

CHILE

Economic growth moderated in 2016, reflecting weaker commodity prices and external demand, while consumer and business confidence have been fragile. Growth is projected to edge up in 2017 and 2018 as a somewhat stronger global economy underpins a gradual recovery in investment and private consumption. As the effects of past currency depreciation wear off, inflation will fall into the central bank's tolerance range.

Monetary policy remains supportive, with the policy interest rate at 3.5%. Recent measures to boost productivity and strengthen investment may help to diversify the economy and support more sustainable growth. However, more needs to be done to address skill mismatches and tackle inequality.

Following a supportive fiscal stance in 2017, medium-term fiscal consolidation is planned to adjust to lower global copper prices, as required by Chile's fiscal rule. Scope for issuing debt to finance a gradual consolidation exists, and can help to sustain the recovery, in part by supporting ongoing education reforms.

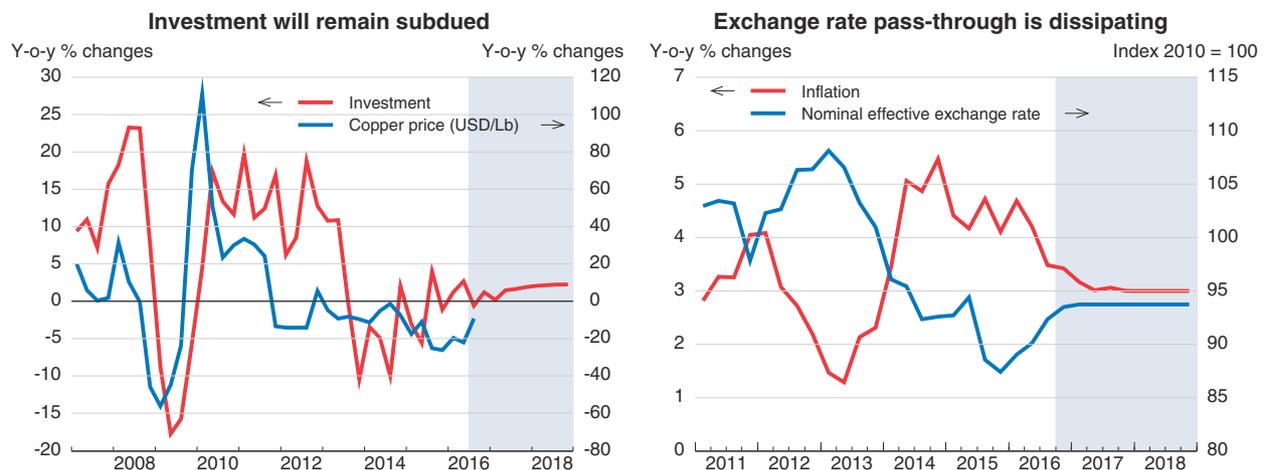
Growth is moderate due to lower commodity prices

Low global copper prices and weak external demand have depressed investment, especially in the mining and real estate sectors. Despite historically low interest rates, weak business confidence has held back investment in new projects. Private consumption growth has also slowed, reflecting weaker real income growth and a deterioration of consumer confidence. As growth has slowed, the labour market has softened and unemployment risen.

Monetary policy is supportive but fiscal consolidation is underway

Inflation is returning to within the central bank's target range of 2% to 4% with the stabilisation of the exchange rate, and as pass-through from the earlier depreciation runs

Chile



Source: OECD Economic Outlook 100 database; Central Bank of Chile.

StatLink  <http://dx.doi.org/10.1787/888933437506>

Chile: **Demand, output and prices**

	2013	2014	2015	2016	2017	2018
	Current prices CLP billion	Percentage changes, volume (2008 prices)				
GDP at market prices	137 229.6	1.8	2.3	1.7	2.5	2.6
Private consumption	87 538.9	2.4	1.9	2.0	2.1	2.5
Government consumption	17 220.3	5.1	5.8	6.1	4.1	2.7
Gross fixed capital formation	32 683.9	-4.2	-1.5	1.1	1.3	2.2
Final domestic demand	137 443.0	1.1	1.6	2.3	2.2	2.5
Stockbuilding ¹	855.5	-1.5	0.4	-1.0	-0.4	0.0
Total domestic demand	138 298.4	-0.2	2.2	1.5	1.8	2.5
Exports of goods and services	44 319.1	1.1	-1.9	-0.1	2.2	2.5
Imports of goods and services	45 388.0	-5.7	-2.8	-1.7	2.1	2.2
Net exports ¹	-1 068.9	2.2	0.3	0.5	0.0	0.1
<i>Memorandum items</i>						
GDP deflator	—	5.6	4.3	4.3	3.3	3.5
Consumer price index	—	4.7	4.3	3.9	3.1	3.0
Private consumption deflator	—	5.3	5.7	4.5	3.8	3.7
Unemployment rate	—	6.3	6.2	6.5	6.4	6.2
Central government financial balance ²	—	-1.8	-2.2	-2.8	-2.8	-2.5
Current account balance ²	—	-1.2	-2.0	-1.4	-1.2	-0.8

1. Contributions to changes in real GDP, actual amount in the first column.

2. As a percentage of GDP.

Source: OECD Economic Outlook 100 database.

StatLink  <http://dx.doi.org/10.1787/888933439007>

its course. The central bank raised interest rates in late 2015 to 3.5%, stating that further increases would likely be needed in the near future. However, since inflation is already showing signs of decline and inflation expectations are well anchored, monetary policy should remain supportive given that substantial economic slack still exists.

Fiscal consolidation measures have been announced to gradually close the budget deficit, in accordance with the recently revised fiscal rule. This was in response to lower expected medium-term copper prices, which will reduce Chile's income. Nevertheless, the fiscal stance for 2017 is slightly expansionary. Persistently weak demand would justify a delay, or a slower pace, of fiscal consolidation. Chile's near zero net debt provides room for a supportive fiscal stance, and low interest rates make financing inexpensive.

More measures to boost productivity and reduce entry barriers are needed to broaden the base of the economy and support inclusive growth. The agenda on productivity, innovation and growth seeks to facilitate entrepreneurship among start-ups, expand programme funding for innovation, and promote services exports. A new law will strengthen the competition framework, increasing penalties for abuse of dominance. Further reforms to bridge skill mismatches in the labour market and to foster jobs for women and youth would reduce inequalities and expand opportunities for all to enjoy the benefits of greater prosperity.

Growth will recover modestly in an uncertain environment

Activity will pick up in 2017 and 2018, driven mainly by exports, reflecting competitiveness gains and somewhat stronger external demand. Better exports will, in turn, spur investment and private consumption. Growth is projected to be enough to broadly stabilise the unemployment rate.

The main risks to growth relate to the performance of Chile's principal trading partners and the evolution of commodity prices. Weaker-than-projected growth in China and Latin American neighbours, or volatile global financial conditions, would reduce external demand. Growth could also be weakened if current uncertainty in the business sector does not dissipate or if trade remains sluggish. On the upside, a recovery of the price of copper would boost confidence and investment, and increase government revenues. New measures to boost competition and productivity could improve the business climate more than assumed. Risks for inflation remain closely tied to the evolution of the exchange rate and oil prices.