

The Chilean Economy in 2001

During the year 2001, the Chilean economy recorded a moderate growth, with external factors that contributed to delaying the onset of reactivation. The gross domestic product grew only 3 percent, well below the 5.4 percent achieved in 2000 and the 6.5 percent average that the country recorded throughout the 90s. The domestic demand, in turn, showed little dynamism, falling 0.5 percent during the year. This economic performance may be explained by both domestic and external factors. Among the latter, the most relevant are a global slow-down, which became sharper after the terrorist attacks on the United States; a deterioration of exchange rates, which exhibited a 7 percent drop; and the instability in Argentina.

As regards foreign accounts, both exports and imports showed negative variations, falling 4 and 7 percent, respectively. Although the trade balance recorded a US\$ 1,550 million surplus, lower volumes of foreign trade were evident. The trade contraction did not generate any financial problems for the country, and its current account, traditionally a negative one, was easily financed without the need to significantly resort to international reserves, which now stand at some US\$ 14,000 million.

On the other hand, inflation is being kept under

control, reaching only 2.6 percent during the year, the lowest rate since 1939. This result was achieved in spite of successive revaluations of the American dollar. To keep said control, the Central Bank reduced the nominal interest rate to a historical low of 6.5 percent. In this area, we should highlight the decision taken by the authority in terms of fixing a nominal rate of interest, to thus make further progress toward economic de-indexation. Although this is considered a positive measure, its introduction had undesirable transitory effects, particularly in the financial system and in capital markets in general.

No significant changes regarding the present situation are expected for the year 2002. Projections indicate a similar growth rate to that achieved in 2001, but with an up-trend. This would be achieved based on the eventual recovery of the world economy as from the end of the first half, on an improvement in our domestic situation, and on the gradual stabilization of the Argentine economy. Within this scenario, no significant changes are expected as regards the unemployment rate, which is estimated at around 9 percent, a figure quite similar to that recorded in 2001.

Among positive outlooks for next year is a relative stability in the exchange rate, which would stimulate

exports and export substitutions. In fact, it is likely that we will see higher export volumes coupled with price improvements, something that did not happen in 2001. Thus, the current account deficit is forecast at approximately 1.5 percent of domestic product; this figure would be easily financed without need to use international reserves. Finally, forecasts indicate that the inflation rate would remain within the range observed over the last months of 2001 reaching a 3 percent approximately in 2002.

The Banking Sector

Despite economic stagnation, in 2001 our bank placements showed an annual growth of 7 percent approximately. However, it should be noted that most of this growth does not reflect a higher lending activity, but rather a higher value of the US dollar-denominated portfolio. Although the bad debt exhibited one of the highest levels in recent years, it was kept under relative control at 1.7 percent. In turn, the risk index at year-end reached 2.4 percent.

As regards results, these showed a major improvement in relation to 2000, with the highest returns of the recent years. This good performance, compared to 2000, was mainly due to better spreads, higher incidence of commissions on services, and lower charges for

provisions and write-offs. Further, in spite of higher operating-support expenses, the sector as a whole exhibited better efficiency indicators.

In the regulatory context, we expect new amendments to the capital market legal framework, which should recognize the obvious benefits that greater progress toward a higher complementation of services offered by different intermediaries - such as banks, insurance companies, and pension fund administrators - would have for consumers. On the other hand, capital markets, just like all the rest of the economic sectors, would benefit from the subscription of a free-trade agreement with the United States. These two initiatives may lend renewed dynamism to the domestic banking sector.

In general, the outlook for the sector is good. We forecast a growth in lending operations and a gradual quality improvement in portfolios. On the other hand, like in the rest of Latin America and many other regions worldwide, the Chilean financial sector is tending towards the creation of larger banking institutions, which should lead to larger economies of scale and, therefore, to higher competitiveness. Finally, we should note that expense control and efficiency shall continue to be the strategic building blocks in our sector's development.