INTERNATIONAL MONETARY FUND

IMF Country Report No. 13/198

CHILE

2013 ARTICLE IV CONSULTATION

July 2013

Under Article IV of the IMF's Articles of Agreement, the IMF holds bilateral discussions with members, usually every year. In the context of the 2013 Article IV consultation with Chile, the following documents have been released and are included in this package:

- **Staff Report** for the 2013 Article IV consultation, prepared by a staff team of the IMF, following discussions that ended on May 10, 2013, with the officials of Chile on economic developments and policies. Based on information available at the time of these discussions, the staff report was completed on June 14, 2013. The views expressed in the staff report are those of the staff team and do not necessarily reflect the views of the Executive Board of the IMF.
- **Informational Annex**
- **Public Information Notice** (PIN) summarizing the views of the Executive Board.

The document listed below has been or will be separately released.

Selected Issues Paper

The policy of publication of staff reports and other documents allows for the deletion of market-sensitive information.

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INTERNATIONAL MONETARY FUND

CHILE

June 14, 2013

STAFF REPORT FOR THE 2013 ARTICLE IV CONSULTATION

KEY ISSUES

Setting: Growth has been strong, led by domestic demand, but a deceleration toward potential appears to be underway. The labor market remains tight, while inflationary pressures are subdued. The current account has deteriorated amid swelling capital flows.

Risks: Key downside risks relate to the outlook for copper, an intensification of the euro area crisis, and a sudden stop of capital inflows. Overheating risks remain, as a sustained slowdown in domestic demand is not yet assured.

Policy mix: Economic policies should support the orderly slowdown in activity and domestic demand underway. To this end, the staff recommended a tighter fiscal stance than implied by the 2013 budget, while monetary policy could remain neutral. If downside risks materialize, the floating exchange rate is the first line of defense and there is room for forceful monetary and fiscal policy action to support demand, as warranted. Staff recommended a modest structural surplus for the coming years.

Financial stability: There are no major stability issues. The staff supported the authorities' efforts to improve regulation and supervision, including of financial conglomerates, and encouraged continued vigilant attention to potential financial stability risks.

Medium term: Achieving sustained, strong and inclusive growth will require actions to tackle long-standing issues in energy, education, and the labor market.

Politics: Presidential and congressional elections will be held in November 2013. Former President Bachelet (Socialist Party) has announced her candidacy. She and others have called for tax, pensions, and education reforms.

Past advice: There is broad agreement between the Fund and the authorities on macroeconomic policy and structural reform priorities. In line with Fund advice, the authorities accelerated the withdrawal of the fiscal stimulus injected in 2009. Further, the ongoing substantial financial sector reform agenda addresses FSAP recommendations. Other recent reforms are in line with challenges staff have noted, such as raising labor force participation and productivity and reducing income inequality.

Approved By
Charles Kramer and Tamim Bayoumi

Discussions took place in Santiago during April 30—May 10, 2013. The staff team comprised Messrs. Erickson von Allmen (head), Rodriguez-Delgado, Wu (all WHD) and Arregui (MCM). Messrs. Garcia-Silva and Carrière-Swallow (OED) attended some of the meetings. The mission met with Finance Minister Larraín, Central Bank Governor Vergara, Labor Minister Matthei, senior officials at the Ministry of Economy, the Ministry of Energy, the Ministry of Housing and Urban Development, and the National Statistics Institute, think tanks, academics, and representatives for banks, industry, and unions.

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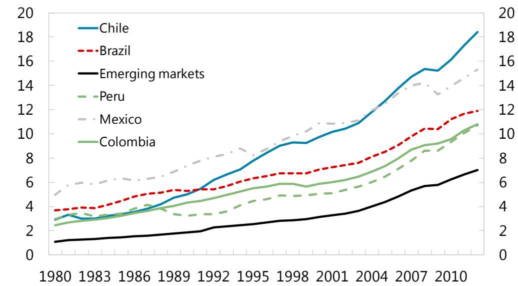
THE SETTING

1. Chile's economic performance in recent years has been impressive. The rebound from the 2009 global financial crisis and the 2010 earthquake was quick and strong, and the economy has outpaced most of its peers over the last 2-3 years.[1] This performance reflects many factors, including the benefits of structural reforms, but two stand out:

Per Capita Income, 1980-2012
(GDP per capita in 1,000 U.S. dollars at Purchasing Power Parity-terms)



Source: IMF *World Economic Outlook* database.

- ***Policies.*** Technocratic, rules-based, and transparent policy management—monetary policy under a floating exchange rate undertaken by a credible central bank, and prudent fiscal policy, since 2001 under a near-legendary fiscal rule—has enhanced policy clarity, reinforced Chile's resilience to shocks, and allowed for vigorous policy responses when needed, as after the global financial crisis and the earthquake. Chile has the highest sovereign debt rating ever for any Latin American country.

- ***External conditions.*** Chile has benefited from strong demand and high prices for copper, its principal export (which accounts for over half of Chile's exports), and from easy global financial conditions. But the global copper boom appears to be coming to an end.

2. The outlook is bright but with important challenges. The key near-term challenge is to support a soft landing in the economy in the context of a widening current account deficit, swelling capital inflows, and an uncertain outlook for copper. The medium and long-term challenge is to foster sustained growth without the boost from rising copper prices and against the headwind of a stagnating working-age population. While Chile's strong policy frameworks and investor-friendly environment will continue to support growth, further actions are needed to achieve a sustained improvement in productivity growth.

CURRENT CONDITIONS

3. Economic activity, which surprised on the upside in 2012, has slowed in 2013.

- ***2012***. Real GDP growth came in at 5½ percent compared with 4.7 percent projected in last year's staff report, powered by surprisingly resilient private domestic demand. Mining investment was particularly strong. Private consumption was boosted by employment and real wage growth, whereas consumer credit growth continued to moderate. Booming domestic demand and a slightly positive (and widening) output gap raised overheating concerns—especially as the current account deteriorated rapidly.

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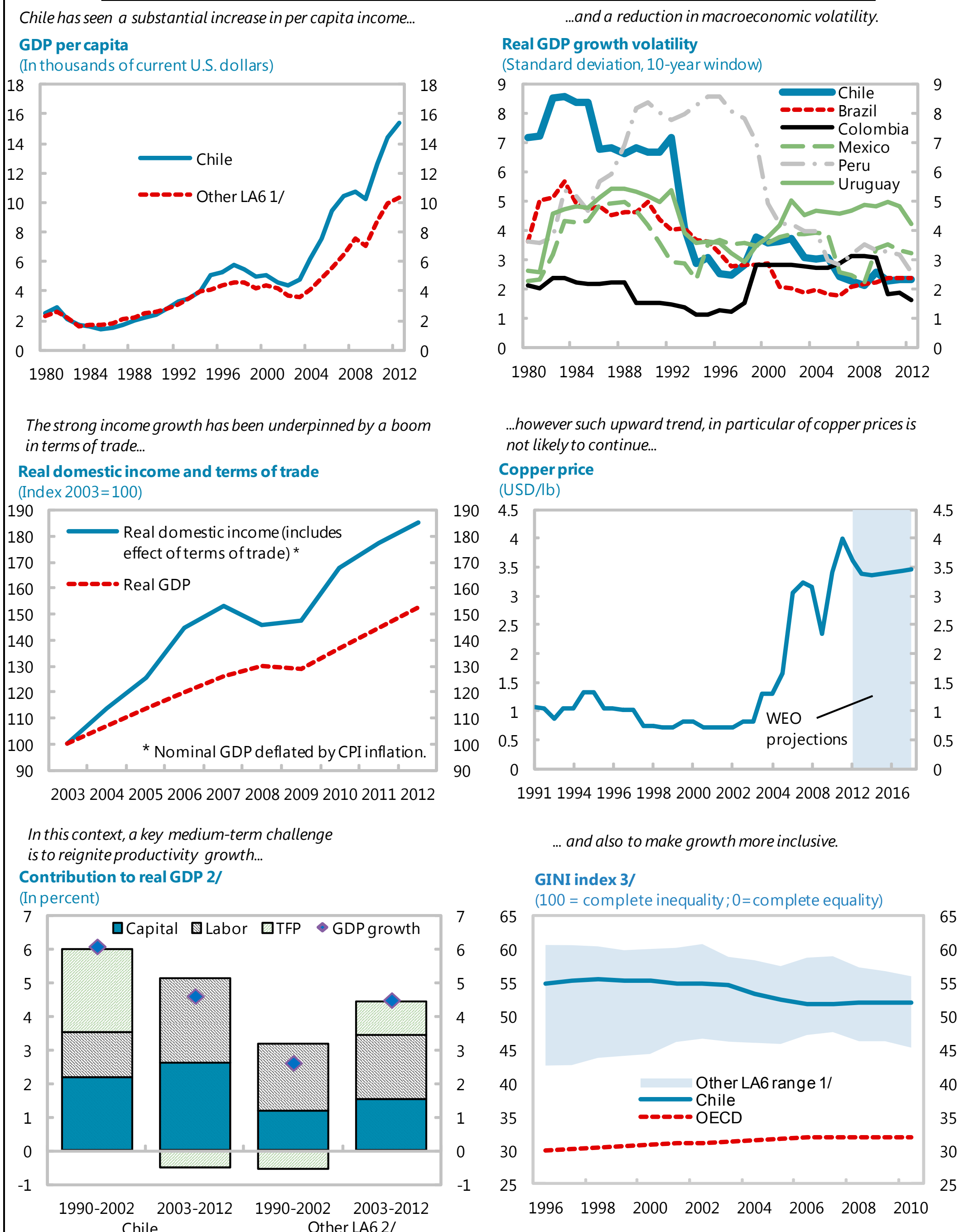
[1] The Selected Issues Paper *A Tale of Two Recoveries*, by D. Rodriguez-Delgado, looks at Chile's growth performance from a business cycle accounting perspective.

Figure 1. Chile: Past Growth Performance and Challenges Ahead

Sustained productivity growth is needed to continue Chile's past strong performance.



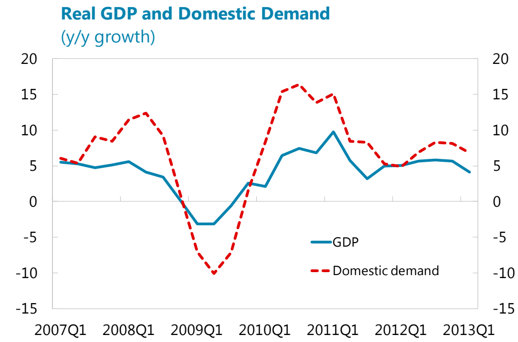
Sources: World Economic Outlook (IMF), OECD, World Development Indicators (World Bank), and Fund staff calculations.

1/ Other LA6 includes Brazil, Colombia, Mexico, Peru, and Uruguay.

2/ Based on Sosa, Tsounta and Kim (2013).

3/ Linear interpolation used to fill in missing data.

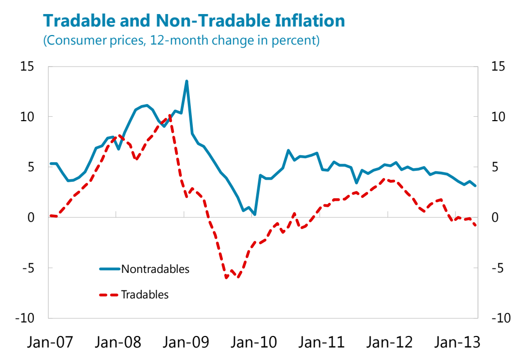
- ***2013 so far***. However, growth slowed to 4.1 percent (y/y) in 2013Q1, from 5.7 percent in 2012Q4. The slowdown is apparent also in recent data on employment, construction, and consumer credit. The monthly GDP proxy (IMACEC) had a fourth consecutive weak reading in April. Still, retail sales and consumer imports remain quite brisk and the drop in copper prices (down 6 percent since end-2012) has not yet sapped consumer and business confidence, both of which remain firm. And even if recent developments do mark a turn in the cycle, supply conditions remain tight. This is most clearly evident in the labor market: unemployment has fallen markedly to a historically low 6.4 percent and there are reported shortages in agriculture, mining, and construction.



Source: Haver Analytics.

4. Meanwhile, fiscal policy has provided some dampening effect. The budget recorded a small surplus in 2012 as the government saved revenue overperformance and kept spending (notably current transfers and capital) below budget. The structural deficit improved to ½ percent of GDP, handsomely beating the authorities' 1 percent target two years ahead of time. On this basis, the fiscal impulse—measured by staff as the change in the non-mining structural primary balance—was negative (mildly) for the third year in a row. The government thereby has clawed back much of the stimulus injected in 2009. Expenditure grew 3.7 percent y/y in real terms in 2013Q1.

5. Inflation has been surprisingly low and declining. The principal factors behind this development seem to include the peso appreciation last year, evident in tradable inflation; a sudden spurt in labor productivity in 2012 that has contained unit labor costs; and falling energy prices. Inflation dropped to 0.9 percent in May, below the official target of 3 (+/-1) percent. There is also downward bias in at least one component of the consumer price index, but this bias does not seem to materially change the picture of low and declining headline inflation.[2] Inflation expectations remain anchored at 3 percent 24 months out. In this environment, the central bank has left the policy rate at 5 percent, a broadly neutral rate, since January 2012**.**



Source: Haver Analytics.

6. The peso has appreciated in the context of swelling capital flows. The peso appreciated 7 percent against the dollar between June 2012 and April 2013, and about 5 percent in real effective terms. The peso has subsequently depreciated, along with other regional

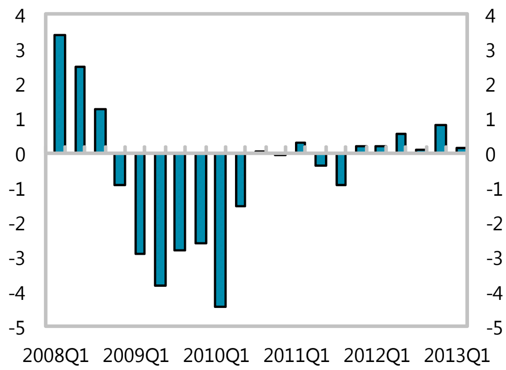
[2] Chile's National Institute of Statistics has announced that it will revise the methodology for measuring the clothing sub-index, which has a downward bias, and to review the methodology for three other sub-indices (rents, domestic services, and electronics).

Figure 2. Chile: Cyclical Position

Strong activity has started to moderate.

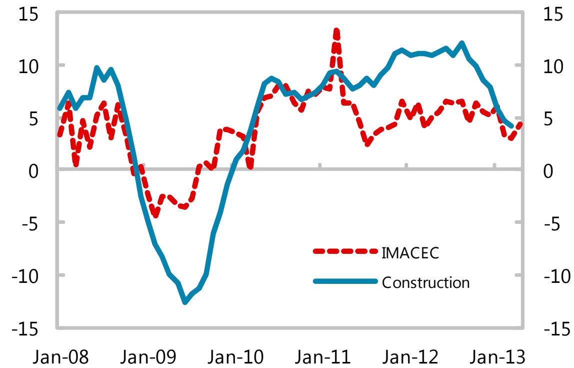
The output gap turned positive in 2012, but it declined in the first quarter of 2013.

Output gap
(In percent of potential GDP)



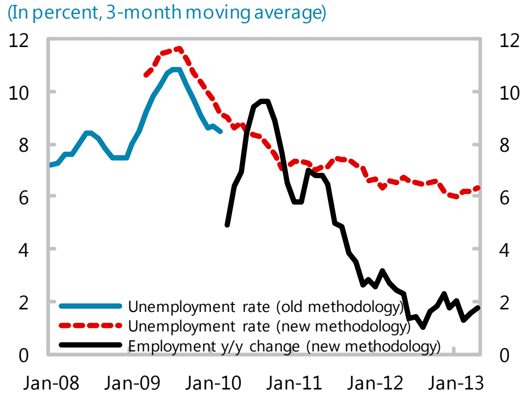
Other indicators also point to a deceleration in activity.

Selected economic activity indicators
(In percent, y-o-y)



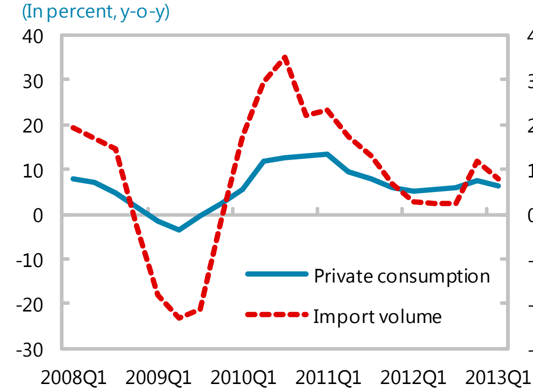
Amid near record low unemployment rate...

Labor market
(In percent, 3-month moving average)



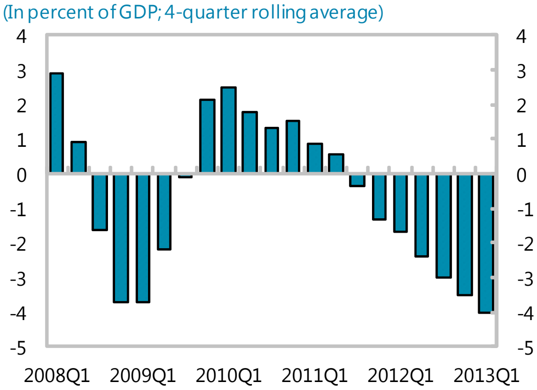
...private consumption has remained strong...

Private consumption and import volume growth
(In percent, y-o-y)



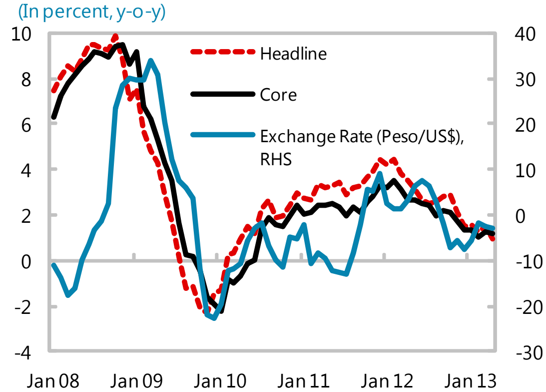
...which, together with high private investment, contributed to the recent deterioration of the current account.

Current account balance
(In percent of GDP; 4-quarter rolling average)



Peso appreciation has helped keep inflation low.

Consumer prices and the exchange rate 1/
(In percent, y-o-y)



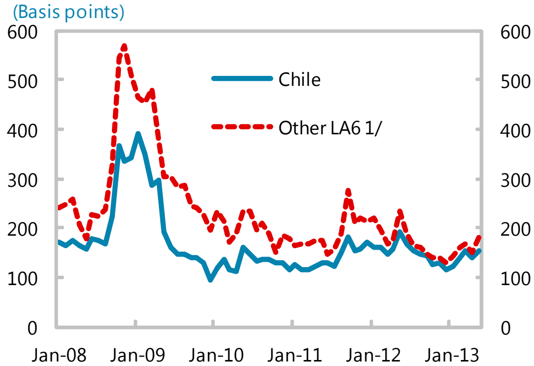
Sources: Central Bank of Chile, Haver Analytics, and Fund staff calculations.
1/ Core inflation excludes fuels, fresh fruits and vegetables.

Figure 3. Chile: Financial Market Developments

Despite overall strong financial performance and ample liquidity, credit conditions have tightened recently.

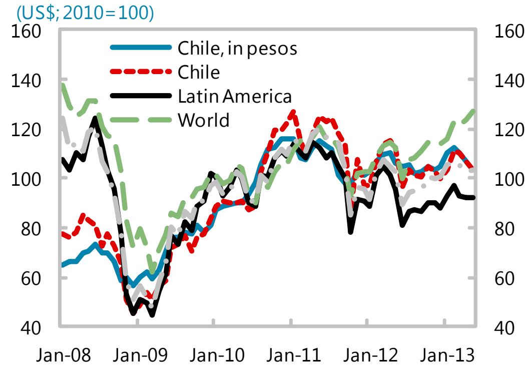
Chile's sovereign spread is among the lowest in the region.

Sovereign spreads
(Basis points)



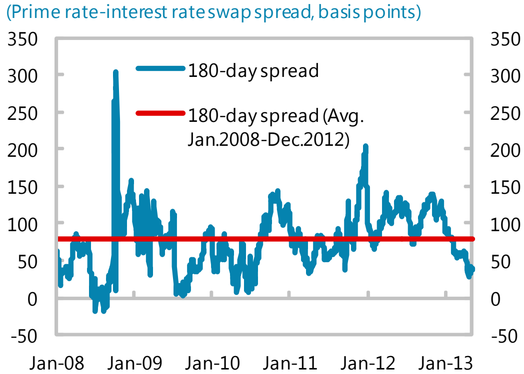
The stock market has outperformed the regional average but lagged the world average.

Stock market performance, MSCI 2/
(US$; 2010=100)



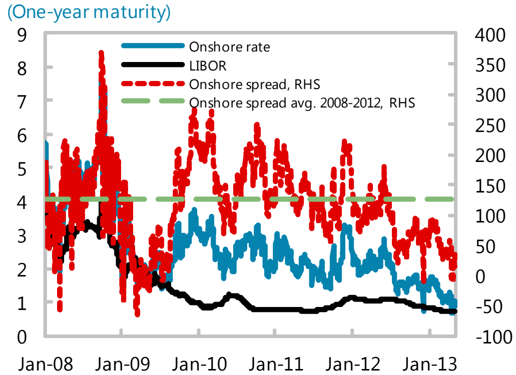
There is ample liquidity in pesos...

Liquidity pressures in the peso money market
(Prime rate-interest rate swap spread, basis points)



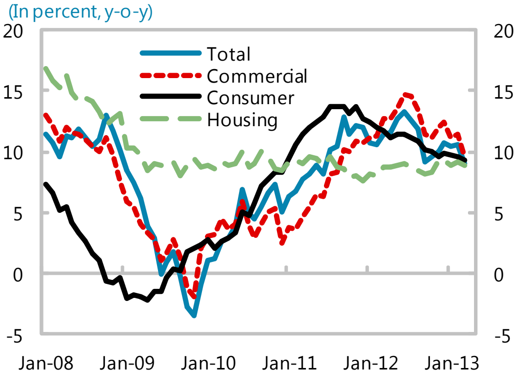
...as well as in dollars.

Liquidity pressures in the dollar money market
(One-year maturity)



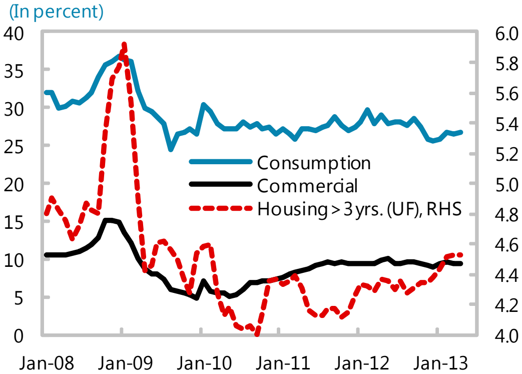
Still, credit growth has moderated somewhat.

Real credit growth
(In percent, y-o-y)



Mortgage rates have increased.

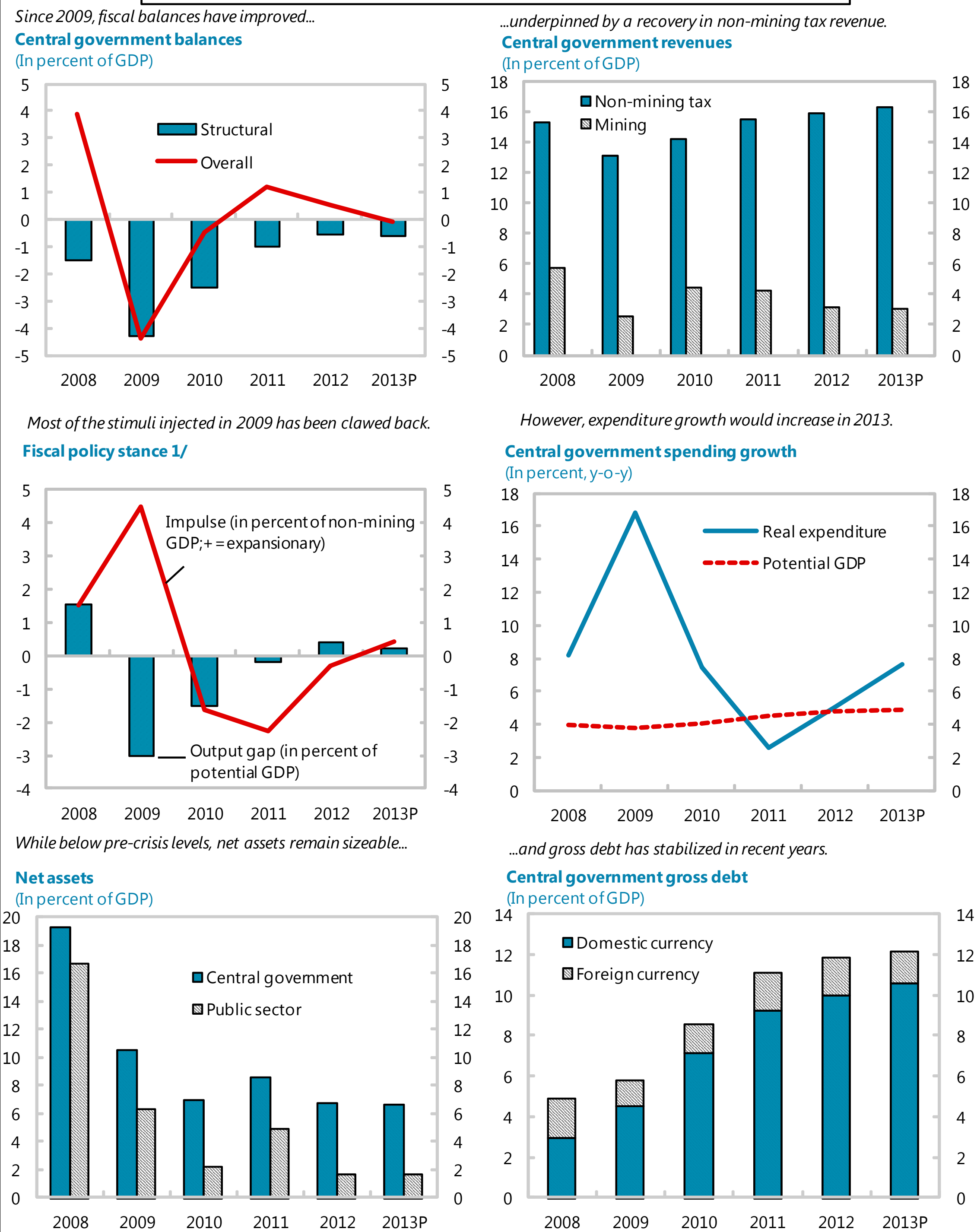
Lending rates by sector 3/
(In percent)



Sources: Bloomberg, Central Bank of Chile, and Fund staff calculations.
1/ Other LA6 includes Brazil, Colombia, Mexico, Peru, and Uruguay.
2/ Morgan Stanley Composite Indices.
3/ Unidad de Fomento (UF) is a unit of account adjusted for inflation.

Figure 4. Chile: Fiscal Policy and Public Finances

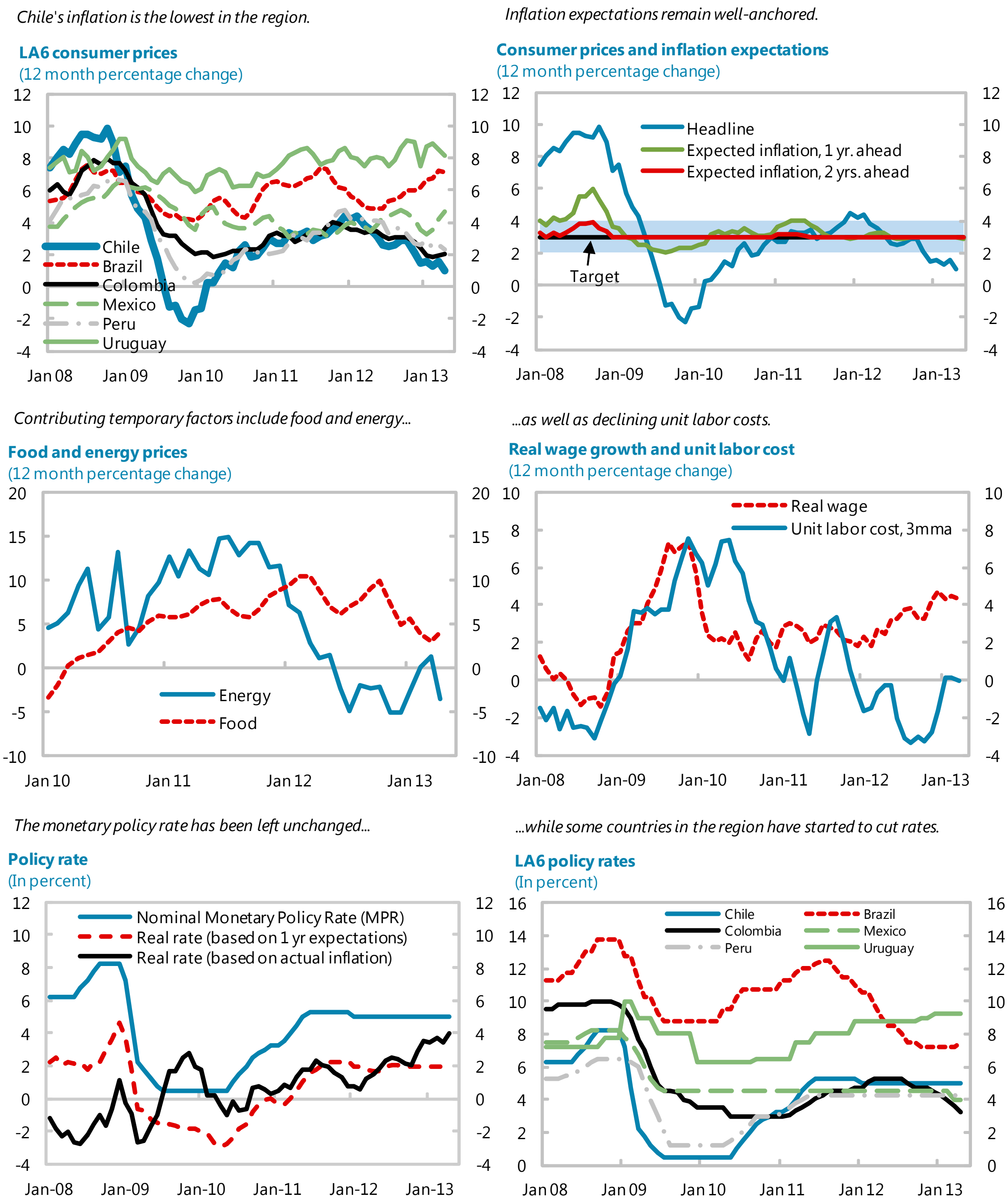
A faster than anticipated consolidation has broadly restored the fiscal stance to its pre-crisis level; net assets remain sizeable, albeit lower than in 2008.



Sources: Ministry of Finance, Central Bank of Chile, and Fund staff calculations.
1/ Change in the non-mining structural primary deficit.

Figure 5. Chile: Monetary Policy and Inflation

Amid temporary factors keeping inflation low, the monetary policy rate has been left unchanged.



Sources: Central Bank of Chile, Haver Analytics, and Fund staff calculations.

currencies, but is still stronger than the low level reached last June. Historically, the peso has moved with copper prices, but over the past year other factors appear to have also been important, e.g., lower global financial distress, QE3, and the carry trade (Box 1). The role of capital flows is less clear, though: Chile has seen a surge in gross inflows, mainly foreign direct investment but *net* inflows actually declined in 2012 as local pension funds reversed an increase in portfolio allocation to domestic assets in 2011. FDI and portfolio inflows and outflows remained strong in 2013Q1.

Capital Flows
(In billions of US$)

	2010	2011	2012		2013
			H1	H2	Q1
FDI 1/	-5.9	-2.6	-2.0	-7.2	-2.2
Abroad	9.5	20.4	10.7	10.4	6.6
In Chile	15.4	22.9	12.7	17.6	8.7
Portfolio 1/	6.4	-11.5	0.6	2.8	0.1
Abroad	15.7	-0.8	5.1	8.8	4.5
In Chile	9.3	10.7	4.5	5.9	4.4
Other 1/	4.5	-6.1	-1.2	-3.0	1.5
Abroad	6.4	-0.6	-1.2	0.2	0.6
In Chile	1.9	5.5	0.0	3.2	-0.9

Source: Central Bank of Chile.
1/ Negative number means net inflows.

7. **And the current account has deteriorated further.** The current account, which shifted from a surplus in 2010 to a deficit in 2011, deteriorated further in 2012 and early 2013 (it was 4 percent of GDP in 2013Q1 (12 month basis)). Resilient domestic demand has boosted imports, while exports have suffered from the weakening of still high copper prices and torpid demand in the euro area, Japan, and in key regional partners (Argentina, Brazil). The deficit is financed mostly by foreign direct investment, though within FDI, the share of debt liabilities jumped to one third in 2012 from nil in 2007–09.

8. **These developments have raised balance of payments risks.** The widening current account deficit and the increased reliance on debt financing have increased balance of payments stability risks and Chile's exposure to sudden stops. But there are mitigating considerations:

- ***REER***. The real effective exchange rate is still only about 10 percent above its 1996-2012 average (as of April 2013), despite Chile's sizeable terms of trade gains over the last decade.
- ***S-I.*** From a savings-investment perspective, there has been a decline in saving, but the major factor behind the swing in the current account is the increase in private investment, predominantly in mining and energy.
- ***Exports***. The bulk of the drop in Chile's exports in 2012 was to markets with weak demand, and exports should be helped by the projected recoveries in Chile's trading partners. Also, Chile's non-mining exports have not lost their global market share.
- ***IIP***. More broadly, Chile's international investment position (level and changes) remains robust, and the external debt is sustainable under a range of adverse scenarios (Annex I).

Saving and Investment Balances
(In percent of GDP)

	2007-10 Average	2011	2012
S - I (current account balance)	1.1	-1.3	-3.5
Private sector	-0.8	-2.7	-4.1
Saving	19.1	18.5	18.6
Investment	19.8	21.1	22.6
Public sector	1.9	1.4	0.5
Saving	4.3	3.7	2.8
Investment	2.5	2.4	2.3

International Investment Position
(In percent of GDP)

	2003	2007	2012
Assets	80	95	109
FDI	19	20	36
Portfolio	28	48	47
FX reserves	21	10	16
Others	13	16	11
Liabilities	130	100	126
FDI	72	62	77
Portfolio	19	12	23
Others	39	26	26
Net assets	-50	-5	-17

Peso Valuation 1/

Methodology	CA Norm/GDP	Overvaluation
EBA/CA	-2.6%	4%
EBA/REER		2%
CGER/MB	-2.6%	4%
CGER/ERER		3%
CGER/ES		5%
2012 CA (actual)	-3.5%	
Big MAC index		0%

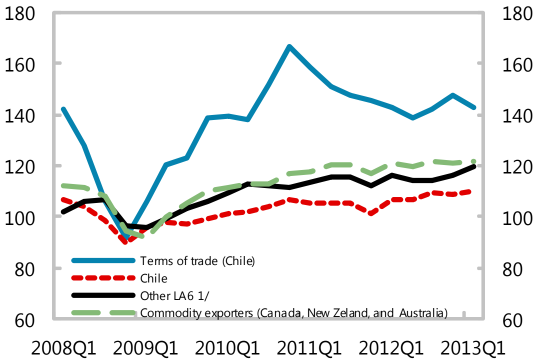
Sources: Central Bank of Chile and Fund staff estimates.
1/ External Balance Assessment (EBA) and Consultative Group on Exchange Rate Issues (CGER) are methodologies developed by the IMF to assess real exchange rate.
Exchange Rate Assessments: CGER Methodologies, IMF, 2008.

Figure 6. Chile: External Stability

Despite the recent widening of the current account deficit, there are no immediate stability or sustainability risks.

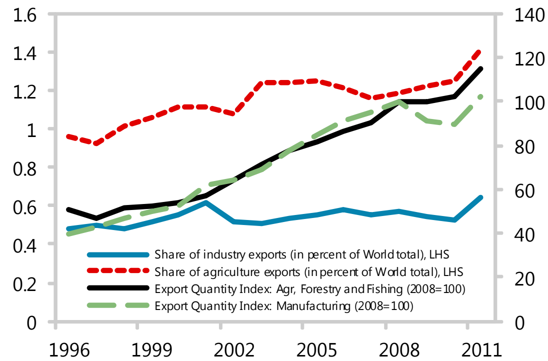
Chile's REER has appreciated in line with improved terms of trade.

Real effective exchange rate
(Index avg. 1996-2012=100)



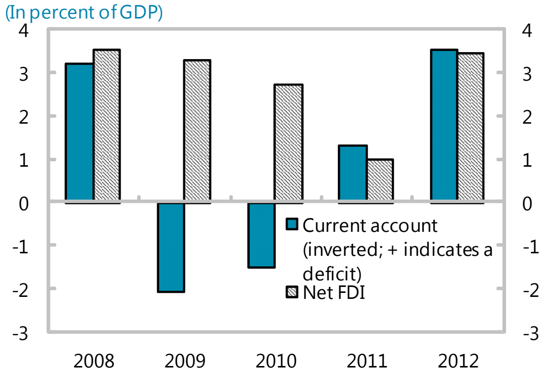
Despite the appreciation, non-mining exports have maintained their world market share.

Non-mining exports performance



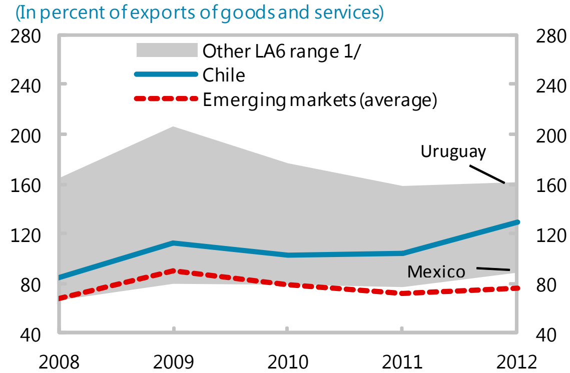
The widening current account deficit remains mostly financed by FDI.

Balance of payments and foreign direct investment
(In percent of GDP)



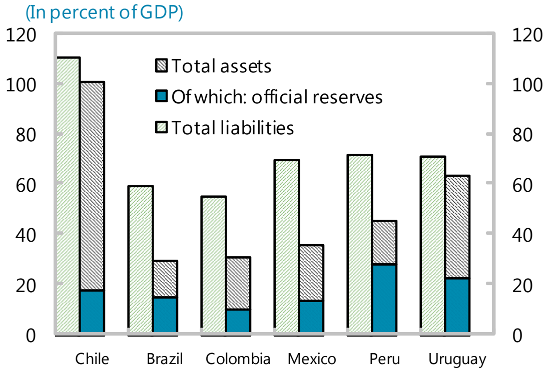
But external debt has increased.

Gross external debt
(In percent of exports of goods and services)



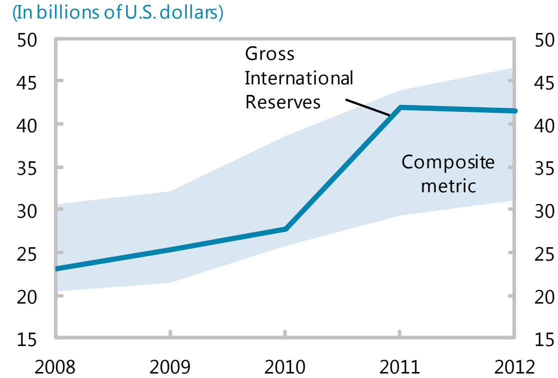
Still, Chile's international investment position remains strong...

International investment position, 2011
(In percent of GDP)



...and gross international reserves are adequate.

Gross reserves and reserve adequacy metric 2/
(In billions of U.S. dollars)



Sources: Central Bank of Chile and Fund staff calculations.
1/ Other LA6 includes Brazil, Colombia, Mexico, Peru, and Uruguay.
2/ *Assessing Reserve Adequacy*, IMF, February, 2011.

On balance, staff's view, corroborated by EBA and CGER estimates, is that the peso is on the strong side, but not clearly overvalued. The main concern is the current account deficit, though it is not large enough to present immediate stability or sustainability risks.

9. Macro-financial risks are contained. There are no clear signs of generalized asset price or credit bubbles:

- ***Banks***. While credit growth remains quite strong across all loan categories, it is on a declining trend and staff analysis does not find evidence of a "credit boom."[3] Nonperforming loans are low and fully provisioned, and indicators on bank capital adequacy, liquidity, and profitability remain healthy. That said, mid-sized banks (about one-third of system assets) are expanding rapidly, particularly in cyclical sectors like real estate, and with a relatively high reliance on wholesale funding.

Financial Soundness Indicators

(In percent)

	2010	2011	2012
Regulatory capital to risk-weighted assets	14.1	13.9	13.3
Of which, large banks 1/	13.5	13.6	12.9
mid-sized banks 1/	13.5	13.0	11.9
retail banks 1/	18.3	17.6	16.1
Reg. tier 1 capital to risk-weighted assets	10.1	10.1	10.0
Regulatory capital to total assets	10.9	10.7	10.5
Non-performing loans to total gross loans	2.7	2.3	2.2
NPLs net of provisions to capital	1.7	0.2	-0.6
Return on assets	1.7	1.6	1.4
Return on equity	20.7	20.8	17.3
Liquid assets to total assets	10.1	15.2	13.3
Foreign financing/bank total liabilities	9.0	10.3	8.7

Sources: IMF, Central Bank of Chile, and Fund staff calculations.
1/ For 2012, end-August.

Financial System Structure

	2012		
	Number of institutions	Assets (% Total)	Assets (% GDP)
Banks	24	52.4	107.7
Domestic private banks	11	25.2	51.9
Foreign banks	12	18.5	38.1
State-owned	1	8.7	17.8
Insurance companies	53	10.0	20.5
Pension fund administrators 1/	6	28.9	59.4
Other fund administrators 1/2/	52	8.7	17.8
Total	135	100.0	205.4

Sources: Superintendence of Banks and Financial Institutions, Superintendence of Pensions, and Superintendence of Securities and Insurance.
1/ Assets under management
2/ Includes mutual funds and investment funds.

- ***Nonbanks***. The major players are *insurance companies* and *pension*. The solvency of the insurance sector (mainly annuities) appears adequate, according to the Superintendence of Securities and Insurance, and the sector's investment returns improved in 2012. The privately-managed pension system does not in itself pose financial stability risks, and pension funds' investments appear diversified both as regards fixed versus variable income and domestic versus foreign.

- ***Households/corporates***. Household indebtedness has remained broadly stable in recent years at about 55 percent of disposable income, while firms have taken advantage of easy liquidity conditions to increase their indebtedness to about 90 percent of GDP. Neither level seems high from an international perspective. For firms, currency mismatches have remained limited, but profits and liquidity conditions have worsened compared with pre-crisis, especially in construction and trade sectors that have the largest share of commercial debt.

- ***Real estate***. Real estate activity (supply and demand) has been dynamic. While residential housing prices in aggregate do not suggest bubbles, these averages hide considerable variation and some regions have seen substantial price increases that could spill over to other parts of the country. One sign of incipient froth in the housing market is the jump in average loan-to-value ratios to above 85 percent since late 2011, as highlighted in recent central bank financial stability reports. Another issue is the above-mentioned worsening in construction companies' financial strength. As for construction, while residential housing activity seems to be cooling off, commercial real estate (for which data are spotty) remains hot with a substantial amount of office space being completed in 2013-14.

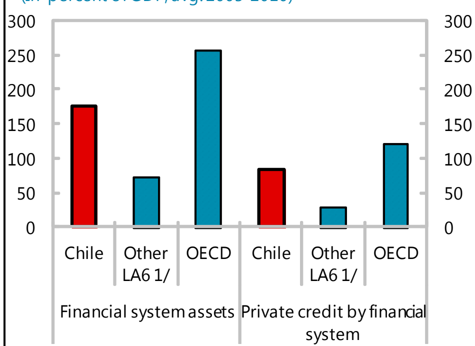
[3] See Selected Issues Paper *Systemic Risk Assessment and Mitigation in Chile*, by N. Arregui.

Figure 7. Chile: Macro-Financial Stability

Chile's large financial system is generally robust but some aspects warrant continued vigilance.

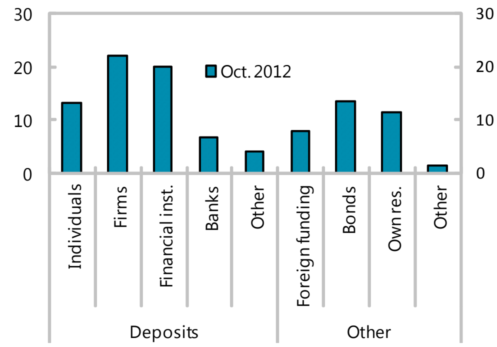
Chile has a relatively large financial system.

Financial sector size
(In percent of GDP; avg. 2005-2010)



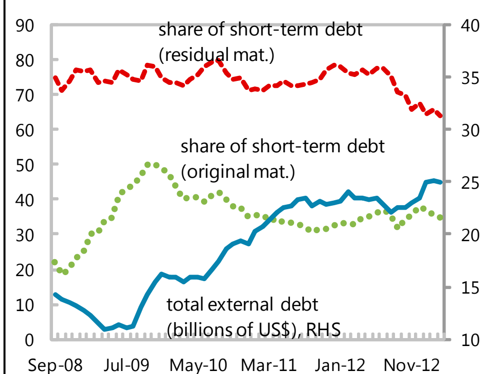
Bank funding is dominated by deposits, one third of which comes from institutional investors.

Sources of bank financing
(In percent of total liabilities)



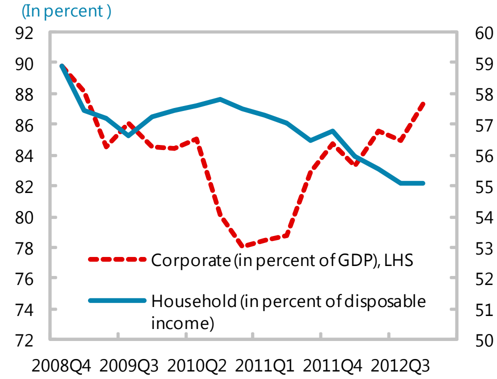
Among banks, external debt has increased somewhat, but the share of short-term debt has remained broadly stable

Bank external debt



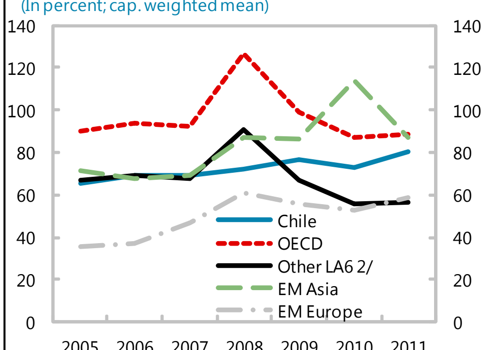
Corporate indebtedness has increased, while household indebtedness has moderated somewhat.

Corporate (non-financial) and household indebtedness
(In percent)



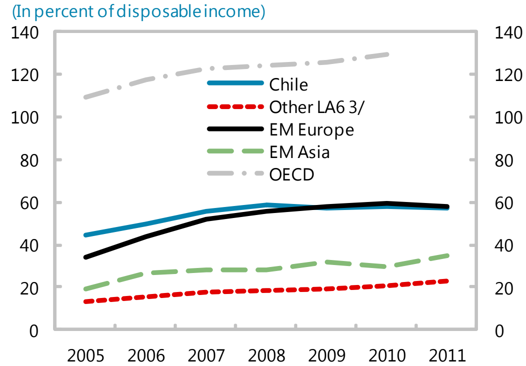
Corporate debt remains broadly in line with other regions...

Corporate debt to equity ratio
(In percent; cap. weighted mean)



....household debt, while higher than in some other emerging markets, remains well below the OECD average.

Household debt
(In percent of disposable income)



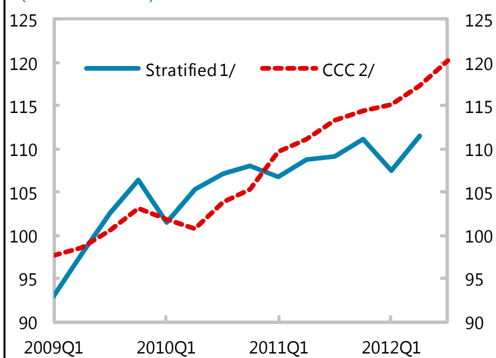
Sources: Central Bank of Chile, Superintendence of Banks and Financial Institutions, World Development Indicators (World Bank), Financial Stability Indicators (IMF), and Fund staff calculations.
1/ Other LA6 includes Brazil, Colombia, Mexico, Peru, and Uruguay.
2/ Other LA6 includes Brazil, Colombia, Mexico, and Peru.
3/ Other LA6 includes Brazil, Colombia, and Mexico.

Figure 8. Chile: Real Estate Developments

There are no clear signs of significant misalignment with fundamentals.

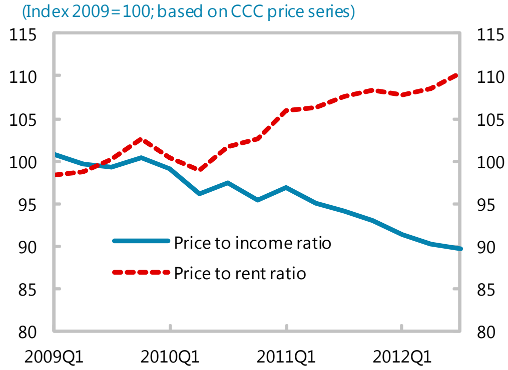
The increase in housing prices has been strong...

Real residential price index
(Index 2009=100)



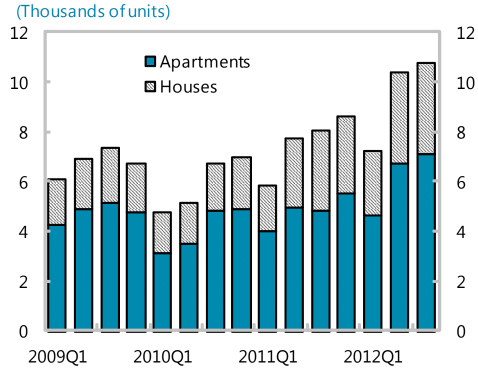
...but standard indicators do not suggest significant misalignment with fundamentals.

Price to income and price to rent ratios
(Index 2009=100; based on CCC price series)



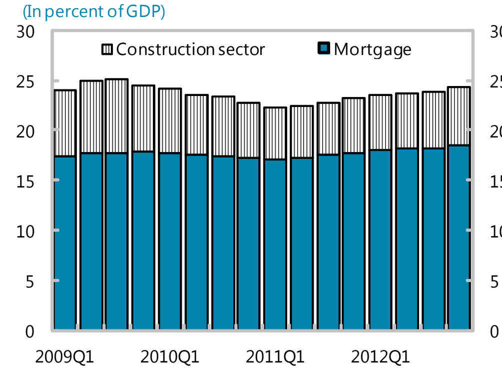
Residential property sales have increased...

Residential property sales in Greater Santiago 3/
(Thousands of units)



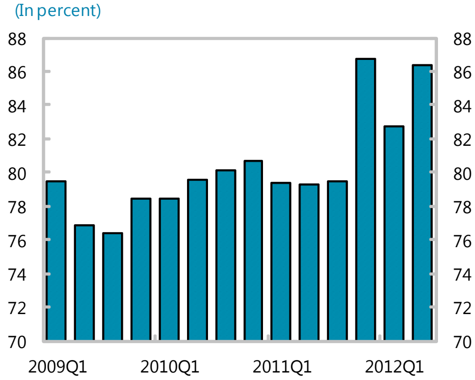
...in part fueled by credit availability.

Banking credit to the real estate sector
(In percent of GDP)



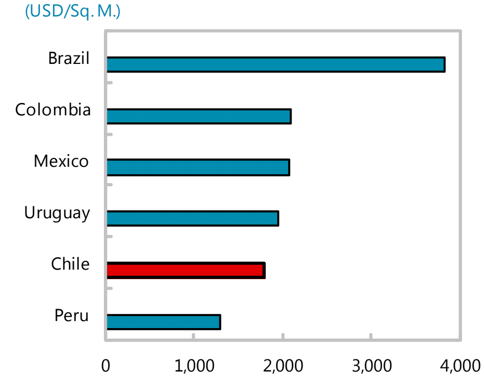
Loan to value ratio has also risen since late 2011.

Mortgage loan to value ratio
(In percent)



Chile's apartment prices are low relative to LA6 countries.

LA6 apartment prices 4/
(USD/Sq. M.)



Sources: Central Bank of Chile, Superintendence of Banks and Financial Institutions, Chilean Chamber of Construction, Global Property Guide, and Fund staff calculations.
1/ Compiled by the Central Bank of Chile controlling for home characteristics.
2/ Compiled by the Chilean Chamber of Construction using the hedonic price methodology.
3/ Includes purchase commitments.
4/ Apartments located in the center of the most important city of each country.

OUTLOOK AND RISKS

10. Barring unpleasant surprises, the baseline outlook is for a deceleration in domestic demand and activity in 2013. Staff projects growth at 4.6 percent in 2013 and thereafter, broadly in line with potential growth. Private investment will cool after three years of high growth, in part as post-earthquake reconstruction winds down, while private consumption will lose pace in line with recent employment and consumer credit developments. The fall in copper prices will also impart a dampening effect although overall exports are poised to benefit from a gradual recovery in partner countries. Staff sees fiscal policy injecting some stimulus in 2013. The current account deficit would rise further in 2013 (to 4½ percent of GDP) and decline thereafter. Inflation will move toward 3 percent by 2014, in line with market expectations.

11. But the outlook is surrounded by considerable uncertainty and risk relating to the twists and turns of the global economy and the strength of the cyclical changes in Chile:[4]

- ***Copper prices.*** The policy frameworks and the floating currency have reduced Chile's vulnerability to copper prices. Still, a large and lasting copper price fall, e.g., triggered by a fall in investment in China (which consumes 40 percent of world copper) would have major effects on the current account and foreign direct investment, public finances (14 percent of central government revenue comes directly from copper in 2012), and medium-term growth prospects. Staff analysis suggests that a 10 percent decline in copper prices reduces GDP by 0.8 percent over 8 quarters.[5]

Risk Assessment Matrix

	Time	Risk	Impact
A large and lasting decline in copper prices (e.g., prompted by a sharp investment slowdown in China).	ST/MT	M	H
Stalled or incomplete delivery of euro area policy commitments triggers re-emergence of financial stress.	ST	M	M
A reversal in capital flows to emerging markets.	ST/MT	M	L/M
Strong domestic demand causes overheating.	ST	L	L/M

- ***European financial stress***. Spillovers via Spanish bank subsidiaries, which have a large presence in Chile, have thus far not been important and the banking system's direct funding exposure to European banks is small. That said, intensified euro area distress could have a major effect on confidence and funding for banks and corporations.[6] A slump in Europe would also hurt Chile's exports (about 15 percent of Chile's exports go to the euro area).

[4] These risks are events that could materially alter the baseline path (the most likely scenario in staff's view). The likelihood of risks listed in the table is the staff's subjective assessment of the risks surrounding the baseline.

[5] See 2012 Selected Issues Paper *External Factors and Output Fluctuations in Chile: A VAR Approach*, by S. Sosa.

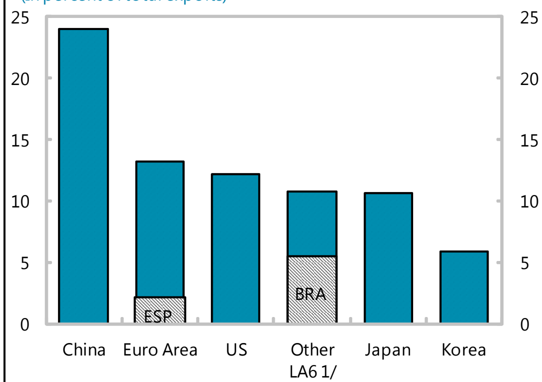
[6] See *Financial Spillovers to Chile*, by J. Podpiera, IMF working paper 12/254.

Figure 9. Chile: Spillovers and Exposures

Chile remains exposed to global conditions both through financial and real channels.

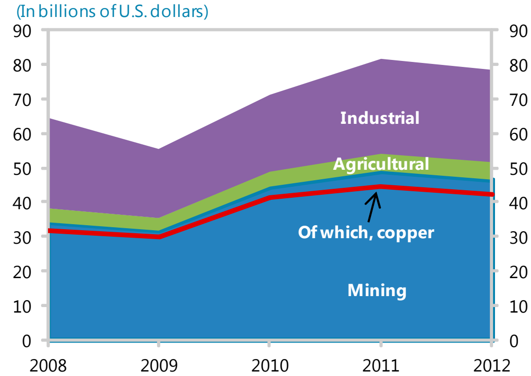
Chile's largest export destinations are China and the Euro Area.

Main export destinations, 2012
(In percent of total exports)



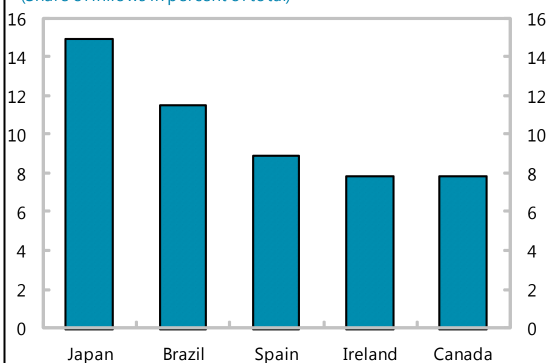
Copper represents more than half of total exports.

Exports by sector
(In billions of U.S. dollars)



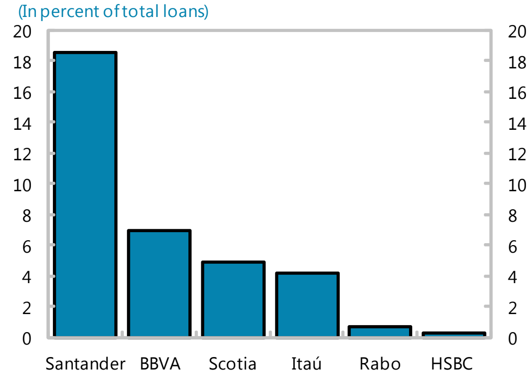
Sources of FDI are more diversified.

FDI by origin, 2009-2011
(Share of inflows in percent of total)



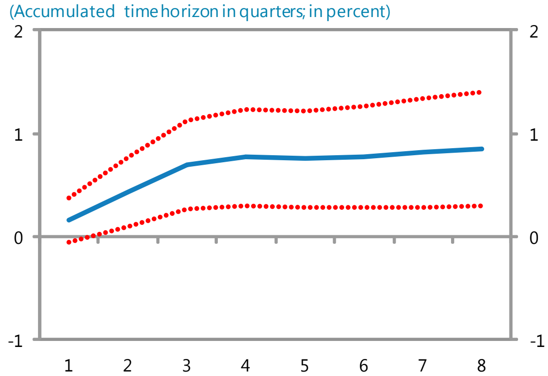
Foreign banks, mostly Spanish, have a large presence in Chile.

Market share of foreign banks, 2012
(In percent of total loans)



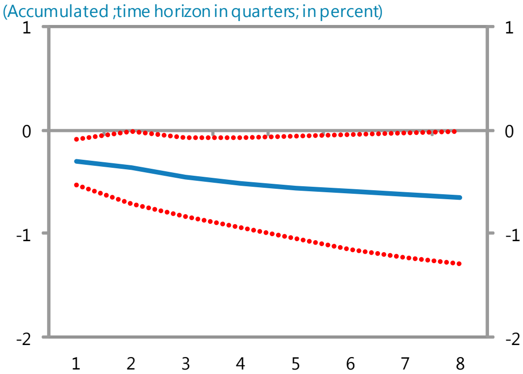
Chile remains exposed to global shifts in copper prices...

GDP response to a rise in copper prices 2/
(Accumulated time horizon in quarters; in percent)



...and global financial risks.

GDP response to a rise in VIX 3/
(Accumulated ;time horizon in quarters; in percent)



Sources: Central Bank of Chile, Superintendence of Banks and Financial Institutions, and Fund staff calculations.
1/ Other LA6 includes Brazil, Colombia, Mexico, Peru, and Uruguay.
2/ Response to one standard deviation shock to copper prices (10 percentage points) ± 1.5 standard errors.
3/ Response to one standard deviation shock to the VIX (4.1 units) ± 1.5 standard errors.

- ***Sudden stop.*** The current account deficit and the gross external financing requirement (18 percent of GDP in 2013) expose Chile to sudden-stop risks (e.g., triggered by a disorderly exit from unconventional monetary policy in advanced economies). Short-run effects could involve sizable depreciation—though balance sheet effects would be contained by the lack of important currency mismatches in the economy—and the above-mentioned effects on funding. At the same time, foreign direct investment, which is the dominant type of capital inflow to Chile, tends to be less susceptible to abrupt reversal than short-term capital but would be affected by a fall in copper prices.

- ***Overheating.*** Although this risk has lessened recently, a sustained moderation in domestic demand is not yet assured. Demand could surprise on the upside, fueled by capital inflows, credit expansion, and real wage growth. In such a scenario, the real exchange rate would appreciate, inflation rise, and the current account deficit widen further—increasing further Chile's exposure to external shocks.

12. The authorities broadly agreed with the contours of the staff's views on the outlook and risks. However, they considered that the current slowdown in activity has materially diminished both the overheating risk and those associated with a sudden stop. The authorities noted that the floating exchange rate is a key shock absorber and would help mitigate the effect of external shocks, e.g., further declines in copper prices, on the current account deficit.

POLICY DISCUSSIONS

A. Supporting the Soft Landing

13. To support the ongoing moderation in activity, staff suggested that the authorities stay the course with broadly neutral fiscal and monetary policy. This strategy, which implies no major shift in policy stance from last year, stands the best chance of supporting a deceleration in economic activity toward trend without triggering additional capital inflows, undue currency appreciation, and further widening in the current account deficit.

14. For fiscal policy, this would mean a tighter stance than implied by the 2013 budget. The 2013 budget, if executed in full, would increase spending by about 8 percent in real terms and inject a fiscal impulse (measured by the non-mining structural primary balance in percent of non-mining GDP) equal to about ½ percent. Given that the economy is moderating toward trend, staff sees no justification for an expansionary fiscal stance this year. Rather, the staff recommended that the government seek to ensure a broadly neutral stance by keeping spending below the budget ceiling as in the last two years (while protecting infrastructure and social spending). This would bring the structural balance closer to zero. The authorities took note of the staff's view and reiterated their commitment to a structural deficit equal to 1 percent of GDP in 2013, but noted that, as in the past, they would save any revenue overperformance.

15. Monetary policy considerations are finely balanced. Staff and the central bank agreed that a broadly neutral stance is appropriate and that this might call for a rate cut if inflation and inflation expectations remain low, domestic demand weakens faster than expected, or the external outlook deteriorates. In this context, the authorities and many analysts also noted that Chile's policy rate (at 5 percent) is high among emerging markets. At the same time, staff noted that if domestic demand does not cool as envisaged, a policy rate increase might be needed, despite the likely effect on peso appreciation.

B. Coping with External Spillovers

16. Chile is in a strong position to deal with external shocks even though buffers are smaller than before Lehman. Chile's stellar macro-financial performance in response to the double-shock of the global financial crisis and the earthquake attests to the economy's resilience—supported by vigorous fiscal and monetary policy responses, though the recovery was also helped by the rebound in copper prices.

Selected Indicators: Pre-Lehman and Latest

	Pre-Lehman	Latest
Cyclical position		
Headline inflation (in percent)	9.2	1.0
Real credit growth (in percent)	11.0	9.7
CA (12m sum in percent of GDP)	-1.5	-4.0
Monetary policy space		
Policy rate (in percent)	8.3	5.0
Inflation expectations (24m; in percent)	3.9	3.0
Fiscal policy space		
Overall balance (12m sum in percent of GDP)	5.8	0.2
Net assets (end of year; percent of GDP)	19.3	6.7
Reserves and external debt		
Gross reserves (in percent of M3)	16	15
External debt (in percent of exports)	83	131
Corporate debt (in percent of GDP)	84	87

Sources: Haver Analytics and Fund staff calculations.

17. It was agreed that there is ample room for a robust policy response, if needed.

- ***Exchange rate.*** The floating exchange rate (and Chile's demonstrated lack of fear of floating) is a key shock absorber, including in a tail risk scenario with a sharp and lasting drop in copper prices or a sudden stop. Foreign exchange reserves could be used to avoid excessive currency depreciation, if needed.
- ***Monetary policy.*** The low inflation and well-anchored inflation expectations would allow a forceful monetary policy action, as in 2009.
- ***Fiscal policy.*** The rude health of public finances—gross public debt (including debt of the central bank and non-financial public enterprises) at 34 percent of GDP and a net asset position for the central government, even if less than half the size than pre-Lehman in percent of GDP, at an enviable 7 percent of GDP—provides room for the operation of automatic stabilizers and (as a last resort) for fiscal stimulus if output falls (Box 2).
- ***Liquidity operations.*** Finally, as post-Lehman crisis and in late 2011, the authorities should be prepared to deploy measures to contain liquidity pressures, including expanding repo operations, broadening the range of eligible collateral, and introducing dollar swap auctions.

C. Medium-Term Fiscal Policy

18. Staff encouraged the authorities to consider a modest structural surplus over the next couple of years to ensure sizable fiscal buffers. A modest surplus would stabilize government net assets as a share of GDP on current copper price and growth projections. Achieving and maintaining a small surplus will be challenging, though, since unlike in the past, the spending room under the fiscal rule is unlikely to benefit from increases in structural copper price and revenue—and the authorities may even have to confront a decline in structural copper revenue for the first time in the life of the fiscal rule. It will be important that permanent spending commitments are matched with permanent revenue increases. The authorities broadly agreed with staff's considerations but noted that it would be for the next administration to define the structural balance target for its term. The staff also welcomed the authorities' work to incorporate long-run expenditure and revenue projections into the budget framework

19. The staff welcomed the creation of a Fiscal Council in April 2013. The Fiscal Council, created in April this year, will advise the Minister on the implementation and operations of the fiscal rule, and on any methodological changes to it. The Council, whose views will be made public but not binding, will help enhance the rigor and transparency of the rule.

D. Reinforcing Financial Stability

20. Chile's financial system is generally robust but it also presents challenges. As discussed, banks and nonbank financial institutions are well-capitalized and liquid. In the central bank's stress-tests, the banking system is solvent even under extreme scenarios.[7] Importantly, financial sector developments and risks are subject to close monitoring and proactive supervision by the central bank and the three supervisory agencies (Superintendence of Banks and Financial Institutions (SBIF), Superintendence of Pensions (SP), and Superintendence of Securities and Insurance (SVS)) and the proactive Financial Stability Council (created in 2011). Nonetheless, given its size (assets equal to 200 percent of GDP), its exposures to global and euro area tail risks, and the important presence of financial conglomerates, the financial system merits continued robust monitoring.

21. Staff welcomed the authorities' ambitious policy agenda to strengthen regulation and oversight further. Many of the reforms follow advice of the 2011 FSAP (Annex II).

- ***Progress:*** Key recent achievements include the strengthening of the SBIF (18 percent more staff) with a growing focus on nonbank institutions; efforts (including within the Financial Stability Council) to identify and quantify the systemic importance of conglomerates; and the revised credit card norm, which strengthens capital and liquidity requirements and levels prudential regulation between bank and nonbank issuers. As part of the intended adoption of a risk-based supervisory system for the insurance industry, SVS has issued for public consultation its first risk-based capital model.
- ***Reforms under way*.** The following legislation is under preparation or in Congress: the law that introduces risk-based supervision of insurance companies; legislation to expand the credit registry to include comprehensive credit history from banks and nonbanks; and a revised corporate bankruptcy law. Further, the General Banking Law is being revised, focusing on adopting Basel III capital standards (Box 3). The revisions will not address 2011 FSAP recommendations on strengthening SBIF independence and the legal framework for bank

[7] In a test that involves a sharp contraction in output and a moderation of growth in the medium term, an interest rate hike of 300 basis points in the short term and 100 basis points in the long term, and a 20-percent currency depreciation, 90 percent of banks maintain capital adequacy ratio above 8 percent.

resolution; the staff encouraged the authorities to tackle these issues as soon as feasible. Finally, the staff commended the work to improve supervision of conglomerates, and encouraged continued effort on a legal framework for consolidated oversight.

22. As for macro-prudential policies, though there are no systemic risks that warrant immediate action, some modifications could be considered. Staff welcomed the decision to strengthen the Financial Stability Council's legal underpinning by establishing it in law. This law would also enhance information sharing among the Financial Stability Council members and information collection with regard to conglomerates. Although there is no urgent need for macro-prudential policy changes, in view of the recent rise in average loan-to-value (LTV) ratios to about 85 percent (high by international standards), staff recommended that some form of LTV and debt-to-income (DTI) regulation be applied to *all* mortgages: currently the so-called non-endorsable mortgages, which have grown rapidly and now account for 85 percent of mortgages, are the only ones without LTV or DTI caps (Box 4). Other macro-prudential measures could be considered as needed. The authorities agreed that some form of LTV measures could be useful, perhaps linked to provisioning requirements.

E. Fostering Strong and Inclusive Growth over the Medium term

23. Reinforcing the prospects for strong and inclusive growth requires concerted actions on two fronts.

- ***Productivity***. Over the past decade, growth and rising real incomes have benefited from high copper prices (directly and via large mining investments) and employment growth. Total factor productivity performance has lagged the region as well as Chile's past performance but this reflects in part declining productivity in the mining sector.[8] With the global copper boom winding down, investment already at high levels, and the scope for employment growth curbed by low unemployment and slowing growth in working-age population (to 0.9 percent a year by 2020, from 1.7 percent in 2010), growth will depend on a sustained reinvigoration of productivity growth, including in mining. It is unclear what explains the jump in productivity in 2012 but it would be premature to assume it heralds a major shift in the economy's performance.

Alternative Scenarios for Medium-Term Growth
(Average annual percentange change)

	2013-2018
Baseline	4.6
Continuation of recent trend /1	3.3
Sustained TFP spurt /2	5.7

Sources: Central Bank of Chile and Fund staff estimates.
1/ Capital and TFP growth at their 2001-2012 average.
2/ TFP growth at its 2012 level.

- ***Inclusiveness***. There is also scope to make growth more inclusive. Chile has the most skewed income distribution among OECD countries and its Gini index has declined only modestly to 0.52 in 2011 from 0.56 in 2003.

[8] See *Is the Growth Momentum in Latin America Sustainable?*, by S. Sosa, E. Tsounta and H. Kim, in "Regional Economic Outlook—Western Hemisphere Department," May 2013, for an analysis of productivity in the region.

24. The staff commended the authorities on recent efforts and it was agreed that important challenges remain. By most metrics, Chile has the best investment climate in the region. Recent initiatives to reduce international trade costs and shorten the time it takes to start a business (to one day) should improve the climate further. The staff also welcomed the efforts to update Chile's bankruptcy procedures. Key areas where further action is needed include:

- ***Energy*.** Strengthening Chile's energy generation and infrastructure is crucial for medium-term growth prospects. The authorities' plan to connect the two main electricity grids is an important step but more action is needed to tackle costs and foster investment in the sector.
- ***Education; social policies*.** More equal access to high-quality education and training would help improve productivity and income inequality, while well-targeted transfer programs would improve social mobility and skill-formation among low-income groups. The efforts to establish an education quality assurance system, improve access to education through scholarships and reduced costs of state-guaranteed loans, and strengthen Conditional Cash Transfer programs are welcome.
- ***Labor market*.** Recent measures, including subsidies to low-income women and an extended maternity leave scheme, can help encourage higher female labor participation which in turn would help with growth and income equality. In line with OECD recommendations, a reconsideration of the relatively high severance payments and the rigid working hours, and strengthened training programs could help ensure efficient labor allocation.

25. The authorities broadly concurred with the staff's views. They agreed that achieving a sustained increase in productivity is important and they were encouraged by the rebound in productivity in 2012 that they considered mostly a trend increase. They also noted the difficulty in reaching political consensus on labor market reforms and large hydroelectric power projects.

F. Other Issues

26. Chile has a long record of high-quality statistics and data are adequate for surveillance. Recent months have seen controversy surrounding the 2012 population census and certain sub-components of the consumer price index. The staff urged prompt, transparent, and credible resolution to these controversies. They welcomed the authorities' announcement of a speedy audit of the population census with the involvement of an expert committee, as well as the plans to address methodological issues in the consumer price index in a timely manner. Furthermore, the staff supported the idea of strengthening the National Institute of Statistics' independence, as is being proposed.

STAFF APPRAISAL

27. Growth in recent years has been strong, led by domestic demand, but a slow down appears underway. Growth surprised on the upside in 2012 and on the downside in the first quarter of 2013. These ups and downs appear to be part of a bumpy transition toward a more sustainable rate of expansion in economic activity. The moderation in activity is also reflecting a shifting outlook for copper prices.

28. The main cloud over the strong performance is the rapid shift in the current account. The ballooning current account deficit and the increased reliance on debt financing have raised balance of payment risks. Still, staff's assessment is that the peso is on the strong side but not clearly overvalued.

29. Macroeconomic policies have been prudent. In recent years, fiscal policy has provided a welcome dampening effect on demand, thereby helping prevent overheating and a more substantial real appreciation and current account deterioration. Monetary policy has been on hold since early 2012 and is broadly neutral.

30. And macro-financial risks appear contained thanks in large part to the authorities' active supervision and monitoring. There are no clear signs of broad asset price or credit bubbles. Liquidity and solvency indicators and stress tests suggest that the financial sector is generally healthy and robust. That said, some mid-sized banks are expanding fast, with relatively high reliance on wholesale funding. As for real estate, aggregate price developments do not suggest bubbles but continued close monitoring will be important, including of commercial real estate construction which remains very dynamic.

31. The near-term priority is to support the ongoing moderation in domestic demand and activity, amid swelling capital inflows and a widening current account deficit. In this context, a neutral fiscal stance would be desirable and can be achieved through a tight grip on spending in the remainder of the year, and saving any revenue over performance. This would bring the structural balance closer to zero.

32. There is a great deal of uncertainty and risks surrounding the outlook stemming both from real and financial channels. The main downside risks to the outlook are a sharp and lasting drop in copper prices, re-emergence of financial stress in the euro area, or a sudden stop in capital inflows. At the same time, there is also a chance that domestic demand does not abate as envisaged, raising overheating risks.

33. Monetary policy should be ready to respond to changes in the economic outlook and fiscal automatics stabilizers should be allowed to operate unimpeded. As a last resort, there is ample space for fiscal stimulus if output falls. The floating currency provides a natural buffer against external shocks and the ample reserves could be used to avoid excessive depreciation.

34. Further strengthening of the medium-term fiscal framework is appropriate. Staff recommends aiming for a small structural surplus over the next few years, as this would help maintain strong fiscal buffers while stabilizing net assets as a share of GDP. The establishment of the Fiscal Council is welcome as it further strengthens the transparency of the fiscal framework. Staff also commends plans to incorporate long-run expenditure and revenue projections into the budget framework.

35. The staff applauds the authorities' proactive work on financial stability issues. Recent progress in strengthening supervision of nonbanks and financial conglomerates is welcome. Current legislative initiatives, notably the General Banking Law, the law on the Financial Stability Council, the law on risk-based supervision of insurance companies, the legislation to expand the credit registry, and the corporate bankruptcy law, will strengthen prudential oversight. Looking ahead, the broad-based banking regulation reform scheduled for this year will be an important improvement. However, addressing pending FSAP recommendations, including a legal framework for consolidated oversight of financial conglomerates, should remain a priority. And while there are no systemic risks that warrant immediate action, the authorities should consider extending some form of loan-to-value and debt-to-income regulation to all mortgages.

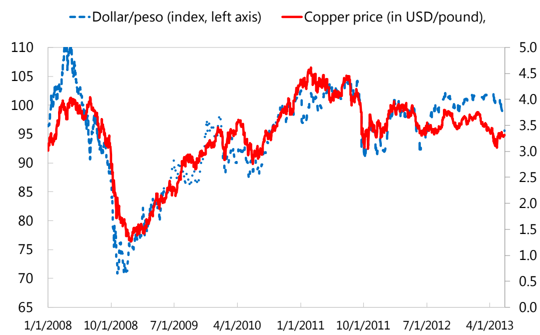
36. The medium-term challenge is to foster sustained and inclusive growth. Boosting productivity and labor force participation will be needed to sustain growth without the benefit of the tailwind of rising copper prices and with slowing growth of working-age population. To this end, key areas for further reform include: make access to high-quality education and training more equal, and consider well-targeted social transfers to spread growth benefits; promote investments in the energy sector to ensure sufficient and competitive energy supply; and make the labor market more flexible.

37. A prompt and transparent resolution of the recent statistical controversies would protect Chile's long tradition of high quality data. Staff welcomes authorities' outreach efforts among local analysts and data users, and their plans to obtain advice from international experts.

38. Staff recommends that the next Article IV consultation take place on the standard 12-month cycle.

Box 1. What Explains the Peso Movements?[1/]

The Chilean peso usually moves in tandem with copper prices, but there have been episodes when it deviates, e.g., in the period July 2012-May 2012 when the peso appeared stronger than what could be explained by copper prices (in recent weeks the gap has narrowed). This episode prompted focus on the role of other factors, including carry trade and unconventional monetary policy in advanced economies. While it is notoriously difficult to explain short-term exchange rate movements, this box looks at factors that influence the nominal dollar/peso rate using a simple error-correction model based on weekly data from October 1999 to May 2013.



The following explanatory variables are used: copper price, relative U.S./Chile CPI, the spread between the yields on 90-day Chilean and U.S. government bills, and VIX (the implied volatility of S&P 500 index options)−a common measure of global financial distress. The regression also includes dummy variables to capture the last two foreign exchange interventions by the Central Bank of Chile (April-December 2008 and January-December 2011) and the balance sheet of the Federal Reserve to capture the effect of quantitative easing (QE).

The model fits the in-sample dollar/peso exchange rate movements well. A 10 percent increase in copper prices would strengthen the peso by about 1.7 percent against the dollar over the long run. Higher Chile-U.S. interest spread would strengthen the peso. Higher global financial distress, in contrast, would lead to a stronger dollar. The Central Bank's interventions in 2008 and 2011 did seem to help weaken the peso, although only by about 3½ and 2½ percent, respectively. The result also suggests that QE3 could lead to an appreciation of the peso against the dollar by about 2 percent.

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[1] See Selected Issues Paper *What Explains Movements in the Peso/Dollar Exchange Rate?*, by Y. Wu.

Box 2. The Strength of Government Finances

The Chilean central government is a net creditor. The net asset position at end-2012 equaled about 7 percent of GDP. The average net position among emerging markets is negative 24½ percent of GDP. Chile's consolidated public sector has a net asset position of some 2 percent of GDP.

Gross assets include the two sovereign wealth funds (SWFs) as well as other instruments. The stabilization fund (ESSF) currently stands at about 5½ percent of GDP and represents a flexible fiscal buffer that can be used to cover deficits and amortizations. The pension reserve fund (PRF) stands at about 2¼ percent and is earmarked to cover a fraction of pension related outlays starting in 2016. Further, the government currently holds about 3½ percent of GDP in other liquid foreign currency denominated assets which will be in part used in the near term to strengthen the ESSF and establish a US$4bn (1.5 percent of GDP) Education Fund.

Central government gross debt is relatively low (equal to 12 percent of GDP), and would remain comfortable under various shocks (see Annex I). Also, recent Fund research finds that Chile could withstand tail event-type of shocks—even responding with expansionary policies—without putting fiscal solvency at risk (debt would remain below 40 percent of GDP).[1/]

Contingent liabilities are relatively small. The net present value of contingent liabilities amounted to 3.7 percent of 2012 GDP (or 0.02 percent of GDP on an annual flow basis). [2/]

Central Government Financial Position

(End 2012; in percent of GDP)

Net assets	**6.7**
Gross assets	**18.6**
Peso assets	7.1
Foreign currency assets	11.5
Sovereign Wealth Funds	7.8
PRF	2.2
ESSF	5.6
Other	3.7
Gross debt	**11.9**
Peso debt	10.0
Foreign currency debt	1.9
Contingent liabilities	**3.7**
Deposit guarantee	1.3
Guarantees to public enterprises debt	1.1
Student-loans guarantee	0.7
Disputes against govt.	0.6
Minimum income guarantee to concessions	0.2
Memo items:	
Foreign currency assets w/o PRF	9.3
Public non-financial enterprises gross debt	6.7

Sources: Ministry of Finance and Fund staff estimates.

[1] See G. Adler and S. Sosa (2013), *External Conditions and Debt Sustainability in Latin America*, IMF Working Paper 13/27.
[2] Budget Directorate (2012), *Informe de Pasivos Contingentes*, Ministry of Finance.

Box 3. Chile and Basel III

The capital and liquidity requirements within the Basel III framework are due to be implemented over 2015-19. Estimations carried out by the central bank and the supervisor of banks and financial institutions, and liquidity and solvency stress tests carried out by the 2011 FSAP show that these requirements would not be particularly difficult for Chilean banks to meet. The authorities are working to adopt the main elements of Basel II and III, but no formal road map for Basel III has been announced.

Formally, Chile's *capital adequacy requirements* follow Basel I standards, with complementary central bank regulation bringing in elements of Basel II and III. There are no specific capital charges for operational risk, but some capital (based on the 1996 Market Risk Amendment of the Basel I Capital Accord) must be held in respect of market risk. Preliminary estimates by the central bank show that capital levels are above the minimum level agreed under Basel III and it therefore appears that the new capital standards would not be overly restrictive for Chilean banks.[1]

Banking System Capital Adequacy

	Dec-10	Latest	As at
Effective Capital to Credit Risk-Weighted Assets /1	14.1	13.3	Dec-12
Effective Capital to Credit and Market Risk-Weighted Assets /2	13.1	12.1	Dec-12
Basel II: credit, maket and operational risk /3	12.3	11.5	Jun-12
Basel III: includes adjustments to regulatory capital /3	11.5	10.7	Jun-12

Source: Superintendence of Banks and Financial Institutions (SBIF).

1/ Title VII article 66 General Banking Law.

2/ Effective capital to credit risk-weighted assets plus estimated risk exposure to market risks times 12.5.

3/ Estimates by the SBIF.

The legal framework already includes a *leverage ratio* (Basel III includes a leverage ratio but details are yet to be finalized). The system's leverage (as measured by Tier 1 capital to assets) has always exceeded 6 percent over the last decade.

For the *liquidity standards*, the Chilean regulatory framework establishes 30- and 90-day mismatch limits in domestic and foreign currencies. The liquidity stress tests for the liquidity coverage ratio (LCR) and net stable funding ratio (NSFR), conducted in the context of the 2011 FSAP Update show that the banking system is well positioned to meet the LCR by 2015 and the NSFR by 2019.[2]

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[1] Regarding systemic capital surcharges, a higher capital adequacy ratio (from 10 to 14 percent) is temporarily required (for no less than one year) when a merger or acquisition would result in a bank with a market share above 15 percent.

[2] In 2012, the Basel Committee on Banking Supervision agreed on a revised framework for the Liquidity Coverage Ratio with an extended phase-in period. The design of the Net Stable Funding Ratio is under discussion.

Box 4. Recent Developments in Mortgage Financing

Mortgage debt equals about 21 percent of GDP and represents 57 percent of household debt (as of 2012Q3). Banks provide some 90 percent of mortgage credit and banks' mortgage credit stands at about 24 percent of total bank credit (up from 13 percent in 1990).

Mortgage bonds were introduced in October 2012, as a new type of instrument to finance mortgages. These bonds are so called *covered bonds* –in case the bank becomes insolvent, the mortgage is earmarked to cover the bond—and they are eligible for the central bank repo window. The originating bank absorbs the credit risk of the mortgages which remain on its balance sheet. The new mortgage bond is expected to represent an attractive way to fund mortgages by eliminating some of the restrictions in mortgage bills as it would allow to finance pools of mortgages; Mortgage bonds will be also subject to loan-to-value (LTV) and debt-to-income (DTI) caps. The first issuance is expected shortly.

Bank Mortgages
(in percent of total mortgage credit)

	Non-endorsable	Endorsable	Mortgage Bill	Mortgage Bond
2000	12	24	68	...
2003	15	23	69	...
2009	78	9	15	...
2012	86	9	8	...
Memo items:				
LTV limit	None	80	75*	80
DTI limit	None	None	25**	25

Sources: Superintendence of Banks and Financial Institutions
* Up to 100 percent for highest rated customers and banks
** Only for loans under US$150,000 (UF$3,000)

Table 1. Chile: Selected Social and Economic Indicators

GDP (2012), in billions of pesos	130,466	Quota	
GDP (2012), in billions of U.S. dollars	268.2	in millions of SDRs	856
Per capita (U.S. dollars)	15,410	in % of total	0.36%
Population (2012), in millions	17.4	Poverty rate (2011)	14.4
Main products and exports	Copper	Gini coefficient (2011)	0.52
Key export markets	China, Euro area, U.S.	Literacy rate (2011)	98.9

						Proj.	
	2008	2009	2010	2011	2012	2013	2014
	(Annual percentage change, unless otherwise specified)						
Output							
Real GDP	3.1	-0.9	5.7	5.8	5.6	4.6	4.6
Total domestic demand	9.1	-5.5	13.4	9.1	7.2	6.1	5.1
Consumption	4.3	0.7	9.6	8.0	5.7	5.9	4.8
Private	5.1	-0.9	10.7	9.0	6.0	5.6	5.0
Public	0.3	9.1	4.4	3.2	3.9	6.9	3.8
Investment	21.4	-23.7	27.4	13.1	10.5	9.3	4.2
Fixed	18.3	-12.2	12.1	14.8	12.0	8.3	4.2
Private	20.1	-17.6	17.8	15.7	13.5	7.7	4.4
Public	3.5	37.5	-18.5	7.8	-0.1	14.0	3.3
Inventories 1/	...	-3.1	2.9	-0.2	-0.1	...	...
Net exports 1/	-4.5	4.4	-7.6	-3.9	-1.7	-0.9	-0.5
Exports	-0.6	-4.8	2.5	5.0	0.9	3.9	4.3
Imports	11.8	-16.2	25.8	14.6	4.8	5.5	4.9
Employment							
Unemployment rate (annual average) 2/	7.8	10.8	8.2	7.1	6.4	6.5	6.6
Consumer prices							
End of period	7.1	-1.5	3.0	4.4	1.5	2.6	3.0
Average	8.7	1.5	1.4	3.3	3.0	1.8	3.0
	(In percent of GDP, unless otherwise specified)						
Public sector finances							
Central government revenue	24.2	19.0	21.5	22.6	21.9	22.0	21.5
Central government expenditure	20.3	23.4	22.0	21.4	21.4	22.0	21.8
Central government fiscal balance	3.9	-4.4	-0.5	1.3	0.6	-0.1	-0.3
Structural fiscal balance 3/	-1.5	-4.3	-2.5	-0.9	-0.6	-0.6	-0.8
Nonmining structural primary fiscal balance 4/	-2.6	-7.1	-5.5	-3.1	-2.9	-3.3	-2.9
Fiscal impulse	1.5	4.5	-1.6	-2.3	-0.2	0.4	-0.4
Public sector net debt	-16.8	-6.5	-2.2	-4.9	-1.7	-1.7	-0.2
Public sector gross debt	24.7	27.5	25.9	34.8	34.2	34.0	33.8
Central government gross debt	4.9	5.8	8.6	11.1	11.9	12.2	12.5
Of which, share of FX-denominated debt (in percent)	40.0	22.8	17.3	17.2	16.1	13.0	11.4
Money and credit							
Broad money (% change)	18.6	-5.3	9.3	18.5	7.6	...	...
Credit to the private sector (end of period, % change)	18.7	-1.4	7.1	16.9	12.1	...	...
3-month central bank bill rate (%)	7.3	1.8	1.7	4.9	5.1	...	...
Balance of payments							
Current account	-3.2	2.0	1.5	-1.3	-3.5	-4.7	-4.2
Current account (in billions of U.S. dollars)	-5.8	3.5	3.2	-3.3	-9.5	-13.4	-12.9
Foreign direct investment inflows	8.6	7.5	7.1	9.1	11.3	9.8	9.7
Gross international reserves (in billions of U.S. dollars)	23.2	25.4	27.9	42.0	41.6	41.6	41.6
In months of next year's imports of goods and services	5.5	4.4	3.9	5.6	5.3	5.1	4.9
Gross external debt	35.5	41.8	38.9	39.3	43.9	43.3	43.0
Public	6.5	7.7	7.9	8.2	9.4	9.4	9.4
Private	29.0	34.1	30.9	31.2	34.5	33.8	33.6
	(Annual percentage change)						
Exchange rate							
Real effective exchange rate (real appreciation +)	1.8	-2.2	5.9	0.9	3.4	...	...
Terms of trade	-15.0	4.3	22.0	1.2	-5.2	-3.0	0.5

Sources: Central Bank of Chile, Ministry of Finance, Haver Analytics, and Fund staff estimates and projections.

1/ Contribution to growth.
2/ The methodology to compute the unemployment rate changed in 2009.
3/ Headline balance adjusted for the economic and copper price cycles.
4/ In percent of non-mining GDP.

Table 2. Chile: Summary Operations of the Central Government

(In percent of GDP; unless otherwise indicated)

	2008	2009	2010	2011	2012	Projections 1/ 2013	2014
Revenues	**24.2**	**19.0**	**21.5**	**22.7**	**21.9**	**22.0**	**21.5**
Taxes	17.6	13.9	15.9	17.4	17.5	17.3	17.2
Private mining companies	2.3	0.8	1.7	1.9	1.6	1.1	0.8
Other tax revenues, non-mining	15.3	13.0	14.2	15.5	15.9	16.2	16.3
Social contributions	1.4	1.4	1.3	1.3	1.4	1.4	1.4
Grants	0.1	0.1	0.1	0.1	0.1	0.1	0.0
Other revenue	5.2	3.7	4.3	3.9	3.0	3.2	2.9
Codelco revenues	3.4	1.7	2.7	2.3	1.5	1.9	1.6
Income on assets	0.8	0.7	0.4	0.5	0.5	0.7	0.7
Operating income	0.6	0.6	0.5	0.5	0.5	0.4	0.4
Other income	0.4	0.8	0.6	0.7	0.6	0.2	0.2
Expenditures	**20.3**	**23.4**	**22.0**	**21.4**	**21.4**	**22.0**	**21.8**
Expense	18.2	20.9	19.9	19.3	19.3	19.8	19.7
Compensation of employees	3.8	4.4	4.2	4.1	4.2	4.4	4.4
Purchases of goods and services	2.0	2.3	2.1	2.2	2.1	2.1	2.1
Interest payments	0.5	0.5	0.5	0.6	0.6	0.9	0.9
Subsidies and grants	6.1	7.0	6.7	6.3	6.5	6.8	6.7
Social benefits	4.4	4.8	4.5	4.2	4.0	3.9	3.9
Other expense	1.5	1.9	1.9	2.0	1.9	1.8	1.8
Capital transfers	1.5	1.9	1.8	1.9	1.9	1.8	1.7
Net acquistion of nonfinancial assets	2.1	2.5	2.1	2.1	2.0	2.2	2.2
Investment	2.1	2.6	2.1	2.1	2.1	2.2	2.2
Sale of physical assets	0.0	0.1	0.0	0.0	0.0	0.0	0.0
Gross operating balance	**6.0**	**-1.8**	**1.6**	**3.4**	**2.6**	**2.1**	**1.9**
Net lending/borrowing (overall balance)	**3.9**	**-4.4**	**-0.5**	**1.3**	**0.6**	**-0.1**	**-0.3**
Non-mining overall balance	-1.8	-6.8	-4.9	-2.9	-2.5	-3.0	-2.8
Net financial transactions	**3.9**	**-4.4**	**-0.5**	**1.3**	**0.6**	**-0.1**	**-0.3**
Net acquisition of financial assets	3.7	-4.0	2.0	3.1	1.6	0.8	0.9
Currency and deposits	0.9	0.0	-0.2	-0.2	0.3	-0.2	0.0
Securities other than shares	2.4	-4.1	2.2	3.4	1.3	1.1	0.9
Loans	0.3	0.1	0.0	-0.1	0.0	0.0	0.0
Net incurrence of liabilities	-0.2	0.3	2.5	1.8	1.0	0.9	1.2
Domestic	0.7	1.5	2.5	2.0	1.4	1.8	2.0
Securities other than shares	1.0	1.7	2.8	2.4	1.9	1.8	2.3
Amortization	0.6	0.3	0.3	0.4	0.5	0.0	0.3
External	-0.2	-0.4	0.7	0.5	0.3	-0.3	0.0
Securities other than shares	0.0	0.0	0.7	0.5	0.6	0.0	0.0
Amortization	0.5	0.4	0.1	0.1	0.3	0.3	0.0
Recognizion bonds	-0.7	-0.8	-0.7	-0.7	-0.6	-0.6	-0.7
Memorandum items							
Structural balance 2/	-1.5	-4.3	-2.5	-0.9	-0.6	-0.6	-0.8
Nonmining structural primary balance 3/	-2.6	-7.1	-5.5	-3.1	-2.9	-3.3	-2.9
Fiscal impulse	1.5	4.5	-1.6	-2.3	-0.2	0.4	-0.4
Expenditure growth (in real terms)	8.2	16.9	7.4	2.6	5.1	7.6	3.7
Expense	10.0	16.0	8.3	2.6	5.2	6.9	3.8
Net acquisition of nonfinancial assets	3.6	21.1	-6.6	7.5	-0.3	14.0	3.3
Net assets of the central government	19.3	10.6	7.0	8.6	6.7	6.6	5.8
Gross debt	4.9	5.8	8.6	11.1	11.9	12.2	12.5
Peso-denominated assets	5.7	6.1	6.2	7.7	7.1	7.5	7.7
Foreign currency-denominated assets	18.5	10.3	9.4	12.0	11.5	11.2	10.6
Nominal GDP (trillions of pesos)	93.8	96.3	110.9	121.4	130.5	138.6	149.4
Long term price of copper, USD per pound	1.37	1.99	2.13	2.59	3.02	3.06	3.06
Copper price, USD per pound (WEO)	3.16	2.34	3.42	4.00	3.61	3.38	3.35

Sources: Ministry of Finance and Fund staff estimates.

1/ Based on the authorities' medium-term fiscal projections in the 2012 Budget Law, adjusted for staff's GDP and copper price projections.

2/ Based on staff's output gap estimates and WEO copper prices.

3/ In percent of non-mining GDP.

Table 3. Chile: Summary Operations of the Public Sector 1/
(In percent of GDP)

						Projections	
	2008	2009	2010	2011	2012	2013	2014
Central Government							
Balance	3.9	-4.2	-0.5	1.3	0.6	-0.1	-0.3
Total revenue	24.2	19.1	21.6	22.6	22.0	22.0	21.6
Of which: Intragovernmental receipts	1.2	1.3	0.9	0.9	0.9	0.9	0.9
Total expenditures	20.4	23.3	22.0	21.3	21.4	22.1	21.9
Of which: Intragovernmental transfers	1.0	0.9	0.8	0.8	0.8	0.8	0.8
Current	16.7	18.8	18.1	17.2	17.4	18.0	17.9
Capital	3.6	4.4	3.9	4.1	4.0	4.0	4.0
Net assets	19.3	10.6	7.0	8.6	6.7	6.6	5.8
Municipalities 2/							
Balance	0.0	0.1	0.1	0.1	0.1	0.0	0.0
Total revenue	2.8	3.0	2.9	2.9	2.8	2.9	2.9
Of which: Intragovernmental receipts	1.0	0.9	0.8	0.8	0.8	0.8	0.8
Total expenditures	2.8	2.9	2.8	2.7	2.8	2.9	2.9
Of which: Intragovernmental transfers	1.2	1.3	0.9	0.9	0.9	0.9	0.9
Current	2.5	2.6	2.5	2.5	2.5	2.6	2.6
Capital	0.3	0.3	0.3	0.2	0.2	0.3	0.2
Central Bank							
Balance 3/	2.9	-2.9	-1.3	0.9	-1.6	-0.5	-0.5
Net assets	3.3	1.5	0.7	2.0	1.1	1.2	0.6
State-Owned Non-Financial Enterprises							
Balance	0.9	1.6	1.3	1.1	1.0	0.8	0.8
Total revenue	20.6	12.5	10.9	10.6	10.4	10.1	10.1
Of which: Intragovernmental receipts	0.4	0.7	0.2	0.2	0.2	0.2	0.2
Total expenditures	19.7	10.9	9.6	9.5	9.5	9.3	9.3
Current	17.4	9.1	8.2	8.1	8.1	8.0	8.0
Capital 4/	2.3	1.8	1.4	1.3	1.3	1.3	1.3
Net Assets	-5.9	-5.7	-5.5	-5.6	-6.1	-6.1	-6.1
Consolidated Public Sector							
Balance	7.7	-5.3	-0.5	3.4	-0.1	0.2	0.0
Net assets	16.7	6.4	2.2	4.9	1.7	1.7	0.2

Sources: Ministry of Finance and Fund staff estimates.

1/ This table reflects the authorities' revisions to historical official data to bring the fiscal accounts in line with GFSM 2001.
2/ On a cash basis. Municipalities hold neither sizable financial assets nor debt.
3/ Includes the effects of valuation changes (exchange rate).
4/ The data reported here does not include depreciation as an expense.

Table 4. Chile: Balance of Payments

	2008	2009	2010	2011	2012	Projections 2013	2014
	(In millions of U.S. dollars)						
Current account	-5,800	3,517	3,224	-3,284	-9,497	-13,445	-12,853
Trade balance	6,074	15,361	15,635	10,544	3,421	-91	-53
Exports	64,510	55,463	71,109	81,455	78,277	78,053	81,212
Copper	31,755	29,695	41,361	44,666	42,184	41,183	42,677
Non-copper	32,756	25,768	29,748	36,790	36,093	36,870	38,534
Imports	58,436	40,102	55,474	70,911	74,856	78,144	81,264
Net services	-1,208	-2,011	-2,136	-2,577	-2,435	-3,101	-2,503
Net income	-13,596	-11,396	-14,686	-14,142	-12,675	-12,318	-12,485
Net transfers	2,930	1,563	4,411	2,891	2,192	2,065	2,187
Capital account balance 1/	4	14	6,240	13	13	0	0
Financial account balance	-10,969	2,532	5,944	-17,810	-9,948	-13,445	-12,853
Foreign direct investment	-6,367	-5,654	-5,912	-2,557	-9,233	-11,025	-11,408
Abroad by Chilean residents	9,151	7,233	9,461	20,373	21,090	16,872	17,884
In Chile by foreign residents	15,518	12,887	15,373	22,931	30,323	27,897	29,292
Of which, debt instruments	1,146	463	2,848	2,863	10,078	...	...
Portfolio investment	7,620	12,399	6,421	-11,533	3,409	3,155	3,700
Abroad by Chilean residents	10,253	14,269	15,710	-805	13,891	...	...
In Chile by foreign residents	2,633	1,870	9,289	10,728	10,482	...	...
Of which, equities	1,948	328	1,764	4,529	5,222	...	...
Of which, debt	685	1,542	7,525	6,200	5,260	...	...
Financial derivatives	1,041	1,049	934	2,418	-10	...	...
Other investments	-13,263	-5,261	4,502	-6,138	-4,114	...	...
Abroad by Chilean residents	-5,346	612	6,385	-647	-922	...	...
In Chile by foreign residents	7,917	5,873	1,883	5,491	3,192	...	...
Change in reserves assets (increase -)	6,444	1,648	3,024	14,190	-367	0	0
Errors and omissions	1,272	646	-497	-352	-831	0	0
Change in official reserves ($ billion)	6.3	2.2	2.5	14.1	-0.3	0	0
Central bank operations with commercial banks	6.3	0.0	0.0	12.0	0.0	0	0
Other 2/	0.0	2.2	2.5	2.1	-0.3	0	0
Gross official international reserves	5.5	4.4	3.9	5.6	5.3	5.1	4.9
(In months of imports of goods and services)							
	(In percent of GDP)						
Current account	-3.2	2.0	1.5	-1.3	-3.5	-4.7	-4.2
Trade balance	3.4	8.9	7.2	4.2	1.3	0.0	0.0
Exports	35.9	32.2	32.7	32.5	29.2	27.3	26.9
Copper	17.7	17.3	19.0	17.8	15.7	14.4	14.1
Non-copper	18.2	15.0	13.7	14.7	13.5	12.9	12.7
Imports	32.6	23.3	25.5	28.3	27.9	27.4	26.9
Net services	-0.7	-1.2	-1.0	-1.0	-0.9	-1.1	-0.8
Net income	-7.6	-6.6	-6.8	-5.6	-4.7	-4.3	-4.1
Net transfers	1.6	0.9	2.0	1.2	0.8	0.7	0.7
Financial account balance	6.1	-1.5	-2.7	7.1	3.7	4.7	4.2
	(Annual change in percent)						
Total export volume	-2.2	-2.9	-0.2	4.1	1.9	3.7	4.3
Copper export volume	-4.5	1.3	0.4	-2.0	2.5	4.4	4.5
Agricultural exports volume	10.6	-0.2	2.5	12.5	-0.3	-1.1	4.7
Industrial exports volume	4.8	-8.6	-2.1	13.8	0.7	3.8	4.1
Total import volume	17.2	-19.4	31.4	16.4	5.8	5.2	4.9
Terms of trade	-15.0	4.3	22.0	1.2	-5.2	-3.0	0.5
Total export prices	-4.2	-11.4	28.6	10.2	-5.2	-3.7	-0.3
Copper export prices	-15.1	-9.1	40.4	11.0	-8.2	-6.3	-1.0
Total import price	12.6	-15.4	5.7	9.0	0.0	-0.7	-0.8
Memorandum items:							
Copper price (LME; U.S. cents per pound)	316	234	342	400	361	338	335
Volume of copper exports (2004=100)	98	99	99	97	100	104	109

Sources: Central Bank of Chile, Haver Analytics, and Fund staff estimates.

1/ In 2010 reflects insurance payment associated with the earthquake.

2/ "Other" variations in reserves largely reflect changes in deposits by commercial banks and the government with the central bank.

Table 5. Chile: Monetary Survey
(In billions of pesos; unless otherwise indicated)

	2007	2008	2009	2010	2011	2012
Central bank						
Net foreign assets	8,423	14,630	12,254	12,508	21,307	19,396
Net international reserves	8,384	14,572	12,849	13,051	21,891	19,933
Net international reserves (in millions of US$)	16,909	23,163	25,372	27,865	41,980	42,231
Other foreign assets, net	39	58	-595	-543	-584	-537
Net domestic assets	-4,751	-10,400	-7,672	-6,983	-14,456	-11,505
Net credit to general government	634	738	580	559	143	367
Net claims on banks and financial corporations	-1,228	-1,659	-2,854	-2,964	-4,593	-4,202
Credit to the private sector	946	957	904	861	805	717
Other items (net)	-5,103	-10,436	-6,302	-5,439	-10,811	-8,388
Monetary base	3,672	4,230	4,582	5,525	6,851	7,891
Currency	2,429	2,676	2,935	3,423	3,892	4,480
Required reserves	1,243	1,554	1,647	2,102	2,959	3,411
Other depository institutions						
Net foreign assets	-1,929	-3,395	-4,014	-4,767	-6,995	-6,477
Net foreign assets (in millions of US$)	-3,891	-5,397	-7,926	-10,178	-13,414	-13,722
Net domestic assets	54,178	63,777	64,965	66,513	81,620	84,909
Net credit to general government	-3,599	-3,923	-2,269	-2,240	-1,709	-716
Credit to the private sector	58,849	69,870	68,879	73,786	86,276	96,702
Other items (net)	-1,072	-2,170	-1,645	-5,033	-2,947	-11,077
Liabilities to the private sector	52,249	60,382	60,951	61,746	74,625	78,432
Demand deposits	8,368	8,417	11,150	13,465	14,749	16,080
Quasi-money	43,881	51,965	49,801	48,281	59,876	62,352
Banking system						
Net foreign assets	6,494	11,235	8,240	7,741	14,313	12,919
Net domestic assets	52,098	57,936	61,147	61,579	72,887	79,803
Net credit to general government	-2,965	-3,185	-1,689	-1,681	-1,566	-349
Credit to the private sector	59,795	70,827	69,783	74,647	87,081	97,419
Other items (net)	-4,732	-9,705	-6,710	-11,387	-12,627	-17,268
Liabilities to the private sector	58,592	69,171	69,387	69,320	87,200	92,722
Money	10,797	11,093	14,086	16,888	18,641	20,560
Quasi-money	47,795	58,078	55,301	52,432	68,559	72,162
Memorandum items						
	(Annual percentage change)					
Monetary base	7.8	15.2	8.3	20.6	24.0	15.2
Liabilities to the private sector	13.6	18.1	0.3	-0.1	25.8	6.3
Credit to the private sector	20.6	18.4	-1.5	7.0	16.7	11.9
	(In percent of GDP)					
Monetary base	4.1	4.5	4.7	5.0	5.7	6.1
Liabilities to the private sector	64.9	73.8	71.8	62.9	72.6	71.6
Credit to the private sector	66.2	75.6	72.2	67.7	72.5	75.3

Sources: Central Bank of Chile and Haver Analytics.

Table 6. Chile: Medium-Term Framework

	2010	2011	2012	Projections 2013	2014	2015	2016	2017	2018
National accounts	(Annual percentage change, unless otherwise specified)								
Real GDP	5.7	5.8	5.6	4.6	4.6	4.6	4.6	4.6	4.6
Total domestic demand	13.4	9.1	7.2	6.1	5.1	5.0	5.0	5.0	4.9
Consumption	9.6	8.0	5.7	5.9	4.8	4.9	4.9	5.0	5.0
Private	10.7	9.0	6.0	5.6	5.0	5.1	5.2	5.1	5.1
Public	4.4	3.2	3.9	6.9	3.8	4.0	3.0	4.6	4.5
Investment	27.4	13.1	10.5	9.3	4.2	5.4	5.5	4.8	4.7
Net exports 1/	-7.6	-3.9	-1.7	-0.9	-0.5	-0.8	-0.8	-0.7	-0.7
Consumer prices (average)	1.4	3.3	3.0	1.8	3.0	3.0	3.0	3.0	3.0
Balance of payments	(In percent of GDP)								
Current account	1.5	-1.3	-3.5	-4.7	-4.2	-3.7	-3.3	-3.1	-3.0
Trade balance	7.2	4.2	1.3	0.0	0.0	-0.1	-0.3	-0.4	-0.6
Financial account balance	-2.7	7.1	3.7	4.7	4.2	3.7	3.3	3.1	3.0
Of which, foreign direct investment (net)	2.7	1.0	3.4	3.9	3.8	3.6	3.5	3.3	3.2
Change in reserves assets	-1.4	-5.7	0.1	0.0	0.0	0.0	0.0	0.0	0.0
	(Annual percentage change)								
Total export volume	-0.2	4.1	1.9	3.7	4.3	3.2	3.2	3.4	3.5
Of which, copper export volume	0.4	-2.0	2.5	4.4	4.5	0.8	0.3	0.3	0.3
Total import volume	31.4	16.4	5.8	5.2	4.9	4.5	4.5	4.5	4.5
Terms of trade	22.0	1.2	-5.2	-3.0	0.5	1.0	0.4	0.2	0.2
Total export prices	28.6	10.2	-5.2	-3.7	-0.3	0.3	0.3	0.4	0.4
Copper export prices	40.4	11.0	-8.2	-6.3	-1.0	1.0	0.9	0.8	0.6
Total import price	5.7	9.0	0.0	-0.7	-0.8	-0.6	-0.2	0.2	0.2
External debt	(In percent of GDP)								
Gross external debt	38.9	39.3	43.9	43.3	43.0	41.9	40.9	40.0	39.3
Public	7.9	8.2	9.4	9.4	9.4	9.2	9.0	8.8	8.7
Private	30.9	31.2	34.5	33.8	33.6	32.7	31.9	31.2	30.6
Gross int. reserves (in billions of U.S. dollars)	27.9	42.0	41.6	41.6	41.6	41.6	41.6	41.6	41.6
Savings and investment									
Gross domestic investment	22.4	23.5	24.9	25.5	25.2	25.1	25.0	24.9	24.7
Public	2.4	2.4	2.3	2.5	2.4	2.4	2.4	2.4	2.4
Private	20.0	21.1	22.6	23.1	22.7	22.6	22.6	22.5	22.3
National saving	23.9	22.2	21.4	20.8	20.9	21.4	21.7	21.8	21.7
Public	2.0	3.7	2.8	2.3	2.1	2.0	2.1	2.1	2.1
Private	21.9	18.5	18.6	18.5	18.8	19.3	19.6	19.7	19.6
Public sector finance									
Net debt	-2.2	-4.9	-1.7	-1.7	-0.2	0.9	1.9	2.8	3.5
Excluding public enterprises	-7.8	-10.6	-7.8	-7.8	-6.3	-5.2	-4.2	-3.4	-2.6
Public sector gross debt 2/	25.9	34.8	34.2	34.0	33.8	33.4	33.1	32.7	32.3
Central government gross debt	8.6	11.1	11.9	12.2	12.5	12.9	13.1	13.4	13.5
Central government balance	-0.5	1.3	0.6	-0.1	-0.3	-0.3	-0.3	-0.2	-0.2
Total revenue	21.5	22.6	21.9	22.0	21.5	21.4	21.1	21.1	21.1
Total expenditure	22.0	21.4	21.4	22.0	21.8	21.7	21.4	21.3	21.3
Central government structural balance	-2.5	-0.9	-0.6	-0.6	-0.8	-0.7	-0.6	-0.6	-0.5
Employment	(Annual percentage change, unless otherwise specified)								
Working age population	1.6	1.5	1.5	1.4	1.4	1.3	1.2	1.1	1.1
Labor force	4.2	3.8	1.1	1.4	1.4	1.3	1.2	1.1	1.1
Employment	7.4	5.0	1.9	1.4	1.2	1.3	1.2	1.1	1.1
Unemployment rate (in percent)	8.2	7.1	6.4	6.5	6.6	6.6	6.6	6.6	6.6

Sources: Central Bank of Chile, Ministry of Finance, National Statistics Institute, Haver Analytics, and Fund staff estimates and projections.

1/ Contribution to growth.

2/ Gross consolidated debt of the public sector (central bank, non-financial public enterprises, and general government).

Table 7. Chile: Indicators of External Vulnerability
(In percent; unless otherwise indicated)

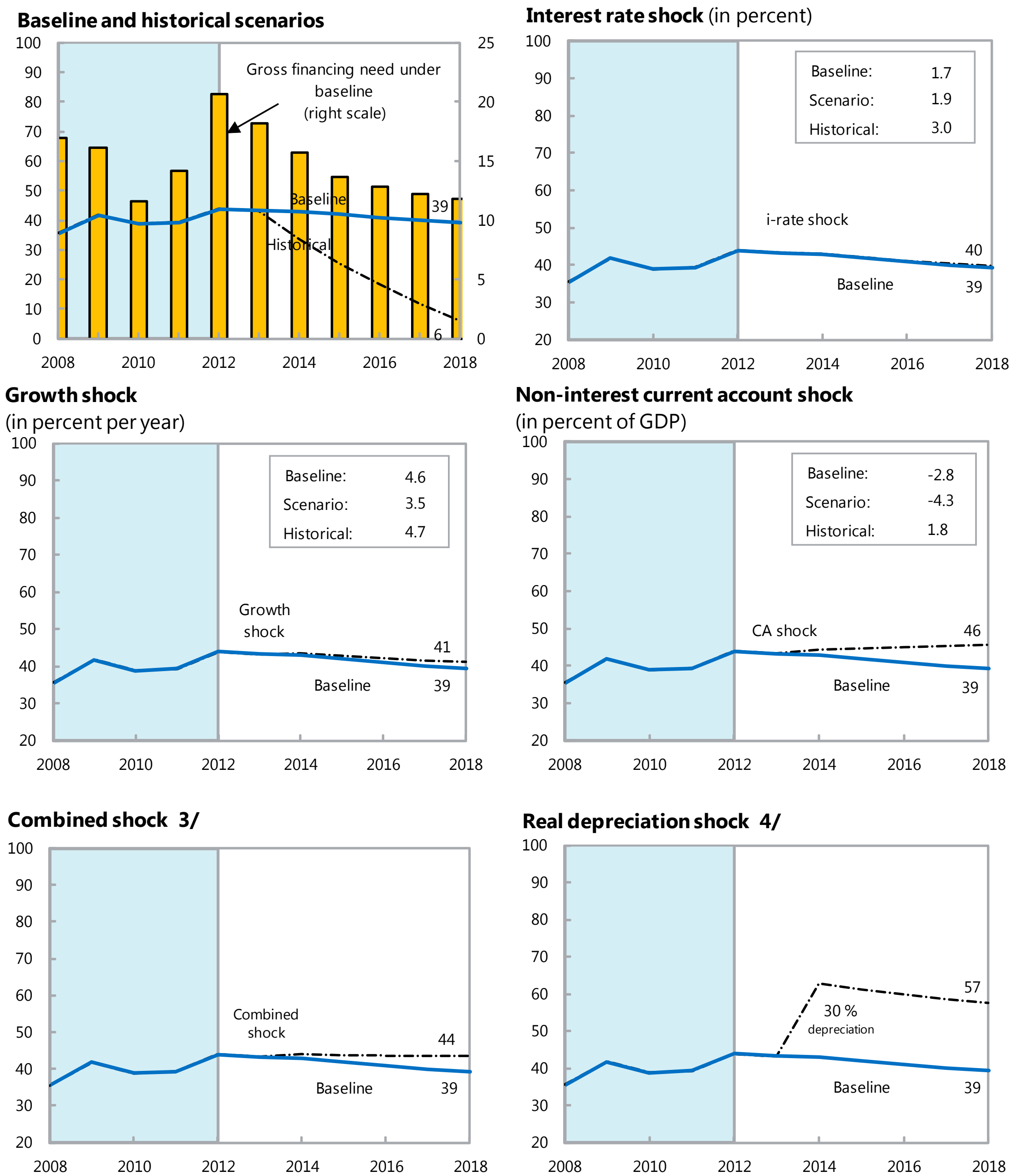
	2008	2009	2010	2011	2012	2013
Financial indicators						
M3 (percent change)	19.1	-1.4	11.2	18.9	6.2	...
Less pension funds' deposits (annual percentage change)	22.4	4.9	13.0	18.5	6.0	...
Private sector credit to GDP	74.5	71.5	66.5	71.1	74.1	...
90-day central bank promissory note (nominal) interest rate (avg.)	7.3	1.8	1.7	4.9	5.1	...
Share of foreign currency deposits in total deposits	14.5	13.2	15.4	12.8	12.7	...
Share of foreign currency loans in total credit	11.8	11.5	10.7	12.7	12.9	...
External indicators						
Exports, U.S. dollars (annual percentage change)	-5.9	-14.0	28.2	14.6	-3.9	-0.3
Imports, U.S. dollars (annual percentage change)	31.5	-31.4	38.3	27.8	5.6	4.4
Terms of trade (annual percentage change)	-15.0	4.3	22.0	1.2	-5.2	-3.0
REER (annual percent change, period average)	1.8	-2.2	5.9	0.9	3.4	...
Exchange rate (pesos per U.S. dollar, period average)	522	560	510	484	486	...
Current account balance (percent of GDP)	-3.2	2.0	1.5	-1.3	-3.5	-4.7
Financial account less reserves accumulation (percent of GDP)	6.8	-1.1	-3.0	7.0	3.4	4.7
Gross official reserves (in billions of U.S. dollars) 1/	23.2	25.4	27.9	42.0	41.6	41.6
Gross official reserves, months of imports of goods and services	5.5	4.4	3.9	5.6	5.3	5.1
Gross official reserves to M3	16.5	14.8	13.5	19.0	16.3	...
Gross official reserves to short-term external debt 2/	86.2	101.8	97.4	109.1	108.0	120.0
Total external debt (percent of GDP)	35.5	41.8	38.9	39.3	43.9	43.3
Of which: External public sector debt	6.5	7.7	7.9	8.2	9.4	9.4
Total external debt to exports of goods and services	84.7	112.5	103.1	104.4	129.6	134.9
External interest payments to exports of goods and services	2.1	2.4	2.3	2.3	3.3	2.8
External amortization payments to exports of goods and services	32.6	48.8	34.6	34.0	50.4	42.1
Financial market indicators						
Stock market index (in U.S. dollars; period average) 3/	1629	1601	2362	2564	2434	...
Sovereign long-term foreign currency debt rating (end of period)						
Moody's	A2	A1	Aa3	Aa3	Aa3	...
S&P	A+	A+	A+	A+	AA-	...
Fitch ratings	A	A	A	A+	A+	...

Sources: Central Bank of Chile, Haver Analytics, WEO, and Fund staff estimates.

1/ Gold valued at end-period market prices.
2/ Includes amortization of medium/long-term debt due during the following year.
3/ Morgan-Stanley Capital International index (Dec/1987=100).

Annex I. Chile—Debt Sustainability Analysis

Figure A1. Chile: External Debt Sustainability: Bound Tests 1/ 2/
(External debt in percent of GDP)



Sources: International Monetary Fund, Country desk data, and Fund staff estimates.
1/ Shaded areas represent actual data. Individual shocks are permanent one-half standard deviation shocks. Figures in the boxes represent average projections for the respective variables in the baseline and scenario being presented. Ten-year historical average for the variable is also shown.
2/ For historical scenarios, the historical averages are calculated over the ten-year period, and the information is used to project debt dynamics five years ahead.
3/ Permanent 1/4 standard deviation shocks applied to real interest rate, growth rate, and current account balance.
4/ One-time real depreciation of 30 percent occurs in 2014.

Table A1. Chile: External Debt Sustainability Framework, 2008-2018

(In percent of GDP, unless otherwise indicated)

	Actual					Projections						
	2008	2009	2010	2011	2012	2013	2014	2015	2016	2017	2018	**Debt-stabilizing non-interest current account 6/**
Baseline: External debt	**35.5**	**41.8**	**38.9**	**39.3**	**43.9**	**43.2**	**43.0**	**41.9**	**40.9**	**40.0**	**39.2**	**-4.4**
Change in external debt	4.6	6.3	-2.9	0.5	4.6	-0.7	-0.3	-1.1	-1.0	-0.9	-0.8	
Identified external debt-creating flows (4+8+9)	-1.9	-3.7	-12.4	-5.6	-0.6	0.1	-0.2	-0.6	-0.8	-0.8	-0.8	
Current account deficit, excluding interest payments	2.3	-2.9	-2.3	0.5	2.4	3.8	3.4	3.0	2.7	2.5	2.5	
Deficit in balance of goods and services	-81.1	-66.6	-69.2	-72.2	-67.4	-65.2	-64.2	-61.7	-59.5	-57.7	-55.9	
Exports	41.9	37.2	37.7	37.7	33.9	32.0	31.7	30.4	29.3	28.3	27.5	
Imports	-39.2	-29.4	-31.5	-34.5	-33.5	-33.2	-32.5	-31.3	-30.2	-29.3	-28.5	
Net non-debt creating capital inflows (negative)	-4.0	-3.2	-2.2	-1.7	-1.6	-2.7	-2.6	-2.4	-2.3	-2.2	-2.1	
Automatic debt dynamics 1/	-0.2	2.4	-7.8	-4.4	-1.4	-1.0	-1.1	-1.2	-1.2	-1.2	-1.2	
Contribution from nominal interest rate	0.9	0.9	0.9	0.9	1.1	0.9	0.8	0.7	0.6	0.6	0.5	
Contribution from real GDP growth	-0.9	0.3	-1.9	-1.9	-2.1	-1.9	-1.9	-1.8	-1.8	-1.7	-1.7	
Contribution from price and exchange rate changes 2/	-0.2	1.2	-6.8	-3.3	-0.4	...	...	...	...	...	...	
Residual, incl. change in gross foreign assets (2-3) 3/	6.5	10.0	9.5	6.1	5.2	-0.8	-0.1	-0.5	-0.2	0.0	0.0	
External debt-to-exports ratio (in percent)	84.7	112.5	103.1	104.4	129.6	134.9	135.5	137.5	139.5	141.2	143.0	
Gross external financing need (in billons of US dollars) 4/	**30**	**28**	**25**	**35**	**55**	**52**	**48**	**45**	**45**	**46**	**48**	
in percent of GDP	16.9	16.1	11.6	14.1	20.6	18.2	15.7	13.7	12.9	12.2	11.8	
Scenario with key variables at their historical averages 5/						**43.2**	**33.7**	**25.5**	**18.3**	**11.8**	**5.9**	**-4.3**
Key macroeconomic assumptions underlying baseline												
Real GDP growth (in percent)	3.1	-0.9	5.7	5.8	5.6	4.6	4.6	4.6	4.6	4.6	4.6	
GDP deflator in US dollars (change in percent)	0.6	-3.3	19.4	9.3	1.2	1.8	1.2	3.2	3.2	3.0	3.0	
Nominal external interest rate (in percent)	3.0	2.4	2.6	2.5	3.0	2.2	2.1	1.7	1.6	1.5	1.5	
Growth of exports (US dollar terms, in percent)	-3.0	-15.0	28.1	15.4	-3.9	0.7	4.7	3.8	3.9	4.2	4.3	
Growth of imports (US dollar terms, in percent)	28.5	-28.1	35.3	26.6	3.8	5.4	3.9	3.8	4.2	4.6	4.7	
Current account balance, excluding interest payments	-2.3	2.9	2.3	-0.5	-2.4	-3.8	-3.4	-3.0	-2.7	-2.5	-2.5	
Net non-debt creating capital inflows	4.0	3.2	2.2	1.7	1.6	2.7	2.6	2.4	2.3	2.2	2.1	

1/ Derived as [r - g - r(1+g) + ea(1+r)]/(1+g+r+gr) times previous period debt stock, with r = nominal effective interest rate on external debt; r = change in domestic GDP deflator in US dollar terms, g = real GDP growth rate, e = nominal appreciation (increase in dollar value of domestic currency), and a = share of domestic-currency denominated debt in total external debt.

2/ The contribution from price and exchange rate changes is defined as [-r(1+g) + ea(1+r)]/(1+g+r+gr) times previous period debt stock. r increases with an appreciating domestic currency (e > 0) and rising inflation (based on GDP defla

3/ For projection, line includes the impact of price and exchange rate changes.

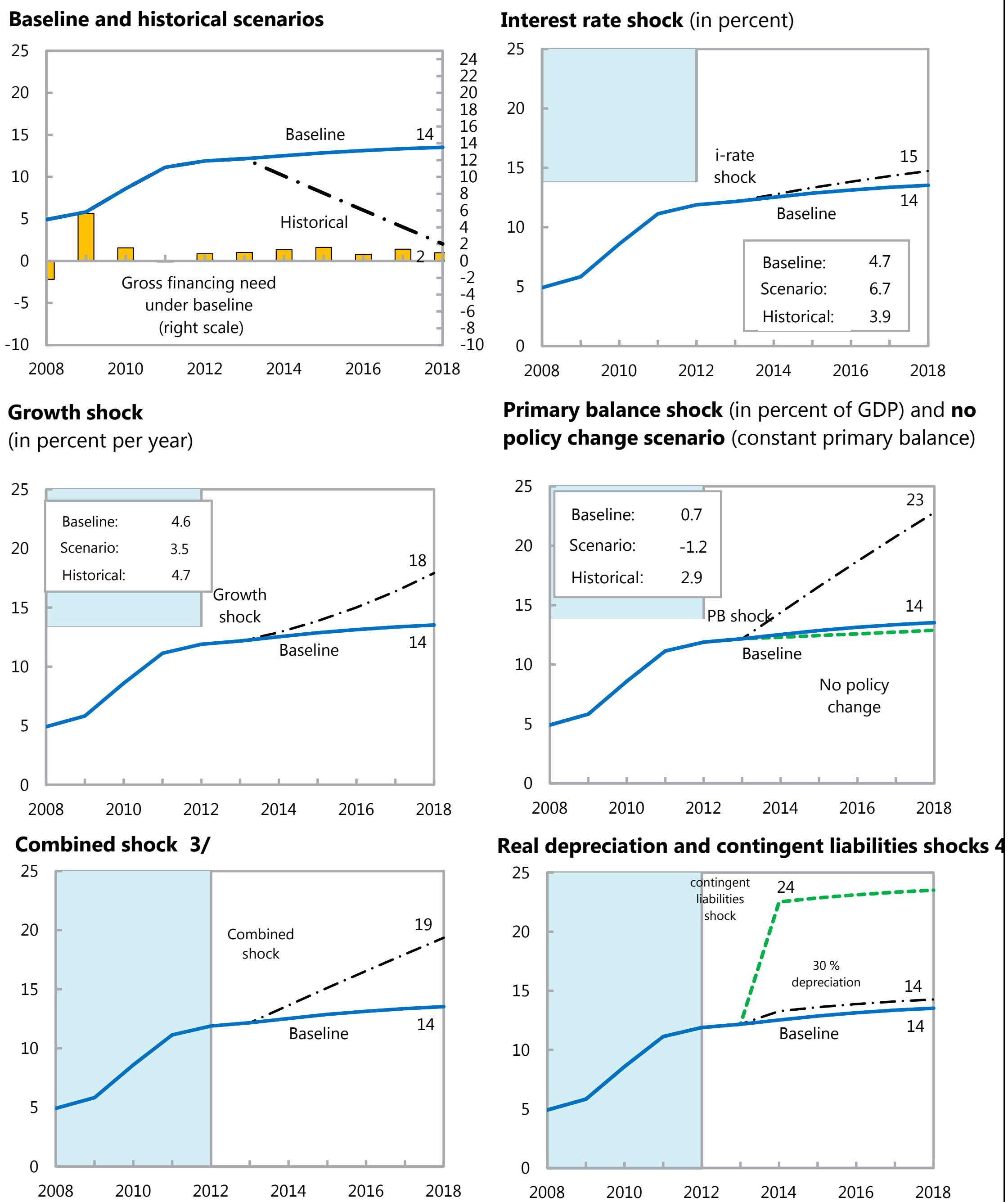
4/ Defined as current account deficit, plus amortization on medium-and long-term debt, plus short-term debt at end of previous period.

5/ The key variables include real GDP growth; nominal interest rate; dollar deflator growth; and both non-interest current account and non-debt inflows in percent of GDP.

6/ Long-run, constant balance that stabilizes the debt ratio assuming that key variables (real GDP growth, nominal interest rate, dollar deflator growth, and non-debt inflows in percent of GDP) remain at their levels of the last projection year.

Figure A2. Chile: Central Government Sustainability: Bound Tests 1/ 2/

(Public debt in percent of GDP)



Sources: International Monetary Fund, country desk data, and Fund staff estimates.

1/ Shaded areas represent actual data. Individual shocks are permanent one-half standard deviation shocks. Figures in the boxes represent average projections for the respective variables in the baseline and scenario being presented. Ten-year historical average for the variable is also shown.

2/ For historical scenarios, the historical averages are calculated over the ten-year period, and the information is used to project debt dynamics five years ahead.

3/ Permanent 1/4 standard deviation shocks applied to real interest rate, growth rate, and primary balance.

4/ One-time real depreciation of 30 percent and 10 percent of GDP shock to contingent liabilities occur in 2014, with real depreciation defined as nominal depreciation (measured by percentage fall in dollar value of local currency) minus domestic inflation (based on GDP deflator).

Table A2. Chile: Central Government Debt Sustainability Framework, 2008-2018
(In percent of GDP, unless otherwise indicated)

	Actual					Projections						
	2008	2009	2010	2011	2012	2013	2014	2015	2016	2017	2018	**Debt-stabilizing primary balance 9/**
1 **Baseline: Public sector debt 1/**	**4.9**	**5.8**	**8.6**	**11.1**	**11.9**	**12.2**	**12.5**	**12.9**	**13.1**	**13.4**	**13.5**	**0.00**
o/w foreign-currency denominated	2.0	1.3	1.5	1.9	1.9	1.6	1.4	1.3	1.2	1.1	1.0	
2 Change in public sector debt	1.0	0.9	2.8	2.5	0.8	0.3	0.4	0.3	0.3	0.2	0.2	
3 Identified debt-creating flows (4+7+12)	-3.4	3.7	-0.4	-1.9	-1.5	-0.6	-0.6	-0.6	-0.7	-0.7	-0.8	
4 Primary deficit	-4.4	3.7	0.0	-1.8	-1.1	-0.8	-0.6	-0.6	-0.7	-0.7	-0.8	
5 Revenue and grants	24.2	19.1	21.6	22.6	22.0	22.0	21.6	21.4	21.1	21.1	21.2	
6 Primary (noninterest) expenditure	19.9	22.8	21.5	20.8	20.8	21.2	21.0	20.8	20.4	20.4	20.4	
7 Automatic debt dynamics 2/	0.9	0.0	-0.4	0.0	-0.3	0.2	0.0	0.0	0.0	0.0	0.0	
8 Contribution from interest rate/growth differential 3/	0.3	0.4	-0.3	-0.2	-0.2	0.2	0.0	0.0	0.0	0.0	0.0	
9 Of which contribution from real interest rate	0.4	0.3	0.0	0.3	0.4	0.7	0.5	0.5	0.5	0.6	0.6	
10 Of which contribution from real GDP growth	-0.1	0.0	-0.3	-0.5	-0.6	-0.5	-0.5	-0.5	-0.5	-0.6	-0.6	
11 Contribution from exchange rate depreciation 4/	0.6	-0.4	-0.1	0.2	-0.2	...	...	...	...	...	...	
12 Other identified debt-creating flows	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	
13 Privatization receipts (negative)	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	
14 Recognition of implicit or contingent liabilities	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	
15 Other (specify, e.g. bank recapitalization)	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	
16 Residual, including asset changes (2-3) 5/	4.5	-2.7	3.2	4.4	2.2	0.9	0.9	0.9	0.9	0.9	0.9	
Public sector debt-to-revenue ratio 1/	20.3	30.6	39.9	49.2	54.2	55.4	58.1	60.1	62.2	63.2	63.9	
Gross financing need 6/	**-2.2**	**5.7**	**1.6**	**-0.1**	**0.9**	**1.0**	**1.4**	**1.6**	**0.8**	**1.4**	**1.0**	
in billions of U.S. dollars	-3.9	9.8	3.4	-0.3	2.3	2.9	4.1	5.3	2.8	5.4	4.0	
Scenario with key variables at their historical averages 7/						**12.2**	**10.1**	**8.1**	**6.0**	**4.0**	**2.0**	**-0.02**
Scenario with no policy change (constant primary balance) in 2013-2018						**12.2**	**12.3**	**12.4**	**12.6**	**12.7**	**12.9**	**0.00**
Key Macroeconomic and Fiscal Assumptions Underlying Baseline												
Real GDP growth (in percent)	3.1	-0.9	5.7	5.8	5.6	4.6	4.6	4.6	4.6	4.6	4.6	
Average nominal interest rate on public debt (in percent) 8/	12.5	10.3	9.6	7.1	5.7	7.7	7.7	7.7	7.7	7.7	7.7	
Average real interest rate (nominal rate minus change in GDP deflator, in percent)	11.9	6.7	0.7	3.5	3.9	6.2	4.7	4.7	4.7	4.7	4.8	
Nominal appreciation (increase in US dollar value of local currency, in percent)	-21.2	24.2	8.1	-10.2	9.0	...	...	...	...	...	...	
Inflation rate (GDP deflator, in percent)	0.6	3.6	8.9	3.6	1.7	1.5	3.0	3.0	3.0	3.0	3.0	
Growth of real primary spending (deflated by GDP deflator, in percent)	19.3	13.5	0.0	2.0	5.8	6.5	3.7	3.7	2.8	4.4	4.5	
Primary deficit	-4.4	3.7	0.0	-1.8	-1.1	-0.8	-0.6	-0.6	-0.7	-0.7	-0.8	

1/ Central government gross debt

2/ Derived as [(r - p(1+g) - g + ae(1+r)]/(1+g+p+gp)) times previous period debt ratio, with r = interest rate; p = growth rate of GDP deflator; g = real GDP growth rate; a = share of foreign-currency denominated debt; and e = nominal exchange rate depreciation (measured by increase in local currency value of U.S. dollar).

3/ The real interest rate contribution is derived from the denominator in footnote 2/ as r - π (1+g) and the real growth contribution as -g.

4/ The exchange rate contribution is derived from the numerator in footnote 2/ as ae(1+r).

5/ For projections, this line includes exchange rate changes.

6/ Defined as public sector deficit, plus amortization of medium and long-term public sector debt, plus short-term debt at end of previous period.

7/ The key variables include real GDP growth; real interest rate; and primary balance in percent of GDP.

8/ Derived as nominal interest expenditure divided by previous period debt stock.

9/ Assumes that key variables (real GDP growth, real interest rate, and other identified debt-creating flows) remain at the level of the last projection year.

Annex II. 2011 FSAP Update—Status of Main Recommendations

Recommendation (priority H/M, time frame S/M)	Update
Reduce information gaps, including through a consolidated credit registry and standardized residential and commercial property price indices (M, M)	A bill was submitted to Congress in August 2011 to create a public credit bureau, which would consolidate data provided by financial institutions (banks, retailers, insurance companies, and others). It will include both positive and negative information for individuals and companies. It will be managed by the Superintendence of Banking and Financial Institutions (SBIF). The Central Bank published residential housing price data back to 2001 in December 2011 and December 2012, and commercial real estate data in June 2012. The data compose three indices: hedonic prices, mixed adjustment, and total sales. The working group on Housing Market of the Financial Stability Council (FSC) has produced data on Loan-to-Value ratios.
Develop a strategy to ensure adequate replacement rate for retirees (H, M)	The 2008 Pension Reform contained several measures to address the issue of low pension and replacement rates, including the introduction of a new solidarity pillar to prevent old-age poverty and measures to reduce the gender gap in old-age income (e.g. division of balance in case of divorce). To increase coverage, subsidies for young workers and a gradual mandatory participation of independent workers were introduced (2012 was the first year of the phase-in transition).The mechanisms for voluntary pension savings with tax incentives were improved and widened. The effectiveness of these measures has been under evaluation in this period; particularly the collective voluntary saving mechanism which has not been successful and will require modifications. More recently, the Superintendence of Pensions (SP) has developed two new methodologies to measure and forecast replacement rates. One model uses administrative and survey data at the individual level. The other is a pension risk model, which is used in a public web-based pension simulator that allows users to estimate their pension under different return assumptions. Since its launching, the simulator has averaged 10 thousand visits per month. The Pension Supervisors has launched a web tool for members to check if employers have paid contributions on behalf of workers. There is also ongoing joint work with the OECD on computing replacement rates. These efforts should lead to an updated assessment of replacement rates, based on which further reforms will be considered.
Strengthen the independence and legal protection of regulatory agencies (H, M)	The Government has prepared a draft law to be submitted to Congress in 2013, which envisages improving governance of the Superintendency for Securities and Insurance (SVS) by converting it to a commission managed by a five-member council, which are protected from dismissal for political reasons. It also proposes improvements to the enforcement process and transparency (an annual report will be published and regulatory impact assessment will be made prior issuing new regulations). The revised General

Recommendation (priority H/M, time frame S/M)	Update
	Banking Law will not include amendments to enhance independence of the SBIF.
Strengthen the enforcement powers of securities regulators (H, S)	Enhancement of enforcement powers of the SVS is envisaged in the draft law mentioned above. The law would establish Securities and Insurance Prosecutor – an autonomous body in charge of investigation and enforcement proceedings. Sanctions will be applied by the Commission, upon conclusion of the investigation by the Prosecutor.
Complete the incorporation of Basel bank capital standards (H, M), and strengthen the legal framework for bank resolution (H, M)	The Government is working on changes to the General Banking Law to fully adopt Basel bank capital standards. However, amendments to enhance independence of the SBIF and major changes to the legal framework for bank resolution will not be included in this reform. The SBIF and the Central Bank are also working on improvements in liquidity regulation and reporting, taking into consideration recent proposals of the Basel Committee on Banking Supervision.
Establish legal framework to enable the consolidated oversight of financial conglomerates (H, M)	The Committee of Financial Superintendents (CSSF) is developing a methodology for supervision of financial conglomerates, including assessment of overall risks and identification of lead supervisors. The CSSF has established formal rules for sharing information relevant for supervision and regulation. The new Financial Stability Council builds up on the work of the CSSF. The Council is supported by three working groups: Risk Analysis, Regulation and Legislation, and Financial Conglomerates, the latter is working on identifying key indicators of financial health for conglomerates. A draft bill will be submitted to Congress to provide the FSC a legal framework and to strengthen the capacity of supervisors to request information on conglomerates.
Enhance uniformity in business conduct regulation for asset management services and investment advice (H, M)	A comprehensive Funds Law that standardizes regulation in the fund industry was submitted to Congress in September 2011. In December 2011, the SVS issued regulation on internal control and risk management for securities intermediaries, which sets minimum requirements for control and risk management. Securities intermediaries will be required to have an Internal Audit Unit, and an internal risk management system consistent with the complexity of operations. The senior executives will be accountable for the implementation of the internal control and risk management. A staff's code of conduct will also be required.
Introduce comparable transparency standards for fixed income securities traded outside exchanges (H, M)	In 2012, an FSAP implementation workshop for securities regulators was organized with the help of the Toronto Centre. The SVS has established an action plan to implement some of the recommendations. The recommendation on OTC fixed income markets has not been included but will be reviewed this year.

Recommendation (priority H/M, time frame S/M)	Update
Adopt a comprehensive approach to custodial, clearing, and settlement infrastructure (M, M)	In 2012, an FSAP implementation workshop for securities regulators was organized with the help of the Toronto Centre. The SVS has established an action plan to detect gaps in the implementation of the CPSS IOSCO principles of Financial Market Infrastructures. Advancing on the implementation of the principles, the SVS will change the norm on management of integral risk and the rule about credit and liquidity risk, and enact, after proper studies about the issue, a new rule on corporate governance and a new rule on trade repositories.
Further enhance the AML/CFT framework (M, M)	In April 2011, the Financial Analysis Unit (UAF), SVS, SBIF, and the SP issued regulations against corruption of senior government officials. They established criteria to define Politically Exposed Persons (PEP), and procedures for financial intermediaries to determine the source and destination of funds of such persons. In addition, all entities supervised by the UAF are required to register all transactions of PEP and inform of any suspicious operations. Progress has been made on GAFISUD recommendation to require foreign subsidiaries to inform about activities carried out in countries that are not in compliance with the set standards. In 2011, the UAF initiated 306 sanctionary processes and 268 between January and September of 2012. IMF's Legal Department has provided technical advice to the Chilean authorities on the development of their national AML/CFT strategy. On March 14, 2013 the ministers of Interior and Finance jointly launched the " National strategy against money laundering," a task force (involving more than 20 public institutions) aiming to provide a diagnosis of the situation of the public sector and provide concrete solutions for the challenges identified. The authorities are expecting to conclude this process during the second half of this year. Chile is still under an enhanced follow up process with GAFISUD given the existence of outstanding issues regarding compliance with key AML/CFT recommendations.
Consider introduction of a premium-based limited deposit insurance system (M, M)	There have been no changes to date.
Examine options to establish a framework for dealing with a systemic crisis and with the potential failure of a financial conglomerate (M, M)	The Finance Ministry, Central Bank, and the SBIF conducted a joint crisis exercise in 2011, coordinated by Crisis Management Analytics. The Financial Stability Council is currently reviewing lessons from the exercise, and plans to prepare a cooperation protocol based on those lessons. In addition, there has been progress in enhancing the supervision of conglomerates. As mentioned above, a draft bill will be submitted to Congress to provide the FSC a legal framework and to strengthen the capacity of supervisors to request information on conglomerates.

INTERNATIONAL MONETARY FUND

CHILE

STAFF REPORT FOR THE 2013 ARTICLE IV CONSULTATION—INFORMATIONAL ANNEX

June 14, 2013

Prepared By | The Western Hemisphere Department

CONTENTS

FUND RELATIONS

(As of April 30, 2013)

Membership Status
Joined: December 31, 1945; Article VIII

General Resources Account	**SDR Million**	**Percent Quota**
Quota	856.10	100.00
Fund holdings of currency	585.41	68.38
Reserve Tranche Position	270.69	31.62
Lending to the Fund		
New Arrangements to Borrow	164.90	

SDR Department	**SDR Million**	**Percent Allocation**
Net cumulative allocation	816.89	100.00
Holdings	788.26	96.50

Outstanding Purchases and Loans
None

Latest Financial Arrangements

Type	**Date of Arrangement**	**Expiration Date**	**Amount Approved** (SDR Million)	**Amount Drawn** (SDR Million)
Stand-By	Nov 08, 1989	Nov 07, 1990	64.00	64.00
EFF	Aug 15, 1985	Aug 14, 1989	825.00	806.25
Stand-By	Jan 10, 1983	Jan 09, 1985	500.00	500.00

Projected Payments to Fund (in SDR Million)[1/]

			Forthcoming		
	2013	**2014**	**2015**	**2016**	**2017**
Principal					
Charges/Interest	0.02	0.02	0.02	0.02	0.02
Total	**0.02**	**0.02**	**0.02**	**0.02**	**0.02**

[1/] When a member has overdue financial obligations outstanding for more than three months, the amount of such arrears will be shown in this section.

Exchange Rate System
Chile has accepted the obligations of Article VIII, Sections 2, 3, and 4 and maintains an exchange rate system free of restrictions on the making of payments and transfers for current international transactions. Chile has a floating exchange rate system.

STATISTICAL ISSUES

(As of June 5, 2013)

Assessment of Data Adequacy for Surveillance	
General: Data provision is adequate for surveillance. The National Institute of Statistics (INE) regularly publishes a full range of economic and financial data. The Central Bank of Chile (CBC) also publishes comprehensive macroeconomic and financial data. The Ministry of Finance publishes fiscal data. Key publicly accessible websites for macroeconomic data and analysis are: National Institute of Statistics: http://www.ine.cl/ Central Bank of Chile: http://www.bcentral.cl/ Ministry of Finance: http://www.minhda.cl/ **Recent Developments:** The Central Bank started to publish housing and commercial real estate price data in 2012, which allows better monitoring and identification of risks. The National Institute of Statistics (INE) has announced that it will revise the methodology for measuring the clothing sub-index, which has a downward bias, and to review the methodology for three other sub-indices (rents, domestic services, and electronics guidelines). Based on the 2011-2012 Household Budget Survey, the Consumer Price Index (CPI) will be updated. As noted, the new CPI will include improved methods regarding imputed rents, seasonal items and quality adjustment.	
Data Standards and Quality	
Subscriber to the Fund's Special Data Dissemination Standard (SDDS) since May 17, 1996.	A data ROSC was published September 17, 2007.
Reporting to STA (Optional)	
The CBC uses the standardized report forms (SRFs) to report monthly data for the central bank, other depository corporations (ODCs), other financial corporations (OFCs), and monetary aggregates. However, data for the ODCs exclude savings and credit cooperatives and OFCs exclude investment funds, general funds, housing funds, foreign capital investment funds, factoring societies, leasing companies, and financial auxiliaries. The CBC reports all core and 7 of 28 encouraged financial soundness indicators on a monthly basis.	

Chile–Table of Common Indicators Required for Surveillance

(As of July 10, 2012)

	Date of Latest Observation	Date Received	Frequency of Data[6]	Frequency of Reporting[6]	Frequency of Publication[6]	Memo items[7]: Data Quality – Methodological Soundness[8]	Data Quality Accuracy and Reliability[9]
Exchange Rates	May 2013	June 4, 2013	D	D	D		
International Reserve Assets and Reserve Liabilities of the Monetary Authorities[1]	April 2013	May 24, 2013	W	W	W		
Reserve/Base Money	April 7, 2013	April 7, 2013	W	W	W	O, O, LO, O	O, O, O, LO, O
Broad Money	March 2013	March 2013	M	M	M		
Central Bank Balance Sheet	March 2013	March 2013	M	M	M		
Consolidated Balance Sheet of the Banking System	March 2013	March 2013	M	M	M		
Interest Rates[2]	April 2013	June 3, 2013	D	D	D		
Consumer Price Index	April 2013	May 16, 2013	M	M	M	LO, LNO, LNO, LO	LO, LO, LO, O, LO
Revenue, Expenditure, Balance and Composition of Financing[3] – General Government[4]	2011	July 9, 2012	A	A	A	O, LO, LNO, LO	LO, O, O, LO, O
Revenue, Expenditure, Balance and Composition of Financing3– Central Government	March 2013	July 9, 2012	M	M	M		
Stocks of Central Government and Central Government –Guaranteed Debt[5]	December 2012	July 9, 2012	Q	Q	Q		
External Current Account Balance	Q1 2013	May 20 , 2013	Q	Q	Q	O, O, LO, LO	O, O, O, O, O
Exports and Imports of Goods and Services	March 2013	July 10 , 2012	M	M	M		
GDP/GNP	Q1 2013	May 20, 2013	Q	Q	Q	O, LO, LO, LO	LO, LO, LO, LO, O
Gross External Debt	March 2013	July 10, 2012	M	M	M		
International Investment Position[10]	Q4 2012	July 10, 2012	Q	Q	Q		

[1] Any reserve assets that are pledged or otherwise encumbered should be specified separately. Also, data should comprise short-term liabilities linked to a foreign currency but settled by other means as well as the notional values of financial derivatives to pay and to receive foreign currency, including those linked to a foreign currency but settled by other means.

[2] Both market-based and officially-determined, including discount rates, money market rates, rates on treasury bills, notes, and bonds.

[3] Foreign, domestic bank, and domestic nonbank financing.

[4] The general government consists of the central government (budgetary funds, extra budgetary funds, and social security funds) and state and local governments.

[5] Including currency and maturity composition.

[6] Daily (D); weekly (W); monthly (M); quarterly (Q); annually (A); irregular (I); and not available (NA).

[7] Reflects the assessment provided in the data ROSC, (published September 17, 2007 and based on the findings of the mission that took place during April 18-May2, 2007) for the dataset corresponding to the variable in each row. The assessment indicates whether international standards concerning concepts and definitions, scope, classification/sectorization, and basis for recording are fully observed (O); largely observed (LO); largely not observed (LNO); not observed (NO); and not available (NA).

[8] Same as footnote 7, except referring to international standards concerning source data, assessment of source data, statistical techniques, assessment and validation of intermediate data and statistical outputs, and revision studies.

[9] Same as footnote 8, except referring to international standards concerning source data, statistical techniques, assessment and validation of source data, assessment and validation of intermediate data and statistical outputs, and revision studies.

[10] Includes external gross financial asset and liability positions vis-à-vis nonresidents.

WORLD BANK—FUND COUNTRY-LEVEL WORK PROGRAM UNDER JMAP

Title	Products	Provisional Timing of Missions	Expected Delivery Date*
1. Bank work program	**A. Investment Loans**		
	1. Second Public Expenditure Management Project (P1035441)		August 2007
	2. Ministry of Public Works Institutional Strengthening TAL (P102931)		June 2007
	3. Tertiary Education Finance for Results Project III (P111661)		March 2012
	B. Technical Assistance		
	1. Tertiary Education Technical Assistance Program		May 2013
	2. Improvement of the Institutional Governance for Water		June 2013
	3. Strengthening of the Planning and Prioritization Process for the Development of Water Infrastructure Projects		June 2013
	4. Strengthening of the System for Consumer Protection for Fuel Price Volatility		June 2013
	5. Operational Risk of Cash Management		June 2013
	6. Economic and Financial Assessment of Concessions		June 2013
	7. Design of the Ministry of Agriculture (MINAGRI) Agricultural Innovation Unit		September 2013

*Delivery date refers to the Board date in lending projects and to delivery to client in case of AAA.

INTERNATIONAL MONETARY FUND
Public Information Notice

Public Information Notice (PIN) No. 13/77
FOR IMMEDIATE RELEASE
July 8, 2013

International Monetary Fund
700 19th Street, NW
Washington, D. C. 20431 USA

IMF Executive Board Concludes 2013 Article IV Consultation with Chile

On July 1, 2013, the Executive Board of the International Monetary Fund (IMF) concluded the Article IV consultation with Chile, and considered and endorsed the staff appraisal without a meeting.[1]

Background

After growing strongly over the past three years, the economy appears to be decelerating toward potential. Chile recovered rapidly from the global financial crisis and the February 2010 earthquake, and the growth surprised on the upside in 2012, powered by strong private domestic demand—in particular investment in mining. Real gross domestic product (GDP) growth slowed in the first quarter of 2013 to 4.1 percent (year on year) from 5.7 percent in the fourth quarter of 2012. Credit growth has been on a declining trend although is still quite strong. The labor market remains tight, with the unemployment rate at a historically low level.

The current account, which shifted from a surplus in 2010 to a deficit in 2011, deteriorated further in 2012 and early 2013. Imports remained robust, underpinned by resilient domestic demand, while exports have suffered from the weakening of still high copper prices and lower demand in the euro area. The current deficit is financed mostly by foreign direct investment (FDI) (about half to the mining sector), though within FDI, the share of intercompany loans has increased significantly in recent years. Both gross capital inflows, in particular FDI, and outflows increased significantly in 2012, but net inflows declined as a result of increased portfolio

[1] Under Article IV of the IMF's Articles of Agreement, the IMF holds bilateral discussions with members, usually every year. A staff team visits the country, collects economic and financial information, and discusses with officials the country's economic developments and policies. On return to Headquarters, the staff prepares a report, which forms the basis for discussion by the Executive Board. At the conclusion of the discussion, the Managing Director, as Chairman of the Board, summarizes the views of Executive Directors, and this summary is transmitted to the country's authorities. An explanation of any qualifiers used in summings up can be found here: http://www.imf.org/external/np/sec/misc/qualifiers.htm.

The executive Board takes decisions under its lapse-of-time procedure when the Board agrees that a proposal can be considered without convening formal discussions.

outflows by Chilean pension funds. The real effective exchange rate is broadly in line with fundamentals.

Inflation has been low and declining, as a result of the peso appreciation last year, an increase in labor productivity, and falling energy prices. There is also downward bias in at least one component of the consumer price index, but this bias does not seem to materially change the inflation picture. Inflation expectations remain anchored at the official target of 3 percent. The central bank has left the policy rate at 5 percent, a broadly neutral rate, since January 2012.

The government recorded a small fiscal surplus in 2012 as it saved revenue overperformance and underspent the budget. The structural deficit improved to ½ percent of GDP, beating the authorities' 1 percent target two years ahead of time. The fiscal impulse—measured as the change in the non-mining structural primary balance—was negative (mildly) for the third year in a row, provided some welcome dampening effect. The 2013 budget targets a structural deficit of 1 percent, and would inject some fiscal impulse.

Macro-financial risks are contained. Despite strong domestic demand, capital inflows, and ample liquidity, there are no clear signs of generalized asset or credit bubbles. The banking system is sound−banks are well-capitalized and liquid, and nonperforming loans are low and fully provisioned. That said, there has been a marked increase in average loan-to-value ratios in mortgages since late 2011, and some mid-sized banks are expanding fast, with relatively high reliance on wholesale funding.

Real GDP is expected to grow 4.6 percent in 2013, broadly in line with potential growth. The current account deficit is expected to widen further in 2013 amid lower copper prices. Inflation is expected to move toward 3 percent over the next year. The near-term challenge is to support a soft landing in the context of a widening current account deficit, swelling capital inflows, and an uncertain outlook for copper. Boosting productivity growth is a key medium-term challenge.

Executive Board Assessment

In concluding the 2013 Article IV consultation with Chile, Executive Directors endorsed staff's appraisal, as follows:

Growth in recent years has been strong, led by domestic demand, but a slow down appears underway. Growth surprised on the upside in 2012 and on the downside in the first quarter of 2013. These ups and downs appear to be part of a bumpy transition toward a more sustainable rate of expansion in economic activity. The moderation in activity is also reflecting a shifting outlook for copper prices.

The main cloud over the strong performance is the rapid shift in the current account. The ballooning current account deficit and the increased reliance on debt financing have raised balance of payment risks. Still, staff's assessment is that the peso is on the strong side but not clearly overvalued.

Macroeconomic policies have been prudent. In recent years, fiscal policy has provided a welcome dampening effect on demand, thereby helping prevent overheating and a more substantial real appreciation and current account deterioration. Monetary policy has been on hold since early 2012 and is broadly neutral.

And macro-financial risks appear contained thanks in large part to the authorities' active supervision and monitoring. There are no clear signs of broad asset price or credit bubbles. Liquidity and solvency indicators and stress tests suggest that the financial sector is generally healthy and robust. That said, some mid-sized banks are expanding fast, with relatively high reliance on wholesale funding. As for real estate, aggregate price developments do not suggest bubbles but continued close monitoring will be important, including of commercial real estate construction which remains very dynamic.

The near-term priority is to support the ongoing moderation in domestic demand and activity, amid swelling capital inflows and a widening current account deficit. In this context, a neutral fiscal stance would be desirable and can be achieved through a tight grip on spending in the remainder of the year, and saving any revenue over performance. This would bring the structural balance closer to zero.

There is a great deal of uncertainty and risks surrounding the outlook stemming both from real and financial channels. The main downside risks to the outlook are a sharp and lasting drop in copper prices, re-emergence of financial stress in the euro area, or a sudden stop in capital inflows. At the same time, there is also a chance that domestic demand does not abate as envisaged, raising overheating risks.

Monetary policy should be ready to respond to changes in the economic outlook and fiscal automatic stabilizers should be allowed to operate unimpeded. As a last resort, there is ample space for fiscal stimulus if output falls. The floating currency provides a natural buffer against external shocks and the ample reserves could be used to avoid excessive depreciation.

Further strengthening of the medium-term fiscal framework is appropriate. Staff recommends aiming for a small structural surplus over the next few years, as this would help maintain strong fiscal buffers while stabilizing net assets as a share of GDP. The establishment of the Fiscal Council is welcome as it would further strengthen the transparency of the fiscal framework. Staff also commends plans to incorporate long-run expenditure and revenue projections into the budget framework.

The staff applauds the authorities' proactive work on financial stability issues. Recent progress in strengthening supervision of nonbanks and financial conglomerates is welcome. Current legislative initiatives, notably the General Banking Law, the law on the Financial Stability Council, the law on risk-based supervision of insurance companies, the legislation to expand the credit registry, and the corporate bankruptcy law, will strengthen prudential oversight. Looking ahead, the broad-based banking regulation reform scheduled for this year will be an important improvement. However, addressing pending Financial Sector Assessment Program (FSAP) recommendations, including a legal framework for consolidated oversight of financial conglomerates, should remain a priority. And while there are no systemic risks that warrant immediate action, the authorities should consider extending some form of loan-to-value and debt-to-income regulation to all mortgages.

The medium-term challenge is to foster sustained and inclusive growth. Boosting productivity and labor force participation will be needed to sustain growth without the benefit of the tailwind of rising copper prices and with slowing growth of working-age population. To this end, key areas for further reform include: make access to high-quality education and training more equal, and consider well-targeted social transfers to spread growth benefits; promote investments in the energy sector to ensure sufficient and competitive energy supply; and make the labor market more flexible.

A prompt and transparent resolution of the recent statistical controversies would protect Chile's long tradition of high quality data. Staff welcomes authorities' outreach efforts among local analysts and data users, and their plans to obtain advice from international experts.

Chile: Selected Social and Economic Indicators

GDP (2012), in billions of pesos	130,466	Quota	
GDP (2012), in billions of U.S. dollars	268.2	In millions of SDRs	856
Per capita (U.S. dollars)	15,410	In percent of total	0.36%
Population (2009), in millions	17.4	Poverty rate (2011)	14.4
Main products and exports	Copper	Gini coefficient (2011)	0.52
Key export markets	China, Euro area, U.S.	Literacy rate (2011)	98.9

						Proj.	
	2008	2009	2010	2011	2012	2013	2014
(Annual percentage change, unless otherwise specified)							
Output							
Real GDP	3.1	-0.9	5.7	5.8	5.6	4.6	4.6
Total domestic demand	9.1	-5.5	13.4	9.1	7.2	6.1	5.1
Consumption	4.3	0.7	9.6	8.0	5.7	5.9	4.8
Private	5.1	-0.9	10.7	9.0	6.0	5.6	5.0
Public	0.3	9.1	4.4	3.2	3.9	6.9	3.8
Investment	21.4	-23.7	27.4	13.1	10.5	9.3	4.2
Fixed	18.3	-12.2	12.1	14.8	12.0	8.3	4.2
Private	20.1	-17.6	17.8	15.7	13.5	7.7	4.4
Public	3.5	37.5	-18.5	7.8	-0.1	14.0	3.3
Inventories 1/	…	-3.1	2.9	-0.2	-0.1	…	…
Net exports 1/	-4.5	4.4	-7.6	-3.9	-1.7	-0.9	-0.5
Exports	-0.6	-4.8	2.5	5.0	0.9	3.9	4.3
Imports	11.8	-16.2	25.8	14.6	4.8	5.5	4.9
Employment							
Unemployment rate (annual average) 2/	7.8	10.8	8.2	7.1	6.4	6.5	6.6
Consumer prices							
End of period	7.1	-1.5	3.0	4.4	1.5	2.6	3.0
Average	8.7	1.5	1.4	3.3	3.0	1.8	3.0
(In percent of GDP, unless otherwise specified)							
Public sector finance							
Central government revenue	24.2	19.0	21.5	22.6	21.9	22.0	21.5
Central government expenditure	20.3	23.4	22.0	21.4	21.4	22.0	21.8
Central government fiscal balance	3.9	-4.4	-0.5	1.3	0.6	-0.1	-0.3
Structural fiscal balance 3/	-1.5	-4.3	-2.5	-0.9	-0.6	-0.6	-0.8
Nonmining structural primary fiscal balance 4/	-2.6	-7.1	-5.5	-3.1	-2.9	-3.3	-2.9
Fiscal impulse	1.5	4.5	-1.6	-2.3	-0.2	0.4	-0.4
Public sector net debt	-16.8	-6.5	-2.2	-4.9	-1.7	-1.7	-0.2
Public sector gross debt	24.7	27.5	25.9	34.8	34.2	34.0	33.8
Central government gross debt	4.9	5.8	8.6	11.1	11.9	12.2	12.5
Of which, share of FX-denominated debt (in percent)	40.0	22.8	17.3	17.2	16.1	13.0	11.4
Money and credit							
Broad money (percent change)	18.6	-5.3	9.3	18.5	7.6	…	…
Credit to the private sector (end of period, percent change)	18.7	-1.4	7.1	16.9	12.1	…	…
3-month central bank bill rate (percent)	7.3	1.8	1.7	4.9	5.1	…	…
Balance of payments							
Current account	-3.2	2.0	1.5	-1.3	-3.5	-4.7	-4.2
Current account (in billions of U.S. dollars)	-5.8	3.5	3.2	-3.3	-9.5	-13.4	-12.9
Foreign direct investment inflows	8.6	7.5	7.1	9.1	11.3	9.8	9.7
Gross international reserves (in billions of U.S. dollars)	23.2	25.4	27.9	42.0	41.6	41.6	41.6
In months of next year's imports of goods and services	5.5	4.4	3.9	5.6	5.3	5.1	4.9
Gross external debt	35.5	41.8	38.9	39.3	43.9	43.3	43.0
Public	6.5	7.7	7.9	8.2	9.4	9.4	9.4
Private	29.0	34.1	30.9	31.2	34.5	33.8	33.6
(Annual percentage change)							
Exchange rate							
Real effective exchange rate (real appreciation +)	1.8	-2.2	5.9	0.9	3.4	…	…
Terms of trade	-15.0	4.3	22.0	1.2	-5.2	-3.0	0.5

Sources: Central Bank of Chile, Ministry of Finance, Haver Analytics, and IMF staff estimates and projections.

1/ Contribution to growth.
2/ The methodology to compute the unemployment rate changed in 2009.
3/ Headline balance adjusted for the economic and copper price cycles.

4/ In percent of non-mining GDP.