

# Monthly Economic Update

June 27th, 2019



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## NEWS IN CHILE

Reacting to the gloomier outlook, President Sebastian Piñera announced a program to reactivate the sluggish economy, promising to double growth (to 3.5% annually) and create over 600,000 new jobs and 400,000 new businesses. Measures include US\$20 billion worth of infrastructure spending over the next four years and legislation to increase competition in the banking industry.

The government's popularity has continued to decline with a survey by thinktank *Centro de Estudios Públicos* finding that just 25% approved of the government, down from 37% last November. Joaquin Lavín, Mayor of Las Condes, has emerged as the country's most popular politician.

To reinvigorate his government, the president implemented a major cabinet reshuffle, naming new ministers of the Economy, Energy, Foreign Relations, Health, Public Works, and Social Development. The new appointments included four politicians from Piñera's 2010-2014 administration.

The government has struggled to advance its legislative agenda in Congress where it lacks a majority. President Piñera has said that he now aims to complete approval of his flagship tax and pensions reforms by the end of the year.

In June, the government presented an amendment to its pensions reform bill to meet an opposition demand that the additional contribution from employers (worth 4% of workers' income) be managed by a public entity rather than the existing privately-run Pension Fund Administrators (AFPs).

Electricity companies agreed to shut all 28 coal-fired power plants in Chile by 2040, including eight over the next five years, as part of a government commitment to make the country's carbon-neutral by the middle of the century. Almost 40% of Chile's electricity is produced from coal, but the fossil fuel is expected to lose ground to renewables, like solar and wind, over the next two decades.

Around 3,200 unionized workers at Codelco's Chuquibambilla division in northern Chile began an indefinite strike

on June 14<sup>th</sup> after rejecting an offer of 1.2% pay rise and bonuses worth Chilean Peso 14.1 million (about US\$20,500) from the state-owned company. The strike halved production at the copper mining and smelting complex.

## ECONOMIC STATISTICS

On June 7<sup>th</sup>, the board of the Central Bank surprised the market by reducing its benchmark interest rate by 50 basis points to 2.50%, marking the biggest cut in interest rates since the global financial crisis. As well as citing the weak domestic economy and the impact of the US-China trade war on external conditions, the Bank highlighted the surge in immigration into Chile in recent years which suggests that there was more slack in the economy than previously thought.

The economy grew by 2.1% in April, according to the Central Bank's monthly indicator of economic activity, compared to an expansion of 1.6% in the first quarter. While mining activity expanded for the first time this year (after torrential rains and flooding slowed copper output in the first

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quarter), the rest of the economy grew by 2.1%, thanks to a robust services sector.

In June, the Central Bank cut its growth forecast for 2019 to 2.75-3.50%, down from 3.00-4.00% predicted in March, following the weak first quarter. Private analysts surveyed by the Bank predicted growth of 2.9%, down from 3.7% predicted six months earlier.

The Bank's lower forecast mirrors a decline in forecast investment which is now expected to rise 4.5% this year, down from 6.2% predicted in March, largely due to slower spending on machinery and equipment. Imports of capital goods were flat during the first five months of the year.

Optimism in the private sector has slipped in recent weeks, with the Adolfo Ibañez University's Monthly Business Confidence Indicator falling to 50.56 points in June, its lowest level this year and down four points from its February peak. The decline reflects increased pessimism among retail and construction executives.

Confidence amongst consumers has continued to fall. GfK's Economic Perceptions Index fell to 40.7 points in May, its lowest level since President Piñera took office in March last year. Confidence among ABC1 consumers moved into negative territory for the first time under this government. With the index now below its five-year average, GfK said it could reflect "structural pessimism about the economy."

Inflation has risen with the government's Consumer Price Index rising 0.6% in May or 2.3% on an annualized basis, up from 1.7% in February. The rise was largely driven by higher electricity prices. Core inflation (which excludes energy and

food prices) rose by 0.4%. Inflation is now expected to end the year at 2.8%.

Unemployment remains stubbornly high, averaging 6.9% in the February-to-April moving quarter. Although the number of people in work rose by a solid 1.4% from twelve months earlier, the public sector and the self-employed, rather than the private sector, accounted for the majority of new jobs created.

In line with share prices around the world, Chilean stocks fell with the Santiago Stock Exchange's IPSA index declining 4.1% in May, bringing the index below 5,000 points for the first time in almost two years. However, the index recovered in June following the Central Banks' cut in interest rates.

International copper prices fell sharply in May after China and the US failed to reach a deal to end their ongoing trade dispute. Copper prices averaged US\$2.73/lb in May, down from US\$2.95/lb in February, and by early June were trading around US\$2.60/lb, their lowest level since mid-2017.

As with most other currencies, the US dollar appreciated sharply against the Chilean Peso, moving above 700 pesos/dollar in early June for the first time in more than three years.

Chile recorded a trade surplus of US\$3.2 billion during the first five months of the year, down 23.5% from a year earlier, as exports fell 4.1%, largely due to lower copper prices.

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