

Latam Flash: Chile's Central Bank Surprises with 75 bp Rate Increase

- Chile: Chile's central bank surprises with 75 bp rate increase

CENTRAL BANK SURPRISES WITH 75 BP RATE INCREASE LEAVING BENCHMARK RATE AT 1.5%; EXPECT MPR TO REACH 2.25% BY DECEMBER

At its meeting on Tuesday, August 31, the Board of the Central Bank (BCCh) surprised the market increasing the policy rate by 75 basis points up to 1.5%, significantly above the consensus which expected between 25 bp and 50 bp. With this, the BCCh accelerated its stimulus withdrawal resulting from extended fiscal injections and ample liquidity in the economy that narrowed the policy capacity gap earlier than expected and added pressure on inflation. The measure is justified by activity data above what was expected in the BCCh's baseline scenario for the second quarter, as well as the extension of new fiscal aid recently delivered by the government that will remain until the end of this year, which implies a fiscal boost greater than that previously considered.

The output gap would turn positive in Q3-2021, while private consumption maintains an "extraordinary" dynamism, according to the BCCH. Although the labor market still shows capacity gaps, some heterogeneous recovery is observed, but which should improve given recent re-opening measures. The outlook for local activity and employment is positive, in general terms, with positive surprises even in the imported component of investment. These factors would support a faster-than-anticipated recovery, with the consequent closing of gaps and higher inflationary pressures, making it necessary to recalibrate the monetary stimulus and modify its normalization pace in the coming quarters.

More details will be needed about the risk scenarios and the adjustment of projections in the BCCH's baseline scenario to infer the expected trajectories of the Monetary Policy Rate (MPR). For now, however, our preliminary assessment is that no adjustments of this magnitude will come at the October meeting, especially if we have a reduction in inflationary expectations and Congress were to reject the 4th withdrawal of pension funds.

Our view is that the BCCH would be concerned about an inflationary acceleration due to the permanence of high logistics costs, the absence of disinflationary pressures from the exchange rate and the increase in gasoline prices. For now, we consider this 75 bp rise as a sharp, decisive signal to appease short- and medium-term inflationary expectations that were markedly above historical averages. If this objective is achieved, we expect the Central Bank to reduce the intensity of the withdrawal of the monetary stimulus, with an increase of 50 bp at the October meeting and a further 25 bp in the December meeting, which would leave the MPR at 2.25% by December 2021. The normalization path would reduce its intensity over 2022.

The financial market would react with a relevant appreciation of the Chilean peso (CLP) that could take it quickly to CLP 750, an increase in nominal swap rates, and decreases in inflation compensations for medium and long term durations driven by increases in inflation-linked rates.

CONTACTS

Adriana Vega
613.564.5204
Scotiabank Economics
adriana.vega@scotiabank.com

Jorge Selaive
+56.2.2619.5435 (Chile)
Scotiabank Chile
jorge.selaive@scotiabank.cl

Anibal Alarcón
+56.2.2619.5435 (Chile)
Scotiabank Chile
anibal.alarcon@scotiabank.cl

Waldo Riveras
+56.2.2619.5465 (Chile)
Scotiabank Chile
waldo.riveras@scotiabank.cl

This report has been prepared by Scotiabank Economics as a resource for the clients of Scotiabank. Opinions, estimates and projections contained herein are our own as of the date hereof and are subject to change without notice. The information and opinions contained herein have been compiled or arrived at from sources believed reliable but no representation or warranty, express or implied, is made as to their accuracy or completeness. Neither Scotiabank nor any of its officers, directors, partners, employees or affiliates accepts any liability whatsoever for any direct or consequential loss arising from any use of this report or its contents.

These reports are provided to you for informational purposes only. This report is not, and is not constructed as, an offer to sell or solicitation of any offer to buy any financial instrument, nor shall this report be construed as an opinion as to whether you should enter into any swap or trading strategy involving a swap or any other transaction. The information contained in this report is not intended to be, and does not constitute, a recommendation of a swap or trading strategy involving a swap within the meaning of U.S. Commodity Futures Trading Commission Regulation 23.434 and Appendix A thereto. This material is not intended to be individually tailored to your needs or characteristics and should not be viewed as a “call to action” or suggestion that you enter into a swap or trading strategy involving a swap or any other transaction. Scotiabank may engage in transactions in a manner inconsistent with the views discussed this report and may have positions, or be in the process of acquiring or disposing of positions, referred to in this report.

Scotiabank, its affiliates and any of their respective officers, directors and employees may from time to time take positions in currencies, act as managers, co-managers or underwriters of a public offering or act as principals or agents, deal in, own or act as market makers or advisors, brokers or commercial and/or investment bankers in relation to securities or related derivatives. As a result of these actions, Scotiabank may receive remuneration. All Scotiabank products and services are subject to the terms of applicable agreements and local regulations. Officers, directors and employees of Scotiabank and its affiliates may serve as directors of corporations.

Any securities discussed in this report may not be suitable for all investors. Scotiabank recommends that investors independently evaluate any issuer and security discussed in this report, and consult with any advisors they deem necessary prior to making any investment.

This report and all information, opinions and conclusions contained in it are protected by copyright. This information may not be reproduced without the prior express written consent of Scotiabank.

TM Trademark of The Bank of Nova Scotia. Used under license, where applicable.

Scotiabank, together with “Global Banking and Markets”, is a marketing name for the global corporate and investment banking and capital markets businesses of The Bank of Nova Scotia and certain of its affiliates in the countries where they operate, including; Scotiabank Europe plc; Scotiabank (Ireland) Designated Activity Company; Scotiabank Inverlat S.A., Institución de Banca Múltiple, Grupo Financiero Scotiabank Inverlat, Scotia Inverlat Casa de Bolsa, S.A. de C.V., Grupo Financiero Scotiabank Inverlat, Scotia Inverlat Derivados S.A. de C.V. – all members of the Scotiabank group and authorized users of the Scotiabank mark. The Bank of Nova Scotia is incorporated in Canada with limited liability and is authorised and regulated by the Office of the Superintendent of Financial Institutions Canada. The Bank of Nova Scotia is authorized by the UK Prudential Regulation Authority and is subject to regulation by the UK Financial Conduct Authority and limited regulation by the UK Prudential Regulation Authority. Details about the extent of The Bank of Nova Scotia's regulation by the UK Prudential Regulation Authority are available from us on request. Scotiabank Europe plc is authorized by the UK Prudential Regulation Authority and regulated by the UK Financial Conduct Authority and the UK Prudential Regulation Authority.

Scotiabank Inverlat, S.A., Scotia Inverlat Casa de Bolsa, S.A. de C.V, Grupo Financiero Scotiabank Inverlat, and Scotia Inverlat Derivados, S.A. de C.V., are each authorized and regulated by the Mexican financial authorities.

Not all products and services are offered in all jurisdictions. Services described are available in jurisdictions where permitted by law.