

Monthly Economic Update

August 30th, 2017

Nº 4



Cámara
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NEWS IN CHILE

The government sent legislation to Congress in August that will require employers to pay into workers' pensions for the first time. The contribution, worth 5% of an employee's salary, is in addition to the 10% currently paid by workers and will be implemented gradually over five years. Three-fifths will go to workers' individual accounts, while the remainder will go towards a new Collective Savings Fund, which will top up the lowest pensions. However, the extra funds will be managed by a new autonomous public entity, rather than the privately-owned AFPs. A Finance Ministry report estimated that the reform will cost up to 394,000 jobs. BHP is to invest US\$2.5 billion to extend the life of its Spence copper mine by fifty years. It is the largest investment in Chile's mining industry for several years and coincides with a sharp rise in copper prices since the end of 2016. However, excitement in the sector was tempered by a government decision to reject a permit for the Dominga iron ore-copper project, citing its proximity to a nature reserve.

On August 11th, Fitch Ratings followed S&P in downgrading Chile's sovereign credit rating, citing "a sustained

deterioration in the sovereign balance sheet" caused by "the prolonged period of economic weakness and low copper prices." Cutting the rating to A+ from AA-, Fitch said it expected that government debt will rise to 30% of GDP by 2019 (from 21% in 2016) as the next administration strives to meet social demands in the face of limited economic growth.

FINANCIAL INDICATORS

The Chilean economy grew by 1.4% in June, according to the Central Bank's Monthly Index of Economy Activity. Although activity in the mining sector continued to contract in June, it did so at a much slower rate than previous months (-0.9% vs -4.0% in April), as the industry recovers from the prolonged strike at the giant Escondida mine and other setbacks. Non-mining activity expanded by 1.6% as growth in services and retail was offset by contractions in the construction and manufacturing sectors. During the second quarter, the economy expanded by 0.9%, a marked improvement from growth of just 0.1% in the first three months of the year. Analysts surveyed by the bank in August forecast the economy will grow by 1.7% in the third quarter.

Prices rose by 0.2% in July, or by 1.7% over the previous twelve months, according to INE's Consumer Price Index (IPC). The annualized figure matches the surprise June inflation figure which marked a sharp drop from inflation of 2.6% in May. Inflation minus volatile food and energy prices rose by 0.3% in July and by 2.0% over the previous twelve months. INE said that higher public transport and food prices were largely offset by falls in the price of new cars and gasoline. Analysts surveyed by the Central Bank in August predicted that inflation will end the year at 2.4%, down from 2.8% predicted in June.

On August 17th, the board of the Central Bank held its benchmark interest rate at 2.50%, but is now expected to approve its fifth 25 basis point cut of the year in September or October following the drop in inflation since May.

Unemployment held at 7.0% in the April-to-June ruling quarter, unchanged from May and up from 6.1% at the end of last year. Although the headline figures suggest the labour market is stabilizing, with salaried employment rising by 1.4% over the last twelve months, partly reversing previously declines, the increase largely reflects the creation of new jobs in the public sector.

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More than 80,000 jobs were added in teaching, healthcare and government, while manufacturing added another 25,000.

Business confidence weakened slightly in July, according to the Monthly Business Confidence Index produced by the Adolfo Ibáñez University and the ICARE business organization, which slipped to 42.41 points, down from 43.20 points in June. However, a survey of executives by the Central Bank found that an increasing number of companies are planning investments on expectations of stronger economic growth in 2018 following this year's presidential elections.

Consumer confidence rose slightly in July to 41 points, according to the Economic Perceptions Index produced by market research firm GfK Adimark, up from a recent low of 37 points in February and reaching its highest level since February 2015. The rise was driven by increased confidence about the outlook for the Chilean economy over the next 12 months, which Adimark linked to increased expectations that Sebastian Piñera will succeed Michelle Bachelet next March. The price of copper, Chile's principle export, has continued to rally, trading in late August above US\$3.00 a pound for the first time in almost three years. Copper gained 7.7% in July alone as the market reacted to stronger than expected growth in China and an expected fall in global mine production following disruptions at mines in Chile, Peru and Indonesia earlier in the year. However, it is not clear whether the higher prices can be sustained. In July, the Chilean Copper Commission predicted that copper prices will average US\$2.64 a pound in 2017 and US\$2.68 a pound in 2018, up from a previous forecast of US\$2.60/lb for both years made in April.

Chile's trade surplus for the first seven months of the year totalled US\$2.7 billion, down 29.5% from the same period of 2016, as imports outpaced exports. While imports rose 11.5% to US\$34.2 billion, on higher imports of consumer and capital

goods, exports rose 6.9% to US\$36.9 billion on higher exports of minerals and industrial goods.

The Chilean Peso traded an average of CLP658 against the US dollar during the month of July, against an average of CLP655 in the first quarter and CLP665 in the second. The peso has since fallen below CLP640 against the US dollar mirroring the rise in the copper price. Analysts surveyed by the Central Bank in August predicted that the peso will end the year at CLP660, down from CLP670 predicted in June.

The Weighted Selective Share Index (IPSA) of the exchange's forty-most traded shares rallied to a record high of 5,176 points on August 25th.

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