BCCh Watch

January 13 2011

Chile

Economic Analysis

Alejandro Puente
Chief Economist
apuente@grupobbva.cl

Carola Moreno
cmoreno@grupobbva.cl

Karla Flores
kfloresm@grupobbva.cl

Soledad Hormazábal
shormazabal@grupobbva.cl

January Monetary Policy Meeting: Pause.

The Central Bank of Chile decided to keep the monetary policy rate at 3.25% annual. With this pause, the first since it started the upward cycle last June, it ruled out an increase in inflation expectations.

Externally, the release highlights moderate growth in developed economies, contrasting with dynamic emerging economies. In addition, concerns on financial markets regarding the situation of some European economies and the increase in raw material prices leading to higher inflation in some economies are mentioned.

On the domestic front, the release refers to continuing dynamic economic activity and employment, particularly in the short term, and exchange rate depreciation following the announcement of the dollar purchase program.

The decision to pause the upward cycle, started last June, was to some extent a surprise for most of the market and for BBVA Research, which expected a 25 bps increase. This pause is clearly a response to the Board's attempt to reinforce the dollar support strategy in the local market through reserve accumulation. However, we think that insofar as a temporary pause is expected, and a monetary policy rate close to the neutral level is expected, this pause will not have an impact on the exchange rate, although it will help to consolidate expectations of greater inflation. The Board itself stated that "it will be necessary to continue reducing the monetary stimulus in the coming months".

However, if concerns over appreciation prompted the central bank to rule out the risk of greater inflation and decoupling inflation expectations on the policy horizon, it is likely that the pause will continue until there are expectations of greater inflation, which will happen with full force from March onwards.