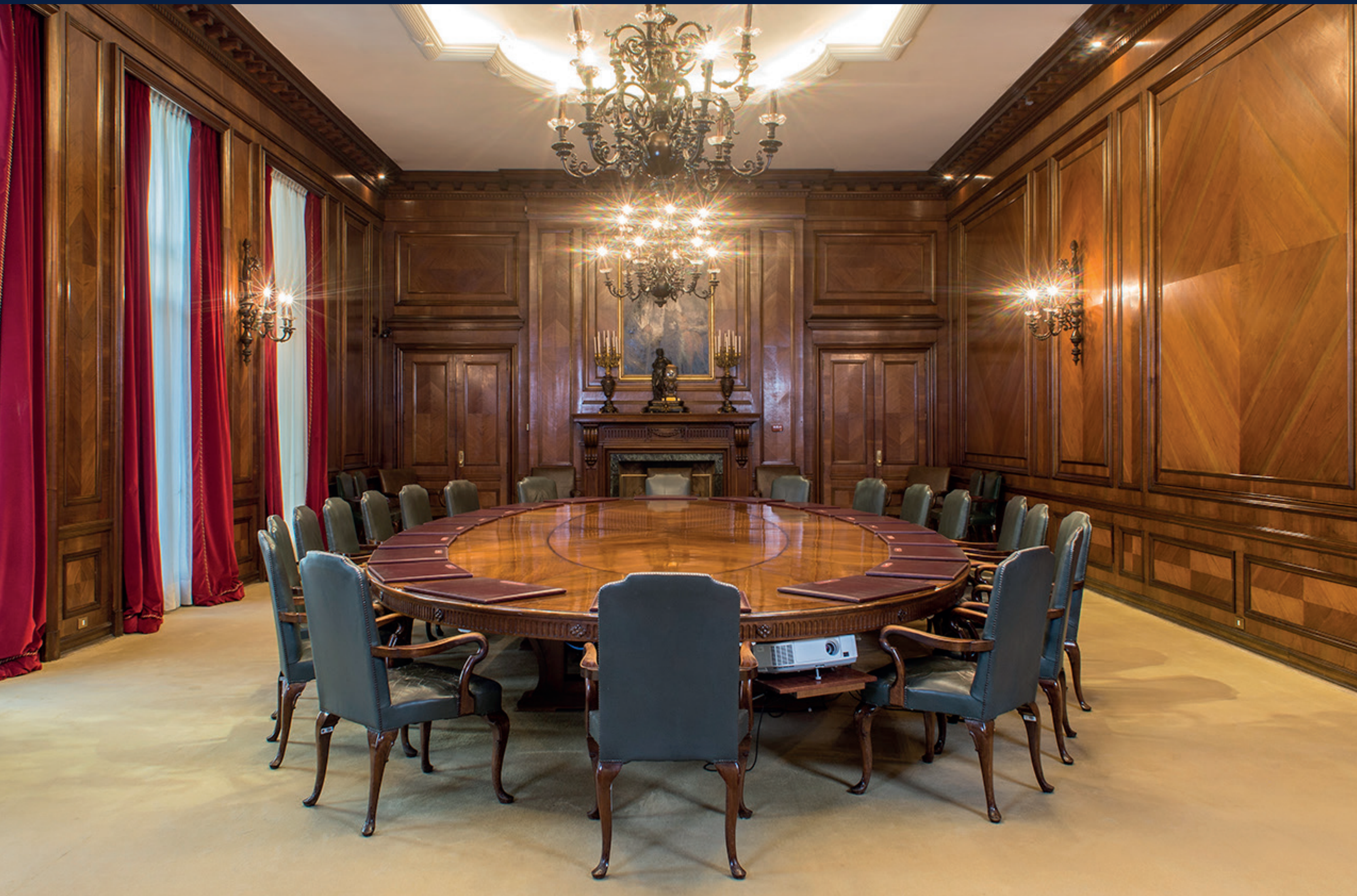
MONETARY POLICY MEETING

DECEMBER 2022



MONETARY POLICY MEETING

Monetary policy meeting No. 294, held on 6 December 2022.

Present: Rosanna Costa, Governor; Pablo García, Vice-Governor; Alberto Naudon, Board member; Luis Felipe Céspedes, Board member; Stepanka Novy, Board member.

Present the Finance Minister, Mario Marcel.

Also present: Beltrán de Ramón, General Manager; Juan Pablo Araya, Legal Counsel and Attestor; Elías Albagli, Monetary Policy Division Director; Juan Carlos Piantini, acting Financial Markets Division Director; Rosario Celedón, Financial Policy Division Director; Gloria Peña, Statistics Division Director; Michel Moure, Institutional Affairs Division Director; Diego Ballivián, Corporate Risk Division Director; Markus Kirchner, Macroeconomic Analysis Manager; Enrique Orellana, Monetary Policy Strategy and Communication Manager; Miguel Fuentes, International Analysis Manager; Sofía Bauducco, Economic Research Manager; Felipe Lozano, Communications Manager; Andrés Sansone, Advisor to the Finance Minister; Marlys Pabst, Secretary General.

1. Background

New information of recent months showed that the Chilean economy continued along its adjustment process after the significant imbalances accumulated during 2021. In line with expectations, annual inflation had peaked in August, when the annual variation of the CPI had reached 14.1%. Pending the data for November, which would be known the day after the Meeting, the data for September and October showed that annual inflation it had slowed to 12.8%, but this was still very high.

Local activity was already beginning to show negative annual variation rates. Measured in seasonally adjusted terms, in the third quarter, non-mining GDP had completed two consecutive quarters of contraction. In this context, private consumption continued to normalize after the rocketing increases of 2021. Investment, on the other hand, had been surprisingly strong, although growth was concentrated mainly in some particular sectors, such as renewable energies.

Meanwhile, the global economic outlook was complex, given the high inflationary persistence worldwide and the rate hikes decided by the main central banks. Projections for 2023 pointed to major world economies, such as the United States and the Eurozone, entering recessions in 2023. In several others, including China, expansion would be slow.

The Central Bank had implemented a significant monetary policy adjustment, taking the MPR to 11.25% at the October meeting. This was contributing to the gradual easing of inflationary pressures and would provide a better position to confront the difficulties of the external scenario.

However, the activity gap was still high, inflation continued at exceptionally high levels and inflation expectations were above the target over the two-year horizon, all signs that the adjustment process of the Chilean economy was not yet complete.

2. Background analysis and discussion

The local inflation outlook had evolved mirroring the forecasts in the September Monetary Policy Report, which was a significant development after several quarters of substantial changes in the macroeconomic scenario from one Report to the next. Annual inflation had declined slightly after peaking in August, driven mainly by volatile items, as well as some goods in the non-volatile basket. Behind the inflation behavior was a sum of factors, including the economy's adjustment, the normalization of global supply chains and the decline in some international prices.

The decline in annual inflation was positive news. However, the risks were far from over. Persistent inflation remained a matter of serious concern. Inflation levels remained well above target and the central scenario projections of this Report exceeded those of the previous one. Despite some moderation, inflation expectations two years ahead remained above 3%. Meanwhile, although the economy's adjustment trend continued, indicators showed a somewhat more dynamic demand in the margin. This development was tempered by the fact that the biggest difference was in investment, concentrated in some specific sectors, with the overall outlook remaining weak towards 2023 and with a smaller impact on inflation. In any case, this issue needed to be carefully monitored.

3. Analysis of monetary policy options

All the Board members agreed that the background information known since the October meeting was, for the most part, consistent with the decision announced at the time. This was that, after raising the Monetary Policy Rate (MPR) to 11.25%, the Board had communicated that the MPR was at the highest point of the cycle begun in July 2021 and that it would be kept there for as long as was deemed necessary to ensure the convergence of inflation to the target over the two-year policy horizon. In this context, the Board agreed that the only plausible option at this Meeting was to keep the MPR at 11.25%.

All five Board Members agreed that the events of recent months indicated that the economy was in an adjustment phase and that inflation would begin to ease. However, this did not imply that efforts to reduce inflation should diminish, much less that the inflationary problem had been solved. On the contrary, there was still a way to go before the macroeconomy would signal that the process of inflation convergence to the target had been consolidated. The full Board agreed that the turning points of monetary policy would be based primarily on an assessment of the state of the economy and not on specific dates.

There was consensus among the Board that the key and essential commitment was to fight for inflation to return to 3% in two years, which was the way to avoid excessive and unnecessary costs for the population. Prematurely starting the process of lowering the MPR might have adverse effects on inflationary persistence and, therefore, on economic activity, as sensitivity scenarios could materialize that would force a pause or even a reversal of the process. Plus, this could adversely affect monetary policy communication and the Bank's credibility. Anyway, there were also scenarios in which inflation falling faster, in which case the Board would also be vigilant.

4. Monetary policy decision

Governor Costa, Vice-Governor García, and Board members Naudon, Céspedes, and Novy voted for holding the MPR at 11.25%.

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