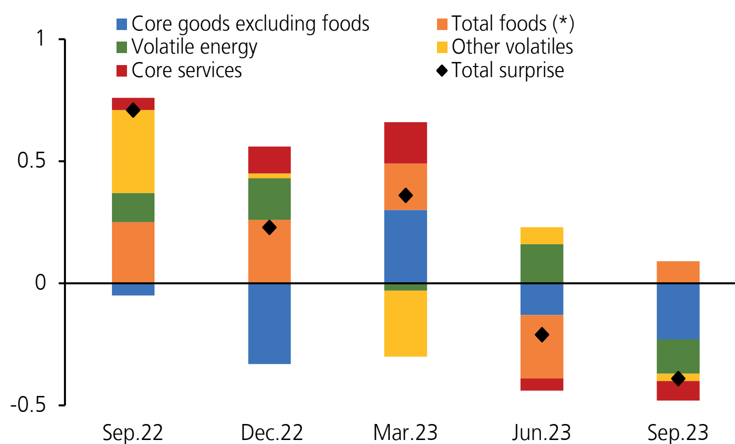


(1) Dashed vertical lines mark the statistical closing date for June 2023 Report. (2) For details on the different groupings and their share in the total CPI basket, see box IV.1 December 2019 Report, Carlomagno and Sansone (2019) and Economic Glossary. (3) Volatile and non-volatile foods added together. (4) Considers sum of administered & indexed (A&I) services and other services.
Sources: Central Bank of Chile and National Statistics Institute.

The decline in inflation has gone hand in hand with the steady reduction in demand and supply pressures from previous quarters. A key element has been the cut in excessive domestic spending, especially private consumption. The pass-through of the appreciation accumulated by the exchange rate until the first half of this year has also contributed and partly explains the rapid decline in goods inflation. In addition, the resolution of bottlenecks, the drop in global transportation fares and the normalization of external prices after the severe shock caused by the pandemic and the war in Ukraine have also played a part. Accordingly, both the Survey of Price Determinants and Expectations (EDEP) and the Business Perceptions Report (IPN) for August report lower cost pressures and their favorable impact on the evolution of prices.

In any case, cumulative inflation between June and July was somewhat lower than forecast in the June Report (figure I.8). The cumulative CPI variation in that period was 0.39 percentage points lower than the projected in the last Report. Nearly 60% was explained by lower prices of core goods — excluding foods— and was concentrated in durable goods. Part of this divergence could be explained by a faster than expected pass-through to prices of the exchange rate appreciation in the first part of the year. Among the items that had the greatest impact were housing equipment, automobiles, and clothing and footwear. In the inflation of services and volatile items, differences were small.

FIGURE I.8 CUMULATIVE INFLATIONARY SURPRISES IN EACH REPORT
(percentage points)

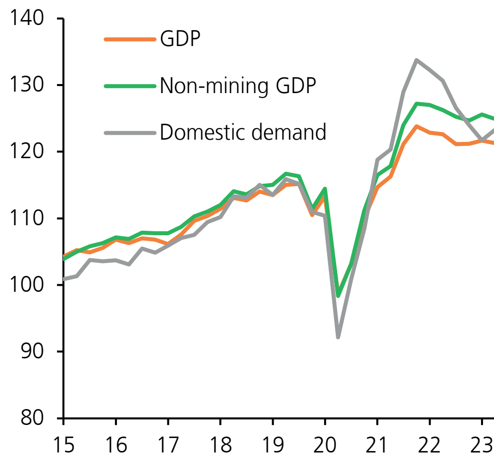


(*) Volatile and non-volatile foods added together.
Sources: Central Bank of Chile and National Statistics Institute.

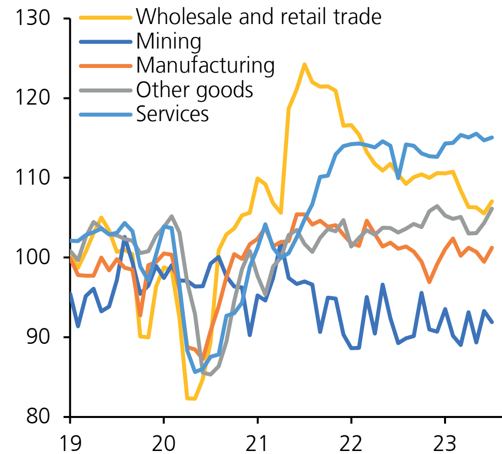
The Chilean economy has evolved in line with forecasts in the June Report (figure I.9). In the second quarter, the seasonally adjusted series of non-mining GDP fell 0.5% quarter-on-quarter (q/q) (-1.1% y/y), while the non-mining Imacec for July grew 0.6% monthly (1.5% y/y), although mainly associated with transitory factors. Meanwhile, deseasonalized domestic demand in the second quarter grew by 1.3% q/q (-5.6% y/y). At the disaggregated level, some heterogeneity in the intensity of the adjustment stands out, with declines in wholesale and retail trade, construction and manufacturing, a transportation sector with no quarterly variation, and weakened mining activity, beyond an increase in the last quarter. This contrasts with the services sector, which remains dynamic.

FIGURE I.9

Activity
(index, 2013.QI = 100, real seasonally-adjusted series)



Imacec by sector
(index, 2018 average = 100; seasonally-adjusted)

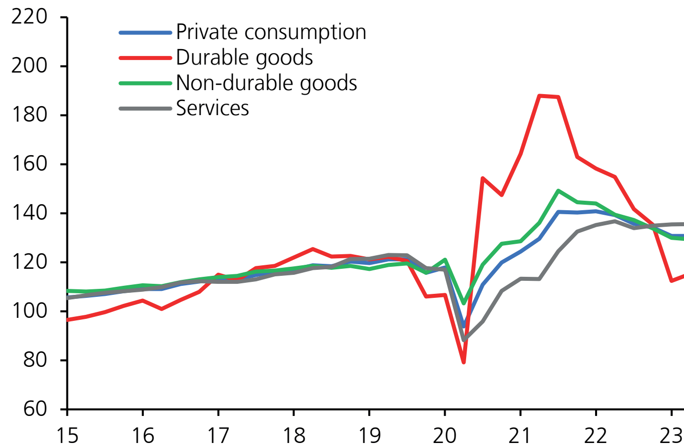


Source: Central Bank of Chile.

On the demand side, the adjustment of private consumption has been losing strength as the year goes by, in line with the projections of the previous Report. Seasonally adjusted, it had a zero quarterly variation in the second quarter (-2.5% in the first one). By components, the stability of services and the slight rebound of durable goods stand out (figure I.10). Partial indicators for the third quarter confirm a more stable performance of private consumption. Retail sales according to different sources (IACM, IVDCM and digital invoicing), automobile sales (ANAC) and consumption imports for July maintain a downward trend, although with some recent moderation.

The fundamentals of consumption restate a more stable behavior of this spending component going forward, particularly due to the stabilization of labor income. The evolution of the labor market has been consistent with the state of the economic cycle. The unemployment rate was 8.8% in the moving quarter ending in July (8.5% in the previous moving quarter and 8.7% reported in the June Report). This is in line with the recovery of the labor force and with employment levels that have not changed recently (figure I.11). In terms of gender, female employment and participation rate have shown a remarkable recovery so far this year, especially in the 25- to 54-year-old segment. Real salaries continue to rise, which has been influenced by the increase in the minimum wage and the decline in inflation. Meanwhile, the financial burden of households has remained relatively stable after its sharp rise during 2022. Consumer confidence (Economic Perception Index) has improved somewhat, although it remains in pessimistic territory.

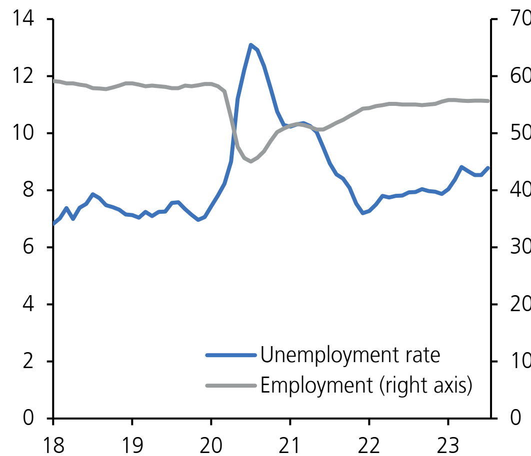
FIGURE I.10 PRIVATE CONSUMPTION BY COMPONENTS
(index, 2013.QI = 100, real seasonally-adjusted series)



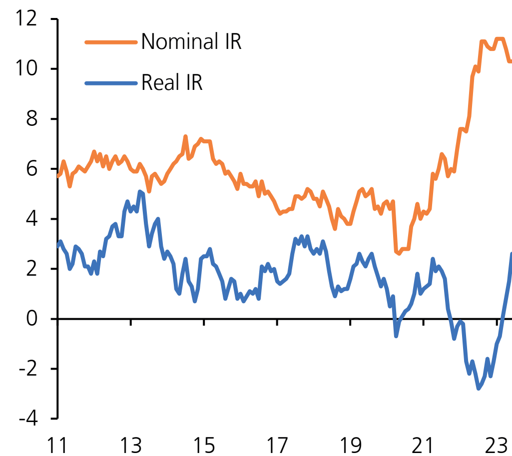
Source: Central Bank of Chile.

FIGURE I.11

Unemployment rate and Employment
(percent)



Compensations Index (IR)
(annual change, percent)

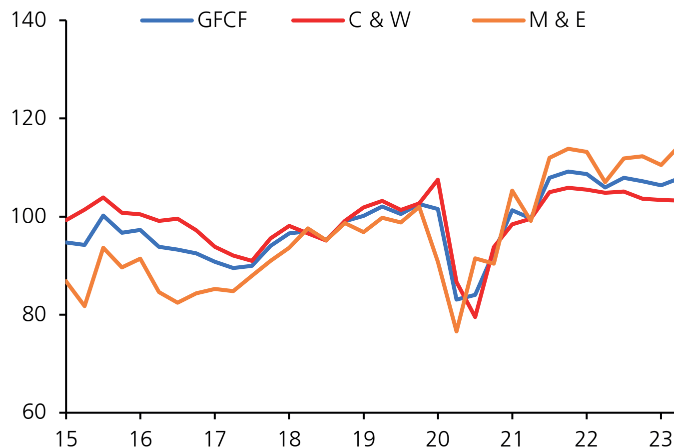


Source: National Statistics Institute.

Investment remains sluggish, beyond some marginal improvement in the machinery and equipment component (figure I.12). In seasonally adjusted terms, it grew by 3.6% q/q, which is linked to a greater impulse from several sectors, although primarily mining and energy. Their evolution explains the entire increase in gross fixed capital formation (GFCF) in that quarter (1.4% q/q). This is confirmed by the upward revision of the projections for both sectors in the latest survey of the Capital Goods Corporation (CBC). Construction and other works contracted slightly (-0.1% q/q), as has been the trend in recent months. All

this occurs in a context of lower domestic uncertainty (DEPUC), consistent with the responses of the August IPN. The Monthly Business Confidence Index (IMCE) has shown a slight recovery in recent months, although it still reflects a negative perception of the economic environment for business.

FIGURE I.12 INVESTMENT
(index, 2013.QI = 100, real seasonally-adjusted series)



Source: Central Bank of Chile.

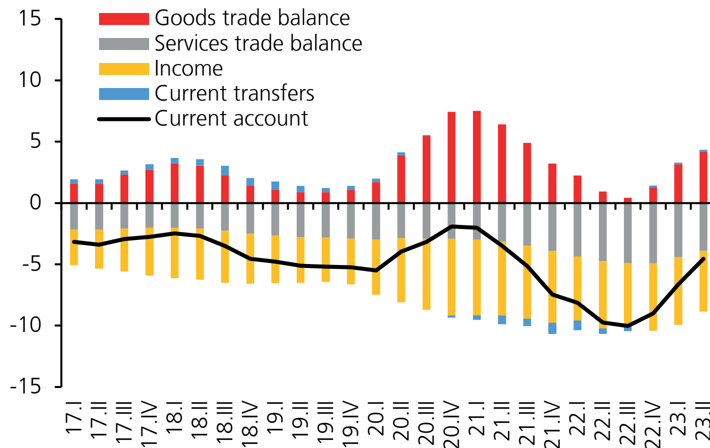
The current account deficit accumulated in one year decreased further (figure I.13). In the second quarter, it reached 4.5% of GDP (6.6% in the previous quarter). All this has gone hand in hand with a recovery of national savings, which in the second quarter reached 18.6% of GDP in the cumulative annual sum. This increase obeys mainly to greater private savings, which is in line with the adjustment in spending. As for the contributions by components of the current account, the balance of trade and services balances improved, along with a fall in corporate remittances abroad.

Two-year inflation expectations continue to be aligned with the 3% target (figure I.14). Both the Economic Expectations Survey (EES) and the Financial Traders Survey (FTS) remain at this value. Breakeven inflation points to inflation expectations of around 2.6% at the end of the monetary policy horizon [1]/. At one year, the EES and the FTS stand at 3.5% and 3.65%, respectively, while business surveys remain above those levels. The Survey of Price Determinants and Expectations corresponding to the moving quarter ending in July shows inflation expectations of 6% in one year and 4.5% in two years.

Growth expectations for 2023 have not been substantially modified. The August EES continues to foresee a GDP contraction of 0.5% this year, and for 2024 it anticipates a 2% growth. Meanwhile, Consensus Forecasts maintained its 2023 forecast at -0.3% (the same as to the June statistical closing) and revised it to 1.9% for 2024.

[1]/ It must be noted that these expectations are affected by premiums that make them difficult to read. See box IV.1 in December 2016 Report and box V.1 in March 2022 Report.

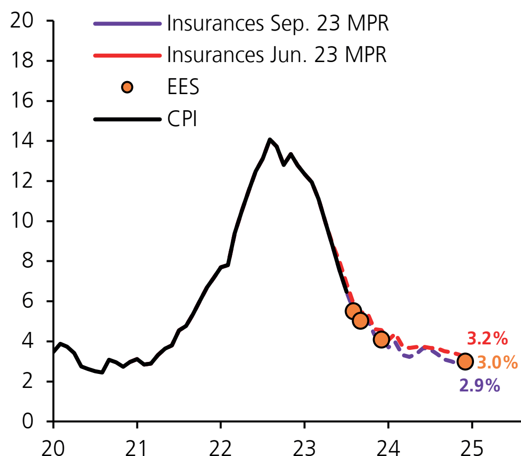
FIGURE I.13 CURRENT ACCOUNT AND CONTRIBUTIONS BY COMPONENT
(percent of GDP, moving annual sum)



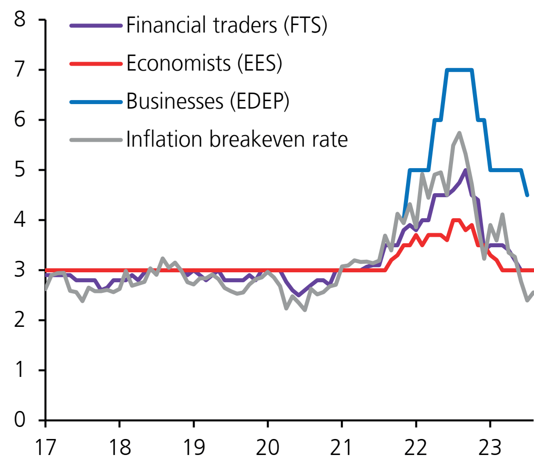
Source: Central Bank of Chile.

FIGURE I.14

Actual and expected annual inflation (1)
(annual change, percent)



Two-year inflation expectation (2) (3) (4)
(annual change, percent)



(1) Inflation insurances consider the average prices of 10 days at the statistical closing of each MPR (June MPR: June 13th; September MPR: August 30th). (2) For the surveys, median responses are shown. (3) The FTS considers the survey of the first half of each month up to January 2018. From February 2018 onwards, it considers the last survey published in the month, including the one prior to the September 2023 monetary policy meeting. In the months where no survey is published, the latest available one is used. (4) Breakeven inflation considers averaged prices of the last 10 days of each month. For August 2023 it takes into account the average of the last 10 days prior to the statistical closing of this Report.

Source: Central Bank of Chile.

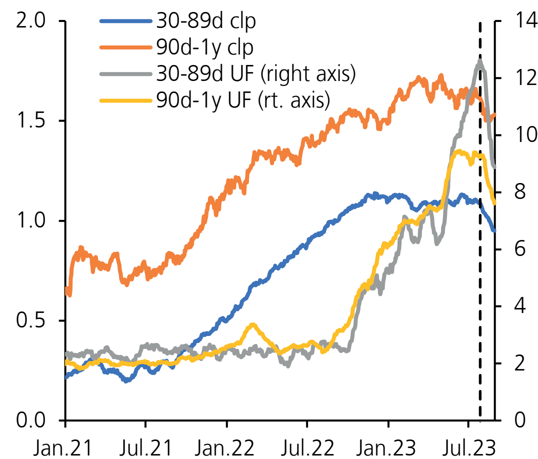
The expected MPR trajectories reflect the ongoing process of monetary policy normalization. Expectations implicit in the overnight index swap (OIS) rate reflect that the MPR would stand at 7.75% by the end of this year, matching the median of expectations in the August FTS, while the August EES foresees a rate of 7.5%. Towards the end of the monetary policy horizon, the MPR would be between 4.0% and 4.75%, considering the surveys and OIC rates (at the statistical closing date for this Report).

Interest rate movements in the local financial market are aligned with expectations for monetary policy. Since our last Report, short-term rates have fallen. Considering the average of the 10 days prior to the closing of this Report, one- and two-year OIC rates have dropped by around 160bp and 100bp, respectively. Long-term rates increased modestly, also affected by external developments. The nominal 10-year bond rate rose slightly over 30 bp, below the increase of around 50 bp exhibited by US Treasury bonds at the same maturity.

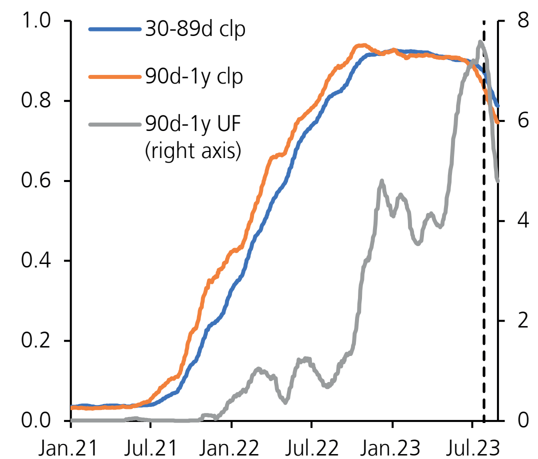
In general, lending and deposit rates have begun to react to the MPR cuts, reflecting the normal functioning of the monetary policy pass-through (figure I.15). Short-term —30 days to one year— deposit rates have decreased since the last monetary policy meeting, showing negative month-to-month variations in both nominal and indexed rates. This is also the case for lending rates for the same term (see box I.3). In turn, recent weekly data suggest that commercial and consumption lending rates have begun to decline after the July monetary policy meeting.

FIGURE I.15

Lending rates (*)
(moving four-week average, percent)



Deposit rates (*)
(moving four-week average, percent)



(*) Dashed vertical line marks July 2023 monetary policy meeting.

Source: Central Bank of Chile.

BOX I.1:

Factors underlying global disinflation and monetary policy outlook

Although inflation has fallen across the board, the magnitude of the declines varies from one economy to another. Several Latin American and other emerging economies show a deeper decline than developed ones. This box discusses the factors behind these differences, which support the possibility that monetary policy paths may diverge in the near term.

Beyond the global declines, the differences across economies remain at levels not seen since the beginning of this century. Compared to their peaks in the second half of 2022, the emerging economies show a greater decrease in the inflation measure that excludes foods and energy compared to developed countries, which contrasts with the historical difference between them. This divergence between emerging and developed economies is visible in the dynamics of goods inflation since the second half of 2022 and, to a lesser extent, in services inflation of recent months (figure I.16).

The same as when it was going up, the drop in inflation is explained by both global and local factors.[1]/ Global factors are those common to most countries. These include the decline in commodity prices, the normalization of global trade in goods and associated transportation costs, and the depreciation of the U.S. dollar. In several economies, these account for the entire fall in recent inflation. Overall, the less favorable outlook for some of these factors suggests that their impact on the decline in inflation will be smaller in the coming months. On the one hand, fuel prices have risen again.[2]/ On the other, the dollar depreciation has been partly reversed in the past few weeks.

The local factors include the correction of macroeconomic imbalances. These adjustment processes have shown different speeds and intensities among countries, in line with monetary and fiscal policy responses. In emerging countries, especially in Latin America, the contraction of monetary policy was bigger and sooner (figure I.17). At the same time, after its initial expansion, there were generally earlier and/or more significant adjustments in fiscal spending (figure I.3). In other countries, especially in the developed world, progress has been slower, with still dynamic consumption and/or tight labor markets, which should make inflationary convergence more difficult.[3]/

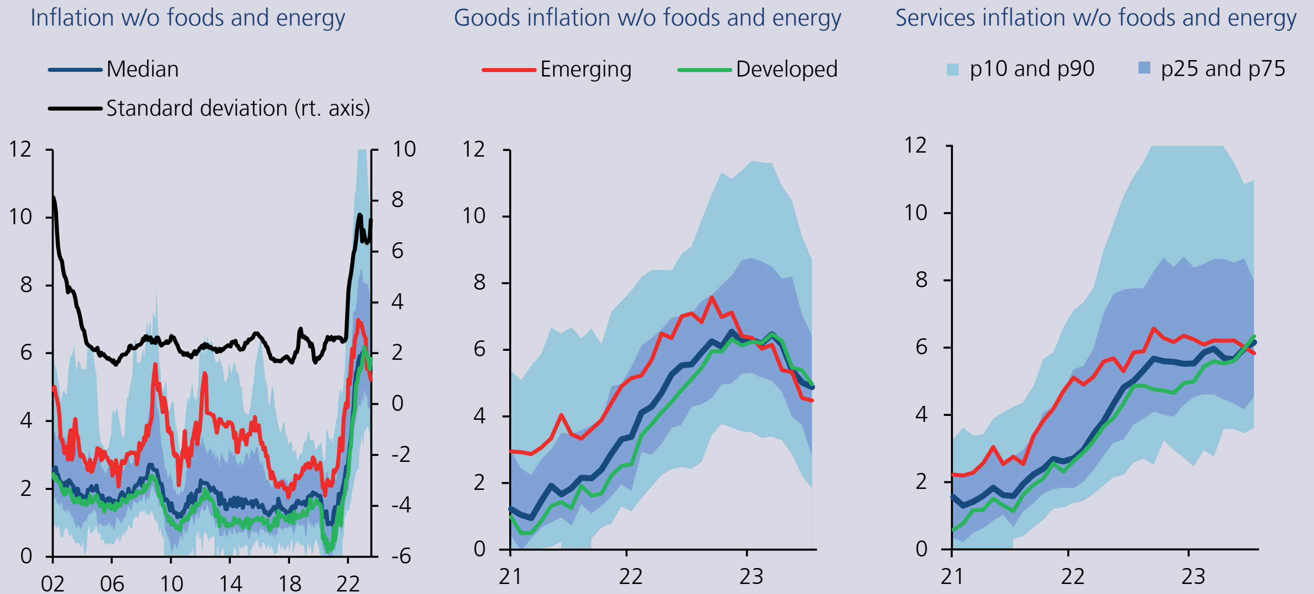
Regarding the implications for monetary policy, in the developed economies interest rates are expected to remain constant or continue to rise. In the U.S., beyond the fall in total inflation, consumption remains resilient and the labor market is tighter than in the rest of the economies. In this context, the Fed has ruled out cuts in the short term and has left the door open to further increases in the fed funds rate, conditional on the future evolution of inflation and activity. The messages from central banks in other developed economies have followed the same lines. Among the emerging economies, some central banks have begun the cycle of cuts, while others are expected to start soon. Nevertheless, and unlike the situation in Chile, medium-term inflation expectations in several of these countries remain above the inflation target, posing a risk to inflationary convergence, which could influence future monetary policy decisions.

[1]/ See Box IV.1 in December 2021 Report.

[2]/ Even without considering the recent price increase, in several countries annual inflation will rise in the coming months due to the negative base effects accumulated in the second half of last year associated in the start of fuel price declines.

[3]/ See Box I.2 in December 2022 Report.

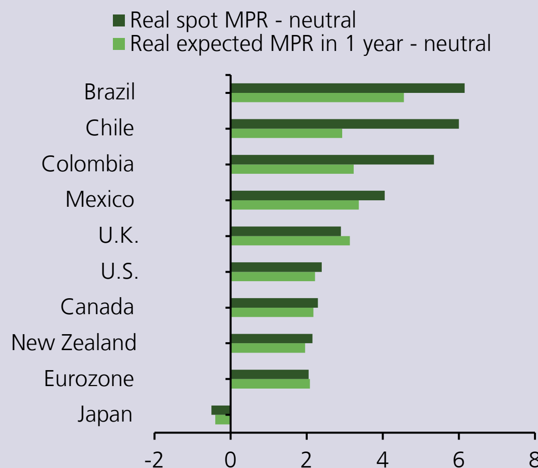
FIGURE I.16 INFLATION IN 49 SELECTED ECONOMIES
(percent)



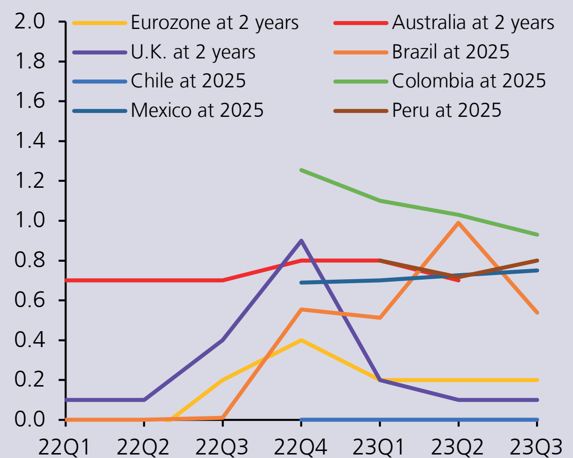
(*) Inflation calculations for each country consider equal weights of the consumer baskets for all economies. Thus, the differences between inflation levels capture changes in price movements and not in the weight of products. Emerging economies stand for a group of 19 economies in Latin America, Asia, Europe and Africa. Developed economies gather 30 economies in Europe, Asia and North America.
Source: Central Bank of Chile based on Bajraj, Carlomagno & Wlasiuk (2023).

FIGURE I.17 REAL MONETARY POLICY RATES AND INFLATION EXPECTATIONS

Deviations of real MPR with respect to real neutral rate (*)
(percent)



Deviations of analysts' inflation expectations with respect to inflation targets
(percentage points)



(*) Real MPR calculated as the difference between the MPR and inflation expectations at 2024Q2. Real MPR expected in one year calculated as the difference between the average expected MPRs between 2023Q3 and 2024Q2 and inflation expectations at 2024Q2.
Sources: Economic expectations surveys of each central bank (Latin America); Bloomberg for all other countries, and each central bank's estimated neutral rate.

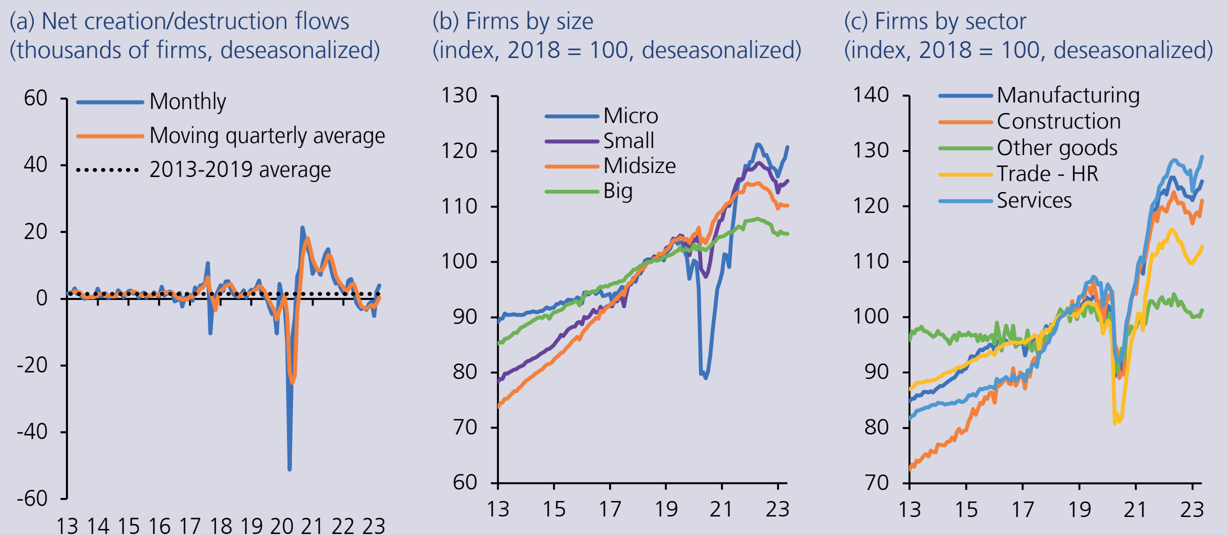
BOX I.2:

Recent evolution of the Chilean economy in light of microdata

During the last few quarters, the Chilean economy has been gradually resolving the strong macroeconomic imbalances accumulated in previous years. Consistent with this, domestic spending has been decreasing, the activity gap has been closing and inflation has come down from its 2022 peaks. Monetary policy has played a significant role in this process, supported by the reduction in fiscal spending that materialized last year. The information available at the close of this MP Report suggests that the economy has evolved as projected. This box provides evidence on this cyclical adjustment from administrative business and employment data, and the results of the Business Perceptions Survey (EPN). This granular evidence complements the analysis with aggregate data that is usually contained in our Monetary Policy Reports.

A first indicator is the evolution of the net creation of firms and the number of firms reporting positive sales by size and by sector. Regarding the flow of net business creation, it has recently been near zero, after a peak of net destruction during 2020 followed by a period of two years with highly positive net creation (figure I.18a)[1]/. The number of firms reporting positive sales experienced a sharp drop early in the pandemic, followed by a recovery in 2021 and 2022. More recently, an increase in the number of businesses is observed. While this is more noticeable for micro-enterprises and service sector firms, it is evident for almost all size and productive sectors (figure I.18b and I.18c)[2]/.

FIGURE I.18 FIRMS' INDICATORS (*)



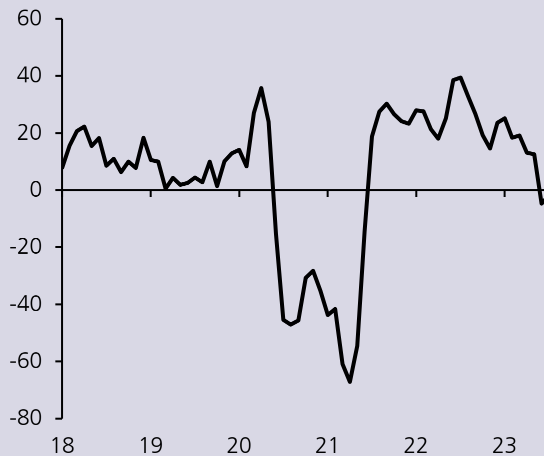
(*) Latest data: March 2023 for net creation flow; May 2023 for number of firms.
Sources: Central Bank of Chile and Internal Revenue Service.

Regarding the labor market, job termination letters, expressed as the difference with respect to the same month of the previous year, are at values near to zero in the most recent period, after an increase in the last few years (figure I.19a)[3]/. Requests to unemployment insurance are returning to normal, after some months of high levels (figure I.19b).

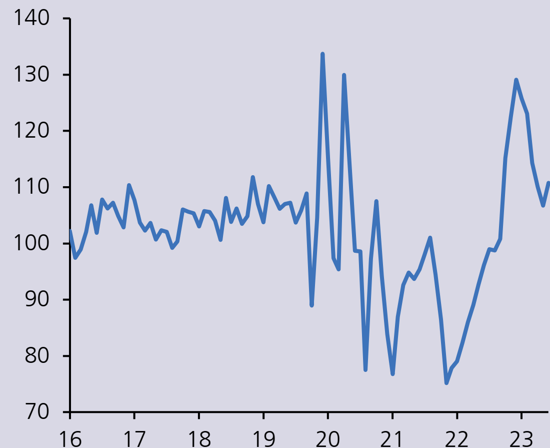
[1]/ Bauducco *et al.* (2023) shows the disaggregated evolution of business startups and closures.
[2]/ While the extension of VAT taxation to service activities may have encouraged the creation of professional partnerships, the recent increase in the number of firms has been widespread across all sectors and is therefore unlikely to be entirely due to a tax change. Moreover, as shown in Bauducco *et al.* (2023), firm exits, which are free of the effects of tax-related entries, have also moderated lately.
[3]/ Throughout 2020, termination letters show a decline to which policies to support businesses during the Covid-19 crisis probably contributed, such as the Employment Protection Law.

FIGURE I.19 LABOR MARKET INDICATORS

(a) Job termination letters
(annual difference, thousands, moving quarterly average)



(b) Requests to unemployment fund (*)
(thousands, deseasonalized)



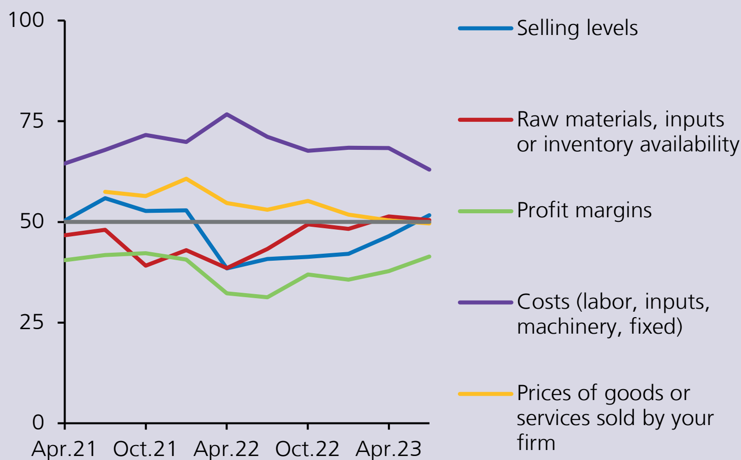
(*) Latest data: June 2023.
Sources: Labor Directorate, Central Bank of Chile and Unemployment Fund Administrator (AFC).

As for business expectations, data from the August Business Perception Report show a return to neutral levels. On the one hand, there is less concern among firms about the evolution of costs and input availability, while at the same time the outlook for sales and profit margins is improving (figure I.20a). On the other hand, the proportion of businesses that expect to perform better than at present, and better than usual, in a year's time, is increasing (figure I.20b).

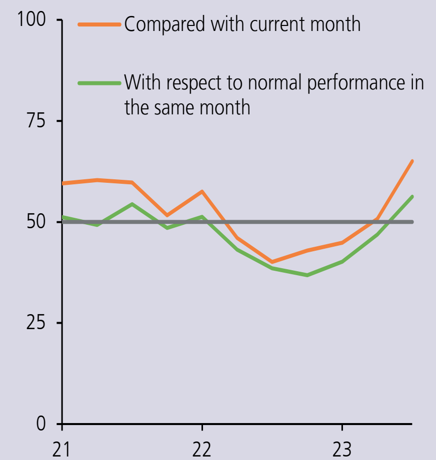
Summing up, and based on information with disaggregated and high-frequency data, it is not observed that more adverse scenarios are materializing relative to the central scenario of this MP Report.

FIGURE I.20 FIRMS' PERCEPTIONS (*)

(a) Evolution of factors over next three months
(diffusion index)



(b) Expected performance in one year
(diffusion index)



(*) For methodological definition, see August 2023's Business Perceptions Report (IPN).
Source: Central Bank of Chile.

BOX I.3:

Credit conditions for the firms: evolution and heterogeneity

The Board began lowering the monetary policy interest rate (MPR) last July. To date, it has accumulated a decrease of 100 basis points (bp). A natural question that arises is how this lower MPR will be passed through to market interest rates. This box contrasts the observed rate cuts with their historical patterns and also uses micro data on commercial loans to understand in more detail how credit conditions have evolved in recent years for different groups of firms. With the information now available, the results show that market rates have fallen in line with expectations since the first cut in the MPR was decided, suggesting that the monetary policy transmission mechanisms are working properly.

Aggregate evolution of commercial credit costs

Figure I.21 shows the effective evolution of the commercial rate for installment loans and its projection based on a model that considers as key variables the MPR and the two-year overnight index swap (OIS) rate[1]/. The model-adjusted rate closely follows the effective rate, which indicates that monetary policy transmission is following its historical patterns.

Microdata-based analysis

In addition to being able to describe the aggregate evolution of the cost of commercial credit, the micro data available to the Central Bank make it possible to characterize the credit operations that each firm has performed in the past few years[2]/. This information enables differentiating whether the observed change in average interest rates is being driven by actual changes in the average cost of credit faced by firms, given their level of risk or other characteristics —intensive margin— or, alternatively, by changes in the composition of the firms receiving loans —extensive margin. For example, if the proportion of firms in riskier categories in the total portfolio increases (extensive margin), average rates will rise, even if the rates charged to each firm, given their level of risk (intensive margin), has remained unchanged.v

The microdata analysis is done using two aggregations. In the first, the firms are grouped according to their size, defined according to sales stratum; in the second, it is based on the risk classification given by each bank to its portfolio, in accordance with current regulations. In both cases, the intensive margin is the main factor behind the changes in the average cost of credit over the last two years, a period that includes both the 2021-2022 rate hike cycle and the cut decided by the Board in July 2023 (figures I.22a and I.22b). In other words, changes in the composition of the loan portfolio have played a minor role compared to the change in average rates charged to different credit groups.

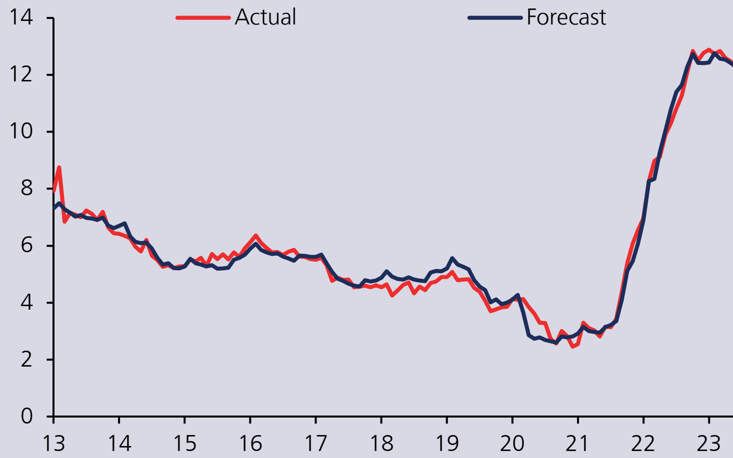
The microdata also make it possible to track the cost of credit faced by each subgroup. As expected, lower-risk firms borrow at lower interest rates (figure I.23a). The analysis also reveals that the rate differentials at which firms in different risk categories borrow have narrowed since the onset of the pandemic (figure I.23b).

Conclusions

The analysis of commercial credit interest rates at the firm level shows that their evolution responds mostly to changes in the cost of credit at the general level —intensive margin. Most recently, there have been falls in the rates charged in line with the usual patterns, which is indicative that the banking sector is transmitting the actual and expected changes in the MPR.

[1]/ The overnight index swap (OIS) captures the banks' funding cost.
[2]/ The information presented in this box considers only installment loans. All the information used for the analysis is anonymized, which guarantees its confidentiality.

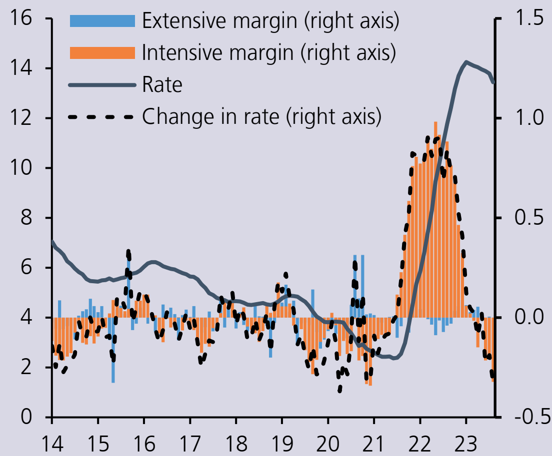
FIGURE I.21 COMMERCIAL RATE ON INSTALLMENT CREDITS (1)(2)(3)
(percent)



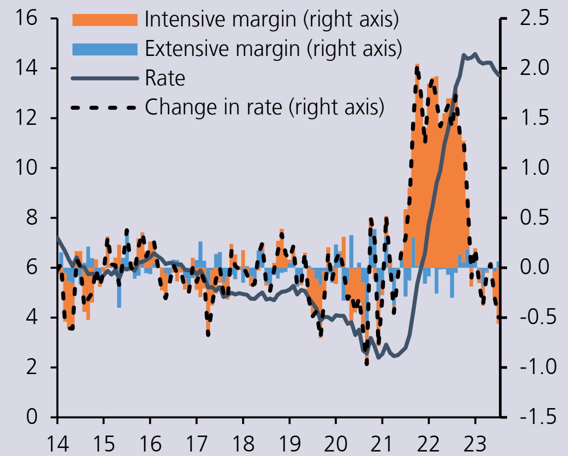
(1) Monthly data. (2) Red line describes average effective interest rate for new installment loans perceived by firms. Blue line shows forecast of said actual rate considering the monetary policy rate (MPR) and the overnight index swap (OIS) and the two-year average swap rate (SPC). (3) Data from January 2013 to July 2023.
Source: Central Bank of Chile.

FIGURE I.22 INTEREST RATE BREAKDOWN INTO MARGINS (1)(2)(3)

(a) Grouped by sales stratum
(percent)



(b) Grouped according to risk rating
(percent)

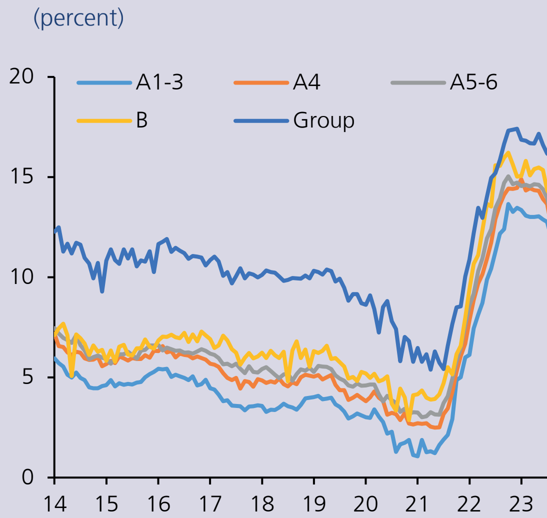


(1) For terms under 12 months. (2) Data from January 2014 to 8 August 2023. (3) In both charts, the orange columns (intensive) represent rate changes that are due to rate adjustments within each subgroup, holding the credit shares of each subgroup constant. The blue columns (extensive) represent rate changes that are due to adjustments of each subgroup's share of total credit, setting a fixed rate charged to each group. The sum of the two columns yields the exact variation in the weighted average interest rate, which is represented by the dotted line. The solid black line corresponds to the level of the average rate, after applying a 3-month moving average. Loans with a term of less than 0.1 months are excluded. Operations with unusually low rates were eliminated.
Sources: Financial Markets Commission (CMF), Internal Revenue Service (SII) and Central Bank of Chile.

FIGURE I.23 BEHAVIOR OF INTEREST RATES ACCORDING TO RISK RATING (1)(2)

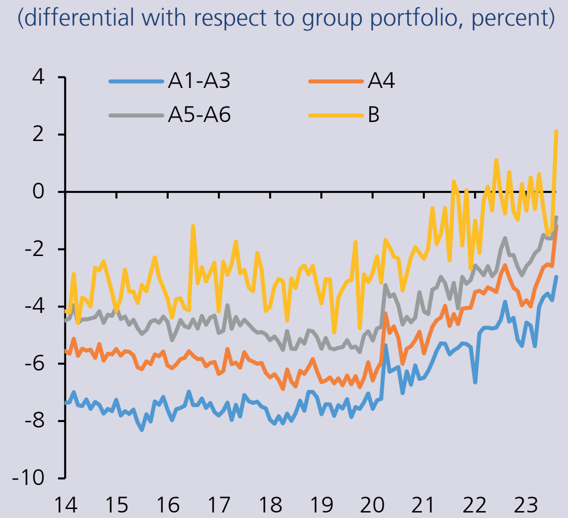
(a) Interest rates by risk rating

(percent)



(b) Average rate differential across firms according to risk rating

(differential with respect to group portfolio, percent)



(1) For terms under 12 months. (2) The left panel depicts the average interest rate perceived by firms for new loans they take within each risk rating, weighted by the share of firms belonging to a risk category in total credit. Operations with unusually low rates were eliminated. The right panel shows the average differential according to an econometric estimation between the rates charged by the same bank, for the same credit term and in the same month to firms with a given risk rating with respect to the rates charged to firms belonging to the group portfolio. Loans for a term of less than 0.1 months and firms with less than five employees are excluded. The results for August only consider the first days of the month. For the last months, preliminary risk rating data are used, which are subject to revision.

Sources: Financial Markets Commission (CMF), Internal Revenue Service (SII) and Central Bank of Chile.

II. FUTURE EVOLUTION OF MONETARY POLICY

In general terms, the macroeconomic scenario has evolved in line with forecasts in the June Report: the economy has continued to advance in its process of reducing macroeconomic imbalances and inflation has continued to fall, although it is still high. The slowdown in private consumption has been moderating, while gross fixed capital formation (GFCF) has improved somewhat at the margin, particularly its machinery and equipment component. Over the next two years, the external impulse to the Chilean economy will remain contained. Our trading partners' growth is forecast to remain weak and the terms of trade will be somewhat lower in the coming quarters following the recent oil price hike, amid still tight external financial conditions. As a result, activity will contract between -0.5 and 0.0% this year, before returning to positive growth rates, ranging from 1.25% to 2.25% in 2024, and from 2.0% to 3.0% in 2025. Headline inflation is projected to decline further, reaching 3% in the second half of 2024. Meanwhile, core inflation —CPI without volatiles— would do so in early 2025. If the central scenario projections of this Report materialize, in the short term the Monetary Policy Rate (MPR) will continue on the path outlined in the July Monetary Policy Meeting. Overall, although wore-case scenarios have been losing importance, the process of inflationary convergence continue to pose significant challenges.

ACTIVITY AND DEMAND PROJECTIONS IN THE CENTRAL SCENARIO

Activity in the second quarter was slightly lower than anticipated in June, due to one-off factors. The biggest difference was concentrated in mining due to operating difficulties in some deposits that affected production. In non-mining activity, manufacturing and wholesale and reatil trade performed below expectations. This was partially offset by a better result in the electricity, gas and water (EGW) sector, which was favored by higher hydroelectric generation thanks to rains that boosted the supply of water in the reservoirs. July's Imacec reported a more positive performance of activity, although partly linked to transitory factors that favored some sectors like personal services and electricity generation, among others.

Regarding domestic demand, second-quarter performance was in line with projections. Consumption remained stable from the previous quarter, while investment was somewhat higher. Regarding the former, zero quarterly growth was observed in the consumption of both goods and services, after the sharp drop in the goods component —especially durables— in the first quarter. Partial third-quarter indicators — such as retail sales and imports— confirm this trend. The durable goods component continues to accumulate the largest drop after its 2021 peak, although its level rebounded slightly in the second quarter. Meanwhile, investment exceeded expectations, in response to the dynamism of machinery and equipment.

With respect to projections, in the central scenario private consumption is expected to remain unchanged for the remainder of the year. By 2024 and 2025 it would resume growth, in line with its fundamentals. Thus, private consumption will close this year with an annual contraction of 4.9%, the same projection as in June, mainly determined by the fall at the beginning of 2023. The projection for the next two years presents no major changes with respect to our June forecasts (1.7% and 1.9% annually, respectively) (table II.1). The estimated behavior of consumption is based on several factors. First, real wages are expected to continue to recover gradually, amid a labor market that continues to perform in line with the business cycle. It is also explained by financial conditions that will become more favorable as the process of MPR cuts advances. Finally, the projection also takes into account the declining pessimism shown by consumer prospects (IPEC).

TABLE II.1 ECONOMIC GROWTH AND CURRENT ACCOUNT

	2022	2023 (f)	2024 (f)	2025 (f)
		(annual change, percent)		
GDP	2.4	-0.5 / 0.0	1.25-2.25	2.0-3.0
National income	1.5	1.3	1.4	2.5
Domestic demand	2.3	-4.3	1.5	2.2
Domestic demand (w/o inventory change)	3.0	-3.1	1.1	2.0
Gross fixed capital form	2.8	-1.2	-0.6	2.4
Total consumption	3.1	-3.7	1.6	1.9
Private consumption	2.9	-4.9	1.7	1.9
Goods and services exports	1.4	0.9	4.0	2.4
Goods and services imports	0.9	-9.8	3.1	1.2
Current account (% of GDP)	-9.0	-3.4	-4.0	-4.0
Gross national saving (% of GDP)	16.4	19.3	19.0	19.1
Gross national investment (% of GDP)	25.4	22.7	23.0	23.1
GFCF (% of nominal GDP)	24.8	23.3	23.1	23.1
GFCF (% of real GDP)	23.6	23.4	22.8	22.8
		(US$ million)		
Current account	-27,102	-11,100	-13,600	-14,500
Trade balance	3,807	14,400	11,100	10,000
Exports	98,548	96,900	99,000	101,900
Imports	94,741	82,500	87,900	91,900
Services	-14,824	-10,500	-10,000	-10,100
Rent	-16,520	-15,500	-15,400	-15,100
Current transfers	434	500	700	700

(f) Forecast.
Source: Central Bank of Chile.

The determinants of GFCF suggest that it will remain weak this and next year, to resume positive growth rates in 2025. The central scenario assumes that this year GFCF will continue with low dynamism due to the construction and other works component, as has been the case for some time. However, a smaller-than-anticipated contraction is now foreseen (-1.2% compared to -3% in June). This is mainly explained by the better performance of machinery and equipment in the second quarter, driven by investments in the energy sector, among others. Going forward, the advance of the cycle of interest rate cuts will gradually ease financial conditions, in a context of less local uncertainty and a reduction in

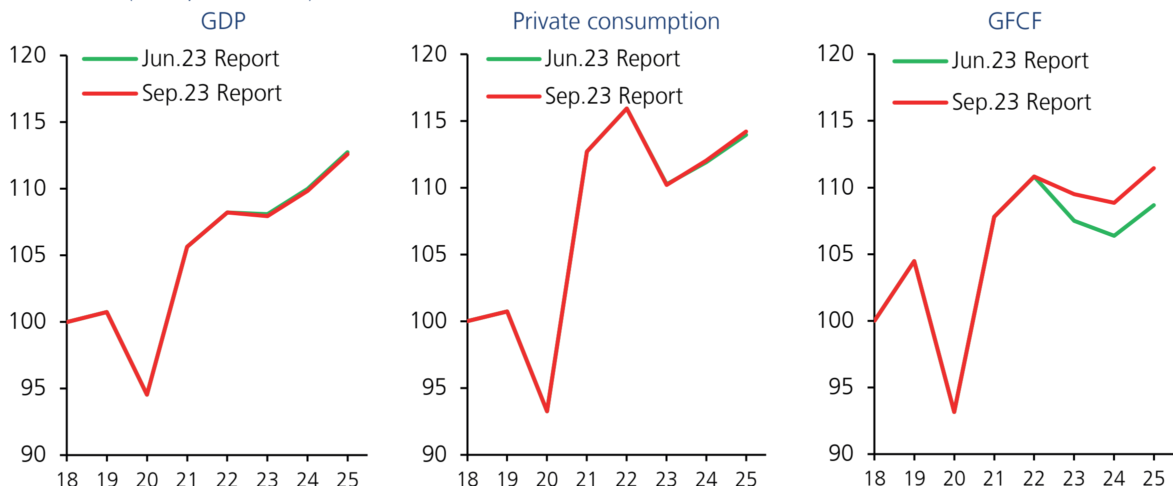
companies' pessimism (IMCE). The Capital Goods Corporation's latest survey reported higher investment amounts for the next two years, particularly in mining and energy projects. Thus, the fall in GFCF is expected to be reduced to -0.6% in 2024 (-1% in June), while for 2025 growth of 2.4% is anticipated (2.2% in June) (table II.1).

On aggregate, the projection for activity for this and the next two years is basically unchanged from June. The main revisions focus on the mining sector. Given the less dynamic evolution of mining GDP in the second quarter compared to the June forecast the central scenario envisages lower mining activity in 2023. However, a rebound in production is projected from the fourth quarter of this year onwards, favored by the start-up of some projects.

In the case of non-mining GDP, second-quarter figures and partial information for the third quarter entail no big variations for forecasts in the projection horizon. Starting in the fourth quarter of this year, it is expected to resume positive quarterly variations, and then gradually approach growth rates consistent with its potential level. Thus, the forecast growth range for this year is between -0.5% and 0.0% (-0.5% and +0.25% in June). For 2024 and 2025, forecasts are unchanged from June: between 1.25% and 2.25% and between 2% and 3%, respectively (table II.1, figures II.1 and II.2).

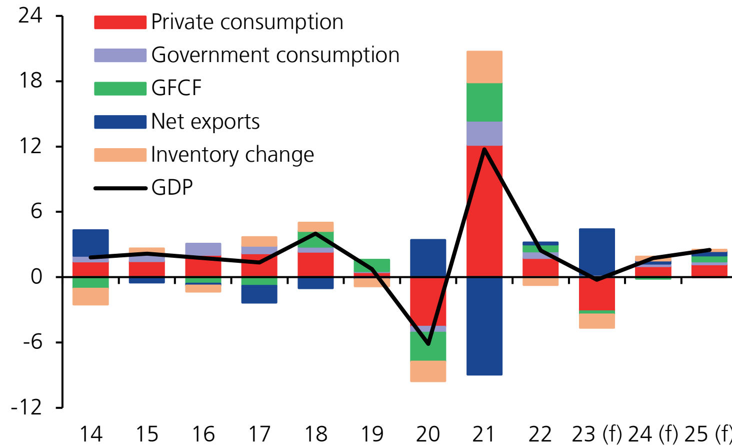
The central scenario maintains the assumption that public expenditure will see a slight annual increase this year. In the latest Public Finance Report (IFP), it estimates that it will rise 0.7% in real annual terms (0.6% in our first-quarter Financial Policy Report), while for next year it was revised down to a real annual rate of 5.1% (6.2% in the previous IFP). Although the structural balance would be somewhat more in deficit this year (-2.1% versus -1.9% in the previous IFP), for 2024 and 2025 it is still projected to be reduced (to -1.8% and -1.1% of GDP, respectively).

FIGURE II.1 ACTIVITY, PRIVATE CONSUMPTION AND GFCF (*)
(index, 2018=100)



(*) For 2023, 2024 and 2025 correspond to the forecast contained in this MP Report. The projections for GDP consider the midpoint of the forecast ranges.
Source: Central Bank of Chile.

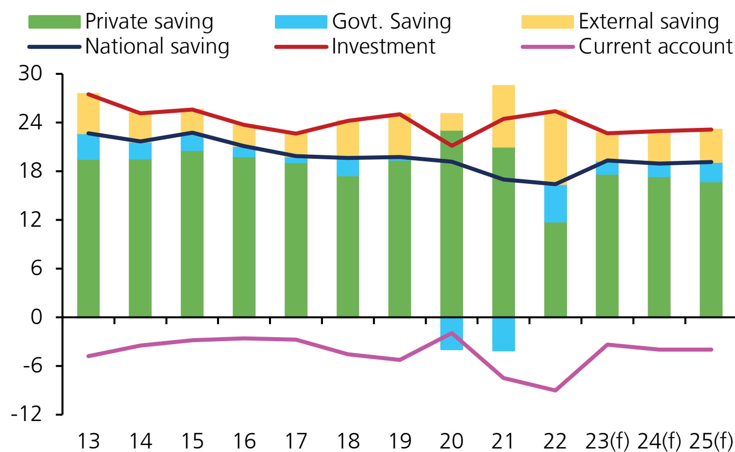
FIGURE II.2 GDP GROWTH AND AGGREGATE DEMAND COMPONENTS CONTRIBUTIONS (*)
(annual change, percentage points)



(*) For 2023, 2024 and 2025, the projections consider the midpoint of the forecast ranges of this MP Report.
(f) Forecast.
Source: Central Bank of Chile.

The current-account deficit will be lower this year, thanks to the recovery of private savings. The private saving rate will reach 17.7% of GDP in 2023, to stand somewhat below 17% of GDP in 2025. Accordingly, the central scenario considers that the current-account deficit as a percent of GDP will be slightly lower in 2023 (3.4% compared with 3.7% in the June Report). This adjustment is explained by a higher trade balance surplus than anticipated in June, in line with the aforementioned improvement in the saving rate, along with lower rents, consistent with the evolution of the mining sector. For 2024 and 2025, the projection for the current account deficit remains at around 4.0% (figure II.3).

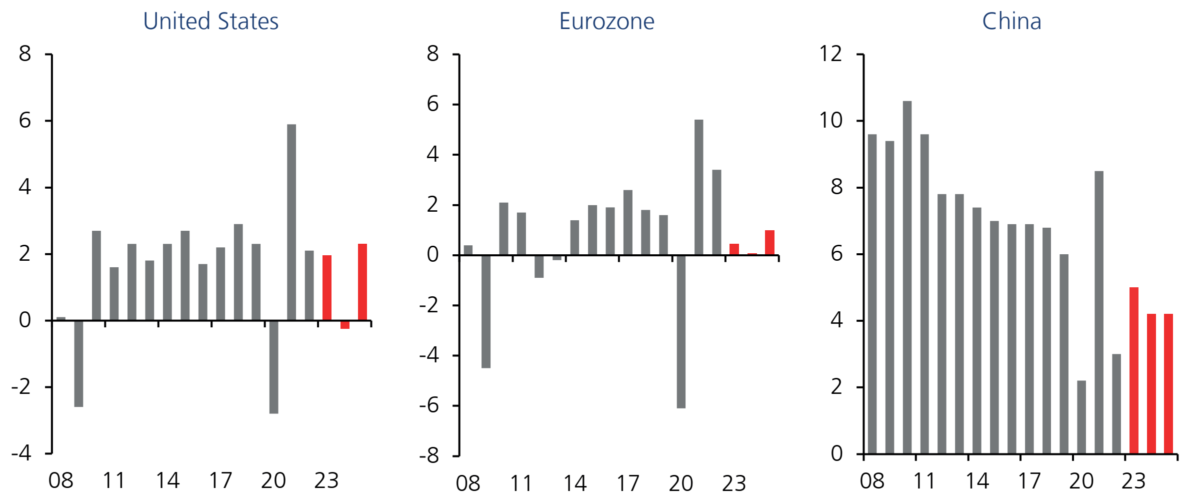
FIGURE II.3 CURRENT ACCOUNT: SAVINGS AND INVESTMENT (*)
(percentage of annual GDP)



(*) The government saving component considers the general government balance as effective data until 2022; for 2023 to 2025, government saving from the central government balance are used as a projection. (f) Forecast.
Source: Central Bank of Chile.

The external scenario will continue to provide a limited boost to the Chilean economy. Between 2023 and 2025, growth prospects for our trading partners remain weak and reflect a rebalancing among some countries. On the one hand, it considers the weaker recent performance of China, whose data surprised on the downside and where the fundamentals of consumption, foreign trade and investment continue to point to low dynamism. Among the latter, it is worth noting the difficulties that its real estate market is facing, the deterioration of consumer confidence and a weak global momentum. Moreover, the high level of private and public debt limits the space for fiscal policy action. On the other hand, although the U.S. economy has been more resilient (Chapter I), it is still expected to face a recession. This is due to the impact on consumption of high interest rates and the steady decline in the savings accumulated during the pandemic. Investment is also expected to underperform due to tightening bank lending conditions. In any case, the recession is expected to be more moderate and delayed than was expected in June (figure II.4 and table II.2).

FIGURE II.4 TRADING PARTNERS GROWTH PROJECTIONS (*)
(annual change, percent)



(*) Red bars correspond to the projections of the central scenario of this MP Report.
Source: Central Bank of Chile.

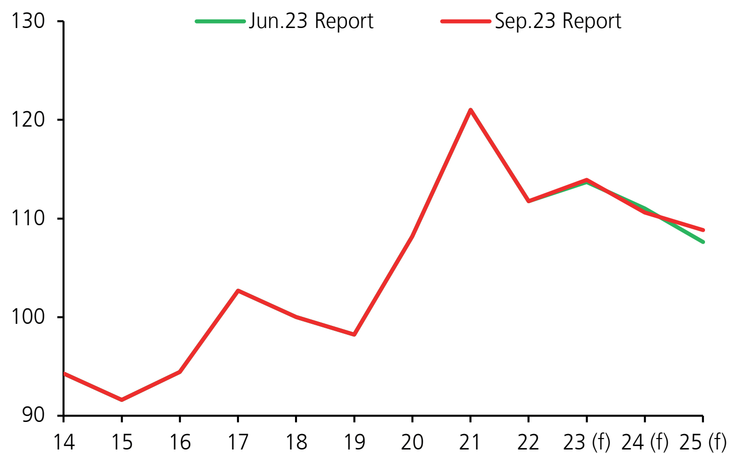
In the coming quarters the terms of trade will be similar to what was forecast in June (figure II.5 and table II.3). The projected price for oil was recently boosted by Saudi Arabia's announced production cut amid recovering demand and a seemingly tight market. As a result, the price of an oil barrel (Brent-WTI average) is expected to average US$79 in 2023, decreasing to US$73 in 2025. For copper, average prices similar to those of the previous report are projected for 2023, 2024 and 2025: US$3.85, US$3.70 and US$3.55 per pound, respectively. Beyond the recent ups and downs, international food price indices declined as anticipated in June and are expected to continue to do so.

TABLE II.2 WORLD GROWTH (*)
(annual change, percent)

	Aveg. 10-20	2021	2022 (e)	2023 (f)	2024 (f)	2025 (f)
World GDP at PPP	3.1	6.3	3.3	2.9	2.2	3.0
World GDP at market exchange rate	2.7	6.3	2.9	2.5	1.6	2.6
Trading partners	3.4	6.7	2.8	3.1	2.3	2.9
United States	1.8	5.9	2.1	2.0	-0.2	2.3
Eurozone	0.7	5.4	3.4	0.5	0.1	1.0
Japan	0.7	2.2	1.0	2.3	1.0	0.7
China	7.2	8.5	3.0	5.0	4.2	4.2
India	5.8	9.1	6.8	5.9	6.0	5.8
Rest de Asia	3.8	4.4	4.2	3.3	3.3	3.1
Latin America (excl. Chile)	1.0	6.4	3.7	1.7	0.4	1.8
Commodity exp.	1.7	5.0	3.2	0.9	0.6	2.5

(*) For definition, see Glossary of economic terms.
(f) Forecast. (e) Estimate.
Source: Central Bank of Chile based on a sample of investment banks, Consensus Forecasts, the IMF, and statistics bureaus of respective countries.

FIGURE II.5 TERMS OF TRADE
(level, 2018=100)



(f) Forecast.
Source: Central Bank of Chile.

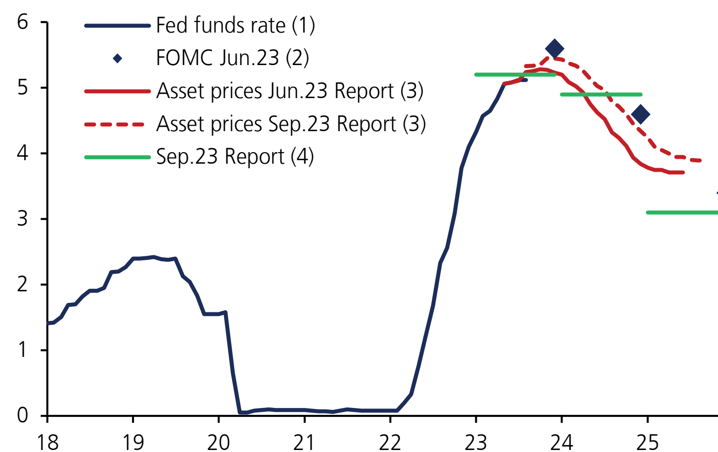
TABLE II.3 INTERNATIONAL BASELINE SCENARIO ASSUMPTIONS

	Aveg. 10-20	2021	2022	2023 (f)	2024 (f)	2025 (f)
			(annual change, percent)			
Terms of trade	1.8	11.9	-7.7	1.9	-2.9	-1.6
External prices (in US$)	0.5	9.3	4.4	-0.5	3.7	4.6
			(levels)			
LME copper price (US$cent/pound)	304	423	400	385	370	355
WTI oil price (US$/barrel)	69	68	94	77	76	70
Brent oil price (US$/barrel)	76	70	100	82	80	75
Gasoline parity price(US$/m3) (*)	585	579	850	745	666	595
US Federal Funds Rate (%)	0.7	0.3	1.9	5.2	4.9	3.1

(*) For definition, see Glossary of economic terms.
(f) Forecast.
Source: Central Bank of Chile.

External financial conditions are still expected to remain tight, in line with efforts to control inflation in developed economies and financial risks that continue to be considerable. Inflation has receded in most economies, albeit with differences in the magnitude of the declines and their outlook. Several factors —domestic and external— explain these discrepancies and the divergences between the monetary policy expectations of the two groups for the near term. Indeed, in the developed world, current levels of tightening are expected to be maintained or to increase further, while some emerging economies have started their tightening cycles while others are expected to follow soon (Box I.1) (figure II.6).

FIGURE II.6 EVOLUTION AND FORECASTS FOR THE FED FUNDS RATE
(percentage points)

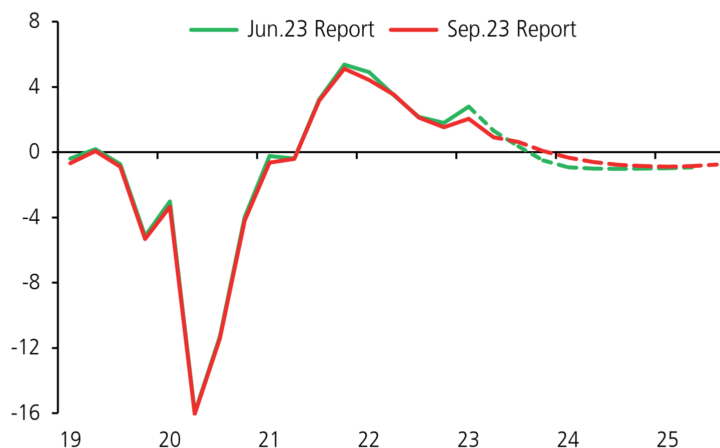


(1) Effective Fed funds rate. Consider information as of August.
(2) Forecast by the the Federal Open Market Committee (FOMC) at the indicated meeting.
(3) Asset prices consider the statistical cut-off dates of each MP Report.
(4) Annual average for the Fed funds rate in 2023, 2024 and 2025, according to the central scenario of this MP Report.
Sources: Bloomberg and Federal Reserve.

THE ACTIVITY GAP AND CONVERGENCE OF INFLATION TO THE TARGET

The central scenario assumes that the activity gap will continue to close in the remainder of this year, consistent with the conditions needed to ensure the convergence of inflation (figure II.7). The gap has narrowed significantly, after several quarters of positive values. Towards 2024 and 2025, our projection continues to see it in negative levels, which will allow completing the inflationary convergence process within the policy horizon.

FIGURE II.7 ACTIVITY GAP (1) (2)
(level, percentage points)



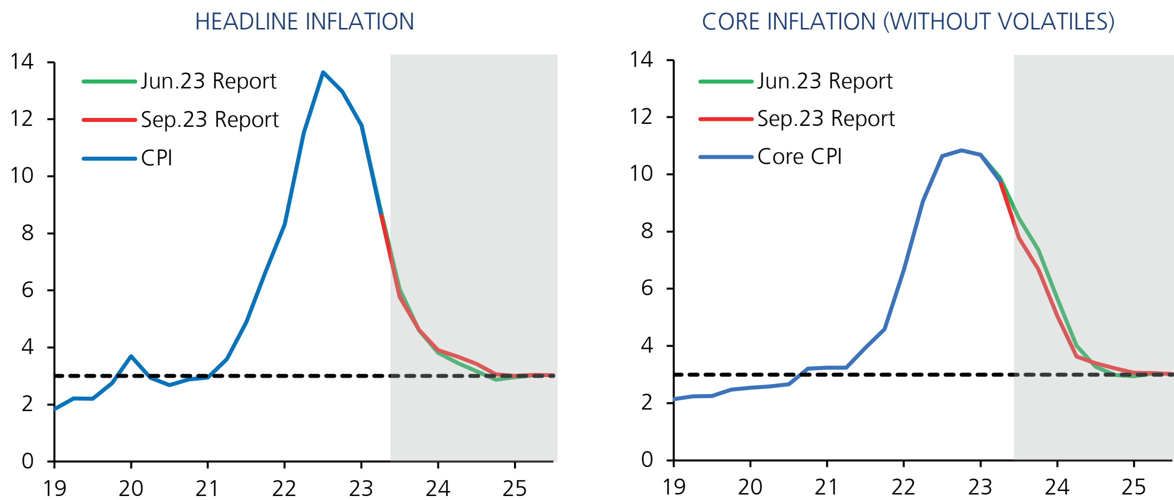
(1) Slashed lines show forecast.
(2) Forecast assumes structural paramenters updated in December 2022 Report (trend GDP) with methodological review of potential GDP.
Source: Central Bank of Chile.

In the central scenario, headline inflation will end this year at 4.3% annually, to converge to 3% in the fourth quarter of 2024 (figure II.8). This projection factors in the lower numbers of recent months (Chapter I). This is offset by the pass-through to prices of the recent peso depreciation, higher international fuel prices, as well as the impact of recent floods on some food prices. The combination of these factors explains why in 2024 inflation will average somewhat more than was projected in June.

Core inflation will be slower to decline than headline inflation. However, for most of the projection horizon, its trajectory will be below the June forecast and will end this year at 6.3% reaching 3% at the beginning of 2025. In the near term, the services component will sustain high monthly variation rates, even above their historical averages, consistent with wages and prices readjustment processes through indexation mechanisms that will still take into account the high inflation of the past year. The central scenario assumes that the multilateral real exchange rate (RER) will remain around its current levels during the projection horizon. Goods inflation will continue to fall, influenced by the moderation of both demand and external and internal costs pressures. These last elements, coupled with the negative surprise accumulated since the previous MP Report (Chapter I), explains why the projected core inflation trajectory will be lower than the one forecast in June for much of the projection horizon.

The volatile components of inflation will take longer to decline than was projected in June. For foods, a transitory increase in prices is considered due to the floods of last August. In energy, inflation was lower than expected in June due to the elimination of the winter electricity tariff that came into effect in the second half of July. However, the upward revision in the oil price and the recent exchange rate depreciation are factors that will constrain a more rapid decline in the projected path for volatile inflation.

FIGURE II.8 INFLATION FORECAST (*)
(annual change, percent)



(*) Gray area, as from the third quarter of 2023, shows forecast.
Sources: Central Bank of Chile and National Statistics Institute (INE).

TABLE II.4 INFLATION (1)
(annual change, percent)

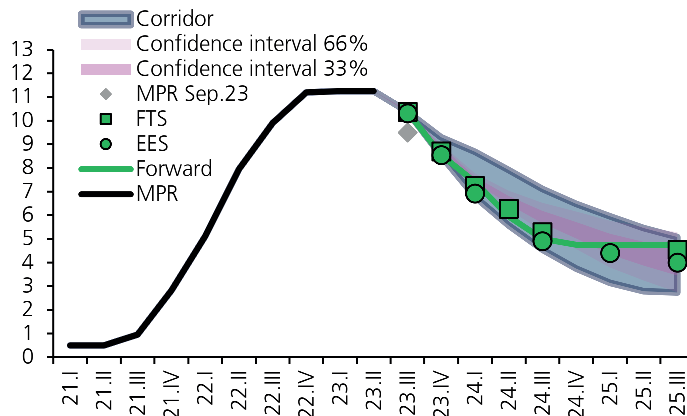
	2022	2023 (f)	2024 (f)	2025 (f)
Average CPI	11.6	7.6	3.5	3.0
December CPI	12.8	4.3	3.0	3.0
CPI in around 2 years (2)				3.0
Average core CPI	9.3	8.7	3.8	3.0
December core CPI	10.7	6.3	3.1	3.0
Core CPI around 2 years (2)				3.0

(1) Core inflation is measured using the CPI without volatiles.
(2) Inflation forecast for the third quarter of 2025.
(f) Forecast.
Sources: Central Bank of Chile and National Statistics Institute (INE).

MONETARY POLICY STRATEGY: THE CENTRAL SCENARIO, SENSITIVITIES AND RISKS

The macroeconomic scenario has evolved as anticipated, with inflation projected to converge to the 3% target in the second half of 2024. If the central scenario projections of this Report materialize, in the short term the MPR will continue on the path outlined in the July Meeting. This means that, at the end of the year, the MPR would be between 7.75 and 8%. In any case, the magnitude and timing of the process of MPR reductions will take into account the evolution of the macroeconomic scenario and its implications for the inflation trajectory and the achievement of the 3% target within the policy horizon.

FIGURE II.9 MPR CORRIDOR (*)
(quarterly average, percent)



(*) The corridor is built by following the methodology described in boxes V.1 of March 2020 Report and V.3 of March 2022 Report. Includes August EES, FTS pre-policy-meeting of September and the average smoothed forward curve of quarter to 30 August. This is calculated by extracting the implicit MPR considering the forward curve on the interest rate swap curve up to 2 years, discounting the fixed rates at every maturity at the simple accrual of the ICP. For the current quarter the surveys and the forwards consider the average daily effective and are completed with the respective sources.
Source: Central Bank of Chile.

The borders of the MPR corridor reflect sensitivity scenarios where the speed of the inflationary convergence process yields the way to interest rate adjustments other than those considered in the central scenario central (figure II.9). On this occasion, the Board considers that this type of situation is linked to the evolution of both the global and the local economy. In any case, as always, the conduct of monetary policy will be contingent on how incoming information will affect the projected dynamics of inflation.

The upper bound of the corridor is defined by sensitivity scenarios where the process of inflationary convergence to the 3% target is less favorable than expected. For example, this could occur if a stronger world economy is observed, particularly in the U.S., along with increases in commodity prices. In the short term, this would push global inflation up, which would be transmitted to local inflation. Its medium-term inflationary effects could be more persistent if inflation expectations are affected.

The lower bound of the corridor reflects scenarios in which the inflationary convergence is faster than anticipated. This could be the case if the economy faces lower-than-expected pressures from the demand side. Such a situation would arise if activity is subject to shocks that reduce the external impulse; if

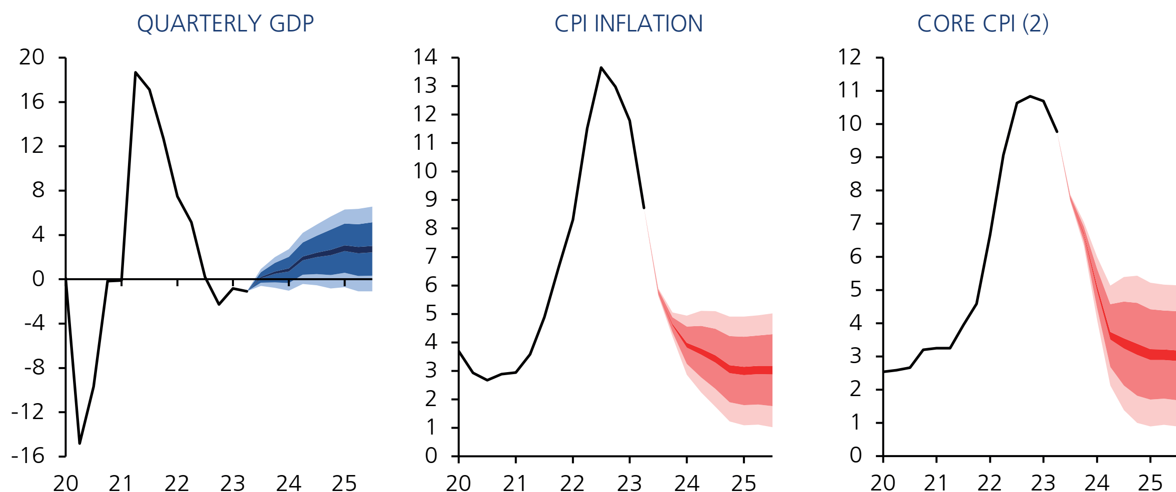
there is a deterioration in business and household confidence that impairs the performance of investment and consumption; or if the impact of still constrained credit conditions is greater than initially estimated.

On this occasion, an intermediate scenario was analyzed in which China's activity is affected by a shock of similar magnitude to that observed during the 2015-16 period, due to a worsening of the crisis in its real-estate market. Such a situation would significantly reduce the prices of commodities, including oil and copper. Financial conditions would also tighten, particularly for the economies with the strongest trade relations with China, as is the case of Latin America. Although in the short term the exchange rate depreciation would increase inflation, medium-term inflationary pressures would be significantly reduced by the weakness of the local economy. This would lead to a medium-term path for the MPR below the central scenario. In any case, this trajectory would run above the one at the lower bound of the MPR corridor.

In addition to the sensitivity scenarios, other situations are analyzed in which more drastic changes in the economy would have a more significant impact and would require a monetary policy response that exceeds the limits of the MPR corridor (figure II.10).

The Board considers that, as depicted in the June Report, risks remain linked mainly to the global macro-financial situation. In the event of a further deterioration, this could trigger episodes of volatility in the financial markets, reduce liquidity and stimulate capital to flow out of emerging economies. Added to this are the concerns that have arisen regarding China, particularly the evolution of its economy and financial market. If any of these risks materialize, their implications for monetary policy would depend on how the combination and magnitude of these elements would affect the outlook for the medium-term inflationary convergence.

FIGURE II.10 GROWTH AND INFLATION FORECASTS (1)
(annual change, percent)



(1) The figure shows confidence interval of central projection at the respective horizon (colored area). Confidence intervals of 10%, 70%, and 90% around the baseline scenario are included. Confidence intervals are built using the RMSE of XMAS-MEP models' 2009-2017 average. (2) Measured with the CPI without volatiles.
Sources: Central Bank of Chile and National Statistics Institute (INE).

ANNEX A:

The Central Bank of Chile balance sheet

This annex presents and analyzes the situation and projections of the main items of the financial statements of the Central Bank of Chile. First, the evolution of the balance sheet for the first half of 2023 is reviewed. Second, the composition of the balance sheet is analyzed. Finally, the projection for 2023 is presented.

EVOLUTION IN THE FIRST HALF OF 2023

Compared to the close of 2022, the first half of this year saw a decrease in assets and an increase in liabilities, resulting in a drop in net worth (table A.1). Thus, between 31 December 2022 and 30 June 2023, the size of assets decreased by C$2,558 billion, going from 26.2% to 24.2% of GDP, while liabilities increased by C$1,027 billion, closing the period at 25.9% of GDP. As a result, the Central Bank went, in 6 months, from having negative net worth of C$1,024 billion (equivalent to -0.4% of GDP) at the end of 2022 to negative net worth of C$4,609 billion (equivalent to -1.7% of GDP) at the end of June. This result was mainly explained by the higher cost associated with the issuance of Central Bank Discount Notes (PDBC) and the variation of the exchange rate in that period (as of 30 June, the Chilean peso had appreciated 6.6% with respect to the end of 2022).

The decrease in assets during the period was close to 1.9% of GDP (table A.1) and was mainly explained by the lower value of international reserves measured in pesos, for C$1,950 billion. This variation was due to a reduction in overnight deposits held by commercial banks by C$419 billion and to a lower value of the investment portfolio and other reserve assets by C$1,531 billion, mainly explained by the appreciation of the peso (6.6%)[1]/. Assets in local currency decreased by C$405 billion due to a lower stock of bank bonds of C$388 billion (maturities of C$549 billion and a higher value of C$161 billion), maturity of the Permanent Liquidity Facility (FPL) of C$19 billion, and the higher value of the balance of fiscal transfers (law 18,401) of C$3 billion. All in all, assets in local currency went from 13.4% to 12.6% of GDP in the first half of 2023.

In contrast, liabilities decreased by 0.6% of GDP, where the monetary base decreased by C$744 billion, from 6.7% to 6.2% of GDP between December 2022 and June 2023. On the other hand, secondary market notes increased by C$4,798 billion—PDBCs increased by C$4,934 billion, while long-term debt decreased by C$136 billion—, from 14.5% to 15.7% of GDP in the same period. In addition, policy instruments with banks (essentially the Permanent Deposit Facility, PDF) decreased by C$2,408 billion, from 3.6% to 2.6% of GDP during the first half of 2023. On the other hand, other liabilities with banks (mainly overnight deposits of commercial banks) decreased by C$419 billion, from 0.6% to 0.4% of GDP, as well as other liabilities by C$200 billion, due to the lower value of liabilities abroad, which went from 1.1% to 1.0% of GDP (table A.1).

[1]/ As a proportion of GDP, international reserves represented 11.6% as of June 2023, which compares to 12.8% at the end of 2022. The ratio is calculated by converting the stock of reserves from US dollars to Chilean pesos, using the period-end exchange rate. GDP is reported in Chilean pesos. These figures may differ from those used in publications where the US dollar is considered as a numeraire.

The period ended with negative net worth of C$4,609 billion (-1.7% of GDP), explained by a component of initial capital and other reserves that was negative C$611 billion (-0.2% of GDP) and also by a negative net result for the year of C$3,998 billion (-1.5% of GDP). The latter figure is mainly explained by the variation in the exchange rate (-C$2,099 billion), results of operations with currency derivatives associated with the program for the sale of foreign exchange hedging instruments (NDF) for C$644 billion, net interest payments of -C$2,623 billion and non-financial costs of -C$67 billion. These negative results were partly offset by gains associated with the UF variation of C$159 billion (mainly related to the investment in UF-denominated bank bonds). Non-financial costs in the balance sheet are mainly attributable to administrative and personnel expenses of C$37 billion and to the issuance of working capital of C$28 billion.

TABLE A.1 CENTRAL BANK OF CHILE BALANCE SHEET: SUMMARY STATEMENTS AND RESULTS (percent of GDP

	2020	2021	2022	Jun.23	2023 (f)
ASSETS	**29.5**	**32.8**	**26.2**	**24.2**	**27.0**
International reserves (1)	13.8	18.1	12.8	11.6	14.0
Fiscal promissory notes and other loans to government	0.2	0.1	0.1	0.1	0.1
Monetary policy instruments (2)	11.0	12.0	11.0	10.6	11.0
Bank bonds (3)	4.2	2.3	1.9	1.7	1.6
Term deposits	0.1	0.0	0.0	0.0	0.0
Other assets	0.1	0.1	0.3	0.2	0.2
LIABILITIES	**30.3**	**31.4**	**26.6**	**25.9**	**29.4**
Promissory notes with secondary market	10.5	17.8	14.5	15.7	18.3
Policy instruments with banks	3.8	1.9	3.6	2.6	3.1
Other liabilities with banks	0.6	1.5	0.6	0.4	0.6
Other liabilities except monetary base (4)	0.5	1.3	1.1	1.0	1.1
Monetary base	15.0	8.9	6.7	6.2	6.3
NET WORTH (A+B+C)	**-0.9**	**1.4**	**-0.4**	**-1.7**	**-2.4**
A. Initial capital	-0.6	-1.0	0.7	-0.2	-0.3
B. Net results	-0.2	2.4	-1.1	-1.5	-2.1
Non-financial	0.0	-0.1	-0.1	0.0	-0.1
Net interests (5)	-0.2	-0.1	-1.8	-1.0	-1.6
Due to change in exchange rate and UF	0.0	2.5	0.7	-0.5	-0.4
C. Capital contribution	0.0	0.0	0.0	0.0	0.0
Payable position in foreign currency (FC) (6)	12.9	15.4	11.4	10.0	12.4

(1) International reserves as a percent of GDP, measured in Chilean pesos, may present marginal difference with other measures in dollars.
(2) Includes Credit Facilities Conditional on Increased Bank Lending (FCIC I, II, and III) and Liquidity Credit Line (LCL, It was valid until March 2022).
(3) Includes spot purchase and forward sale transactions (CC-VP) of bank bonds.
(4) Includes other foreign liabilities (mainly SDR allocations with the IMF).
(5) Difference between interest earned on investments and monetary policy instruments under assets and interest paid on debt certificates and monetary policy instruments under liabilities.
(6) Assets minus liabilities payable in foreign currency.
(f) Forecast.
Source: Central Bank of Chile.

The results associated with the assets acquired as part of the special measures adopted by the Central Bank of Chile during 2020 and 2021, and the foreign exchange intervention program during the second half of 2022, explain part of the net worth result for the first half of 2023. Regarding assets denominated in local currency, the bank bond portfolio generated total gains of C$146 billion, which includes interest and readjustment gains of C$152 billion and a lower market value of C$6 billion. On the other hand, interest income associated with the Conditional Credit Facility for Increased Placements (FCIC) of $73 billion was recorded. Finally, forward sales of dollars (NDF) associated with the 2022 foreign exchange intervention program (in April the reduction of the stock began at a rate of 1/10 per month) generated revenues of C$644 billion in the period (table A.2).

TABLE A.2 NET WORTH EFFECTS OF SPECIAL MEASURES IMPLEMENTED BY THE CENTRAL BANK OF CHILE (1)
(billions of Chilean pesos)

	Ammount realized/current stock (4)	Profit/Loss
Bank bonds (2)	4,535	146
Loans FCIC (2)	28,930	73
Forward sales of dollars (NDF) (3)	6,710	644
Total		863

(1) Earnings or losses with an impact on net worth of special measures implemented by the Central Bank of Chile during first half of 2023
(2) Measures announced as of March 2020, due to financial tensions related to Covid-19 and withdrawals from pension funds.
(3) Measure announced on July 14, 2022 as part of the exchange intervention program for the second half of 2022.
(4) Amounts correspond to current stocks at 30 June 2023.
Source: Central Bank of Chile.

In terms of flows and consistent with the above, during the first half of this year, variations in the balance sheet explained a C$744 billion drop in the monetary base and an increase in the foreign currency payable position equivalent to C$385 billion. The latter was the result of the foreign currency purchase program to replenish and expand international reserves announced on 9 June 2023, for a total of US$10 billion. By the end of 2023, the foreign currency payable position is projected to increase to C$4.303 billion or US$5.36 billion (table A.3).

In addition to the structure and size of the balance sheet, changes in relevant financial variables were also observed during the first half of 2023. The negative asset-liability yield gap increased to 527 basis points (bp), from 514 bp at the end of 2022, due to the restructuring of liabilities (increase in the amount and cost of PDBCs, and reduction of the monetary base). On the other hand, the duration gap between assets and liabilities decreased by 2.8 months, due to the reduction in the duration of assets in local currency. Finally, in both assets and liabilities, the balance sheet exposure to foreign currencies decreased due to lower overnight deposits from commercial banks and the lower value of assets and liabilities in foreign currency due to the appreciation of the peso (table A.4).

TABLE A.3 FLOWS IN CENTRAL BANK OF CHILE BALANCE SHEET (1)
(billions of Chilean pesos)

	2020	2021	2022	Jun.23	2023 (f)
1. Reservas Internacionales Netas	-1,168	9,294	-5,730	-198	3,720
2. Instrumentos de política en moneda nacional (MN)	17,895	-14,066	3,983	-3,097	-8,125
3. Otras operaciones en MN excepto base monetaria (2)	26	-291	-2,188	1,968	3,485
4. Otras operaciones en moneda extranjera (ME) (3)	1,129	-3,737	120	583	583
Base Monetaria (variación=1+2+3+4)	17,883	-8,800	-3,815	-744	-337
Posición pagadera en ME (operaciones de cambio=1+4) (4)	-39	5,557	-5,610	385	4,303

(1) Exchange flows. Corresponding balances are affected also, and where appropriate, by interests, monetary corrections, and price changes.

(2) Servicing of UF tax notes, servicing of subordinated debt, and other local currency transactions.

(3) Fiscal and bank deposits and other operations in foreign currency.

(4) Includes forex market operations related to policy decisions and forex operations with operating purposes of the Central Bank of Chile.

(f) Forecast. For the purposes of this exercise, the exchange rate at the close of June is used.

Source: Central Bank of Chile.

TABLE A.4 MAIN FINANCIAL VARIABLES IN CENTRAL BANK OF CHILE BALANCE SHEET

	Jun.23		Dec.22	
	Assets	Liabilities	Assets	Liabilities
Average rate of return (%)	3.1	8.4	3.1	8.2
Average duration (months) (*)	21.3	0.8	24.1	0.7
Foreign currencies (%)	48.8	5.4	50.0	6.4
Local currencies, UF (%)	7.2	0.1	7.5	0.1
Local currencies, Chilean peso (%)	44.0	94.6	42.6	93.6

(*) Liabilities include the monetary base with zero duration. UF-denominated assets and liabilities are corrected by a factor of 0.5.

Source: Central Bank of Chile.

COMPOSITION OF THE BALANCE SHEET

At the end of the first half of 2023, 48.8% of assets were denominated in foreign currencies (50.0% at the end of 2022). These are composed of US dollars (69.9%), IMF Special Drawing Rights (SDRs) (10.2%), Chinese renminbi (6.8%), euros (4.4%), British pound (or pound sterling, 3.6%), Australian dollar (2.6%) and South Korean won (2.5%)[2]/. In absolute terms, assets denominated in foreign currency decreased by $2,017 billion, which owes mainly to the lower peso value of international reserves and by lower commercial bank deposits in the cash portfolio. Assets in local currency accounted for 51.2% of total assets (85.9% in pesos and 14.1% in UFs), which is equivalent to a decrease of C$549 billion due to the maturity of bank bonds.

[2]/ The most important portfolio in foreign currency is the investment portfolio of international reserves (86.4% of total assets). The currency composition of the benchmark comparator of the investment portfolio is US dollar (77%), Chinese renminbi (8%), euro (5%), pound sterling (4%), Australian dollar (3%), and South Korean won (3%).

With respect to total liabilities, the proportion of notes and policy instruments increased from 54.6% to 60.6%. This movement was partially offset by a decrease in the monetary base from 25.3% at the end of 2022 to 23.9% at the end of June 2023. On the other hand, the reduction in the monetary base was mainly explained by a decrease in currency, specifically in the balance of bills and coins for $1,391 billion.

BALANCE SHEET PROJECTIONS FOR 2023

The short-term projection considers two main working assumptions: (i) the foreign exchange purchase program proceeds as scheduled (purchase of close to US$ 5 billion in 2023) and (ii) in line with what was announced, the purchase of reserves is sterilized with debt issuance. Regarding the financial assumptions, the central scenario contemplates a decrease in the cost of PDBC issuance. In relation to macroeconomic assumptions, the projection of nominal GDP for 2023 uses projected values of real GDP growth and average inflation from the June 2023 MP Report.

Under these assumptions, net interest payments are projected to reduce the net worth by approximately 1.6% of GDP by 2023. In turn, due to changes in the valuation of international reserves and local currency assets, net worth is projected to decrease by 0.4% of GDP in 2023. Nevertheless, net worth will increase its deficit to 2.4% of GDP in 2023 and the size of balance sheet assets is estimated at 27.0% of GDP.

ANNEX B:

International reserves management

International reserves are the liquid assets in foreign currency held by the Central Bank of Chile and constitute a policy tool for the achievement of its main objectives: to ensure the stability of the currency and the normal functioning of internal and external payments. Its management seeks to provide, in an efficient manner, secure access to international liquidity in accordance with the legal framework defined in Article 38, Title III, of its Constitutional Organic Law.

In order for the international reserves to be an effective tool to fulfill the objectives of the Central Bank of Chile, they must have adequate level and liquidity. When this is met, international reserves may vary due to price and parity movements, but these changes will not alter the Bank's ability to honor its commitments. In this context, the objectives of liquidity and capital preservation are two central axes for the management of reserves, since they ensure that the Central Bank, with a certain level of confidence, will be able to have at any time the amount of resources necessary to achieve its policies, within a limited period of time and at a reasonable cost.

For the management of international reserves, the Bank has a separation of responsibilities at different hierarchical levels, in line with international recommendations on this matter. Likewise, internal and external audits are carried out periodically to review the different processes. This ensures that the Bank's decision-making and management evaluation processes are well defined and that risks are controlled.

For the administration of international reserves, the principles of segregation of duties are applied. The Market Operations Area manages international reserves taking into consideration the guidelines established in the Investment Policy approved by the Bank's Board. The Strategic Business Area participates in the design of the investment policy proposed to the Board, functionally administers the transactional system where operations are carried out and is responsible for analyzing investment performance. The Operations and Payment Systems Area is responsible for the perfecting of investment operations, meaning the recording, accounting and generation of all payment instructions and/or fund movements that ensure compliance with the rights and obligations contracted. These three units report functionally to the Financial Markets Division.

In turn, the Corporate Risk Division is responsible for identifying, evaluating, measuring and monitoring the corporate, financial and strategic risks of the Central Bank of Chile. Accordingly, it performs the functions of financial compliance, measurement of risk applicable to the management of international reserves and validation of the methodologies used. At the same time, the Corporate Risk Division acts as technical counterpart of the Financial Markets Division in the processes of risk management of the Bank's financial operations and definition of policies.

On the other hand, the Bank's Comptroller reports directly to the Board and is responsible for periodically evaluating the efficiency and effectiveness of internal control, operational risk management and the governance of the integrated reserve management process.

The strategic asset allocation or benchmark, which serves as a guide for reserve management, is reviewed periodically to ensure that the return and risk profile is consistent with the policy framework and strategic objectives established by the Board. The design of the Investment Policy considers, among other variables, the Bank's potential liquidity needs and the financial impact on the Bank's balance sheet.

In accordance with the Investment Policy, the Investment Portfolio (table B.1) consists of two portfolios: Liquidity (60%) and Diversification (40%). The objective of the Liquidity portfolio is to guarantee the liquidity necessary to comply with the policy mandates, which is why this portfolio is invested only in U.S. Treasury bonds, one of the most liquid fixed income markets in the world. On the other hand, the Diversification portfolio aims to diversify risks and contribute to obtaining returns in the medium and long term, consistent with the expected evolution of the Bank's balance sheet, although it also has high levels of liquidity.

TABLE B.1 BENCHMARK STRUCTURE OF INTERNATIONAL RESERVES INVESTMENT PORTFOLIO (1)(2)

Structure	Credit risk	Share	Benchmark comparator
Liquidity portfolio	Sovereign	60%	Bloomberg Barclays Index: Global Aggregate Treasuries. (100% USD)
Diversification portfolio	Sovereign	40%	Índice Bloomberg Barclays: Global Inflation-Linked. (27.5% USD), (12.5% EUR), (10.0% GBP) Bloomberg Barclays Index: Global Aggregate Treasuries. (20.0% CNY), (15.0% USD), (7.5% AUD), (7.5% KRW)
Total portfolio	Sovereign	100%	

(1) Global Inflation-Linked EUR index includes only those issued in France, Germany, and Spain.

(2) Global Treasury KRW index includes only Treasury bonds from South Korea.

Source: Central Bank of Chile.

The International Reserves Investment Portfolio, together with the Cash Portfolio (balances held in current accounts by the Treasury, public enterprises and commercial banks) and the Other Assets Portfolio (Special Drawing Rights of the International Monetary Fund (SDRs), certified gold and others), make up the International Reserves Portfolio.

The benchmark composition of the Investment Portfolio includes a total of six currencies: US dollar (77%), Chinese renminbi (8%), euro (5%), British pound (4%), Australian dollar (3%) and South Korean won (3%). The Liquidity Portfolio benchmark is composed entirely of nominal U.S. Treasury bonds. The Diversification Portfolio benchmark includes nominal sovereign bonds (50%) denominated in: Chinese renminbi (20%), US dollar (15%), Australian dollar (7.5%) and South Korean won (7.5%), as well as inflation-indexed bonds (50%) denominated in US dollar (27.5%), euro (12.5%) and British pound (10%).

In terms of credit risk, the benchmark comparator contemplates 100% exposure to sovereign risk. The overall interest rate risk of the Investment Portfolio benchmark, measured by duration, is approximately 31.3 months. In turn, the Liquidity Portfolio has a duration of 31.9 months and the Diversification Portfolio has a duration of 30.4 months (table B.2).

TABLE B.2 BENCHMARK STRUCTURE OF CURRENCIES, TERMS, AND DURATION OF INVESTMENT PORTFOLIO (1)(2)(3)
(percent)

		Investment portfolio				Total
Currency	**Share/ Duration**	**Liquidity portfolio (LP)**	**LP subtota**	**Diversification portfolio (DP)**	**DP subtotal**	**Investment portfolio**
USD	Share	60.0%	100.0%	17.0%	42.5%	77.0%
	Duration (months)	**31.88**		**28.72**		**31.18**
CNY	Share			8.0%	20.0%	8.0%
	Duration (months)			**32.02**		**32.02**
EUR	Share			5.0%	12.5%	5.0%
	Duration (months)			**29.84**		**29.84**
GBP	Share			4.0%	10.0%	4.0%
	Duration (months)			**32.17**		**32.17**
AUD	Share			3.0%	7.5%	3.0%
	Duration (months)			**33.41**		**33.41**
KRW	Share			3.0%	7.5%	3.0%
	Duration (months)			**31.55**		**31.55**
Total	Share			40.0%	100.0%	100.0%
	Duration (months)			**30.43**		**31.30**

(1) U.S. dollar liquidity portfolio is comprised of nominal bonds only (100%). U.S. dollar diversification portfolio is composed of nominal (15.0%) and inflation-indexed bonds (27.5%).
(2) Euro (12.5%) and pound sterling (10.0%) diversification portfolios are comprised of indexed bonds only.
(3) Duration of indexed bonds is adjusted by a factor of 0.5.
Source: Central Bank of Chile at 30 June 2023.

For the management of credit risk associated with the investment of international reserves, i.e., definition of eligibility and maximum exposure allowed to countries, supranational entities, commercial banks and agencies, variables such as risk rating, level of institutions' net worth, market size, debt ratios and explicit guarantees, among others, are used. For market risk management, a risk budget (tracking error) is mainly used. Said risk budget contemplates a limit of 40 basis points (bp) as a monthly average and a limit of 50 bp that cannot be exceeded at any time.

As a complement to internal reserve management, since 1995 the Bank has maintained external management programs for a fraction of its reserves. The purpose of this has been to have an active comparator to evaluate internal management, add economic value and facilitate the transfer of knowledge and technology.

At the end of the first half of 2023, a portion of the Investment Portfolio (3.3%) was managed independently by two external managers: BNP Paribas Asset Management USA, Inc. (BNPP AM) and Allianz Global Investors GmbH (AGI). These firms began their mandate in November 2021, following a selection process that took place during the second half of that year.

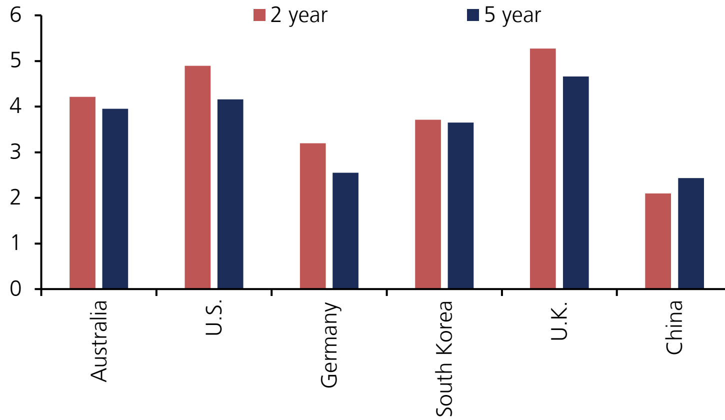
In the first half of 2023, the return obtained in the management of international reserves was 1.11% measured in currency of origin, a figure that does not incorporate appreciations or depreciations of the portfolio's currencies. Measured in US dollars, the return was 0.93% (table B.3), a figure which, in addition to incorporating the yields of assets in the currency of origin, considers the trajectory of the parities in which the assets are invested with respect to the US dollar. In general terms, the positive performance expressed in dollars is explained by the interest accrual recorded during the period, considering the higher level of sovereign interest rates in force in the relevant economies for the portfolio during the first half of 2023 (figure B.1). The effect of this increase in market value was partially offset by the appreciation of the US dollar against the rest of the portfolio's basket of currencies. It should be noted that, measured in pesos, the profitability for the first half of the year was -5.74%, which is mainly explained by the weakening of the basket of currencies in which the portfolio is invested with respect to the local currency. On the other hand, the differential return for the first half of the year attributable to the management of international reserves was 4.2 bp under the benchmark comparator.

TABLE B.3 ABSOLUTE AND DIFFERENTIAL RETURNS, INTERNATIONAL RESERVES MANAGEMENT (1)(2)(3)
(percent)

Period	In currency of origin		In US dollars		Differential
	IR	BMK	IR	BMK	
2023	1.11	1.15	0.93	0.97	-0.04
2022	-3.20	-3.32	-4.71	-4.82	0.11
2021	0.58	0.52	-0.13	-0.04	-0.09
2020	2.42	2.39	5.64	5.63	0.02
2019	5.67	6.25	5.39	6.09	-0.70
2018	1.70	1.66	-0.35	-0.32	-0.03
2017	0.77	0.62	4.17	4.06	0.11
2016	0.90	0.90	0.13	0.17	-0.04
2015	0.73	0.90	-3.74	-3.58	-0.16
2014	1.65	1.52	-2.94	-3.14	0.21

(1) Figures for 2023 are non-annualized and correspond to the first half of the year.
(2) Excludes holdings in monetary gold, special drawing rights, reserve position in the IMF, and other reserve assets.
(3) In 2019 and 2021, adjustments were made to the benchmark comparators. The returns shown for those years do not include the waiver periods granted for the implementation of the policy changes.
Source: Central Bank of Chile.

FIGURE B.1 BENCHMARK RATES FOR 2 AND 5-YEAR GOVERNMENT BONDS (*)
(percent)



(*) Sovereign interest rates observed at the end of the first half of 2023.
Source: Bloomberg.

In June 2023, the Board of the Central Bank of Chile decided to initiate a gradual program of replenishment and expansion of international reserves to strengthen the country's international liquidity position. The program, which began on 13 June 2023, contemplates the purchase of US$10 billion through regular dollar purchases of US$40 million per day in competitive auctions. As of 30 June 2023, the program amounted to US$480 million.

As of 30 June 2023, international reserves reached US$39,497.4 million (figure B.2). Of the total of these reserves, US$34,140.9 million corresponded to the Investment Portfolio, US$1,317.1 million to the cash portfolio, and US$4,039.3 million to other assets. Of the total international reserves, 69.9% were invested in US dollars, 4.4% in euros and 25.7% in other currencies. It should be mentioned that within the other currencies are the SDRs, with a share of 10.2% and the Chinese renminbi with a share of 6.8%.

FIGURE B.2 INTERNATIONAL RESERVES
(stock, USD billion)

Source: Central Bank of Chile.

As of 30 June 2023, international reserves totaled US$343.2 million more than at the end of 2022. On the one hand, there was a decrease in the cash portfolio (US$411.5 million), whose variation reflected changes in the stock of deposits and balances in accounts held by the financial system with the Bank. On the other hand, the Investment Portfolio increased by US$672.8 million with respect to the end of the previous year, mainly due to purchases made as part of the reserve expansion and replenishment program (US$480 million) and to positive net results associated with interest earnings and market price variations. In addition, during the period there was an increase of US$82 million in other assets, mainly due to SDR operations with the IMF (table B.4).

TABLE B.4 INTERNATIONAL RESERVES BREAKDOWN
(USD million)

Type of portfolio	Currency	2022		2023	
		Dec.	%	Jun	%
Investment portfolio		**33,468.2**	**85.5**	**34,140.9**	**86.4**
Currencies and deposits	U.S. dollar	150.0	0.4	61.3	0.2
	Euro	0.4	0.0	0.9	0.0
	Canadian dollar	0.0	0.0	0.0	0.0
	Australian dollar	0.2	0.0	0.4	0.0
	Other foreign currencies	3.2	0.0	114.4	0.3
Securities	U.S. dollar	25,529.3	65.2	26,227.9	66.4
	Euro	1,679.0	4.3	1,725.9	4.4
	Canadian dollar	0.0	0.0	0.0	0.0
	Australian dollar	1,017.1	2.6	1,029.0	2.6
	Other foreign currencies	5,089.1	13.0	4,981.1	12.6
Totals	U.S. dollar	25,679.3	65.6	26,289.2	66.6
	Euro	1,679.4	4.3	1,726.8	4.4
	Canadian dollar	0.0	0.0	0.0	0.0
	Australian dollar	1,017.3	2.6	1,029.4	2.6
	Other foreign currencies	5,092.2	13.0	5,095.5	12.9
Cash portfolio		**1,728.6**	**4.4**	**1,317.1**	**3.3**
Currencies and deposits	U.S. dollar	1,728.6	4.4	1,317.1	3.3
Other assets		**3,957.4**	**10.1**	**4,039.3**	**10.2**
Monetary gold	Other foreign currencies	14.4	0.0	15.1	0.0
IMF SDRs	Other foreign currencies	3,265.3	8.3	3,344.5	8.5
IMF Reserves position	Other foreign currencies	677.6	1.7	679.7	1.7
Currencies and deposits	U.S. dollar	0.0	0.0	0.0	0.0
Total international reserves		**39,154.1**	**100.0**	**39,497.4**	**100.0**
	U.S. dollar	27,407.9	70.0	27,606.3	69.9
	Euro	1,679.4	4.3	1,726.8	4.4
	Canadian dollar	0.0	0.0	0.0	0.0
	Australian dollar	1,017.3	2.6	1,029.4	2.6
	Other foreign currencies	9,049.6	23.1	9,134.8	23.1

Source: Central Bank of Chile.

Regarding the Investment Portfolio's exposure by type of risk and country, at the close of this report there were appropriate degrees of diversification for the different types of risks in which the international reserves are invested. At the end of June 2023, investments in sovereign risk represented 95.7% of the Investment Portfolio and were mainly in the United States (73.3%), China (7.5%), United Kingdom (4.4%) and France (3.5%). At the end of the period, investments in supranational risk represented 2.3%, agency risk 0.5% and banking risk 0.5% (tables B.5 and B.6)[1]/.

TABLE B.5 INTERNALLY MANAGED PORTFOLIO. INVESTMENT BY COUNTRY AND TYPE OF RISK (*)
(USD million)

Country	Sovereign	Banks	Agencies	Supranational	TOTAL
Australia	620	0	0	0	620
Canada	65	0	0	0	65
China	2,460	0	0	0	2,460
France	1,041	83	20	0	1,144
Germany	396	0	5	0	400
Israel	29	0	0	0	29
Japan	205	0	0	0	205
Poland	10	0	0	0	10
Qatar	23	0	0	0	23
Saudi Arabia	63	0	0	0	63
South Korea	988	0	23	0	1,012
Spain	298	0	0	0	298
Supranational	0	0	0	709	709
Sweden	0	0	70	0	70
Switzerland	0	28	0	0	28
United Arab Emirates	42	0	0	0	42
United Kingdom	1,411	48	0	0	1,459
United States	24,365	0	1	0	24,366
Other	0	0	0	0	0
TOTAL	**32,017**	**158**	**118**	**709**	**33,002**

(*) The Other category includes FX operations, balances in correspondent accounts and cash flows payable/receivable.
Source: Central Bank of Chile.

[1]/ Tables B.5 and B.6 show the breakdown of the investment portfolio into internal and external management.

TABLE B.6 EXTERNAL MANAGEMENT PORTFOLIO. INVESTMENTS BY COUNTRY AND TYPE OF RISK (USD million)

Country	Sovereign	Banks	Agencies	Supranational	TOTAL
Australia	13	0	0	0	13
Austria	13	0	0	0	13
Belgium	1	0	0	0	1
Canada	17	0	0	0	17
China	103	0	0	0	103
Finland	7	0	0	0	7
France	35	0	0	0	35
Germany	40	0	5	0	45
Japan	15	0	0	0	15
Norway	0	7	0	0	7
Poland	8	0	0	0	8
Qatar	3	0	0	0	3
Saudi Arabia	13	0	0	0	13
South Korea	34	0	6	0	40
Spain	13	0	0	0	13
Supranational	0	0	0	85	85
United Arab Emirates	6	0	0	0	6
United Kingdom	53	0	0	0	53
United States	634	0	27	0	661
TOTAL	**1,009**	**7**	**38**	**85**	**1,139**

Source: Central Bank of Chile.

As of 30 June 2023, the currency composition of the Investment Portfolio was: 77.0% in US dollars, 7.8% in Chinese renminbi, 5.1% in euros, 4.1% in British pounds, 2.9% in South Korean won and 3.0% in Australian dollars (table B.7).

TABLE B.7 INVESTMENT PORTFOLIO BY CURRENCY (1)(2) (percent)

Currency	Share
US dollar	77.0
Chinese renminbi	7.8
Euro	5.1
Pound sterling	4.1
South Korean won	2.9
Australian dollar	3.0
Other currencies	0.0
TOTAL	**100.0**

(1) Includes positions in currency forwards.

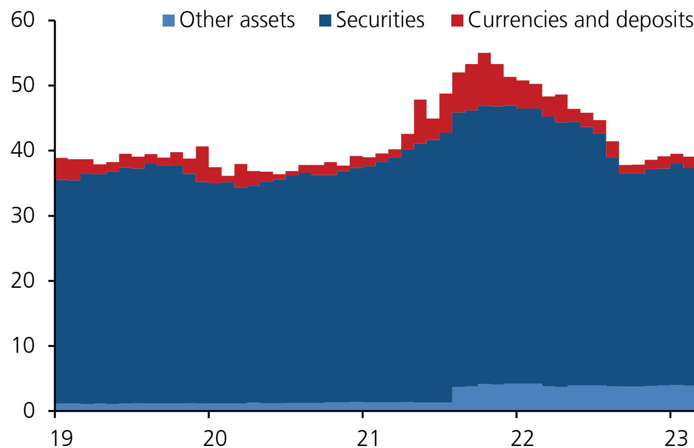
(2) Excludes positions of cash portfolio and other assets.

Source: Central Bank of Chile.

At the end of June, the external managers BNPP AM and AGI managed a total of US$1,139 million, belonging to the Investment Portfolio.

The Central Bank of Chile, in its periodic publications (Annual Report and September Monetary Policy Report) systematically presents the information contained in Table B.4 of this Report, in order to communicate the variations in international reserves attributable to their different components. Figure B.3 shows the recent evolution of international reserves, separating the "currencies and deposits" component, which is largely associated with the cash portfolio described above. This breakdown can be found in the Central Bank's statistical database.

FIGURE B.3 INTERNATIONAL RESERVES BREAKDOWN
(stock, USD billion)



Source: Central Bank of Chile.

It is important to highlight that international reserves are the main source of foreign currency liquidity available to the Central Bank of Chile. However, the Bank has complementary sources of liquidity of a different nature. Since 29 August 2022, the Flexible Credit Line granted by the International Monetary Fund (IMF - US$18,500 million) is available, which is of a precautionary and transitory nature (2 years). To this must be added the potential access to the Latin American Reserve Fund (FLAR - up to US$1,250 million) and the resources that could be obtained from the RMB/CLP swap line with the People's Bank of the Republic of China, for US$6,900 million. Thus, the complementary liquidity buffers reach US$26.65 billion, which are added to the Bank's own holdings of international reserves (table B.8). This is part of the Central Bank of Chile's strategy to strengthen its liquid position in foreign currency against the risk of external shocks.

TABLE B.8 TOTAL INTERNATIONAL RESERVES AND LIQUIDITY LINES
(USD million)

International reserves (1)	**39,497**
Investment portfolio	34,141
Cash portfolio	1,317
Other assets (2)	4,039
Active liquidity lines	**26,650**
IMF - "Flexible credit line" (3)	18,500
PBoC - "Swap line"	6,900
FLAR - "Balance of Payments"	1,250

(1) At 30 June 2023.
(2) Includes, mainly, positions held with the IMF.
(3) Access to this line was granted on 29 August 2022.
Source: Central Bank of Chile.

ANNEX C:

Main measures taken by the Central Bank of Chile during 2023

JANUARY

23. The Central Bank of Chile (CBC), through Resolution No. 2530-01-230119, approved its Strategic Plan 2023- 2027, which contains the definitions of the vision, mission and values, from which are derived objectives, strategic focuses and initiatives that this institution intends to achieve in the period between 2023 and 2027, having as main basis the compliance with the mandate established in its Constitutional Organic Law[1]/.

26. At its Monetary Policy Meeting, the Board of the Central Bank of Chile agreed to maintain the monetary policy interest rate at 11.25%. The decision was adopted by the unanimous vote of its members[2]/.

MARCH

2. Within the framework of its actions to strengthen the country's international liquidity position, the Central Bank of Chile, by means of Resolution No. 2536-02-230302, approved an increase in the capital subscribed in the Latin American Reserve Fund (FLAR), to be paid through the capitalization of profits it is entitled to receive[3]/.

30. Resolution No. 2543-01-230330 modified Chapter III.K.1 of the Compendium of Financial Regulations of the Central Bank of Chile, to determine the financial instruments in which the Special Guarantee Fund created by Law No. 21,543 may invest its resources[4]/.

APRIL

4. At its Monetary Policy Meeting, the Board of the Central Bank of Chile agreed to maintain the monetary policy interest rate at 11.25%. The decision was adopted by unanimous vote of its members[5]/.

5. The Central Bank published the Monetary Policy Report corresponding to March 2023[6]/.

[1]/ For further details, see: Central Bank of Chile Strategic Planning.

[2]/ For more information, see: MP meeting Press Release of January 2023.

[3]/ See: Resolution approving capital increase subscribed in the Latin American Reserve Fund.

[4]/ More details in: Resolution that amends Chapter III.K.1 of the Compendium of Financial Standards.

[5]/ For more information, see: MP meeting Press Release of April 2023.

[6]/ More information in: MP Report Press Release of March 2023.

21. The Board of the Central Bank of Chile announced its decision to initiate a process of gradual reduction of the short position (US$ 9,110 million) held in NDF (forward sales contracts for difference), starting on 24 April[7]/. It was determined that the process will be carried out through a mechanism of partial renewal of the maturity of these operations, at a rate of 1/10 monthly of the remaining stock, which is equivalent to an average daily reduction of US$ 50 million, at which rate the position would be closed in 10 months. This measure was adopted considering the correct functioning of the foreign exchange market, even in times of recent external shocks. The daily calendar for the renewal and rescheduling of forward sales will be informed every Friday during the indicated gradual reduction period.

28. The Central Bank began publishing the Housing Price Index on a quarterly basis and with new breakdowns, with a lag of 4 months.

30. The Central Bank published its Integrated Report 2022[8]/.

MAY

4. Starting this month, the Central Bank of Chile began publishing the monthly Survey of Price Determinants and Expectations (EDEP), a survey that investigates the price determination dynamics of companies and their economic expectations, including 12 and 24-month inflation estimates. The EDEP has information available since November 2021. Its results will be available on the Central Bank's website and Statistical Database. Publication dates fluctuate between the third and sixth day of each month. From a methodological point of view, the EDEP is composed of a rotating panel of approximately 450 companies whose information is collected monthly, but reported on a rolling quarterly basis. A very important aspect of this survey is its inquiry into firms' inflation expectations. With this information, the EDEP becomes the only instrument in Chile that allows knowing the inflation expectations of companies for the monetary policy horizon, complementing the projections of other agents, such as analysts and financial operators.

5. Within the framework of "Regional Statistics" and "Experimental Statistics", the Central Bank initiated the monthly publication of regional sales and purchases indicators (ICVR) based on electronic invoicing. These indicators provide aggregated statistical information on sales and purchases between companies operating in the national territory, with relevant breakdowns such as region of sale (issuer), region of purchase (receiver), activity and company size.

11. The Board of the Central Bank of Chile appointed by Resolution 2553E-01-230511, Mr. Ricardo Consiglio Fonck as Manager of the Financial Markets Division[9]/.

12. At its Monetary Policy Meeting, the Board of the Central Bank of Chile agreed to maintain the monetary policy interest rate at 11.25%. The decision was adopted unanimously by its members[10]/.

[7]/ For more details, see: Press Release on the start of the phasing out of forward operations.

[8]/ More information in: Publication of CBC 2022 Annual Report.

[9]/ See: Press Release on the appointment of Ricardo Consiglio as Manager of the Financial Markets Division.

[10]/ Further details in: MP meeting Press Release of May 2023.

23. At its Financial Policy Meeting, the Board of the Central Bank of Chile agreed to activate the Countercyclical Capital Requirement at a level of 0.5% of risk-weighted assets, due within one year. The decision was adopted by unanimity of its members, with the prior favorable report of the CMF[11]/.

24. The Central Bank published its Financial Stability Report for the first half of 2023[12]/.

JUNE

5. In order to promote the dissemination of Central Bank statistics to a more transversal public, the account "Statistics Central Bank of Chile" was created in the social networks Instagram, X (Twitter) and LinkedIn.

8. By means of Resolution No. 2559-02-230608, the Board approved amendments to the regulations of Chapter III.H. 6 of the Compendium of Financial Standards related to the implementation of the regulation of Clearing Houses for Low Value Payments (CPBV) and approved the Operating Regulations of the CPBV to be operated by Centro de Compensación Automatizado CCA S.A.[13]/.

8. The Central Bank of Chile published the results and main conclusions of the National Survey on Cash Use and Preferences (ENUPE), conducted by the Issuing Institute annually since 2012, which explores people's preferences for the use of different means of payments[14]/.

9. By means of Resolution No. 2560E-01-230609, and in the context of the current floating exchange rate regime, the Board of the Central Bank resolved to initiate a program of replenishment and expansion of international reserves for a total of US$ 10 billion to strengthen the country's international liquidity position, which will be extended for a period of 12 months, through regular purchases of dollars for US$ 40 million per day, through competitive auctions. The monetary effects of this measure will be sterilized through PDBC issuances consistent with the monetary policy stance[15]/.

15. By means of Resolution No. 2562-01-230615, the modification of the structure of the Statistics Division Management was approved, changing its name to Statistics and Data Division Management and creating the Experimental Statistics Department. The change is due to the new roles that have been assigned to it, related to promoting the safe exploitation of data within the Bank. The new Department will focus on the development of experimental statistics and the development of the natural capital agenda.

19. At its Monetary Policy Meeting, the Board of the Central Bank of Chile agreed to maintain the monetary policy interest rate at 11.25%. The decision was adopted with the votes of the President, Ms. Costa, and Board Members Messrs. Naudon and Céspedes. Vice President Mr. García and Board Member Ms. Griffith-Jones voted to reduce the rate by 50 basis points[16]/.

20. The Central Bank published the Monetary Policy Report (MP Report) for June 2023[17]/.

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[11]/ More details in: RPF Press Release for the first half of 2023.

[12]/ For more information, please visit: IEF Press Release for the first half of 2023.

[13]/ More details in: Resolution regarding proposals related to the implementation of CPBV regulation.

[14]/ More information at: Press Release on the results of the National Survey of Cash Use and Preferences (ENUPE).

[15]/ For further details, see: Press Release of the international reserves replenishment and expansion program.

[16]/ For more information, see: MP meeting Press Release of June 2023.

[17]/ More details in: MP Report Press Release of June 2023.

22. Through Resolution No. 2564-01-230622, in its capacity as Fiscal Agent, the Central Bank agreed on modifications to the Guidelines for Monitoring Compliance with the Investment Limits of the Economic and Social Stabilization Fund, the Pension Reserve Fund and the Strategic Contingency Fund; and new Execution Guidelines associated to the investment of the resources of the Economic and Social Stabilization Fund[18]/.

JULY

6. By Resolution No. 2567E-01-230706, Mr. Miguel Fuentes Díaz was appointed as Financial Stability Manager.

19. By Resolution No. 2570E-01-230719, Ms. Silvana Celedón Porzio was appointed as Communications Manager.

20. By Resolution No. 2571-01-230720, it was agreed to appoint Mr. Alejandro Zurbuchen Silva as a new member of the Audit and Compliance Committee of the Central Bank of Chile[19]/.

20. By Resolution N°2571-03-230720, it was agreed to initiate a public consultation process of a set of improvements to the regulation on the operation of Payment Cards and issuance of Prepaid Payment Cards, modifying Chapters III.J.1.3 and III[20]/. The amendments refer to the incorporation into the regulatory and supervisory perimeter of the so-called Payment Processing Service Providers –sub-Operators– that perform payment or settlement activities for affiliated entities; as well as to the regulation of cross-border acquiring and sub-acquiring activities by Operators and PSP sub-Operators; and the closed or semi-closed Prepaid Cards models recognized by the FinTech Law. The aim of this is to adapt the regulatory framework to the dynamic environment of retail means of payment, ensuring that it is in line with the development of the market and allows ensuring the security and efficiency of these payment systems, while applying criteria of proportionality in the regulatory burden according to the risk involved for the normal operation of the payment system.

27. By means of Resolution No. 2572-01-230727, the Board of the Central Bank appointed Ms. Romina Torres Torres as a new member of the Information Technology Advisory Committee for three years, and appointed Mr. Gonzalo Acuña Leiva as Chairman of the Committee for one year[21]/.

28. At its Monetary Policy Meeting, the Board of the Central Bank of Chile agreed to reduce the monetary policy interest rate by 100 basis points to 10.25%. The decision was adopted by the unanimous vote of its members[22]/.

[18]/ For more details, see: Resolution on modifications to the Guidelines for Monitoring Compliance with the Investment Limits of the Economic and Social Stabilization Fund, the Pension Reserve Fund and the Strategic Contingency Fund.

[19]/ For more information, see: Resolution to appoint Mr. Alejandro Zurbuchen Silva as a member of the Audit and Compliance Committee.

[20]/ More details in: Resolution to publish for comments the proposed regulation that modifies Chapters III.J.1.2 and III.J.2, on payment cards with provision of funds and operation of payment cards, respectively, of the Compendium of Financial Regulations of the Central Bank of Chile.

[21]/ For more information, see: Resolution to appoint a new member and Chairman of the Information Technology Advisory Committee.

[22]/ For further details, see: MP meeting Press Release of July 2023.

AUGUST

3. By means of Resolution No. 2573-01-230803, the Central Bank of Chile initiated the public consultation process for amendments to chapter III.B.4 of its Compendium of Financial Regulations, which establishes regulatory requirements applicable to the sale and acquisition of banks' portfolios to securitization companies, in order to encourage and facilitate the development of the securitized financial instruments market and expand financing alternatives and improve banks' liquidity risk management[23]/.

This regulatory proposal establishes the requirements and conditions applicable for banks to carry out "retained securitization" or "self-securitization" operations, through which they may sell or assign documents from their loan portfolio to a securitization company, so that the latter, through a separate net worth, may issue securitized debt securities to be acquired by the same banking institution, for their possible use as guarantee or collateral, instead of placing the securitized bond in the market.

8. The Board of the Central Bank of Chile (CBC) approved the second edition of the Payment Systems Report (ISiP), corresponding to the year 2023. Through this document, the Issuing Institute communicates to the public recent trends related to the use of means of payment, financial market infrastructures, as well as development and policy perspectives. This report also includes details of the CBC's Payments Agenda, which is part of its Strategic Planning for the period 2023-2027[24]/.

10. The Board approved, by means of Resolution No. 2574-01-230810, to amend the Communications Policy, with respect to meetings with financial market players to deal with issues related to the economic situation[25]/.

SEPTEMBER

5. At its Monetary Policy Meeting, the Board of the Central Bank of Chile agreed to reduce the monetary policy interest rate by 75 basis points, to 9.5%. The decision was adopted by the unanimous vote of its members[26]/.

[23]/ More information in: Resolution that submits for public consultation a proposal to amend Chapter III.B.4 of the Compendium of Financial Regulations to incorporate the possibility of acquiring self-securitized instruments by banking companies.

[24]/ For more details, see: Central Bank of Chile publishes Payment Systems Report for 2023.

[25]/ More information at: Modifies the Communications Policy, regarding meetings with financial market players to discuss economic issues.

[26]/ For further details, see: MP meeting Press Release of September 2023.

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