CHILE

THE ECONOMY REMAINS DEPENDENT ON THE MINING SECTOR

GDP growth is holding up rather well in Chile, buoyed by the mining sector and a solid domestic demand. The outlook is relatively favourable: inflation is contained, fiscal consolidation should continue and political risk remains moderate in the run-up to the presidential election at the end of the year. Lastly, apart from the announcements regarding the copper sector, the direct impact of the increase in tariffs imposed by the Trump administration on the Chilean economy is relatively low. Indirect effects, volatile commodity prices and uncertainties over the pace of progress in the global low-carbon transition, on the other hand, represent a very significant risk for the Chilean economy.

GROWTH HOLDS UP

Buoyed by the mining sector, economic activity held up rather well in Chile over the first four months of the year. GDP grew by 2.3% year-on-year in Q1, and the monthly activity index showed a further acceleration to 3.3% in April. The outlook remains rather favourable for the months ahead: we expect GDP growth to be close to 2.2% in 2025, after 2.4% in 2024.

Domestic demand should remain solid, supported by the recent increase in the minimum wage and a healthy job market. Following growth of 1.1% in 2024, household consumption rose by 1.5% y/-y in Q1. Nevertheless, the expected slowdown in global demand will translate into a slowdown in exports.

INFLATIONARY PRESSURES PERSIST

Inflation slowed in May for the second month in a row (to 4.4% y/y, after 4.5% in April), but remains above the 3% target set by the Central Bank, as it has been since July 2024. Underlying inflation remained stable at 3.7%. Inflationary pressures remain high, reflecting rising prices for certain utilities (electricity). The inflation rate should remain above target over the coming months. In June, the Central Bank again left its key rate at 5%, unchanged since December 2024.

FISCAL CONSOLIDATION CONTINUES

The budget deficit widened in 2024 (to 2.9% of GDP, exceeding the government's 2% target), as lower-than-expected revenues (particularly in the non-mining sector) were not fully offset by the spending cuts implemented at the end of the year.

At the end of April, the government raised its public deficit target for 2025 to 1.4% (from 1.1% previously) and announced additional spending reduction measures, over and above those set out in the initial budget. We expect the deficit to fall in 2025, but it is likely to be higher than the government's target: the approach of the presidential elections (in November 2025) makes it unlikely that strict spending reduction measures will be implemented.

In addition, a reform of the pension system (under discussion for over 15 years) was adopted at the end of January 2025. The main objectives were to improve coverage (many Chileans are totally or partially excluded from the current system), the lack of transparency in the management of private pension funds and, above all, the replacement rate (i.e., the percentage of working income received by an employee when he or she claims his or her pension rights). Currently, the replacement rate is around 38% for a man and 35% for a woman. This is well below the OECD average of 63%.

After significant concessions on the part of the government, the reform includes a further (gradual) 7 percentage point increase in the total contribution rate paid by employers (which, added to the current 10% rate financed by employees, would gradually bring Chile closer to the OECD average contribution rate of 18%), and an increase in the Guaranteed Universal Pension (PGU), while maintaining the principles of the Chilean individual capitalisation model. Another long-term objective is to rebuild retirement savings. These have fallen sharply following the multiple withdrawals authorised by the government at the time of the Covid-19 crisis to support business activity. Whereas they accounted for 80% of GDP in 2019, retirement savings assets accounted for 60% of GDP by the end of 2024.

According to government estimates, the total fiscal cost of the planned reforms could reach around 1% of GDP by 2032, and remain at this level thereafter. However, we expect the net cost to be slightly lower.

FORECASTS

	2022	2023	2024e	2025e	2026e
Real GDP growth, %	2.4	0.2	2.4	2.2	1.8
Inflation, CPI, year average, %	11.6	7.6	3.9	4.5	3.0
Central Gov. balance / GDP, %	1.1	-2.5	-2.9	-1.8	-1.9
Public debt / GDP, %	38.0	39.4	41.7	42.4	42.6
Current account balance / GDP, %	-8.7	-3.5	-2.5	-2.6	-2.7
External debt / GDP, %	76.4	71.1	77.5	76.5	76.6
Forex reserves, USD bn	39.1	46.3	47.8	46.3	47.1
Forex reserves, in months of imports	4.9	7.0	7.3	7.5	7.6

TABLE 1

e: ESTIMATES & FORECASTS
SOURCE: BNP PARIBAS ECONOMIC RESEARCH

CHILE : TOTAL AND COPPER EXPORTS

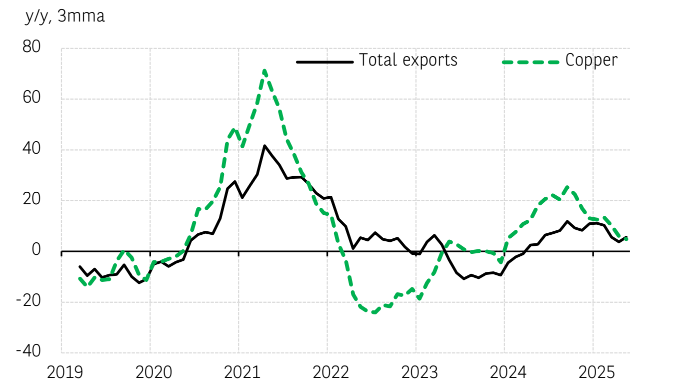

CHART 1

SOURCE: CENTRAL BANK, BNP PARIBAS

In fact, the increase in the PGU should be partly offset by the gains linked to the anti-tax evasion bill.

All in all, the government's objective of achieving structural balance by 2029 seems difficult to attain: financial support for Codelco (the national copper mining company) could be substantial in the years ahead (its debt has increased over the past five years, between the need for massive investment to maintain infrastructure and the decline in production for technical reasons). In addition, social spending will remain high, whatever government is elected at the end of the year, while the revenues generated by tax reform remain uncertain.

Central government debt increased but remained moderate, standing at 41.7% of GDP in 2024 (versus 28% of GDP in 2019). This dynamic is set to continue, with debt reaching 42.6% of GDP in 2026.

THE COPPER SECTOR AWAITS TRUMP'S DECISIONS

As with most countries in the region (excluding Mexico), the Trump administration has imposed 10% «reciprocal» tariffs on goods from Chile.

To date, the direct impact on the Chilean economy has been limited: on the one hand, exports to the United States account for only 17% of total Chilean exports, or around 5% of GDP (compared with almost 40% of total exports to China, the country's leading trading partner). Secondly, as the copper sector is not currently subject to taxes, the effective rate for Chile is only 5%.

However, Chile is highly exposed to fluctuations in raw material prices: the country is the world's leading producer and exporter of copper and the second largest producer of lithium (behind Argentina). The mining sector in its broadest sense (to which copper makes a very large contribution) accounts for over 18% of GDP and just over 55% of total exports.

Copper prices and Chilean exports rose sharply in the first few months of the year (in anticipation of potential tariff hikes announced by the US government), encouraging new investment in the Chilean mining sector.

According to forecasts by the International Energy Agency, demand for copper should remain robust in 2025 and 2026. Even in the event of a sharper-than-expected slowdown in Chinese demand (50% of global demand), the emergence of new markets (India and Vietnam, in particular) should keep global demand buoyant. On the supply side, several technical problems and maintenance requirements will limit production in Peru, the Democratic Republic of Congo and Panama. Although the National Copper Commission has announced an increase in Chilean copper production of 3% per year in 2025 and 2026 (after several years of stagnation, also due to maintenance operations), this will not be enough to offset the global shortage.

At the beginning of June, the Trump administration's announcements regarding the steel and aluminum sector rekindled fears of higher copper tariffs. In our central scenario, these threats will have no effect: around 12% of Chilean copper exports are destined for the USA, while Chilean copper accounts for around 60% of US copper imports. Therefore, if additional tariffs were imposed specifically on copper, the US would mainly harm its own importers and users, while remaining heavily dependent on Chile.

CHILE : INFLATION AND POLICY RATE

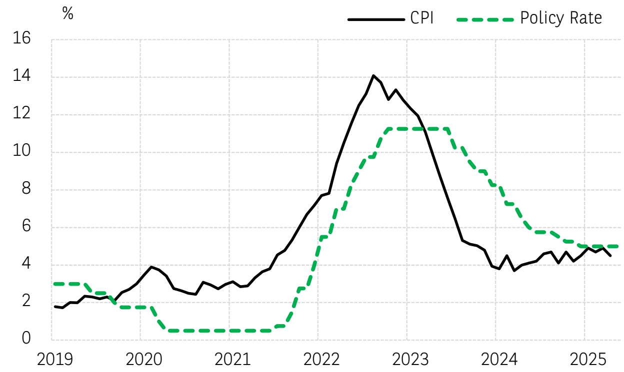

CHART 2

SOURCE: CENTRAL BANK, BNP PARIBAS

What's more, with over half of the world's refining capacity located in China (or, as is the case in Chile, owned by Chinese companies), raising tariffs on a critical material would likely result in a substantial rise in geopolitical tensions. The Chilean government could come under strong pressure from the Trump administration to reduce its economic ties with China, its biggest trading partner, and, above all, the main player in the entire value chain of critical materials, and mainly copper and lithium.

In the medium term, the possible slowdown in the pace of progress in the global ecological transition (linked in particular to the Trump administration's economic policy), synonymous with lower demand for copper, represents a significant risk for the Chilean economy. In particular, copper and lithium prices have a direct impact on tax revenues and may have repercussions on business activity, including in non-mining sectors.

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