

# Monthly Economic Update

May 31st, 2022

## Chile News

After months of intense debate, the Constitutional Convention completed voting on the contents of the draft constitution on May 14<sup>th</sup>. The document's 499 articles promise to bring significant change to Chile's system of government and economic model, but some of the most radical proposals, such as nationalizing the mining industry and eliminating the second legislative chamber, were finally rejected. The draft must now undergo an editing process to create a coherent document that will be put to a referendum on September 4<sup>th</sup>. Polls continue to show that more voters would vote to reject the proposed Constitution than approve it.

Support for the new government has declined. According to the weekly poll by Cadem, approval of President Gabriel Boric's performance fell from 50% in early March to 38% by May 23<sup>rd</sup>, a much faster decline than previous presidents have suffered during their first months in office.

In April, the government announced a US\$3.7 billion package of measures to mitigate the impact of rising prices and the slowing economy on vulnerable households. They include lower fuel prices, wage subsidies, a freeze on bus and train fares and more support for working parents.

In May, lawmakers approved the largest rise in the minimum wage in almost thirty years. Following talks between the government and labour unions, the monthly minimum wage will rise to CLP 380,000 (US\$456) from May 1<sup>st</sup> and to CLP 400,000 by the end of the year, up from CLP 350,000 previously. Support will be provided to help small businesses to shoulder the cost of the increase.

Legislation that would allow savers to make a fourth withdrawal of up to CLP 4.9 million (US\$5,850) from their pensions savings failed to secure the two-thirds

majority in the Chamber of Deputies required to approve a constitutional reform. During the April vote, deputies also rejected the government's alternative proposal which would have limited savers to using withdrawals to cover alimony payments, mortgage down payments and healthcare costs.

In May, environmental authorities in Santiago rejected a US\$3.0 billion project presented by Anglo American to expand its Los Bronces copper mine, arguing that the investment could represent a risk to human health. The mining company plans to appeal the decision.

## Economic Statistics

Activity has slowed with the economy growing by 7.2% during the first three months of 2022, down from 12.0% in the final quarter of last year. On a seasonally-adjusted basis, activity contracted 0.8% compared to the previous quarter, reflecting weaker mining and retail activity. In May, the government adjusted its official growth forecast to 1.5%, down from the previous administration's outgoing forecast of 3.5%, which had been widely dismissed as overoptimistic.

Despite growing demands to increase support to households as the economy slows, the new administration has committed to implementing the 20% cut in public spending approved by Congress late last year. As a result, the government expects to end the year with a deficit of 1.7% of GDP (down from 7.8% in 2021) and aims to reduce the structural deficit (based on long-term growth and copper price forecasts) to 0.3% by the end of its four-year term.

Inflation has continued to rise faster than expected with the government's Consumer Price Index, jumping by 1.4% in April (following a 1.9% increase in March) or by 10.5% on an annualized basis. The increase was driven by food prices, which rose by 2.3% in April alone. As

inflation continues to outpace official forecasts, many see no let-up this year. Surveyed by the Central Bank in May, analysts predicted that the index would end the year at 8.9%, up from 4.5% predicted in December last year.

To counteract soaring inflation, the Central Bank raised interest rates for the third time this year. In a unanimous decision, the board voted in May to increase its benchmark rate by 125 basis points to 8.25%, its highest level in a decade and ahead of the policy corridor outlined in its latest Monetary Policy Report. The market now expects the rate to rise as high as 9.00% in the coming months.

Optimism in the business sector has continued to weaken. The Monthly Business Confidence Indicator, produced by the Adolfo Ibáñez University and ICARE, fell to 44.14 points in April, its lowest level in almost two years, with construction, manufacturing, and retail all now in negative territory. Executives surveyed by the Central Bank in April were worried that although sales continue to grow, rising costs are squeezing margins.

Consumer confidence has also fallen with GfK's Economic Perceptions Index dropping to 25.6 points in April, down more than 10 points from December and its lowest level in 12 months. Concern has grown about the state of the economy, the long-term outlook for Chile and shoppers' ability to buy household items.

Unemployment reached 7.8% in the three months to March, its highest level in five months, as more people return to a slowing labour market in the wake of the

pandemic.

Copper prices have fallen to below US\$4.30/lb in recent weeks (from over US\$4.60/lb during most of March and April) as concerns grow about the state of the Chinese economy and the impact of inflation on global demand. However, after briefly breaching US\$4.10/lb in early May, prices rebounded.

In the face of lower copper prices, the Chilean peso has fallen significantly against the US dollar, moving from CLP780/dollar in early April to CLP870/dollar one month later.

After slowing significantly earlier in the year, Chile's foreign trade has recovered into the second quarter, driven by higher metals and energy prices and demand for consumer goods. Exports reached US\$33.7 billion in the first four months of 2022, up 11.1% from a year ago while imports rose 26.8% to US\$30.4 billion. As a result, Chile's trade balance fell by almost half to US\$3.5 billion.

Shares prices in Chile have rallied this year with the IPSA index reaching 5,000 points in mid-May for the first time in almost three years. Gains have been driven by rising commodity prices, with shares in lithium and nitrates producer SQM almost doubling since the start of the year.

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