

Chile

The Chilean economy is estimated to have grown by about 3.8% in 2008, less than the 5.1% posted the previous year. Since mid-2007, the main risks the economy faces materialized: the provision of natural gas from Argentina was suspended; international prices soared, first for food and then for fuel; and most recently, the crisis in the United States, despite alleviating inflationary pressure by bringing down commodity prices during the second semester, deepened and spread to other developed economies, which began to have a negative effect on Chile's exports. In short, the external boom that started in mid-2003 seems to have come to an end in 2008. In addition, the country has had to cope with internal upsets (droughts, technical and labour-related problems in natural-resource-based sectors) that also hindered growth. In response, the government has implemented a series of countercyclical measures, which, together with the fiscal and monetary policies applied since 2000 to stabilize growth and the vast external reserves accumulated during the recent boom, should help mitigate the crisis' negative impact on economic activity and employment in 2009.

Fiscal policy continued to pursue a structural surplus of 0.5% of GDP, which allows public expenditures to expand according to the medium-term values of its main determinants. Spending thus increased at a rate of just over 5% per year, in keeping with the growth pattern of the last few years.

Of the components of aggregate demand, gross fixed capital formation continued to be highly dynamic. During the first semester it expanded at an annual rate of 23% because high international commodity prices up to the middle of the year stimulated numerous investment projects in the energy and mining sectors. Total consumption in turn posted moderate growth of close to 6%, while private consumption, in particular of durables, slowed because the spike in inflation and the sluggish increase in employment slowed the expansion of the real pay-roll at a time when credit was tightening.

According to estimates, national unemployment stood at 7.9% in 2008, higher than in 2007; this was because, although the employment rate has risen, more people entered the workforce.

Monetary policy continued to pursue the target inflation range of between 2% and 4% within two years. Twelve-month inflation, as measured by the CPI and its

CHILE: GDP, INFLATION AND UNEMPLOYMENT



Source: Economic Commission for Latin America and the Caribbean (ECLAC), on the basis of official figures.

trend components, soared above target, however, reaching close to 10% during the second semester. This was the result of the sharp rise in international prices for food as of 2007 and for fuel in the first part of 2008, which spread to domestic prices thanks to indexation and the intense rise of demand.

The central bank reacted by incrementing the monetary policy rate on several occasions, from 5% when inflation began to climb in April 2007 to 8.25% in September 2008. In the last two months of the year, the drop in international prices partially alleviated inflationary pressure, and 12-month inflation is expected to end the year at around 8.5%.

The exchange rate appreciated steadily up to the middle of the year, which led the central bank, in anticipation of the effects of the external crisis, to implement a foreign-exchange purchasing programme aimed at boosting international reserves by US\$ 8 billion by the end the year. Subsequently, as the crisis unfolded, the real exchange rate rose sharply and, towards the end of the year, reached levels comparable to those prior to the crisis. This counteracted efforts to reduce the inflationary pressure, however, and in the second semester, the bank suspended the foreign-exchange purchasing programme.

In 2009, the projected decline in world demand is expected to lower international prices, particularly for fuel and certain foodstuffs, and inflation is therefore expected to drop as well, especially in the second semester. Monetary authorities estimate that towards the end of 2009, inflation will once again be within the target range.

Exports of goods and services continued to slide in 2008, at first owing to technical and labour problems that reduced the volume of mining exports, and then because the prices and volumes of commodities traded on world markets slumped when the external crisis worsened in September that year. In October, a major credit crunch created serious liquidity shortages in several developed economies. This had two repercussions: on the one hand, without the necessary credit, export orders shrank; on the other, financial entities began to liquidate their commodity-related positions as these became unsustainable owing to the lack of liquidity. Commodity sales volumes and prices consequently plunged as the inventories on the world's main commodities markets swelled. According to information available up to October, copper export volumes were down by 29% and total mineral exports were down by 23% on the previous year.

Imports remained buoyant, especially machinery and equipment imports, whose rise of almost 25% was closely linked to investment dynamics. After three successive years of posting a surplus, the current account is therefore estimated to record a deficit in 2008 of about 2.7% of GDP.

CHILE: MAIN ECONOMIC INDICATORS

	2006	2007	2008 ^a
Annual growth rates			
Gross domestic product	4.3	5.1	3.8
Per capita gross domestic product	3.3	4.0	2.8
Consumer prices	2.6	7.8	8.9 ^b
Average real wage ^c	1.9	2.8	-0.3 ^d
Money (M1)	13.2	18.1	13.4 ^e
Real effective exchange rate ^f	-2.2	1.3	-4.1 ^g
Terms of trade	31.4	3.8	-7.2
Annual average percentages			
Urban unemployment rate	7.7	7.1	7.7 ^d
Central government overall balance / GDP	7.7	8.8	6.9
Nominal deposit rate	5.5	5.9	7.8 ^h
Nominal lending rate	14.4	13.6	15.2 ^h
Millions of dollars			
Exports of goods and services	66 310	76 429	78 863
Imports of goods and services	44 351	53 938	70 502
Current account	6 838	7 200	-5 639
Capital and financial account	-4 841	-10 414	10 839
Overall balance	1 997	-3 214	5 200

Source: Economic Commission for Latin America and the Caribbean (ECLAC), on the basis of official figures.

^a Preliminary estimates.

^b Twelve-month variation to November 2008.

^c General hourly wage index.

^d Estimate based on data from January to October.

^e Twelve-month variation to October 2008.

^f A negative rate indicates an appreciation of the currency in real terms.

^g Year-on-year average variation, January to October.

^h Average from January to November, annualized.

The economy is expected to slow in 2009 in response to the projected reduction in external demand, tighter internal and external liquidity conditions and a significantly higher level of uncertainty. Growth is expected to remain positive, however, thanks to the countercyclical measures adopted by the authorities and the ongoing buoyancy of other emerging economies.

The country's fiscal and monetary authorities announced measures geared towards ensuring sufficient liquidity and stimulating domestic demand. The central bank increased the amounts and terms of its liquidity supply in dollars and pesos and authorized the use of bank deposits as additional collateral in these programmes. New temporary subsidies were created, and existing subsidies for buying homes were expanded. Capital was pumped into the Small Enterprise Guarantee Fund (FOGAPE) to boost its credit support capacity by US\$ 2 billion, and medium-sized enterprises were granted access to the Fund. Some US\$ 200 million was injected into the Production Development Corporation (CORFO) to support commercial bank loans to small and medium-sized enterprises. The capital of BancoEstado will be raised US\$ 500 million to increase its capacity to lend to small businesses and home buyers.

In short, although the external context deteriorated in 2008, the Chilean economy is projected to continue recording positive, albeit modest, growth in 2009, and inflation is expected to fall, thanks to the recently adopted measures

and the continued action of the set of macroeconomic policies implemented over a number of years to create countercyclical capacities, which have helped ensure the country's fiscal and external solvency.