



CHILE

OUTLOOK 2026

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1.0 Executive summary

Chile steps into 2026 under new leadership following conservative candidate José Antonio Kast's victory in the December 14 presidential runoff, in an abrupt – though largely anticipated – ideological pivot that will reshape the country's political and economic trajectory. Whilst markets have rallied on expectations of pro-business reforms and fiscal discipline under the incoming Kast administration, Chile's president-elect will inherit stubborn structural challenges that constrain the country's ability to achieve growth rates sufficient to meet heightened social expectations.

Kast's triumph over Communist Party candidate Jeannette Jara, following his second-place finish in the November 17 first round, consolidated right-wing voters around his platform of fiscal discipline, security enforcement, and immigration control. The president-elect has assembled a formidable economic team including former Finance Minister Felipe Larraín and ex-Central Bank Governor Vittorio Corbo, promising market-friendly policies that resonate with investors anxious about fiscal sustainability under the outgoing Gabriel Boric administration.

Yet Kast's hardline social agenda, including plans to eliminate abortion access and force expelled migrants to pay for their own deportation, threatens to reignite the tensions that sparked Chile's 2019 social uprising.

The economic fundamentals the Kast administration will inherit present a mixed picture. Chile's GDP expanded 2.9% between September 2024 and September 2025, with investment growth surging 10% in the third quarter—the strongest performance since 2012, excluding the post-pandemic rebound. The Central Bank has successfully guided inflation back towards its 3% target, with two-year expectations now anchored at that level, whilst the financial system remains stable and foreign investor confidence appears robust.

However, third-quarter growth of 1.6% fell short of forecasts due to mining sector disruptions, underscoring Chile's continued vulnerability to commodity price volatility and operational setbacks in its dominant export industry. Fiscal consolidation will prove the incoming administration's most immediate challenge. Chile recorded deficits of 12.7% and 13.3% of GDP in 2023 and 2024 respectively, with debt approaching 43.2% of GDP—near the 45% threshold that business leaders consider a "prudent maximum." The Boric administration's 2026 budget projects a structural deficit of 1.1% of GDP, down from an estimated 2.2% in 2025, though analysts question whether revenue projections remain realistic after successive over-optimistic forecasts since 2023.

Kast pledged during the campaign to cut \$6bn in public spending within 18 months, a proposal critics argue would inevitably undermine social programmes whilst supporters insist will target "political expenditure" rather than benefits like the Universal Guaranteed Pension.

The structural backdrop remains sobering. Chile's average annual growth has decelerated from 6.2% in the 1990s to barely above 2% in recent years, a slowdown the IMF attributes to demographic headwinds, less favourable global conditions, and exhaustion of the easy productivity gains that characterised the country's earlier development phase. Forecasters project GDP expansion of 2.3-2.6% in 2025 and 2.2-2.3% in 2026—rates insufficient to generate the employment and income growth that could durably address social discontent. The OECD characterises the outlook as "fragile" and "subject to substantial risks," noting that increased global tariffs will gradually translate into higher prices whilst reducing consumption and investment.

External vulnerabilities compound domestic constraints. Chile's heavy dependence on copper exports leaves it exposed to global demand fluctuations and supply disruptions, as demonstrated by third-quarter mining setbacks that shaved a full percentage point off growth. Wells Fargo's November vulnerability assessment placed Chile among the world's currencies most at risk should US monetary policy trigger financial market disruption, modelling potential peso depreciation from 939 to 1,154 per dollar under stress scenarios. The IMF's August review of Chile's \$13.8bn Flexible Credit Line noted that external risks have intensified since the facility was approved in 2024, with the small open economy particularly susceptible to capital flow reversals triggered by escalating trade tensions.

Chile's external trade in 2025 remains strongly concentrated among a few key partners, with China and the United States at the forefront. In the first half of 2025, trade with partners under existing free-trade agreements accounted for over 96% of Chile's total external commerce, underscoring the pivotal role of preferential market access. China continued as Chile's largest trading partner, dominating as both the main destination for its mineral and agricultural exports and a leading source of imports of machinery and manufactured goods. The United States ranked as the second most important partner, especially for industrial and processed food exports, while also supplying significant imports of fuel and technology products.

The European Union collectively held a major share as the third partner, engaging with Chile through deep economic ties and reciprocal trade flows in metals, agriculture, and manufactured equipment. Other notable trading relationships in 2025 include the members of the Comprehensive and Progressive Agreement for Trans-Pacific Partnership (CPTPP) and Mercosur, which together help diversify Chile's export markets and supply sources. Chile's overall trade balance has remained positive, supported by strong mining exports — particularly copper — even as imports of capital goods and intermediate inputs grow with domestic investment and industrial activity. However, sectoral dynamics reveal both opportunities and fragilities.

State copper producer Codelco successfully raised \$1.4bn through October bond sales despite a fatal accident at its largest mine, demonstrating investor confidence in Chile's flagship exporter but also highlighting operational risks that could disrupt production. The telecommunications sector faces upheaval as Spain's Telefónica exits its Chilean operations, with América Móvil and local player Entel negotiating a joint acquisition bid that could trigger antitrust scrutiny if consolidation creates a dominant market position. Private debt markets expanded 3% in the first quarter as investors sought higher-yielding alternatives amid falling interest rates, though the sector's continued growth depends on maintaining economic stability and managing credit risks.

The immigration dimension adds complexity to Chile's political transition. An estimated 330,000 undocumented migrants, predominantly Venezuelan, now reside in the country, with many Chileans attributing rising violent crime to foreign gangs. Kast's campaign warning that migrants had "111 days to leave Chile voluntarily" has already triggered population movements, with Peru deploying military forces to its southern border as northward flows reverse a pattern that for years saw Chile serve as a premier destination for those fleeing Venezuela's crisis.

For 2026, the central scenario involves Kast assuming office with a mandate for fiscal consolidation and market-oriented reforms but limited congressional support for aggressive policy changes. Growth will likely settle in the 2.2-2.3% range as consumption moderates following 2025's recovery whilst investment faces headwinds from global uncertainty and domestic political tensions. Inflation should converge towards the 3% target by year-end, allowing the Central Bank to cautiously resume rate cuts to 4.25% as external risks remain elevated. The fiscal deficit will narrow modestly to perhaps 1.5-1.8% of GDP as spending restraint partially offsets revenue shortfalls, though achieving the 1.1% structural target appears increasingly optimistic absent additional adjustment measures.

The principal downside risk stems from social unrest should Kast pursue his most polarising agenda items aggressively. Elimination of abortion access, mass migrant deportations, and sharp spending cuts could trigger protests reminiscent of 2019, potentially disrupting economic activity and deterring investment despite the administration's pro-business orientation. Conversely, markets could rally further if Kast demonstrates political skill in advancing fiscal consolidation whilst moderating his social conservatism, though his ideological rigidity during the campaign suggests this represents an upside scenario rather than the base case. Either way, Chile's ability to sustain higher growth trajectories depends less on short-term policy adjustments than on deeper structural reforms that successive administrations have struggled to implement.

1.0 Politics

1.1 The Kast victory

Chile's political landscape underwent a dramatic realignment with José Antonio Kast's victory in the December 14 presidential runoff against Communist Party leader Jeannette Jara. Despite trailing Jara in the November 17 first round—27% to his 20%, with libertarian Johannes Kaiser capturing 14% and conservative Evelyn Matthei finishing fourth—Kast prevailed decisively as supporters of other right-wing candidates consolidated behind him. Markets celebrated immediately, with Chilean stocks surging 3.1% following the first-round results as investors anticipated a pivot towards fiscal discipline and market-friendly policies after four years of progressive governance under Gabriel Boric.

Kast's political profile defies simple categorisation. The 59-year-old father of nine is the son of a German immigrant who founded a sausage business after World War II, embodying both the entrepreneurial ethos of Chile's business community prizes and the social conservatism that alarms human rights advocates.

His brother served as a minister during Augusto Pinochet's 1973-1990 infamous dictatorship, a regime Kast has praised, cementing his credentials amongst Chile's unreconstructed right whilst marking him as beyond the pale for those who view that era as a dark chapter requiring continued reckoning. This polarising heritage has proven politically potent in a country where voters exhausted by crime and economic stagnation increasingly prioritise security and stability over progressive social reforms.

The sophistication of Kast's economic team contrasts sharply with the inflammatory rhetoric that characterises his campaign messaging. By assembling former Finance Minister Felipe Larraín, ex-Central Bank Governor Vittorio Corbo, previous Undersecretary of Finance Alejandro Weber, and former OECD chief economist Klaus Schmidt-Hebbel, Kast signalled that his administration would pursue orthodox macroeconomic management rather than the heterodox experiments investors feared under a Jara presidency. This pairing of social reaction with economic orthodoxy—reminiscent of Argentina's Javier Milei but without the latter's libertarian radicalism on monetary policy—appears calibrated to reassure markets whilst mobilising a base animated by cultural grievances and security concerns.

1.2 Immigration as electoral catalyst

No issue has proven more politically potent than immigration, with Kast building his campaign around pledges to restore order along Chile's porous northern border. The transformation has been stark: an estimated 330,000 undocumented migrants, predominantly Venezuelan, now reside in Chile, a surge that many Chileans blame for rising violent crime attributed to foreign gangs. Whilst the causal link between immigration and criminality remains contested, the perception has proven politically decisive, driving a rightward shift in voter sentiment that extends well beyond Kast's core supporters. Kast's proposed remedies represent the region's most aggressive immigration stance.

His promise to construct a Trump-style border wall along Chile's desert frontier with Bolivia captured headlines, but his operational threats carried greater immediate impact. In an October campaign video filmed at the Peruvian border, Kast issued an explicit warning: "You have 111 days to leave Chile voluntarily. If not, we will stop you, we will detain you, we will expel you." His pledge that expelled migrants would finance their own deportation—a logically dubious proposition that nonetheless resonated with voters—exemplified his willingness to advance maximalist positions that shift the Overton window on immigration policy.

The electoral mathematics proved compelling even for voters uncomfortable with Kast's rhetoric. With Kaiser's libertarian supporters and Matthei's conservative base overwhelmingly prioritising immigration control, Kast's path to consolidating right-wing support appeared straightforward. Jara's attempt to broaden her appeal by downplaying her Communist roots whilst proposing to end banking secrecy to combat organised crime failed to neutralise the immigration issue, leaving her vulnerable amongst swing voters prioritising security over ideological purity.

The immediate consequences of Kast's anti-immigration campaign have already manifested along Chile's borders. Peru deployed military personnel to patrol its southern frontier with Chile in early December, declaring a state of emergency as Venezuelan migrants increasingly fled northward—reversing a migration pattern that for years saw Chile serve as a premier destination for those escaping economic collapse and authoritarian rule in Venezuela. The establishment of a Peru-Chile Binational Committee on Migration, complete with joint patrols and unified verification criteria, reflects both governments' recognition that uncoordinated border management could escalate into broader security crises. Yet the fundamental tension remains unresolved:

Chile's transformation from regional migration destination to departure point marks a significant shift in Latin American population movements that will reverberate under the incoming Kast administration.

1.3 Social policy reversals

Beyond immigration, Kast campaigned on pursuing the most significant rollback of reproductive rights Chile has seen in decades. His explicit commitment during the campaign to eliminating the three legal exceptions for abortion—risk to maternal life, fetal viability, and rape—that ended Chile's total prohibition inherited from Pinochet's dictatorship represents a direct assault on the 2017 partial decriminalisation that required years of advocacy to achieve. Catalina Calderon, advocacy director at the Women's Equality Centre, warned before the election that "there is an imminent threat to the reproductive rights of girls and women in Chile, putting at risk access to contraceptives, the morning-after pill, and abortion by three exceptions."

Kast's social conservatism extends across multiple dimensions. He opposes same-sex marriage and morning-after contraception, has blocked legislative efforts by the Boric administration to expand reproductive rights, and has proposed enhanced police powers alongside increased law enforcement firepower. His platform would require expelled undocumented migrants to finance their own deportation—a proposal that combines his immigration hardline with a punitive approach that critics view as both cruel and impractical. This agenda aligns closely with Chile's Catholic hierarchy and appeals to socially conservative voters who view the country's recent progressive turn as an aberration requiring correction.

The political sustainability of such reversals remains uncertain. Chile's 2019 social explosion—triggered initially by a transport fare increase but rapidly expanding to encompass demands for healthcare, education, and pension reforms—demonstrated the fragility of any government's mandate when perceived as unresponsive to popular demands. Kast's social agenda risks reigniting those tensions amongst demographics that view reproductive rights and LGBTQ+ equality as settled questions rather than matters open for re-litigation. The parliamentary arithmetic compounds this challenge: Kast's Republican Party lacks the congressional majority required to advance his most ambitious proposals, potentially forcing uncomfortable compromises that alienate his core supporters whilst failing to reassure opponents.

1.4 Fiscal politics and budget battles

The 2026 budget debate revealed the poisonous political atmosphere the Kast administration will inherit. President Boric's September 30 proposal—projecting a 1.7% expenditure increase and targeting a 1.1% structural deficit—immediately triggered fierce controversy extending beyond typical fiscal policy disagreements. The exclusion of the "republican clause," a discretionary budget allocation traditionally reserved for incoming governments, provoked particular fury from opposition candidates. Kast denounced the omission as "un-republican" and "an act of corruption," whilst Matthei called it "unprecedented since the return to democracy." The dispute, whilst procedurally arcane, illuminated deeper questions about whether Chile's political class retains sufficient institutional trust to navigate the country's fiscal challenges cooperatively.

The substantive budget challenges transcend partisan point-scoring. Chile recorded deficits of 12.7% and 13.3% of GDP in 2023 and 2024 respectively, with the 2025 structural deficit revised repeatedly upward from an original 1.1% target to an estimated 2.2% as revenues fell short and spending pressures mounted. Finance Minister Nicolás Grau attributed these shortfalls to Congress's failure to approve corrective legislation, though critics countered that the administration's revenue projections had been over-optimistic from the outset. With debt approaching 43.2% of GDP—near the 45% threshold that

Susana Jiménez, president of the Confederation of Production and Commerce, characterised as Chile's "prudent maximum"—the fiscal trajectory requires correction regardless of who governs.

Kast's pledge to cut \$6bn in public spending within 18 months crystallised the competing approaches. Boric seized on this commitment to warn that such reductions would "inevitably undermine social programmes," accusing Kast of threatening benefits like the Universal Guaranteed Pension that enjoys broad popular support. Kast responded that he would target "political expenditure" rather than social transfers, though the arithmetic suggests such distinctions offer limited scope for meaningful savings absent painful choices about healthcare allocations, pension adjustments, or education funding.

The Autonomous Fiscal Council's call for a medium-term consolidation strategy focusing on stronger revenue sources, greater spending efficiency, and tighter tax evasion control points towards the uncomfortable reality: restoring fiscal sustainability will require both expenditure discipline and revenue enhancements that neither political camp has embraced fully. The budget's sectoral allocations revealed the Boric administration's final priorities. Health spending increased 5.6% (equal to \$947mn), pensions rose 8.9%, and housing grew 7.6%, whilst public security received a modest 1.2% boost despite crime dominating electoral discourse.

Grau's subsequent clarification that certain sectors would see larger increases than headline figures suggested—16.7% in security, 37% in housing, 55% in pensions—highlighted how budget presentations often obscure the real distributional choices embedded in fiscal policy. The Universal Guaranteed Pension's increase to CLP250,000 (\$260) for those over 75 exemplified Boric's attempt to cement social policy gains before leaving office, potentially constraining his successor's fiscal flexibility.

1.5 Regional defence and geopolitical positioning

Chile's geopolitical orientation has shifted subtly as regional dynamics evolve. The September 2025 meetings between Brazilian and Chilean defence officials signalled both countries' interest in strengthening bilateral cooperation, though the modest media coverage suggested this represented incremental deepening rather than strategic realignment. Brazil's pragmatic engagement with both the Trump administration and China positions it as a potential bridge for Chile as global trade tensions intensify, though the practical implications for Chilean security policy remain unclear.

The Peru border tensions introduced unexpected complexity to Chile's regional relationships. Lima's December deployment of military personnel to patrol its southern border, accompanied by a 60-day state of emergency for the districts of Palca, Tacna, and La Yarada-Los Palos, reflected both governments' struggles to manage irregular migration flows that neither country generated but both must address. The establishment of a Binational Committee on Migration represented an attempt at institutionalised cooperation, with joint patrols, unified verification criteria, and expanded information-sharing mechanisms. Yet allegations of police corruption—truck drivers reporting that Peruvian officers allegedly accepted \$100 to enable irregular crossings—highlighted how border management failures could undermine diplomatic initiatives if operational gaps persist.

The broader implications of Chile's rightward turn for its international relationships remain speculative. A Kast administration would likely align more closely with Argentina's Javier Milei, potentially creating a right-wing axis in the Southern Cone that views Brazil's Lula administration with suspicion. Relations with the United States could improve as Kast's anti-immigration and pro-business positions resonate with the Trump administration's preferences, though Chile's historical pragmatism on trade and investment suggests continuity will prevail over ideology in economic diplomacy. The real test will

come if Kast's domestic policies—particularly around human rights and social policy—trigger international criticism that forces choices between ideological consistency and economic pragmatism.

1.6 Parliamentary arithmetic and governance prospects

The composition of Chile's Congress will prove crucial in determining whether Kast can advance his agenda or finds himself blocked by an opposition coalition mobilised to prevent the most controversial reversals. Chilean presidents govern without the decree powers that characterise many Latin American executives, requiring legislative majorities or at minimum workable coalitions to enact significant policy changes. Kast's Republican Party lacks such a majority, potentially forcing uncomfortable compromises on fiscal policy, social legislation, and institutional reforms.

This constraint could prove beneficial for economic stability. Markets often perform better under a divided government that prevents radical policy swings in either direction, and Kast's most market-moving proposals—fiscal consolidation, regulatory reforms, investment incentives—might attract broader support than his social agenda. The economic team he has assembled signals capacity for pragmatic engagement with opposition legislators concerned about fiscal sustainability even if they reject his social conservatism. Whether Kast possesses the political flexibility to pursue this path remains unclear: his campaign rhetoric suggested ideological rigidity rather than dealmaking instinct, though the imperatives of office often moderate even the most uncompromising candidates.

The alternative scenario—legislative gridlock that prevents Kast from implementing either fiscal consolidation or social policy reversals—presents its own risks. A prolonged stalemate could disappoint the market expectations that drove the post-election rally, whilst failing to address the crime and immigration concerns that propelled Kast to victory. This combination could erode his political capital rapidly, potentially making him a lame duck president well before his term concludes. Chilean democracy has demonstrated resilience through multiple political cycles, but the polarisation evident in the 2025 campaign suggests the institutional norms that enabled previous compromises face unprecedented strain.

2.0 Macro Economy

2.1 Growth: modest recovery on fragile foundations

Chile's economic expansion through 2025 revealed both resilience and vulnerability, with growth oscillating between quarters as mining sector disruptions offset otherwise positive consumption and investment trends. The economy expanded 2.9% between September 2024 and September 2025, a respectable performance that nonetheless underscores Chile's struggle to achieve the rates necessary to generate substantial employment gains and income growth. The quarterly trajectory proved instructive: after starting strongly with 2.6% growth in the first quarter (revised upward from an initial 2.5% estimate) and accelerating to 3.3% in the second quarter (also revised higher from 3.1%), the economy stumbled to 1.6% in the third quarter—below the 1.8% forecast and a sharp deceleration that Finance Minister Nicolás Grau attributed to "isolated disruptions in the mining sector."

The mining sector's disproportionate impact on aggregate growth underscores Chile's continued dependence on copper exports despite decades of diversification efforts. Grau's contention that growth would have reached 2.6% in the third quarter absent mining disruptions highlights how production setbacks at major facilities can shave a full percentage point off national GDP—a vulnerability that will persist as long as copper dominates Chile's export basket and global supply chains remain susceptible to operational accidents, labour disputes, and infrastructure failures.

State producer Codelco's fatal accident at its El Teniente mine in July exemplified these operational risks whilst also demonstrating the company's continued ability to access capital markets, having raised \$1.4bn through October bond sales at spreads tighter than initial guidance.

Investment dynamics provided the most encouraging signal for Chile's medium-term prospects. Third-quarter investment surged 10% year-on-year, prompting Grau to note that "if you discount the post-pandemic rebound, this is the largest growth we've seen since 2012." This performance exceeded expectations and suggested businesses retained confidence in Chile's economic trajectory despite electoral uncertainty and fiscal challenges.

The second quarter had already shown strength, with national income rising 9.1% and consumption increasing 7.7% annually, whilst the savings rate reached 21.6% of GDP—driven by non-financial corporations and households apparently postponing consumption in favour of precautionary balance sheet strengthening.

Yet the investment surge's sustainability remains questionable. Much of the growth likely reflected catch-up from years of underinvestment following the 2019 social crisis and pandemic, with businesses finally executing projects delayed by uncertainty rather than responding to expectations of durably higher demand. The OECD's characterisation of Chile's outlook as "fragile" and "subject to substantial risks" captures the tentativeness underlying current investment decisions. Secretary General Mathias Cormann's December warning that "increased tariffs will gradually translate into higher prices, reducing growth in household consumption and business investment" points to external headwinds that could quickly reverse recent momentum if global trade tensions escalate or developed market demand softens materially.

2.2 Forecasting consensus and structural constraints

Forecasters have coalesced around modest expectations for 2026, projecting growth in a narrow 2.2-2.3% range that reflects Chile's limited capacity to exceed its potential output given structural constraints. The convergence of independent forecasts suggests confidence in the underlying economic fundamentals despite political uncertainties, though the projections themselves underscore Chile's inability to achieve the rates necessary to generate substantial employment gains and income growth that could durably address social discontent.

2025 Growth Projections:

- Central Bank Economic Expectations Survey (August): 2.3%
- Central Bank Economic Expectations Survey (November): 2.3% (confirmed)
- Chilean Ministry of Finance: 2.5%
- World Bank (October): 2.6% (upgraded from June estimate of 2.1%)
- OECD (December): 2.4%
- IMF: 2.5%
- Central Bank target range: 2.25-2.75%

2026 Growth Projections:

- Central Bank Economic Expectations Survey (November): 2.3% (upgraded from 2.2%)
- Central Bank Economic Expectations Survey (August): 2.1%
- World Bank (October): 2.2%
- OECD (December): 2.2%
- IMF: 2.0%

2027 Growth Projections:

- OECD (December): 2.2%
- IMF: 2.7%

The narrow dispersion of 2025 forecasts—clustered tightly between 2.3% and 2.6%—indicates unusual consensus amongst analysts about Chile's near-term trajectory, whilst the wider range for 2026-2027 (2.0% to 2.7%) reflects greater uncertainty about medium-term dynamics. The World Bank's October upgrade to 2.6% for 2025 represented the most optimistic near-term assessment, driven by expectations of strengthening private consumption and mining exports.

The IMF's notably lower 2.0% projection for 2026 suggests more cautious expectations about the sustainability of recent momentum, though its 2.7% forecast for 2027 implies potential recovery as structural reforms take hold or external conditions improve. Finance Minister Nicolás Grau welcomed this revision, noting it exceeded the government's own 2.5% projection and predicting that "investment will now grow by over 5%, and our effort as a government is to accelerate this growth as much as possible so that it reaches salaries and the creation of quality jobs as quickly as possible."

The OECD's December assessment provided the most comprehensive forward guidance, projecting Chilean GDP growth of 2.4% in 2025 before easing to 2.2% in both 2026 and 2027, with consumption supported by rising real incomes whilst investment remains robust but declining. This characterisation captures the fundamental tension in Chile's outlook: positive near-term momentum that gradually dissipates as temporary factors fade and structural constraints reassert themselves. The organisation's observation that Chile's headline inflation should approach 3% by end-2026, with net exports projected to contribute positively during 2026-27, offers modest comfort but does not alter the central reality that Chile appears stuck in a 2-2.5% growth corridor absent significant policy reforms or external tailwinds.

The structural backdrop explains this sluggishness. Chile's average annual expansion decelerated from 6.2% in the 1990s to barely above 2% in recent years, a slowdown the IMF attributes to demographic headwinds from an aging population, less favourable global growth environment, and exhaustion of easy productivity gains from earlier reforms. GDP per capita has tripled since 1990 to around \$26,000, positioning Chile as Latin America's wealthiest major economy but also limiting the scope for rapid catch-up growth that characterised earlier decades.

The country now confronts the middle-income trap that ensnares nations unable to transition from factor accumulation to productivity-driven expansion—a challenge requiring institutional improvements, education reforms, and innovation policies that successive administrations have struggled to implement effectively.

2.3 Consumption and income dynamics

Private consumption rebounded through 2025 as real incomes recovered from pandemic-era compression and employment stabilised following earlier disruptions. The 7.7% annual consumption increase recorded in the second quarter represented genuine momentum rather than base effects, suggesting Chilean households felt sufficiently confident about job security and income prospects to reduce precautionary savings and increase discretionary spending. This recovery proved crucial for maintaining overall growth given consumption's dominant share in Chilean GDP, though it also raised questions about sustainability if employment growth remains modest and real wage increases moderate.

The distribution of income gains shaped consumption patterns in ways that complicate macroeconomic assessment. Formal sector workers benefited from modest real wage growth as inflation declined faster than nominal wage adjustments, whilst informal workers and self-employed individuals faced more precarious circumstances with incomes tied closely to economic activity levels. The Universal Guaranteed Pension's increase to CLP250,000 (\$260) for those over 75 provided support for vulnerable retirees, though pension adequacy remains a persistent political flashpoint given the privatised system's failure to deliver retirement security for many contributors. Finance Minister Grau's statement that "our effort as a government is to accelerate this growth as much as possible so that it reaches salaries and the creation of quality jobs" reflected official recognition that headline GDP figures mask distributional realities that fuel social discontent.

The savings rate's climb to 21.6% of GDP in the second quarter merits closer examination. High savings can reflect either strength—optimism about future investment opportunities that encourages deferred consumption—or weakness—precautionary behaviour driven by employment insecurity and economic anxiety. Chile's case appears tilted towards the latter interpretation, with households and corporations building balance sheet cushions against uncertain political transitions and external shocks rather than positioning for

ambitious expansion plans. This interpretation aligns with survey evidence showing persistent concerns about crime, economic stability, and social tensions despite improved macroeconomic indicators.

2.4 Inflation: convergence towards target

Chile's inflation trajectory through 2025 demonstrated the Central Bank's success in guiding price pressures back towards its 3% target range following earlier pandemic-era overshoots. November inflation held steady at 0.3% monthly and 3.4% annually, matching market expectations and maintaining the controlled deceleration from earlier peaks. Year-to-date price growth reached 3.7% through November, whilst two-year inflation expectations anchored at the Central Bank's 3% target—a critical psychological threshold indicating markets believe price stability has been durably restored rather than representing a temporary respite before renewed pressures.

The composition of November's price movements revealed familiar patterns. Transport costs rose 0.7%, contributing 0.090 percentage points to the headline figure, whilst clothing and footwear surged 2.6%, adding 0.063 points. International air transport prices spiked 28.6% month-over-month—likely reflecting seasonal demand combined with capacity constraints—whilst restaurant food climbed 0.8%. Staple prices showed persistent upward pressure, with cheese jumping 4% and bread increasing 1.6%, reflecting cost pressures in agricultural supply chains that transmit slowly to final consumers. Offsetting these increases, alcoholic beverages and tobacco fell 2.4%, subtracting 0.088 points, whilst common expenses dropped 3.8% and wine declined 6.1%.

October's unexpected zero monthly variation had raised questions about whether disinflation might prove faster than anticipated, potentially allowing more aggressive monetary easing. November's rebound to 0.3% suggested such hopes were premature, reinforcing the Central Bank's cautious approach to further rate cuts. President Rosanna Costa's September statement that "the risk of further persistent inflation requires gathering more information before continuing the process of converging the MPR to its neutral range" proved prescient, validating the decision to pause easing at 4.75% following July's 25-basis-point reduction. The message to markets was clear: Chile had successfully reduced inflation from earlier peaks, but declaring victory prematurely risked reigniting price pressures that could prove even more difficult to contain.

The inflation outlook for 2026 appears constructive if external conditions cooperate. Forecasters project the Consumer Price Index will reach 3% by year-end 2026, aligning with the Central Bank's target range for what Finance Minister Grau described as a "healthy Chilean economy." The OECD concurred that headline inflation should approach 3% by end-2026, barring significant external shocks. This convergence depends critically on global commodity price stability, Chilean peso resilience against external volatility, and continued labour market moderation that prevents wage-price spirals. The political transition introduces additional uncertainty: Kast's proposed spending

cuts could prove disinflationary if implemented aggressively, though accompanying tax policy changes could offset those effects depending on their design.

2.5 Monetary policy: cautious normalisation

The Central Bank of Chile's unanimous decision to hold its policy rate at 4.75% in September marked a deliberate pause in the easing cycle that began earlier in 2025. Having reduced rates 25 basis points to 4.75% in July from the 5% level maintained since earlier tightening, the board concluded that rising inflation concerns warranted gathering additional data before continuing towards the neutral range estimated at 4-4.5%. This patience reflected the bank's commitment to ensuring price stability remains durably restored rather than prematurely declaring success, particularly given persistent uncertainties surrounding US tariff measures affecting global trade flows.

International factors weighed heavily in the decision. Federal Reserve policy expectations evolved throughout 2025, with markets initially pricing aggressive cuts before moderating those expectations as US economic resilience persisted. The prospect of the Fed resuming rate reductions provided some relief through declining global interest rates and recovering stock markets, creating a more accommodative external financial environment. Yet Wells Fargo's November warning that emerging market currencies—including Chile's peso—faced heightened vulnerability to Fed-induced shocks should US monetary policy disappoint market expectations underscored the precariousness of external conditions.

The bank's modelling suggested the Chilean peso, trading at 939 per dollar, could weaken to 1,154 under stress scenarios, a depreciation that would import inflationary pressures requiring monetary tightening precisely when domestic economic weakness might argue for accommodation.

The domestic financial market stability cited by the Central Bank offered reassurance that monetary conditions remained appropriate. The IPSA stock index continued accumulating gains through the September policy meeting, suggesting investors viewed the 4.75% policy rate as neither excessively tight nor dangerously loose.

This Goldilocks assessment could prove fragile if political tensions escalate following Kast's anticipated inauguration or if external shocks materialise, but through year-end 2025 the central bank appeared confident its patient approach balanced competing risks effectively. The announcement of a new International Reserve Accumulation Programme, praised by the IMF during its August Flexible Credit Line review, signalled additional commitment to building buffers against external volatility.

The forward guidance embedded in market expectations suggested cautious rate cuts resuming in 2026. Economists surveyed by the Central Bank anticipated the policy rate would decline to 4.5% in the near term before falling further to 4.25% by December 2026. This gradual trajectory reflects recognition that global economic uncertainties and risks surrounding international tariff

policies warrant preserving policy flexibility rather than rushing towards neutrality. The cautious pace also acknowledges that Chile's neutral rate may have risen from historical levels given structural changes in the global economy, though estimating this unobservable parameter with precision remains impossible. The Central Bank's emphasis on data dependency—assessing incoming information before committing to further moves—represents orthodox central banking that prioritises credibility over market expectations.

2.6 External accounts and currency vulnerability

Chile's external position presents a study in contrasts: a current account historically sustained by strong copper export revenues, balanced against a small open economy's vulnerability to global demand fluctuations and capital flow reversals. The IMF's August observation that Chile remains "exposed to global economic slowdowns, commodity price volatility, and capital flow disruptions that could be triggered by escalating trade tensions" captures this fundamental fragility. As a price-taker in global copper markets, Chile cannot insulate itself from demand shocks emanating from China—its largest export destination—or supply disruptions elsewhere that affect global metal balances.

Wells Fargo's November currency vulnerability assessment placed Chile alongside Colombia, Argentina, and Poland in the highest-risk category based on five metrics: external account positions, inflation-adjusted interest rate gaps with US borrowing costs, foreign reserve adequacy for imports, perceived political stability, and confidence in economic management. The methodology's emphasis on fundamentals rather than short-term sentiment suggested these vulnerabilities reflect structural characteristics unlikely to improve rapidly absent significant policy shifts.

With the peso trading at 939 per dollar and potential stress-scenario depreciation to 1,154 modelled, Wells Fargo essentially warned that Chile's exchange rate could weaken 23% should global financial conditions deteriorate sharply—a move that would boost export competitiveness but import significant inflation through higher prices for imported goods and dollar-denominated debt service.

The currency vulnerability sits uneasily alongside Chile's substantial foreign investor interest. The 40% surge in non-residents' holdings of peso-denominated government bonds from \$6.6bn at end-2024 to \$9.3bn by July—the largest boost to local government debt since 2017—demonstrated genuine appetite for Chilean assets despite electoral uncertainty.

Anders Faegermann of Pinebridge Investments attributed this inflow to the Trump administration's trade policies creating uncertainties in developed markets, driving investors towards emerging economies with declining inflation and stable central bank policies. Chile's bonds offered attractive yields relative to developed market alternatives, whilst the country's relatively strong fiscal position and institutional framework provided comfort that many emerging markets cannot match.

Yet this capital inflow contains the seeds of potential reversal. Foreign

investors responding to relative value opportunities rather than fundamental conviction about Chile's long-term prospects will prove flighty if developed market conditions improve or if Chilean politics disappoint expectations. The market's positive response to Kast's polling strength reflected hopes for fiscal discipline and market-friendly reforms, creating vulnerability should he prove unable or unwilling to deliver on these expectations. The IMF's maintenance of Chile's \$13.8bn Flexible Credit Line provides insurance against sudden stops, though drawing on the facility would signal distress that could itself trigger additional outflows in a self-fulfilling crisis dynamic.

2.7 Copper dependence and diversification limits

Chile's inability to meaningfully reduce dependence on copper exports despite decades of diversification efforts represents perhaps its most fundamental structural constraint. The metal's price volatility and production disruptions at major facilities continue exerting disproportionate influence on aggregate economic performance, as demonstrated by the mining sector issues that shaved a full percentage point off third-quarter growth. This dependence creates asymmetric policy challenges: Chilean authorities must calibrate macroeconomic settings for an economy whose performance depends substantially on factors beyond their control, from Chinese infrastructure investment to global supply disruptions to climate patterns affecting mining operations.

The brightening copper price outlook through late 2025—driven by global supply shortages from production setbacks and strong demand from electrification trends—provided temporary relief. Codelco's successful October bond issuance, with 2035 and 2055 notes yielding 125 and 152 basis points above US Treasuries after initial guidance suggested 150 and 180 basis points, demonstrated investor confidence in Chile's flagship producer despite operational challenges. The timing coincided with copper's biggest weekly gain in three months, illustrating how price momentum improves financing conditions even as operational risks persist. Yet the fatal accident at El Teniente mine that preceded the bond sale served as a stark reminder that production disruptions can emerge unexpectedly, with consequences extending beyond immediate output losses to encompass safety regulatory reviews, potential production stoppages, and reputational damage affecting financing costs.

Diversification beyond copper has proven frustratingly elusive. Chile's nascent technology sector, recognised as Latin America's AI leader by the 2025 Latin American Artificial Intelligence Index, offers promise but remains too small to materially reduce copper dependence. AMD's agreements with Chile's National AI Center for AI and supercomputing research partnerships signal international recognition of Chilean capabilities, though translating research excellence into substantial economic activity that can offset commodity volatility requires sustained policy support and private investment that may prove difficult to maintain through political cycles. The OECD's observation that AI investment surges remain concentrated in US data centres, and that US GDP would have contracted 0.1% in the first half of 2025 without technology

sector dynamism, underscores how difficult capturing meaningful shares of such investments proves for countries without established ecosystems. The structural impediment transcends commodity dependence per se: Chile's productive structure reflects decades of accumulated advantages in copper extraction and processing that cannot be easily replicated in alternative sectors. The human capital, infrastructure, regulatory frameworks, and supply chain linkages that make Chile competitive in copper represent sunk investments yielding ongoing returns, creating path dependencies that resist diversification even when economically rational. Successive governments have recognised this limitation whilst proving unable to overcome it, suggesting Chile's copper dependence will persist regardless of who governs or what policies are implemented. The challenge becomes managing volatility and building fiscal buffers during boom periods rather than achieving diversification that may be structurally unattainable.

3.0 Real Economy

3.1 Mining: operational risks amid market strength

Chile's mining sector entered 2026 navigating the uncomfortable duality of strengthening global copper prices alongside persistent operational and safety challenges that threaten production targets. State producer Codelco's fatal accident at El Teniente mine in July 2025—the company's largest operation—crystallised concerns that decades of underinvestment in maintenance and safety protocols could undermine Chile's position as the world's premier copper producer precisely as demand fundamentals improve. The incident prompted immediate regulatory scrutiny whilst raising uncomfortable questions about whether Codelco's ambitious investment programme adequately prioritised operational safety over expansion priorities.

Despite these operational setbacks, Codelco demonstrated continued capacity to access capital markets on favourable terms. The company's October bond issuance raised \$1.4bn through notes maturing in 2035 and 2055, with final yields of 125 and 152 basis points above US Treasuries—significantly tighter than initial guidance of 150 and 180 basis points and comparing favourably to January's \$1.5bn sale at 165 and 185 basis point spreads. The market's willingness to accept lower spreads despite the El Teniente accident reflected several factors: copper prices were experiencing their biggest weekly gain in three months, global supply disruptions elsewhere tightened markets, and investors retained confidence that Chile's institutional frameworks would ensure appropriate regulatory responses without triggering sustained production disruptions.

S&P Global Ratings analysts Amalia Bulacios and Flavia Bedran characterised the successful issuance as "a sign that Codelco maintains favourable conditions to access capital markets despite the recent noise stemming from

the incident at its El Teniente mine." This assessment, whilst accurate regarding immediate market access, understated longer-term risks. Chile's mining sector faces an uncomfortable reality: maintaining global competitiveness requires sustained capital investment in both brownfield optimisation and greenfield development, yet operational incidents that highlight safety deficiencies could trigger regulatory interventions or labour disruptions that delay projects and inflate costs.

Codelco's substantial debt load—necessary to finance its investment programme—creates financial fragility should copper prices soften or production disruptions prove more severe than currently anticipated. The third quarter's mining sector disruptions that Finance Minister Grau blamed for shaving GDP growth from a potential 2.6% to the actual 1.6% illustrated copper's continued dominance over Chile's economic performance. This dependence creates asymmetric policy challenges: policymakers must calibrate fiscal and monetary settings for an economy whose trajectory depends substantially on operational factors at a handful of major mining facilities.

When production proceeds smoothly, Chile enjoys substantial export revenues and tax receipts that ease fiscal constraints. When accidents occur, labour disputes erupt, or infrastructure failures disrupt operations, the immediate GDP impact materialises regardless of broader economic fundamentals. This volatility, endemic to commodity producers, frustrates macroeconomic management whilst resisting obvious policy solutions.

3.2 Retail: divergent fortunes in a shifting consumer landscape

Chile's retail sector presented a story of stark contrasts through 2025, with Chilean giant Cencosud's aggressive regional expansion juxtaposed against domestic closures exemplified by Corona's collapse. Cencosud's January acquisition of Dutch wholesale chain Makro's Argentine operations for \$122.5mn—potentially adjusted based on net debt and working capital conditions—marked the Chilean retailer's entry into Argentina's wholesale segment at a valuation substantially below the approximately \$200mn figure when SHV Holding initiated the sale process. CEO Rodrigo Larraín's satisfaction with "this opportunity for growth in Argentina, a market where we have been present for more than 40 years" reflected confidence that President Javier Milei's market reforms would create conditions favourable for foreign retail investment.

The Makro acquisition formed part of Cencosud's \$610mn regional investment plan for 2025, signalling ambitions extending well beyond Chile's modest growth prospects. The deal's strategic logic appeared sound: Makro's locations and operations offered complementary positioning relative to Cencosud's existing Cash & Carry operations in Brazil, whilst entering Argentina's wholesale market provided diversification from Chile's mature retail environment where growth opportunities proved limited. Yet the timing carried risks—Argentina's economic volatility and unresolved inflation challenges mean retailers betting on that market accept considerable uncertainty about

consumer purchasing power trajectories and competitive dynamics as Milei's adjustment programme unfolds.

Corona's demise offered a cautionary counterpoint to Cencosud's optimism. The 70-year-old clothing retailer, founded in 1955 by Dutch immigrant Leonard Schupper, closed all 51 stores across Chile in July, putting approximately 1,800 jobs at risk as the family business ceased operations. The company's failure to complete a second reorganisation process to settle debts with creditors left little alternative to liquidation, with large crowds descending on stores during the June 27 clearance sales that commenced the winding-down process. Corona's collapse illustrated how established retailers face increasingly difficult conditions navigating between e-commerce competition, changing consumer preferences, and the cost pressures that make traditional multi-location operations economically marginal absent substantial scale advantages.

The divergent fortunes of Cencosud and Corona reflect broader structural shifts in Latin American retail. Scale advantages and operational sophistication increasingly separate winners from losers, with mid-sized regional players like Corona squeezed between discount competitors and premium specialists. Chile's modest economic growth prospects amplify these pressures: absent substantial consumption expansion, retailers must gain market share from competitors to grow, intensifying competitive dynamics in ways that favour operators with deep pockets and professional management. Cencosud's regional diversification strategy recognises these constraints, seeking growth opportunities beyond Chile's saturated market whilst leveraging operational capabilities developed in its home market.

The employment implications merit consideration. Corona's 1,800 job losses represent a non-trivial shock in Chile's modest-sized labour market, concentrated geographically in ways that could create local distress even as national employment statistics show resilience. These displacements feed perceptions of economic insecurity that transcend headline GDP figures, potentially influencing political attitudes in ways that macroeconomic data alone would not predict. The fact that Corona's troubles emerged despite overall consumption growth through 2025 underscores how aggregate indicators can mask sectoral and firm-level distress with significant social consequences.

3.3 Telecommunications

Chile's telecommunications sector entered a period of upheaval as Spain's Telefónica advanced plans to exit its Chilean operations, part of CEO Marc Murtra's broader "Transform & Grow" strategy that will leave Brazil as the company's sole Latin American presence. The implications for Chilean consumers and competitors depend critically on which bidder ultimately acquires Movistar and what regulatory authorities permit regarding market concentration.

Telefónica's retrenchment reflects European telecommunications companies'

broader retreat from Latin American markets where growth has disappointed and returns failed to justify the capital requirements of 5G network deployment and fibre expansion.

The company reported a net loss of €1.08bn through September 2025 compared with €954mn profit a year earlier, whilst Hispam division revenues fell 11.3% year-on-year to €3.15bn. Asset sales across the continent have generated more than €3bn in proceeds, with ongoing transactions potentially reaching €3.6bn according to analyst estimates, though immediate restructuring costs include a redundancy programme affecting up to 7,000 employees.

Fitch Ratings warned in September that a Movistar acquisition by an existing competitor "could create a market leader with approximately 50% mobile market share and 30-50% fixed broadband share, potentially enabling more rational competition and improved sector profitability," though such consolidation "would likely face significant antitrust scrutiny." Chile's fragmented telecommunications market currently features four main nationwide operators with no single player exceeding 40% market share, creating intense competition that has severely pressured operators' margins.

The shift to 5G technology and fibre network expansion has further strained free cash flow generation through significant capital expenditure requirements. América Móvil and local player Entel's reported joint acquisition bid presents the most likely scenario, though América Móvil's recent VTR purchase may limit its appetite for additional Chilean exposure. WOM recently exited Chapter 11 bankruptcy protection with minimal debt capacity, whilst GTD's elevated leverage constrains acquisition financing. The sale's outcome will significantly impact Chile's telecommunications landscape for years, determining whether consumers benefit from preserved competition or improved network investment, and whether operators achieve returns sufficient to justify continued capital deployment in a mature market facing structural headwinds.

3.4 Private debt markets: expansion amid falling rates

Chile's private debt market demonstrated continued growth through early 2025, reaching \$6.6bn in the first quarter versus \$6.4bn in the final quarter of 2024—a modest 3% expansion that nonetheless signalled investor appetite for higher-yielding alternatives as central bank rate cuts reduced returns on traditional fixed income instruments. Jorge Garcia, chief investment officer at Nevasa, characterised the environment as "favourable" for flows into private debt, explaining that declining rates "will obviously cause investors to seek higher returns in other types of assets, coupled with a lower perception of credit risk as economic activity has also been normalising."

The composition of private debt growth provided insights into which sectors attracted investor capital. The automotive industry led expansion with a 25% surge from the fourth quarter of 2024 to the first quarter of 2025, reaching \$201mn, suggesting both supply-side financing availability and demand-side consumer confidence in making significant purchases requiring credit. The

ACAFI-supervised private debt funds encompass direct financing across housing, real estate, automobiles, machinery, invoices, and short-term debt—a diversified exposure that offers investors sector-level granularity whilst maintaining aggregate exposure to Chilean economic conditions through the pool of underlying borrowers whose repayment capacity depends on employment and income trends.

The sector's growth trajectory carries implications extending beyond immediate financing volumes. Private debt markets offer businesses alternative funding sources beyond traditional bank lending, potentially enhancing financial system resilience by diversifying credit provision across multiple channels. This diversification proves particularly valuable during periods when banks face regulatory or balance sheet constraints limiting their lending capacity, allowing continued credit flow through alternative channels that maintain economic activity. Yet private debt's growth also concentrates risks in non-bank financial intermediaries potentially subject to less stringent regulatory oversight than traditional banks, creating vulnerabilities if credit quality deteriorates or if investor sentiment shifts rapidly in response to adverse economic developments.

The interest rate environment's role in driving private debt growth merits emphasis. Garcia's observation that falling rates push investors towards higher-yielding alternatives reflects portfolio rebalancing dynamics operating across all financial markets: as central banks cut policy rates, returns on safe assets decline, forcing investors seeking specific yield targets to accept additional credit risk, longer duration exposure, or reduced liquidity. This search for yield can prove self-stabilising if it channels capital towards productive economic activities generating the income required for debt service. Yet it can also prove destabilising if investor risk appetite encourages lending to marginal borrowers unlikely to repay, building credit quality deterioration that eventually materialises in losses requiring provisions.

Chile's regulatory framework for private debt markets will prove crucial in determining whether growth proves sustainable or sows seeds of future instability. ACAFI supervision provides regulatory oversight, though questions persist about whether current frameworks adequately address risks emerging from rapid growth in relatively new market segments. International experience suggests private debt often grows fastest during benign economic periods when default rates remain low and credit quality concerns appear overstated, only to face stress when economic conditions deteriorate and the inadequacy of credit underwriting becomes apparent. Chilean authorities must balance supporting financial innovation and alternative credit channels against ensuring prudential frameworks prevent excessive risk accumulation that could threaten financial stability during downturns.

The \$6.6bn market size, whilst representing growth, remains modest relative to Chile's total credit markets, suggesting private debt serves as a complement rather than substitute for traditional bank lending. This scale limits systemic risks whilst allowing continued experimentation with alternative financing models. The sector's evolution through 2026 will indicate whether current

growth trajectories prove sustainable or whether tighter monetary conditions, reduced investor risk appetite, or emerging credit quality concerns constrain further expansion. For borrowers, continued availability of private debt financing could ease credit constraints that might otherwise emerge if banks prove conservative in extending new credit given macroeconomic uncertainties. For investors, the asset class offers yield pickup relative to traditional fixed income, though returns ultimately depend on underlying credit performance through economic cycles.

4.0 Fiscal Policy

4.1 Deficit dynamics and debt sustainability

Chile's fiscal position deteriorated sharply through 2023-2024, with deficits of 12.7% and 13.3% of GDP, respectively revealing the extent to which pandemic-era spending increases and revenue shortfalls created fiscal imbalances requiring correction. These figures substantially exceeded the structural deficit framework Chile established to insulate fiscal policy from copper price volatility, suggesting the fiscal rule's credibility had eroded through repeated modifications and missed targets. The Boric administration's projection of a 2.2% structural deficit for 2025—repeatedly revised upward from an original 1.1% estimate—illustrated how optimistic revenue assumptions combined with political difficulty constraining expenditure produced sustained fiscal slippage.

Finance Minister Nicolás Grau's attribution of deficit overruns to "Congress's failure to approve corrective legislation" reflected political reality: Chile's separation of powers means executive branch fiscal proposals require legislative approval that opposition parties can withhold when politically advantageous. Yet this explanation understated the administration's role in proposing budgets premised on revenue forecasts that consistently proved over-optimistic. Cristina Torres, former head of the Budget Directorate (Dipres), cautioned in October that although the 2026 budget's 1.7% expenditure growth appeared moderate, the real variation could reach 4.1% once deviations in 2025 spending were incorporated—a warning that headline budget discipline sometimes masks underlying fiscal looseness through technical adjustments.

The 2026 budget's structural deficit target of 1.1% of GDP, with a longer-term commitment to eliminate deficits by 2029, represents an ambitious consolidation trajectory given the political constraints and social spending pressures any government confronts. President Boric's September 30 assertion that "Chile does not have to choose between fiscal irresponsibility and social indifference" captured the political rhetoric surrounding fiscal debates, though the arithmetic suggests uncomfortable tradeoffs prove unavoidable absent substantially stronger revenue growth or willingness to constrain spending categories currently considered sacrosanct. The sectoral allocations—health increasing 5.6% (\$947mn), pensions rising 8.9%, housing

growing 7.6%, with more modest security increases of 1.2%—illustrated how competing priorities absorb available fiscal space before infrastructure investment, education improvements, or deficit reduction can be addressed. Grau's subsequent clarification that security spending would actually increase 16.7%, housing 37%, and pensions 55% when measured against appropriate baselines highlighted how budget presentation conventions can obscure real distributional choices.

These larger increases, whilst politically defensible given social demands for enhanced security and pension adequacy, create rigidities that constrain fiscal flexibility in future years when cyclical revenues decline or when priorities shift. The debt trajectory adds urgency to consolidation imperatives. With debt approaching 43.2% of GDP—near the 45% "prudent maximum" identified by Confederation of Production and Commerce president Susana Jiménez—Chile risks breaching self-imposed thresholds that trigger adverse market reactions.

Whilst 43% debt-to-GDP ratios appear modest by developed economy standards or relative to regional peers like Brazil, Chile's historical fiscal conservatism means markets interpret rising debt as signalling deteriorating discipline rather than temporary accommodation of cyclical factors. Arrears in housing and health financing, noted by Jiménez as remaining unresolved, compound concerns that reported debt figures may understate true fiscal obligations once contingent liabilities and delayed payments are properly accounted for.

4.2 Political economy of fiscal adjustment

The Autonomous Fiscal Council's call for a medium-term consolidation strategy emphasising stronger revenue sources, greater spending efficiency, and tighter tax evasion control points towards the uncomfortable reality that restoring fiscal sustainability requires both expenditure discipline and revenue enhancements. Yet Chile's political fragmentation makes implementing comprehensive fiscal reforms extraordinarily difficult. Opposition parties can block revenue measures whilst demanding spending increases on priorities their constituents favour, creating asymmetry where fiscal loosening proves politically easy whilst consolidation requires extraordinary political capital.

José Antonio Kast's pledge to cut \$6bn in public spending within 18 months crystallised competing approaches to fiscal adjustment. The figure represents roughly 2% of GDP, a substantial consolidation that would meaningfully improve fiscal trajectories if implemented without offsetting tax reductions. Yet Kast's simultaneous commitment to avoid touching benefits like the Universal Guaranteed Pension, combined with promises of enhanced security spending and infrastructure investment, leaves unclear which expenditure categories would absorb cuts of this magnitude. His response that reductions would target "political expenditure"—presumably referring to bureaucratic overhead, consultancies, and discretionary programmes—suggests insufficient specificity to reassure markets that meaningful consolidation will materialise. President Boric's warning that Kast's proposals would "inevitably undermine social programmes" captured opposition rhetoric whilst glossing over the

current administration's fiscal record. The deficits of 12.7% and 13.3% of GDP in 2023-2024 emerged partly from deliberate policy choices to maintain spending during economic weakness, reflecting the administration's prioritisation of social cohesion over fiscal discipline.

Defenders argue this approach prevented deeper recession and social unrest, whilst critics contend it squandered fiscal space during commodity price strength that should have been banked for future downturns. The reality likely encompasses both perspectives: countercyclical spending proved appropriate given circumstances, yet the scale and persistence of deficits exceeded levels consistent with long-term sustainability.

The exclusion of the "republican clause" from the 2026 budget illustrated how fiscal policy became weaponised during political transitions. This discretionary allocation traditionally reserved for incoming governments serves practical purposes—allowing new administrations to fund priority initiatives without waiting for subsequent budget cycles—but its removal by Boric reflected either fiscal stringency or political calculation to constrain his successor's flexibility.

4.3 Revenue challenges and structural reform needs

The persistent gap between revenue projections and realisations since 2023 raises fundamental questions about Chile's tax system's adequacy for financing the social spending levels democratic politics now demand. Matías Acevedo, former Dipres director, noted in October that "the credibility of revenue projections will be central," observing that estimates have been "consistently over-optimistic since 2023, contributing to larger-than-planned deficits." This optimism bias could reflect technical forecasting errors—underestimating economic impacts on tax bases or overestimating compliance improvements—or political economy dynamics where proposing realistic revenue projections would require acknowledging that preferred spending plans cannot be financed without tax increases.

Chile's copper-dependent revenue structure amplifies forecasting challenges. Government revenues fluctuate significantly with metal prices and production volumes, creating pro-cyclical fiscal patterns where spending commitments made during boom periods become difficult to unwind when prices soften. The structural fiscal balance framework attempted to address this volatility by adjusting spending targets for copper price deviations from long-run trends, yet the framework's credibility eroded through repeated modifications and missed targets. Restoring fiscal discipline requires either stricter adherence to the existing framework—constraining spending regardless of political pressures—or designing new institutions that more effectively depoliticise fiscal policy.

Tax evasion control, highlighted by the Autonomous Fiscal Council as requiring attention, represents an appealing revenue enhancement strategy politically, since closing compliance gaps theoretically raises receipts without increasing statutory rates that generate taxpayer resistance. Chilean authorities estimate evasion rates across various taxes, with value-added tax gaps receiving particular scrutiny given VAT's substantial revenue contribution. Yet

international experience suggests that achieving major evasion reductions proves harder than advocates anticipate: sophisticated evasion schemes require equivalent sophistication in detection and enforcement, whilst resources devoted to anti-evasion efforts face diminishing returns as authorities pursue increasingly marginal cases. The revenue potential from improved compliance likely proves sufficient to merit additional enforcement resources but insufficient to close fiscal gaps without complementary measures.

Structural reforms to improve spending efficiency offer another theoretically attractive but practically challenging path. Every government identifies wasteful programmes meriting elimination and administrative overhead requiring reduction, yet the political coalitions supporting such spending make actual cuts difficult. Public sector employment in Chile has grown significantly, though determining whether this expansion reflects necessary service provision improvements or represents inefficient bureaucratic bloat depends on assessments inevitably coloured by ideological priors. Kast's "political expenditure" rhetoric suggests he views substantial scope for efficiency gains, whilst Boric defenders contend that spending increases funded necessary social programmes and infrastructure investment. The actual efficiency improvements achievable likely fall short of what either camp claims, with genuine savings requiring difficult choices about service levels and programme design rather than painless elimination of obvious waste.

5.0 Markets

5.1 Foreign investment resurgence

Chile's sudden emergence as a destination for foreign portfolio investment through 2025 defied expectations that electoral uncertainty would deter capital inflows. Non-residents' holdings of peso-denominated government bonds surged 40% from \$6.6bn at end-2024 to \$9.3bn by July—the largest boost to local government debt since 2017—signalling genuine confidence in Chile's economic management despite presidential transition uncertainties.

Anders Faegermann of London-based Pinebridge Investments attributed this appetite to US President Donald Trump's trade policies creating uncertainties in developed markets, pushing investors towards emerging economies with stabilising inflation trajectories and credible central bank frameworks. Chile's bonds offered attractive yields relative to developed market alternatives whilst the country's institutional quality provided comfort unavailable in many emerging markets.

The market's positive response to José Antonio Kast's emergence as polling frontrunner illustrated how investor priorities sometimes align imperfectly with broader social concerns. Chilean stocks rallied 3.1% following the November 17 first-round results as traders priced in expectations of fiscal discipline and market-friendly reforms under a Kast administration. This reaction reflected

judgements about economic policy rather than endorsement of Kast's social conservatism—investors focused on his assembled economic team and commitment to spending restraint whilst discounting risks that aggressive social policy reversals might trigger unrest.

Faegermann's observation that markets viewed Kast's business-friendly platform as "favourable for economic stability" captured this calculus: investors betting that economic orthodoxy would prevail over ideological rigidity regardless of campaign rhetoric.

Yet this confidence contains seeds of potential disappointment. Foreign investors responding to relative value opportunities rather than fundamental conviction about Chile's long-term trajectory will prove flighty if developed market conditions improve or if domestic politics frustrate reform expectations.

The inflows through mid-2025 occurred during a period of dollar weakness that Oxford Economics research suggested particularly benefited Chile and Colombia amongst emerging markets, with each percentage point of dollar depreciation potentially increasing economic growth by more than 0.3 percentage points. Should this dollar weakness reverse—as Wells Fargo's November warning about emerging market currency vulnerabilities suggested could occur if Fed policy disappoints market expectations—the Chilean peso could face renewed depreciation pressure that erodes foreign investors' total returns and triggers capital flight.

The sustainability of capital inflows depends critically on whether Kast's administration delivers the fiscal consolidation and structural reforms investors anticipate. Markets have priced in optimistic scenarios; implementation disappointments could trigger sharp reversals. The Congressional arithmetic complicates this outlook: Kast's Republican Party lacks the legislative majority required to advance controversial proposals without opposition cooperation, potentially constraining his reform agenda regardless of executive branch intentions. This political reality could prove stabilising—preventing radical policy swings that alarm investors—or destabilising if gridlock prevents addressing fiscal imbalances that markets increasingly view as unsustainable. Either way, the gap between market expectations embedded in current prices and political realities suggests volatility ahead.

5.2 Banking sector stability and concentrated risks

Chile's banking system entered 2026 displaying resilience despite modest economic growth and persistent uncertainties about political transitions. HSBC Bank Chile's maintenance of triple-A national ratings from Fitch in December exemplified this stability, though the case study illuminated interesting dynamics about how parent support from highly-rated international institutions can override modest domestic market positions in credit assessments. HSBC Chile commands merely 0.14% of the country's banking sector yet maintains top-tier ratings based on Fitch's assessment that extraordinary parent support from HSBC Holdings plc (carrying an A+ international issuer default rating) remains highly probable given the Chilean subsidiary's negligible impact on consolidated balance sheets.

HSBC Chile's September 2025 fundamentals demonstrated strong risk management: operating profit on risk-weighted assets of 1.92%, zero delinquencies beyond 90 days, provisions covering 4.9% of the portfolio, and a CET1 ratio of 14.8%. Liquidity metrics remained robust with a loan-to-coverage ratio of 226% and net stable funding ratio of 152%, offsetting concentrated wholesale funding risks inherent in the bank's treasury, investment, and corporate banking focus rather than retail client relationships. This wholesale-focused model provides insulation from retail competition whilst capitalising on cross-border transaction flows between Chilean corporates and international markets—a niche likely to remain viable given Chile's export-oriented economy and need for trade finance.

Yet HSBC Chile's negligible market share illustrates the sector's concentrated nature, with a handful of large domestic institutions dominating retail and commercial banking whilst international banks occupy specialist niches. This concentration creates systemic risks should major domestic banks face stress, whilst limiting competitive pressures that might otherwise constrain lending margins and force efficiency improvements. Chilean banking regulation has proven generally prudent, with capital adequacy requirements and liquidity standards exceeding international minimums, though recent years' modest credit growth suggests banks remain cautious about expanding exposure given macroeconomic uncertainties. This conservatism protects balance sheets but also constrains credit availability for businesses and consumers whose spending drives economic activity.

The telecommunications sector's potential consolidation carries implications for bank lending exposures. Major banks hold significant claims on Chilean telecommunications companies whose business models face pressure from intense competition and capital-intensive 5G deployment requirements. The Movistar sale and broader sector restructuring could affect bank asset quality depending on how transactions are structured and whether acquirers honour existing obligations. Banks with concentrated telecommunications exposures face heightened risks should sector difficulties materialise, though diversified lending portfolios mitigate institution-level impacts. Chilean banking supervisors will need to monitor these developments closely, particularly if sector consolidation creates too-big-to-fail institutions whose difficulties could threaten broader financial stability.

The private debt market's growth adds another dimension to financial system resilience. By providing alternative financing sources, private debt markets reduce Chilean businesses' dependence on bank credit, potentially enhancing system stability through diversification. Yet this growth also concentrates risks in non-bank financial intermediaries subject to lighter regulatory oversight than traditional banks, creating potential vulnerabilities if credit quality deteriorates. Chilean authorities must balance supporting financial innovation against ensuring that private debt growth does not create systemic risks that could amplify economic downturns when credit conditions inevitably tighten.

5.3 Exchange rate dynamics and external vulnerabilities

The Chilean peso's dual nature as both emerging market currency and commodity-linked exchange rate creates complex dynamics that amplify economic volatility whilst offering natural hedges against specific shocks. The currency's 40% gain in foreign government bond holdings through mid-2025 occurred despite Wells Fargo's November assessment placing Chile amongst the world's currencies most exposed to steep falls should US monetary policy trigger financial market disruption. This apparent contradiction reflects how different types of capital flows respond to different factors: long-term portfolio investors attracted by Chile's institutional quality and attractive yields can coexist with short-term traders positioning for currency weakness based on vulnerability metrics.

Wells Fargo's framework, weighing external account positions, inflation-adjusted rate gaps with US borrowing costs, foreign reserve adequacy, political stability perceptions, and economic management confidence, placed Chile alongside Colombia, Argentina, and Poland in the highest vulnerability category. The modelling suggested the peso, trading at 939 per dollar in November, could weaken to 1,154 under stress scenarios—a 23% depreciation that would substantially boost export competitiveness but import significant inflation through higher prices for imported goods and dollar-denominated debt service. This vulnerability reflects structural characteristics—Chile's small open economy status and copper dependence—that cannot be easily remedied through policy adjustments, suggesting exchange rate volatility will persist regardless of political developments.

Oxford Economics' July research offered a more optimistic perspective, identifying Chile and Colombia as positioned to gain most from dollar weakness amongst emerging market economies. The consultancy's argument centred on balance sheet dynamics favouring countries with significant dollar-denominated debt, capital flow patterns benefiting nations with existing sovereign vulnerabilities, and deleveraging pressures easing in economies with high private credit levels. Under scenarios where sustained dollar depreciation alleviated balance sheet risks and improved growth prospects, Chilean assets appeared undervalued relative to fundamentals. This assessment proved prescient through mid-2025 as dollar weakness coincided with strong capital inflows, though the analysis implicitly acknowledged how quickly conditions could reverse should dollar strength resume.

The IMF's maintenance of Chile's \$13.8bn Flexible Credit Line provides insurance against sudden external shocks, though this safety net carries its own complexities. The Washington-based lender's August mid-term review praised Chile's "very strong economic fundamentals and institutional policy frameworks" whilst noting that "external risks have increased since the credit line was approved" in 2024. Chilean authorities' reiteration that they view the arrangement as precautionary—with no intention to draw funds unless facing severe external shocks—reflects understanding that actually utilising the facility would signal distress potentially triggering additional capital outflows.

This creates a peculiar dynamic where the FCL's value lies primarily in its existence rather than use, providing market confidence through availability rather than actual liquidity provision.

The exchange rate's role in macroeconomic adjustment complicates policy settings. Currency depreciation theoretically cushions external shocks by making exports more competitive and import-competing industries more viable, whilst currency appreciation rewards consumers and businesses relying on imported inputs. Yet peso volatility creates planning difficulties for businesses unable to hedge currency exposures effectively, potentially deterring investment even when underlying economic fundamentals appear sound. The Central Bank's inflation-targeting framework with floating exchange rates represents orthodox policy for a small open economy, yet this orthodoxy provides limited comfort when currency swings amplify boom-bust cycles rather than dampening them. Chilean policymakers have few tools beyond foreign exchange intervention—which risks burning through reserves if defending indefensible levels—and interest rate adjustments whose domestic impacts may prove disproportionate to exchange rate effects.

6.0 Conclusion

Chile finds itself at a critical juncture where political transformation intersects with stubborn economic constraints to shape an outlook characterised more by uncertainty than confidence. José Antonio Kast's election victory in December promises market-friendly policies and fiscal discipline that have already begun attracting foreign investment, but his polarising social agenda risks reigniting tensions that destabilised Chile back in 2019. The incoming administration will inherit an economy growing at rates insufficient to address persistent social demands, with structural factors limiting potential output gains regardless of policy adjustments. Navigating these crosscurrents will require political skill and economic pragmatism that Kast's campaign rhetoric suggests he may lack.

For investors and businesses planning 2026 operations, Chile presents opportunities wrapped in uncertainties. The country's institutional quality, copper endowment, and strategic location provide enduring advantages that persist across political cycles, making Chile a more stable platform than many regional alternatives despite current challenges. Yet the political polarisation evident in the 2025 campaign suggests that consensus on economic policy direction remains fragile, with potential for disruption if social tensions re-emerge or if Kast pursues his most controversial proposals aggressively.