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# Chile Holds Key Rate at 5% on Steady Prices and Surging Growth

By Randall Woods - Oct 18, 2012

Chile's central bank kept its key interest rate unchanged yesterday for a ninth straight month as the world's top copper producer combined Latin America's slowest inflation with some of the region's fastest growth.

The policy board, led by bank President Rodrigo Vergara, held the key interest rate at 5 percent, as forecast by all 20 analysts surveyed by Bloomberg. Policy makers last changed borrowing costs in January with a quarter-point reduction.

Inflation rates have held below the central bank's target for the past four months even as economic growth continues to exceed estimates made by economists. While analysts view monetary tightening as increasingly likely in 2013 or 2014, risks of a further slowdown in China or deeper recession in Europe are keeping policy makers in a wait-and-see mode.

"Two forces remain at play: there's uncertainty abroad, although the panorama has improved somewhat, and internally consumption continues to grow at a strong pace," Matias Madrid, an economist at Banco Penta in Santiago, said by phone after yesterday's decision. "With both forces at play, the central bank is maintaining a neutral bias."

Policy makers in their statement yesterday removed a reference seen in September to the peso's appreciation, saying only that the U.S. dollar had weakened internationally. Chile's peso has strengthened 9.9 percent this year, the biggest gain among the seven Latin American currencies tracked by Bloomberg.

## Sustained Growth

Economists increased their growth forecast for 2012 and 2013 in an Oct. 9 central bank survey after economic growth data exceeded estimates, unemployment fell and manufacturing surged. The analysts in the monthly poll forecast borrowing costs will increase to 5.25 percent within 23 months after expecting no change in the September survey.

Gross domestic product in the Andean nation expanded 5.4 percent in the first half of the year, while growth as measured by the central bank's Imacec index was 5.3 percent in July and 6.2 percent in August, the fastest pace in half a year. Retail sales surged 11.3 percent in August from last year.

Manufacturing climbed 3.6 percent in August, compared with the median estimate for a 1 percent gain by analysts polled by Bloomberg. The unemployment rate fell to 6.4 percent in the three months through August after economists forecast it would remain unchanged at 6.5 percent.

Chile's GDP will grow 5 percent in 2012, the fastest expansion among major Latin American nations after Peru and Venezuela, the International Monetary Fund said in an Oct. 12 report on the region. The economy of Brazil will expand 1.5 percent while that of Mexico, which is Latin America's second-largest economy, will increase 3.8 percent, the Washington-based lender said.

## Inflation Rate

"Domestically, output indicators have evolved around trend rates and private consumption has strengthened," policy makers said in yesterday's statement. "The labor market remains tight."

Inflation quickened to 2.8 percent in September, the highest rate in four months, on gains in the price of food and beverages, health care and transportation. Policy makers target 3 percent inflation, plus or minus 1 percentage point over two years.

Traders estimate inflation will continue to accelerate, and policy makers in minutes from last month's rate meeting warned against "latent risks" to consumer prices as the economy expands.

Two-year breakeven inflation, which is derived from the difference between nominal and inflation-linked yields on swaps, rose 7 basis points, or 0.7 percentage point, to 3.06 percent yesterday from the previous meeting on Sept. 13.

Slowing Down?

Still, Chile has the lowest inflation rate of any major Latin American economy tracked by Bloomberg, and the economy is starting to feel the effect of the global slowdown. Chile in September posted its third consecutive monthly trade deficit and fourth for the year, as exports fell 9.5 percent from the year earlier.

The price of copper, which accounts for more than half of Chile's exports, has averaged $3.64 a pound this year compared with $4.01 a pound in 2011. Prices will fall further in 2013, averaging $3.40 a pound, according to the latest central bank forecasts.

"In Chile, the economy continues to show a strong performance and the effects of the weakened external scenario have been tenuous," Vergara said in a Sept. 28 presentation posted on the bank website. "The board continues to monitor developments in external and internal macroeconomic scenarios and their impact on inflation."

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