

CHILE

Key conditions and challenges

Table 1 **2020**

Population, million	19.1
GDP, current US\$ billion	249.7
GDP per capita, current US\$	13064.1
Upper middle-income poverty rate (\$5.5) ^a	3.6
Gini index ^a	44.4
School enrollment, primary (% gross) ^b	102.2
Life expectancy at birth, years ^b	80.0

Source: WDI, Macro Poverty Outlook, and official data.

Notes:

(a) Most recent value (2017), 2011 PPPs.

(b) Most recent WDI value (2018).

Chile is expected to resume growth in 2021, as the government continues the stimulus and mobility restrictions are eased with the vaccination rollout. Chile's medium-term prospects depend on its capacity to meet demands for more equitable access to opportunities while preserving strong macroeconomic management, restoring private sector confidence, and unlocking productivity gains for a more diversified economy. The same policies would be instrumental in reducing poverty caused by the pandemic and set the ground for more inclusive growth.

Over the last few decades, Chile achieved important progress on main economic and social indicators. Progress came on the back of a conducive business environment, strong institutions, and sound macroeconomic management. However, after achieving high-income status, the existing policy framework has been insufficient to foster productivity and economic diversification, increase labor opportunities, and further tackle deep-rooted inequality.

The pandemic-led recession in 2020 has amplified demands for higher social expenditure and reforms that preceded the social unrest of 2019, resulting in the vote to rewrite the constitution. The reform process adds to the political uncertainty already associated with subnational elections (April 2021), primaries elections (July 2021), the general election (November 2021), and a referendum on the new constitution (2022).

The constitutional reform process opens opportunities to reform institutions and address long-standing structural challenges. Long-term implications will depend on the balance between fulfilling demands for more equitable policies and other medium-term challenges such as preserving a traditionally sound macroeconomic environment, restoring private sector confidence, and unlocking productivity gains and diversification. Chile still

needs to tackle long-standing barriers to productivity such as low competition, innovation, education quality, and female labor participation.

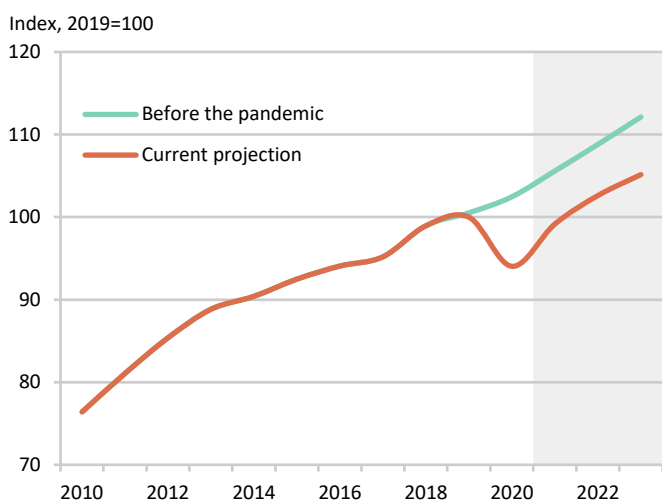
Recent developments

GDP contracted 6.0 percent in 2020, although looser lockdown measures allowed a partial recovery towards the end of the year. Over one million jobs were lost, affecting mostly women and workers in commerce, agriculture, and hospitality. The effects of mobility restrictions and uncertainty were only partially offset by one of the largest policy responses in the region. This response included cash transfers, a job retention scheme, tax deferrals and reductions, liquidity provisions and guarantees, and early withdrawals from pension funds.

The Central Bank reduced the policy rate to 0.5 percent and implemented unconventional monetary policies. Although a food price surge increased annual inflation to around 3.0 percent in recent months, accommodative monetary policy is expected to continue into the medium-term.

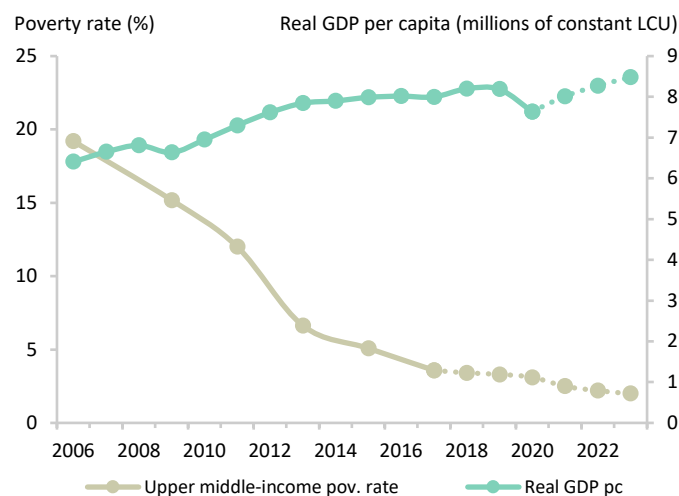
In conjunction with the economic contraction, the fiscal deficit increased to 7.5 percent of GDP in 2020, the largest in over three decades. Although the authorities tapped into fiscal buffers, public debt rose from 28 percent in 2019 to 33 percent in 2020. Additional measures to support the recovery include measures to streamline regulations, higher public investment, tax

FIGURE 1 Chile / Real GDP



Sources: Central Bank of Chile and staff's estimates.

FIGURE 2 Chile / Actual and projected poverty rates and real GDP per capita



Sources: World Bank. Notes: see Table 2.

incentives for firms, hiring subsidies, and transfers to low-income households.

As imports collapsed, the current account recorded a sizable surplus in 2020. However, the Central Bank had to intervene to prevent a larger depreciation linked with subdued private external inflows.

Targeted social protection measures cushioned the effects of the crisis. In 2020, the share of the population living on less than US\$5.5 a day and the inequality Gini coefficient are estimated to have remained stable at 3.3 and 44.3 percent, respectively. However, these estimates mask a downward slide in household income among the vulnerable and lower middle class, especially in female-headed households. Using the national poverty line, poverty is expected to have increased from 8.1 to 12.2 percent, meaning that about 780 thousand people are expected to have fallen into poverty.

Outlook

Although the second wave of the pandemic triggered some new mobility restrictions, the economy is projected to

rebound by 5.5 percent in 2021 on the back of a successful vaccine rollout—Chile is the fourth country globally and the leader in the region in terms of per capita vaccination rates. Although uncertainty will curb private investment recovery, domestic demand will be spurred by accommodative policies, including the lagged effects of the early withdrawals from the pension funds. Exports would benefit from a strong recovery in advanced economies, China, and higher copper prices.

After that, GDP growth is expected to gradually decrease to 2.5 percent in 2023 as the output gap is reduced, allowing for fading out of the policy stimulus. However, medium-term growth could be constrained by uncertainty around the constitutional reform.

After sustaining a positive fiscal impulse in the upcoming two years, the government is expected to start a gradual consolidation to reach the medium-term structural balance goal. Revenue growth will account for most of the fiscal consolidation as fiscal expenditures will remain above pre-pandemic levels due to higher social spending resulting from the constitutional reform. Maintaining key social safety measures will be needed to ensure

an inclusive recovery. However, public debt is projected to increase to 40 percent of GDP by 2023, the highest in the last three decades.

The recovery of imports and factor payments abroad will shift the current account balance into a deficit over the projection period. However, this deficit is expected to be financed by private capital flows, mainly foreign investment, limiting pressures on the exchange market.

The labor market recovery and cash transfers are expected to reduce poverty in 2021. The share of the population living on US\$5.50 a day may be reduced slightly to 2.7 percent. Nevertheless, it will take longer for the incomes of the middle class to recover, and poverty rates based on the national poverty line are not expected to revert to the pre-pandemic level until 2022.

TABLE 2 Chile / Macro poverty outlook indicators

(annual percent change unless indicated otherwise)

	2018	2019	2020 e	2021 f	2022 f	2023 f
Real GDP growth, at constant market prices	3.9	1.1	-6.0	5.5	3.5	2.5
Private Consumption	3.7	1.1	-8.5	6.3	3.7	2.7
Government Consumption	4.3	-0.3	-1.9	-4.6	3.3	2.4
Gross Fixed Capital Investment	4.8	4.2	-15.6	17.9	5.6	1.8
Exports, Goods and Services	5.0	-2.3	-4.8	4.5	3.3	1.7
Imports, Goods and Services	7.9	-2.3	-15.4	9.9	5.3	1.5
Real GDP growth, at constant factor prices	4.0	1.2	-6.0	5.5	3.5	2.5
Agriculture	1.7	-1.6	-2.2	3.2	2.2	2.2
Industry	4.9	0.4	-3.2	4.6	3.1	2.9
Services	3.6	1.7	-7.5	6.0	3.7	2.3
Inflation (Consumer Price Index)	2.4	2.6	3.0	3.0	3.0	3.0
Current Account Balance (% of GDP)	-3.6	-3.9	1.5	0.7	-1.1	-1.9
Net Foreign Direct Investment (% of GDP)	2.3	1.2	-0.3	1.9	2.1	2.1
Fiscal Balance (% of GDP)	-1.5	-2.7	-7.5	-3.2	-3.1	-2.2
Debt (% of GDP)	25.6	27.9	33.0	34.5	37.7	40.1
Primary Balance (% of GDP)	-0.6	-1.8	-6.6	-2.3	-1.9	-0.9
Upper middle-income poverty rate (\$5.5 in 2011 PPP)^{a,b}	3.4	3.3	3.3	2.7	2.3	2.1

Source: World Bank, Poverty & Equity and Macroeconomics, Trade & Investment Global Practices.

Notes: e = estimate, f = forecast.

(a) Calculations based on SEDLAC harmonization, using 2017-CASEN.Nowcast: 2018-2020. Forecast are from 2021 to 2023.

(b) Projection using and microsimulation model for 2020.