

Latam Daily: Hawkish but Flexible Hold from Chile's BCCh; Colombia Jobs Recovery

- Chile: BCCh held at 0.5% with shift in forward guidance, better growth prospects, stable inflation outlook; we bring forward our projected first rate hike from Q2-2022 to Q1-2022
- Colombia: Labour market resumed its gradual recovery in February

CHILE: HAWKISH, BUT MORE FLEXIBLE HOLD FROM THE BCCh

I. Central bank holds and maintains a highly stimulative, but slightly more hawkish and flexible stance

The Board of the BCCh met on Tuesday, March 30, and voted unanimously to hold its benchmark policy rate at its record low of 0.5%, where it has been since March 30, 2020 at the outset of the pandemic. In its [statement](#), the Board shifted its forward guidance in a slightly more hawkish, but more flexible and data-dependent direction amidst signs that growth is coming in a bit stronger than anticipated in the December [Monetary Policy Report](#) while the inflation outlook remains stable.

The Board's characterization of the Chilean economy's ongoing recovery and the central bank's stance prompt us to bring forward our expectation of a first rate hike from Q2-2022 to Q1-2022. While we still expect 100 bps of policy rate increases during 2022 to take the policy rate to 1.50% by December of next year, we previously saw these hikes backloaded into H2-2022; instead, we now have them cautiously profiled at a steady pace of 25 bps in each quarter of 2022 (chart 1). Given the central bank's current assessment of the economy and the Board's still broadly stimulative tone, we don't expect it to telegraph a forthcoming change in policy rates until its September 2021 meeting, with the first adjustment in the headline rate likely to come at the Board's January 2022 meeting.

This projected path for the BCCh's rate normalization process would still be stimulative under our revised outlook. It would keep the central bank's key policy rate markedly below its new nominal neutral level, which we estimate at 3.5%, for all of 2022 and a significant part of 2023. However, we now see less justification for keeping the rate at its technical minimum of 0.5% given Chile's ongoing economic recovery that should generate increasing traction on employment.

Looking in more detail at the statement, we note the following key developments that inform our revised outlook for the BCCh's rate path.

- Slightly more hawkish, but also more flexible forward guidance.** The Board remained clear that monetary policy will continue to be "highly stimulative", as it previously noted in its [January statement](#). However, in January, the Board guided that the monetary-policy rate will remain at its minimum of 0.5% "for a large part of the two-year monetary-policy horizon"; in contrast, the March statement advises more conditionally, and flexibly, that the policy rate would remain at its technical minimum "until the economic recovery takes hold and spreads to the most lagging spending components, which will still take several quarters".

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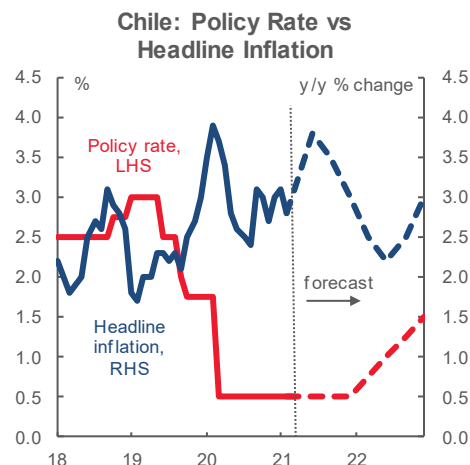
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Chart 1



Sources: Scotiabank Economics, BCCh, INE.

- **Better growth prospects.** The Board pointed out that data from end-2020 and early-2021 point to faster growth than had been anticipated in the December *Monetary Policy Report*. Recent quarantine measures are likely to have only second-order effects on economic activity, but the Board noted that employment continues to lag the cycle, which augurs against an earlier normalization in policy rates.
- **Stable inflation outlook.** Inflation is clearly not a concern for the Board. While it noted month-to-month fluctuations in both directions, it also observed that inflation remains stable around the 3% y/y target and that inflation expectations remain anchored.
- **Greater external impulse.** The Board concluded that the external environment has improved for Chile owing to better economic prospects in its trading partners, improved terms of trade, and still-favourable financial conditions. The statement took specific note of some better-than-expected economic indicators that reflected the world's adaptation to the pandemic, US fiscal package approved a few weeks ago and increases in commodity prices, including copper. Better international economic conditions should translate into improved local growth prospects in 2021.

II. March *Monetary Policy Report* revised forecast for 2021 real GDP growth to 6.0–7.0% y/y range

A day after the Board's rate decision, the BCCh staff released its quarterly *Monetary Policy Report* on Wednesday, March 31. Most notably, the staff raised its forecast for real GDP growth in 2021 from a range of 5.5–6.5% y/y in the December *Report* to 6.0–7.0% y/y. The change reflected better recent data, an improved external environment, and new fiscal stimulus versus the impact of new quarantine measures. We had anticipated a forecast revision along these lines and we maintain our own projection of 7.5% y/y real GDP growth in 2021. No substantial changes were made to subsequent years, with the baseline growth projections for 2022 maintained at 3.0–4.0% y/y and for 2023 at 2.5–3.5% y/y, somewhat below estimates for long-term potential. Table 1 shows that our baseline forecasts are slightly rosier than those of the BCCh owing to our somewhat more optimistic outlook for investment in 2021.

According to the central bank, the Chilean economy has been making progress in its recovery process since the strong shock caused in 2020 by the pandemic. Last year ended with greater dynamism than anticipated, which reflected adaptations to public-health restrictions by businesses and households, as well as support from substantial monetary and fiscal boosts. Thus, although in the short-run we anticipate a brief decline in activity due to the recent tightening of sanitary measures, the prospects for 2021 have been consolidating, underpinned by sustained progress on vaccinations, greater impulses from external sources, and the continuity of expansionary domestic policies. However, significant risks remain related to the unprecedented shocks the Chilean and global economies have suffered. On the one hand, the epidemiological evolution of COVID-19 remains complex, which adds uncertainty to the timing and way in which public-health restrictions will be relaxed. On the other hand, the recovery continues to be heterogeneous, with still relevant lags in the sectors that most intensively rely on social interactions—which helps to explain the significant gaps that persist in the labour market.

Investment has shown a slower recovery than consumption, affected by a high degree of uncertainty in the development of the pandemic and the financial burden it has imposed on companies. In the second half of 2020, however, several large investment projects that had stopped were re-activated and recent data show greater dynamism in imports of capital goods. Nevertheless, the speed of the recovery in investment has been slow and a significant acceleration of its non-mining private component is not expected in the central bank's baseline scenario.

Regarding monetary policy, the *Report* notes that, despite the improving economic outlook, convergence of inflation to the 3% y/y target during the two-year policy horizon requires the central bank's stance to remain highly expansionary. As noted in the Board's March meeting statement, the benchmark rate will remain at its minimum of 0.5% until the recovery of the economy is consolidated and spreads to spending components that are lagging the most, which is expected to take several quarters.

Table 1		
Chile: Baseline 2021 Forecasts, BCCh vs Scotiabank Economics		
	BCCh	Scotiabank
GDP, y/y % change	6.0–7.0	7.5
Consumption, y/y % change	11.5	10.2
Investment, y/y % change	9.2	12.2
Inflation, y/y % change eop	3.0	3.0
Sources: Scotiabank Economics, BCCh <i>Monetary Policy Report</i> , March 2021.		

—Jorge Selaive, Carlos Muñoz, & Waldo Riveras

COLOMBIA: LABOUR MARKET RESUMED ITS GRADUAL RECOVERY IN FEBRUARY

On Wednesday, March 31, DANE reported that the February nationwide unemployment rate came in at 15.9%, still well above February 2020's 12.2%. At the same time, the urban unemployment rate (i.e., for 13 major cities) was 18.1%, higher than the 17.7% expected by market consensus and significantly elevated compared with 11.5% in February 2020. The seasonally adjusted series revealed that the national unemployment rate improved slightly to 14.6% versus 14.8% in January 2021, while the urban unemployment rate deteriorated from 16.1% in January 2021 to 16.6% in February (chart 2).

Despite January's imposition of new lockdown measures that caused a pause in improving labour-market dynamics, employment resumed its recovery trend in February. Total active jobs in February were down by 1.2 mn positions relative to the pre-pandemic period, the smallest gap since the public-health crisis began. But, as expected, marginal gains in employment are gradually declining. Employment numbers remain down principally in Colombia's cities: urban areas accounted for about 90% of ongoing total job losses in February.

From a sectoral perspective, year-on-year employment losses as of February 2021 were concentrated in the leisure sector (-227K), and the public administration, education, and health sectors (-264k), which together accounted for 40% of the total annual employment contraction (chart 3). Employment in these sectors is predominantly tilted toward women, which underpins the widened gap between the unemployment rate for women (21.7% versus 16.5% one year ago) and men (11.7% versus 9.0% in February 2020).

The evolving quality of jobs remains an important concern. Growth in informal jobs continued to lead the overall recovery in February (chart 4). We attribute these dynamics to the relative flexibility of the informal economy. However, it is worth noting that informality increased at a slower pace in urban areas in February 2021 and its share stood at 46.9%.

Summing up, February's labour market data showed that Colombia resumed its recovery path. However, monthly job gains are slowing as some structural losses are appearing under the economy's "new normality", especially in sectors that are still operating below capacity and that account for important shares of the female labour force. We believe the employment recovery will continue at a gradual pace, with a slower decline in the unemployment rate as the currently inactive population returns to the labour market.

—Sergio Olarte & Jackeline Piraján

Chart 2

Colombia: Nationwide and Urban Unemployment

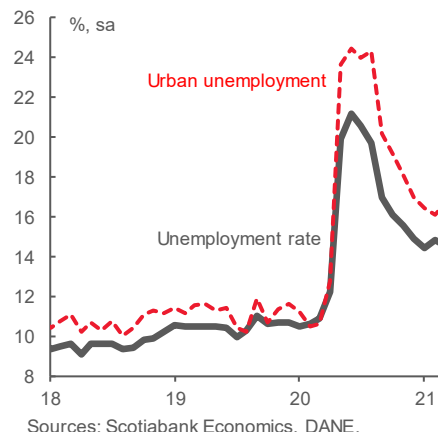


Chart 3

Colombia: Employment Growth, Contributions by Sector

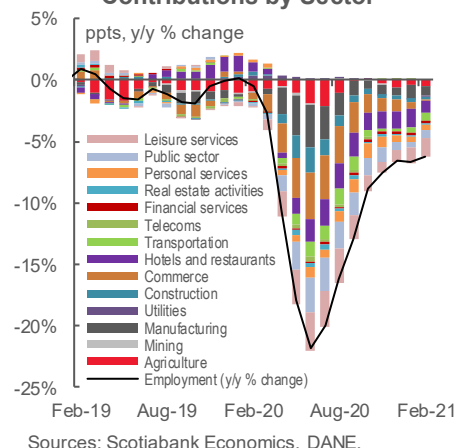
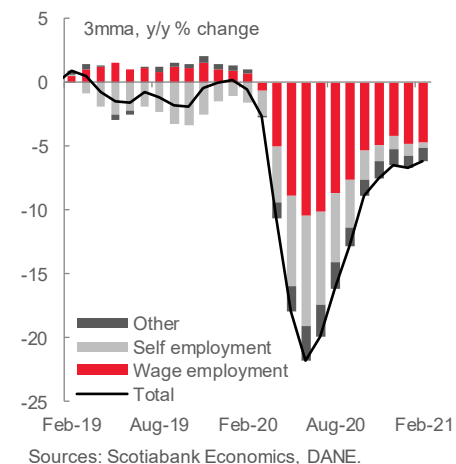


Chart 4

Colombia: Employment Growth



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