MUFG LATIN AMERICA TOPICS

Chile's Macroeconomic Performance: Q3 2017 GDP and Current Monthly Indicators

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Overview

Economic growth in Chile was 2.2% YoY in Q3 2017. This was the highest rate since Q1 2016.

Household consumption remained robust throughout 2017, with the growth rate accelerating in Q3 (2.8 % YoY) when compared to Q2 (2.6% YoY). Among the factors positively affecting household consumption are the increase in real income due to low inflation and lower interest rates.

Gross Fixed Capital Formation (GFCF) declined for the fifth consecutive quarter (-2.2% YoY) in Q3 2017, although this drop was the smallest since Q3 2016. GFCF has been affected by a weak construction sector (-7.5% YoY in Q3, the fifth consecutive contraction) that has led to a dearth of investment projects, especially in the housing sector.

The YoY inflation rate in December 2017 was 2.3%, an acceleration in comparison to the previous month (1.9% YoY) and slightly above the lower band of the inflation target of 2.0%. The continued low inflation has been driven partially by currency appreciation.

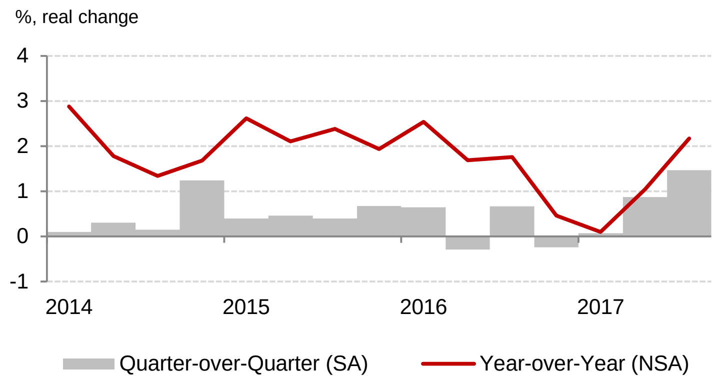
Despite the continued low inflation, during its last meeting in December, the Central Bank decided to keep the interest rate at 2.5% for the eighth consecutive time.

For 2018, an improvement in economic growth (around 3% YoY) is expected. Household consumption will continue to benefit from the low inflation and low interest rates. Investment is also likely to improve in 2018, although the pace of improvement is expected to be slow. In addition, higher copper prices will continue to positively impact the economic recovery.

1. GDP

Economic growth in Chile was 2.2% YoY in Q3 2017 (Figure 1). This was the highest rate since Q1 2016.

Figure 1: GDP Growth



Source: Central Bank of Chile, MUFG

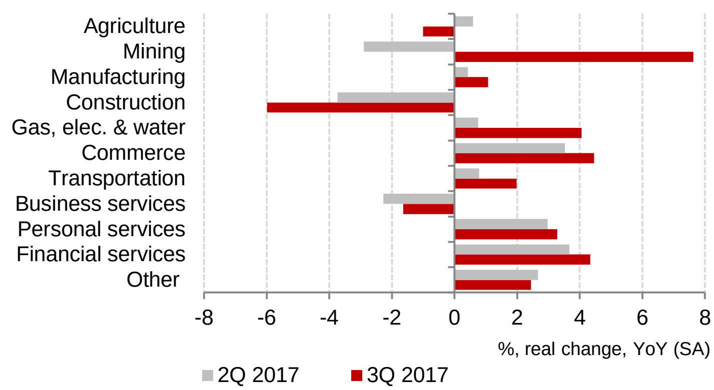
GDP by Sector

On the production side, most sectors registered an acceleration YoY in comparison to the previous quarter. The rebound in the mining sector (7.6% YoY) and the increase in the commerce sector (4.5% YoY) created the impulse for the improvement in the economy during Q3 (Figure 2).

The recuperation in the mining sector in Q3 was the result of higher copper prices and a return to normal production after the strike in Q1.

In contrast, the construction sector continued to experience weak results and reported its fourth consecutive contraction in Q3 2017 (-6.0% YoY). This is explained by a dearth of investment projects, especially in the housing sector. Infrastructure projects have also suffered recently.

Figure 2: GDP by Sector



Source: Central Bank of Chile, DataStream, MUFG

Consumption

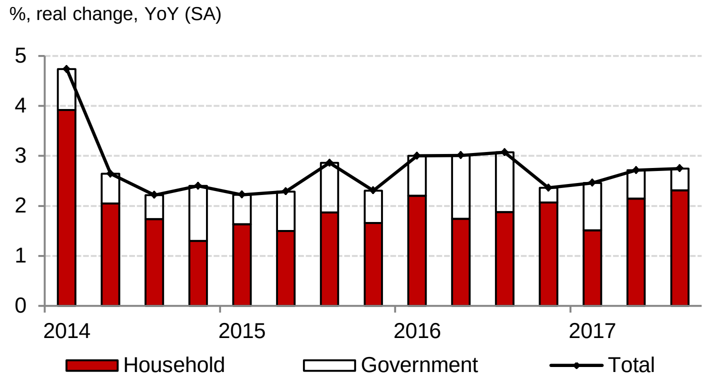
Consumption increased by 2.7% YoY in Q3 2017, driven by an increase in both household and government consumption (2.8% YoY and 2.5% YoY, respectively) (Figure 3).

Household consumption remained robust throughout 2017, with the growth rate accelerating in Q3 (2.8 % YoY) when compared to Q2 (2.6% YoY). Durable goods had steady growth during Q1-Q3 2017 and are contributing the most to the expansion in household consumption (Figure 4).

Among the factors positively affecting household consumption are the increase in real income due to low inflation and lower interest rates.

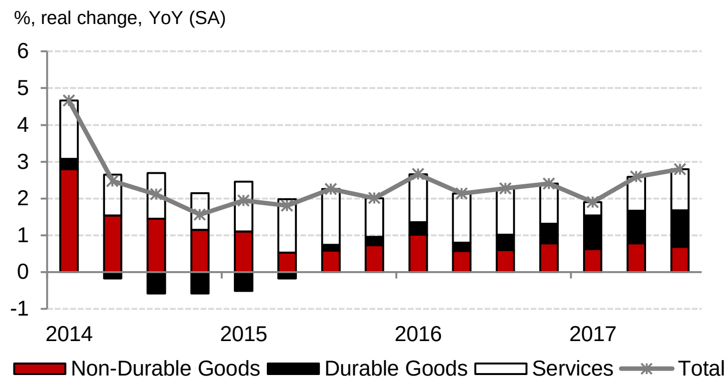
The increase in household consumption coincides with an improvement of household confidence throughout 2017. The consumer confidence index has gained 11.2 points (111.1 in November 2017) after reaching its lowest point of the year in February 2017 (99.9).

Figure 3: Consumption



Source: Central Bank of Chile, DataStream, MUFG

Figure 4: Household Consumption



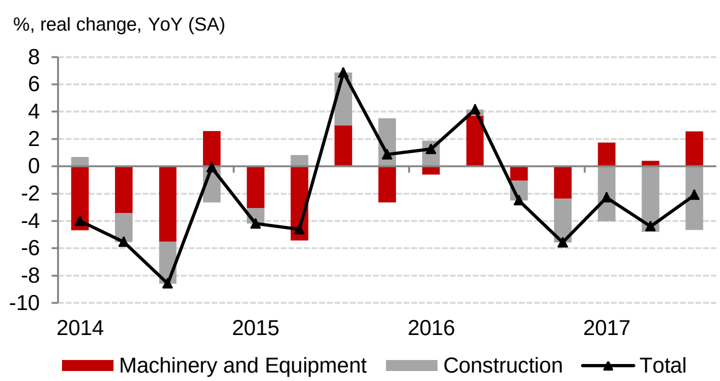
Source: Central Bank of Chile, DataStream, MUFG

Investment

Gross Fixed Capital Formation (GFCF) declined for the fifth consecutive quarter (-2.2% YoY) in Q3 2017, although this drop was the smallest since Q3 2016 (Figure 5).

GFCF has been affected by a weak construction sector (-7.5% YoY in Q3, the fifth consecutive contraction) that has led to a dearth of investment projects, especially in the housing sector. Infrastructure projects have also suffered recently.

Figure 5: GFCF*



*Gross Fixed Capital Formation
Source: Central Bank of Chile, DataStream, MUFG

The smaller contraction of GFCF was supported by increased investment in machinery and equipment (6.8% YoY).

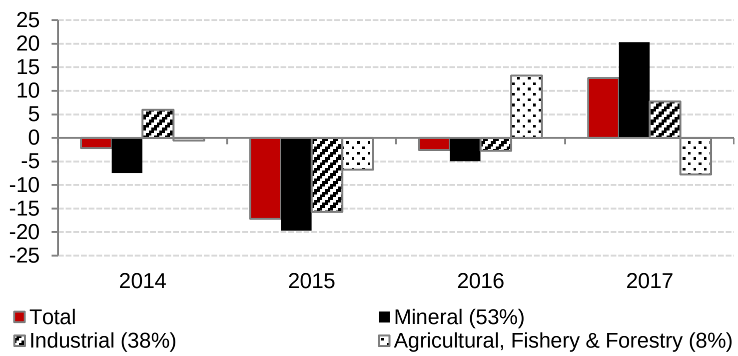
Business confidence is still weak. In December, the business confidence index dropped 3 points from its value in November (from 47.1 points to 44 points). This drop is mainly explained by the presidential elections that took place in December[1].

Exports and Imports

Exports in 2017 increased by 12.7% YoY (Figure 6). The improvement in the global economy and the improvement of copper prices (increase of 20.1% YoY in December 2017) throughout 2017 are the factors behind the increase in exports.

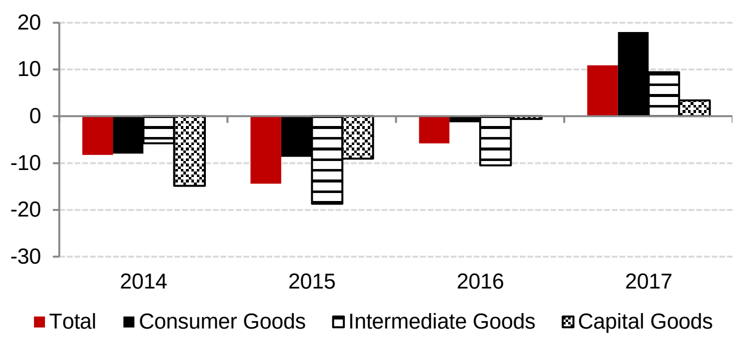
Imports also increased by 10.9% YoY in 2017, mainly due to an increase in imports of consumer goods (18.1% YoY) (Figure 7).

Figure 6: Exports by Types of Goods



Note: The number in the bracket is the weight on total exports.
Source: Central Bank of Chile, MUFG

Figure 7: Imports by Types of Goods

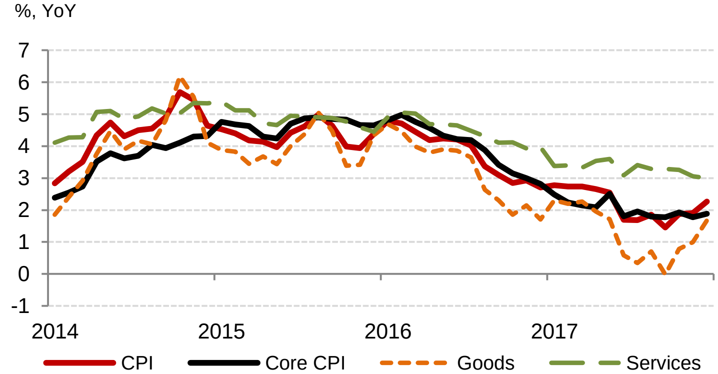


Source: Central Bank of Chile, MUFG

2. Inflation and Monetary Policy

The YoY inflation rate in December 2017 was 2.3%, an acceleration in comparison to the previous month (1.9% YoY) and slightly above the lower band of the inflation target of 2.0% (Figure 8). The continued low inflation has been driven partially by currency appreciation. This is mainly observed when looking at the low prices of goods (the average increase of good prices in 2017 was 1.7%, much lower than the average annual increase during 2014-2016 of 3.4%).

Figure 8: Inflation



Note: Core CPI excludes food and energy prices and makes up 72% of overall CPI.
Source: National Institute of Statistics, MUFG

[1] The survey was taken from November 28 to December 28, 2017. There was a period of uncertainty during this time regarding whether or not Sebastian Piñera would be the next president that may have influenced the fall of the index.

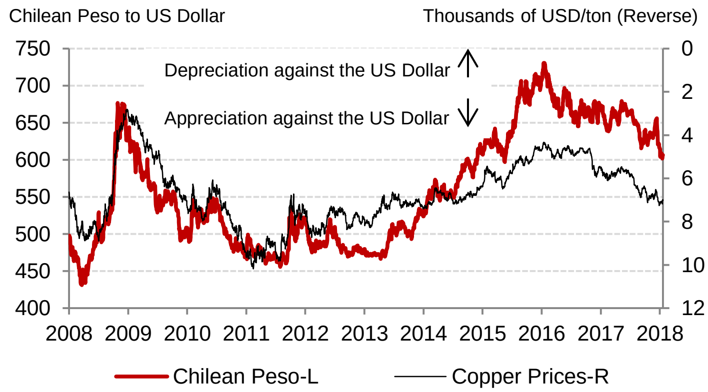
Despite the continued low inflation, during its last meeting in December, the Central Bank decided to keep the interest rate at 2.5% for the eighth consecutive time. The Central Bank, in explaining its decision to keep the interest rate unchanged, highlighted that underlying inflation has performed in line with expectations and that the market's medium-term inflation expectations remain firmly anchored at 3.0%.

3. Exchange rate

The Chilean Peso tends to track copper prices (Figure 9). At the beginning of 2016, copper prices slowly started to improve, causing the Chilean Peso to slowly begin to appreciate. The Chilean Peso has continued gaining value throughout 2017.

Copper prices are expected to continue improving and this will likely result in continued appreciation of the Chilean Peso.

Figure 9: Exchange Rate and Copper Prices



Source: Central Bank of Chile, DataStream, MUFG

4. Outlook

For 2018, an improvement in economic growth (around 3% YoY) is expected. Household consumption will continue to benefit from the low inflation and low interest rates. Investment is also likely to improve in 2018, although the pace of improvement is expected to be slow. In addition, higher copper prices will continue to positively impact the economic recovery.

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