Chile

After registering GDP growth of 1.9% in 2014, the Chilean economy expanded by 2.0% in 2015. Declining investment over several consecutive quarters has caused trend GDP growth between 2015 and 2019 to be revised downward to about 3.5% or even less, revealing a marked deterioration of growth expectations following the end of the mining boom. At the end of 2015, annual inflation was estimated at 4.5% and the current account deficit at 0.7% of GDP, with the public-sector deficit rising to 3.3% of GDP.

In this context of low growth, fiscal spending in 2015 was clearly expansionary, rising by 8.4% in real terms on its 2014 level. Given slower growth in total revenues, this meant a central government deficit of an estimated 3.3% of GDP in 2015, compared with a negative overall balance of 1.6% in 2014.

There was a sharp drop in receipts from the National Copper Corporation of Chile (CODELCO), down from 0.9% of GDP in 2014 to 0.5% in 2015, and a decline in tax revenues from private-sector mining firms, down from 1% to 0.9% of GDP. A rise in the corporation tax rate partly offset the reduction in profits in the sector resulting from the lower copper price. A similar effect is expected in 2016, when there will be a further increase. The effects of the tax reform were also reflected in receipts from non-mining taxpayers, which rose from 15.7% to 16.3% of GDP. For 2016, when the measures in the 2014 tax reform will be implemented in full, VAT receipts are also expected to rise with the application of an enforcement plan that should greatly reduce evasion in the system.

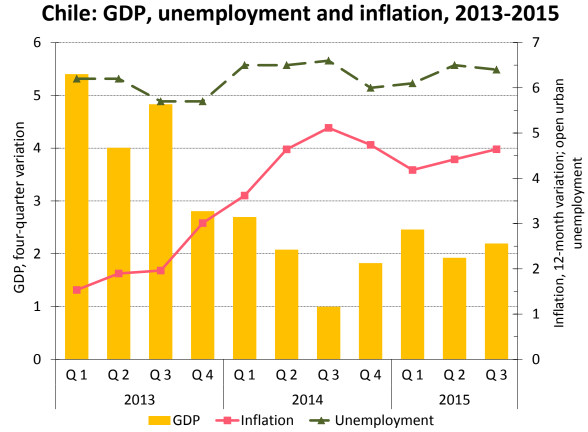
Despite the cyclical deterioration of the public finances in 2015-2016, the financial assets of the public treasury are estimated at US$ 26 billion at year's end, a figure that includes over US$ 8 billion in the Pension Reserve Fund (FRP), US$ 14 billion in the Economic and Social Stabilization Fund (FEES) and US$ 3.5 billion in the Education Fund.

Significant peso depreciation has been a major factor behind the recent rise in effective inflation, as a dollar now buys about 50% more pesos than when the Chilean currency's value peaked in 2013, while the real exchange rate has weakened by 17% from its high point that same year. Although currency depreciation can mitigate the real costs arising from the worsening terms of trade, higher inflation (of 4.0% in the 12 months to October) shows that the country is struggling to contain price rises, given its high import ratios. Inflation has been high, and it outstripped expectations for a time, triggering a rise in the monetary policy interest rate to 3.25% in October.

However, monetary policy will continue to have a clear expansionary bias, as real interest rates will remain negative. This does not necessarily imply a significant recovery in private spending, given an environment of worsening expectations and higher consumer debt. Lending to the private sector is in fact rising less quickly than before, having slowed from double-digit growth rates up to 2013 to a rate of 5.1% in real terms in the third quarter of 2015.

The fall in the copper price resulted in the mining sector exporting 21.7% less in the third quarter of 2015 than in the same period the year before. Exports by the agriculture, forestry and fisheries sector rose 6.2% by value, mainly because

Chile: GDP, unemployment and inflation, 2013-2015



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

of higher volumes. Industrial-sector exports fell significantly, meanwhile, as their prices dropped by 11.2% over 12 months. As regards the geographical destinations of shipments, 48.2% went to Asia, 33.3% to Europe and North America and 15.1% to South America.

External debt, essentially held by the private sector, totalled US$ 148.716 billion at the close of the third quarter, or over 60% of GDP. International reserves totalled US$ 39.705 billion in November 2015, and were thus practically back up to the previous year's level, equating to over six months' worth of goods and services import cover. There was a net inflow of capital in the second and third quarters of 2015, mainly because of disinvestments abroad by pension fund managers. According to information from the Central Bank of Chile, netting out external financial assets and liabilities, the economy was in debt by US$ 47.059 billion (21.4% of GDP) at the end of the third quarter of 2015.

It should be stressed that the external adjustment has been extremely significant, with the current account deficit shrinking from 3.7% of GDP in 2013 to an estimated 0.7% in 2015 in nominal terms.

Chile: main economic indicators, 2013-2015

	2013	2014	2015 [a]
	Annual growth rate		
Gross domestic product	4.2	1.9	2.0
Per capita gross domestic product	3.1	0.8	0.9
Consumer prices	3.0	4.6	4.0 [b]
Real average wage [c]	3.9	1.8	1.8
Money (M1)	10.1	12.1	14.6 [d]
Real effective exchange rate [e]	2.1	11.0	3.0 [b]
Terms of trade	-2.9	-1.2	-3.1
	Annual average percentage		
Open urban unemployment rate	5.9	6.4	6.3 [b]
Central government			
Overall balance / GDP	-0.6	-1.6	-3.3
Nominal deposit rate [f]	5.2	3.9	3.7 [d]
Nominal lending rate [g]	13.2	10.8	9.4
	Millions of dollars		
Exports of goods and services	88,929	86,642	73,902
Imports of goods and services	90,511	82,631	72,480
Current account balance	-10,125	-2,995	-3,064
Capital and financial balance [h]	10,436	4,052	1,211
Overall balance	311	1,057	-1,854

Source: Economic Commission for Latin America and the Caribbean (ECLAC), on the basis of official figures.
a Estimates.
b Figures as of October.
c General index of hourly remuneration.
d Figures as of November.
e A negative rate indicates an appreciation of the currency in real terms. Refers to the extraregional real effective exchange rate.
f Average nominal deposit rates for 90-360 days, non-adjustable.
g Lending nominal rates for 90-360 days, non-adjustable.
h Includes errors and omissions.

In an economy as open as Chile's, with an export ratio of 36% and an import ratio of 38.5% as of 2014, the terms of trade have a critical influence on macroeconomic performance. The simultaneous declines in the prices of copper and oil have had opposing effects, with import prices estimated to have fallen by 10% in 2015 and export prices by 13%, giving a decline of 3% in the terms of trade that year, which implies a substantial drop in real-term available income.

Although it would be very difficult (and even imprudent) to attempt to weigh the importance of external and domestic factors when analysing the economic slowdown, the ending of the mining boom has unquestionably had a strongly negative effect. Investment in the sector has dropped sharply after its strong growth over the last decade and, largely as a result, machinery and equipment investment has fallen steadily and substantially since late 2013.

This fall is beginning to be cushioned by the impetus that public investment and increased housing construction have provided. Domestic demand growth picked up to 3.6% in the third quarter of 2015 because of stronger consumption, both private (up 1.8% on the same quarter a year earlier) and public (5.9%), and higher investment (7.7%). Expansion rates have thus been trending upward since the last quarter of 2014. Domestic demand growth has been contained by the decline in net exports, which represents a shift from previous quarters. Exports dropped 0.9% by volume and imports rose 3.1% in the third quarter of 2015.

In 2016, weak domestic demand is expected to be the main factor bearing down on inflation so that it approaches the central bank target of 3%, since private consumption will continue to be restrained by the slowdown in overall real wage growth. The labour market has been creating few jobs, and real pay growth has slowed. Nonetheless, the unemployment rate has showed signs of resilience, standing at 6.3% in the moving quarter between August and October, which represents a drop on the same period the year before.

ECLAC is projecting growth of 2.1% in 2016, with a modest increase in domestic demand and a small recovery in investment and exports. External sources of growth for Chile will be fewer, both because its trade partners' economies have been slowing and because its terms of trade have declined. Meanwhile, the 2016 public-sector budget bill provides for a deficit of 3.1% of GDP and a 4.4% real-term rise in spending, the smallest in recent years, mainly because it includes a planned drop of 2.4% in public investment.

Even more restrictive is the medium-term fiscal policy target of gradually reducing the structural deficit at a rate of 0.25 percentage points of GDP a year. Given that the main parameter of the structural fiscal rule now in force is the medium-run GDP trend, these revisions risk checking the expansion of public infrastructure in an environment of slow growth.

For the third year running, then, the Chilean economy is expected to grow below potential, in the absence of macroeconomic stimuli that might propel a rapid recovery.