



LATIN AMERICA ECONOMICS UPDATE

Chile's central bank: still focused on inflation risks

- **The *Monetary Policy Report* released by Chile's central bank today revealed that policymakers are more concerned about inflation risks than we'd thought. We still think that Chile's central bank will be among the first to start loosening monetary policy, but we've pushed back the timing of the first interest rate cut in our profile by a month, to July.**
- At its meeting yesterday, Chile's central bank (BCCh) kept its policy rate unchanged at 11.25%, the third consecutive meeting at which interest rates were left unchanged. The decision was never really in doubt and the more interesting part was always going to be if policymakers give any signals about whether interest rate cuts were on the horizon.
- **But the central bank's communications were (surprisingly) hawkish and revealed that policymakers are concerned about the relative strength of the economy and inflationary pressures.** The statement noted that "the economy is adjusting more slowly than expected and inflation is taking longer to come down". The fact that core inflation had remained broadly unchanged at close to 11% over the past few months was noted as a particular point of concern.
- This view was also reflected in the quarterly *Monetary Policy Report* released earlier today. This year's GDP growth forecast range was revised up to -0.5% to +0.5% (from -1.75% to -0.75% in the December report). With the output gap expected to close more slowly than expected, policymakers revised up their end-2023 inflation forecast by 1%-pt, to 4.6%.
- **Against the backdrop of the disinflation process taking "longer than expected in December", policymakers hinted that rates will be kept at their current level for longer than envisaged in their last report.** Indeed, whereas the previous forward guidance was consistent with rate cuts coming in early Q2, the new interest rate corridor suggests that the first cuts may now come in late Q2 or early Q3.
- **For our part, we are sticking with our view that Chile will be among the first EM central banks to start cutting interest rates.** But the central bank's hawkish tone and the persistence of core price pressures, has prompted us to push back the timing of the first cut – we now expect the central bank to kick off its easing cycle in July, rather than June.
- By then, we think that inflation will have fallen far enough (to around 8% in June, from 11.9% currently, see Chart 1) that the central bank feels comfortable to lower rates. And the economy is likely to show more pronounced signs of weakness (following what is looking like a surprisingly strong first quarter). Indeed, the central bank's 2023 growth forecast look optimistic – we expect a drop in GDP of 0.5% this year.
- **All in all, we think that the BCCh will deliver a cumulative of 275bp of cuts this year, taking the policy rate to 8.50% by December. This is a higher path for interest rates than the consensus.** (See Chart 2.)

Chart 1: Consumer Prices (% y/y)

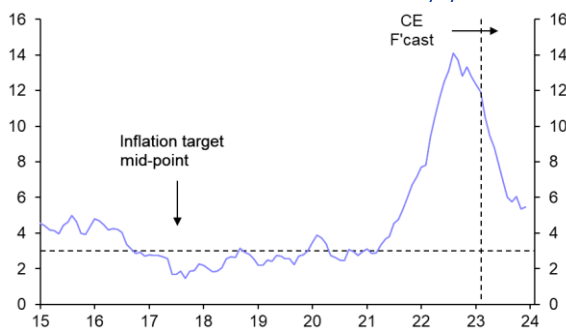
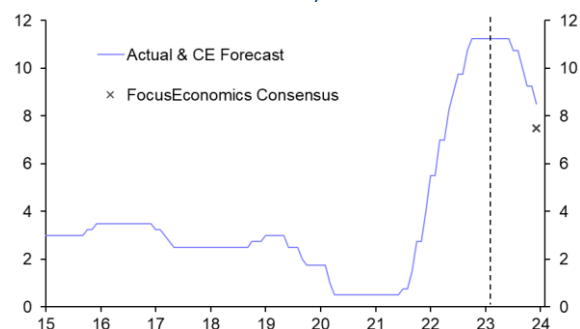


Chart 2: Policy Rate (%)



Sources: Refinitiv, Central Bank of Chile, Capital Economics





Disclaimer: While every effort has been made to ensure that the data quoted and used for the research behind this document is reliable, there is no guarantee that it is correct, and Capital Economics Limited and its subsidiaries can accept no liability whatsoever in respect of any errors or omissions. This document is a piece of economic research and is not intended to constitute investment advice, nor to solicit dealing in securities or investments.

Distribution: Subscribers are free to make copies of our publications for their own use, and for the use of members of the subscribing team at their business location. No other form of copying or distribution of our publications is permitted without our explicit permission. This includes but is not limited to internal distribution to non-subscribing employees or teams.

