

Policy Responses to COVID-19 in Emerging Market Economies: an Open Market Operations Perspective

The X Open Market Operations (Digital) Meeting

CEMLA and Banco de México



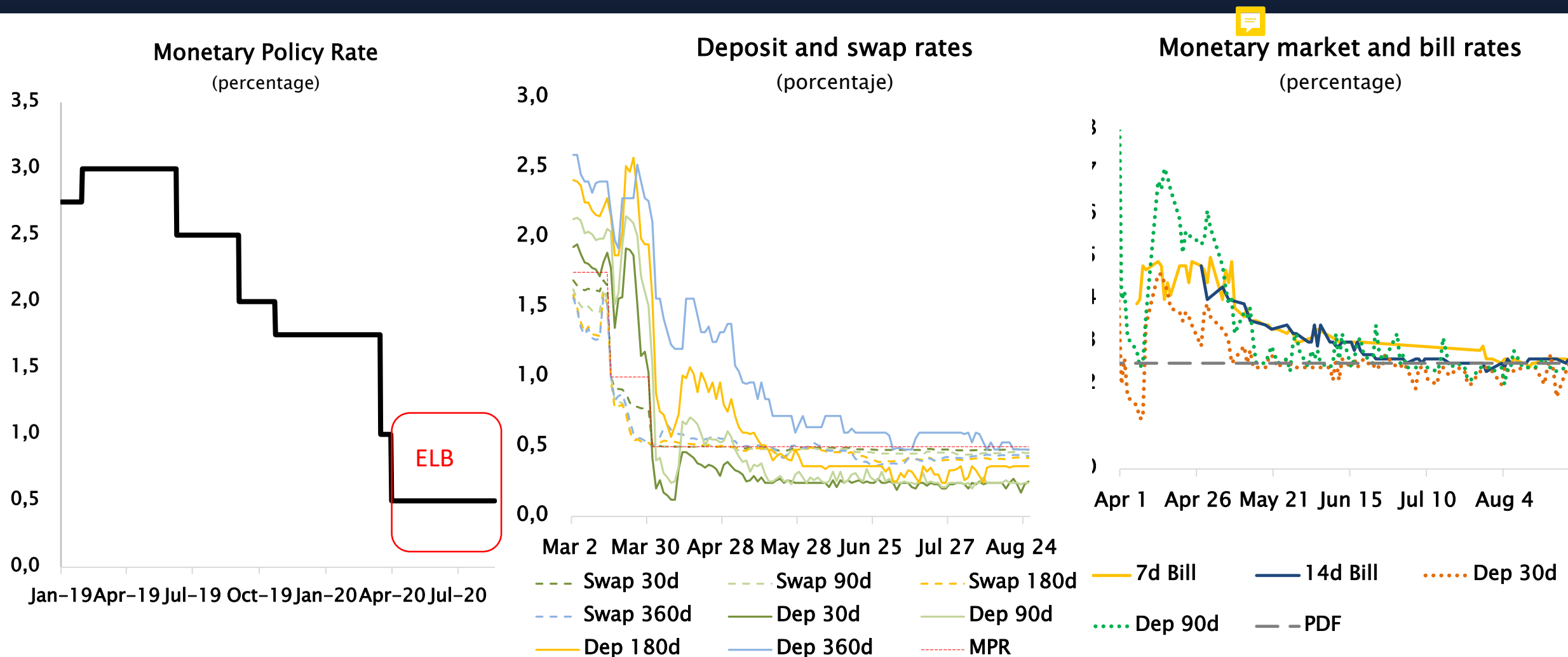
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September 3rd, 2020

Recent developments

- One of the CB's objectives is to ensure the proper functioning of the financial system's chain of payments. In addition, it has the function of seeking financial stability and making market dynamics work.
- For these reasons, from October 2019 the CB has developed measures that seek to manage the impact of both internal and external shocks that have challenged the economy.
- The measures include tools which provide liquidity in pesos and in US\$, and which also maintain financial stability
- During March's MPM, the Board decided to keep the MPR at 0.5% (Effective Lower Bound) and communicate that it **will consider options to boost the monetary impulse by increasing the use of unconventional tools**, if needed

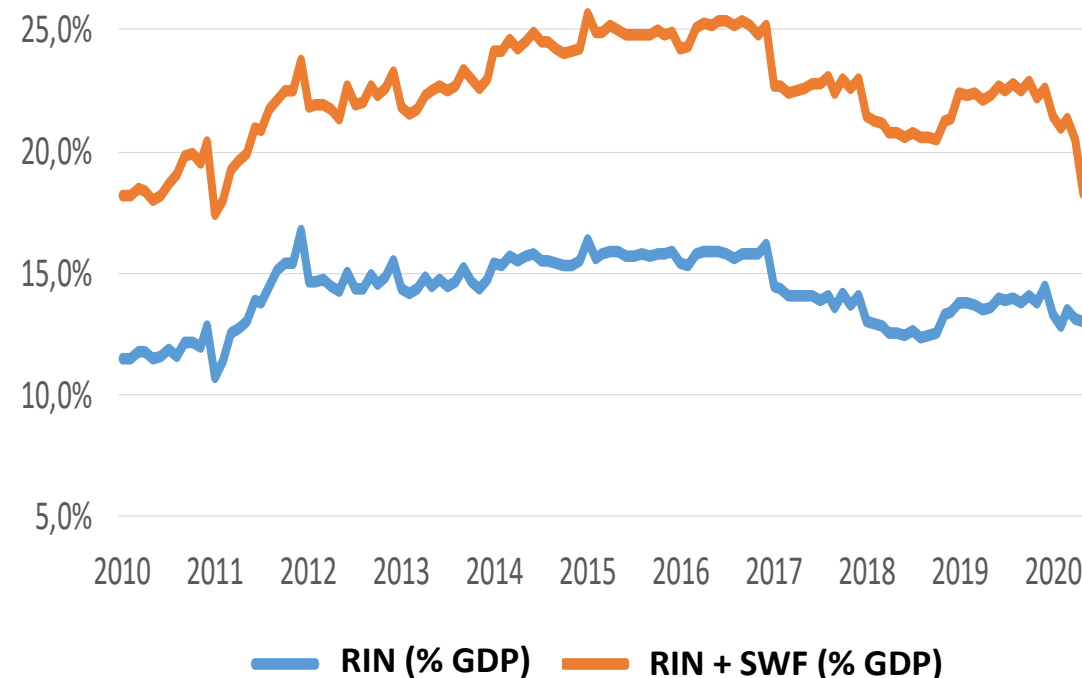
In line with the ELB, the money market has traded under the MPR, very close to the permanent deposit facility (PDF)



In order to strengthen the international liquidity position, the CB has adopted international financing lines in the case of severe shocks to handle a potentially massive capital outflow.

1. FCL: precautionary financing line for US\$ 23.9 billion, for 2 years. The balance sheet is expanded in the case of activation.
2. PBoC Swap Line: Swap line where CB seeks to increase the amount and functions. The balance sheet is expanded in the case of activation.
3. FIMA: FED repo program. This mechanism doesn't expand the balance sheet, because the cash is collateralized with instruments.

International Reserves and Sovereign Wealth Funds



The national and international environment has challenged us to take quick and effective actions to mitigate the impacts on local market

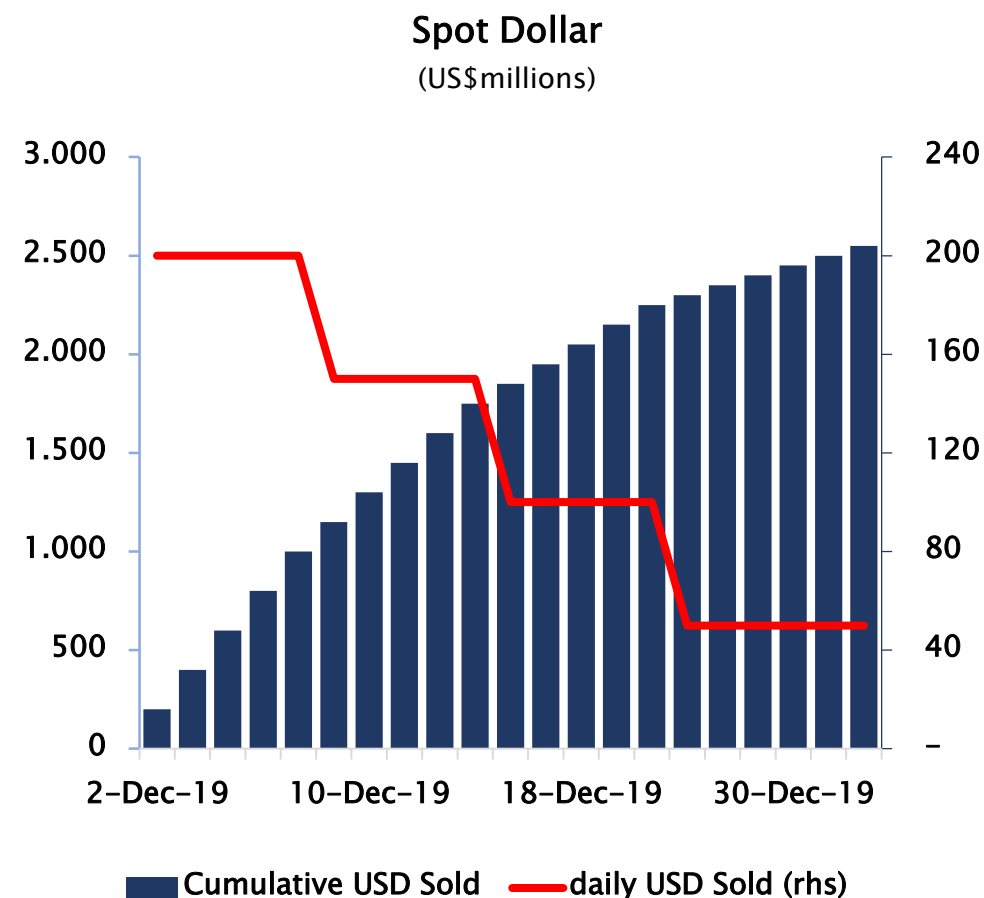
The CB has carried out all the necessary operations to provide liquidity in local and foreign currency.

- It has broadened the accepted collateral for the funding operations to include corporate bonds.
- It has implemented the Bank bond purchase program to mitigate disruptions in fixed income markets.
- It has established the Conditional Funding Facility, FCIC1 and FCIC2, to encourage credit to the most vulnerable sectors.

The description of the measures, their objectives, and their impact on the CB's balance sheet will be detailed in the following slides.

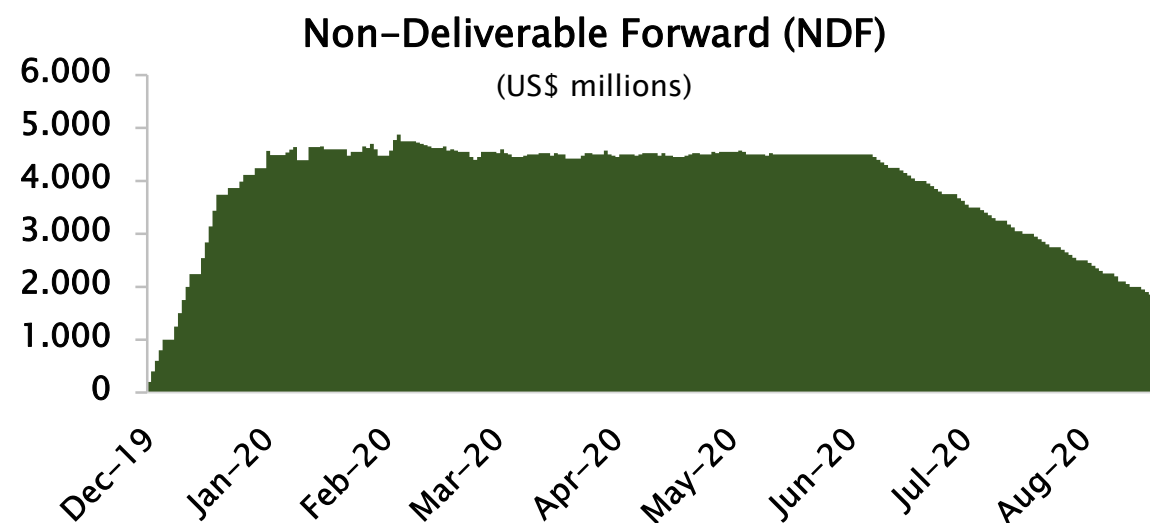
1. Mitigate the volatility of the CLP in order to allow adequate price formation.

- On November 28th, 2019, the CB announced an exchange rate intervention program which lasted until May 2020.
- The program considered amounts up to i) US\$10 billion in **spot sales**, and up to ii) US\$10 billion in stock of **currency hedging instruments**.
- On January 3rd, 2020, temporary spot sales were suspended, totaling US\$2,550 million and US\$4,500 million in forwards, which will be renewed as they expire.



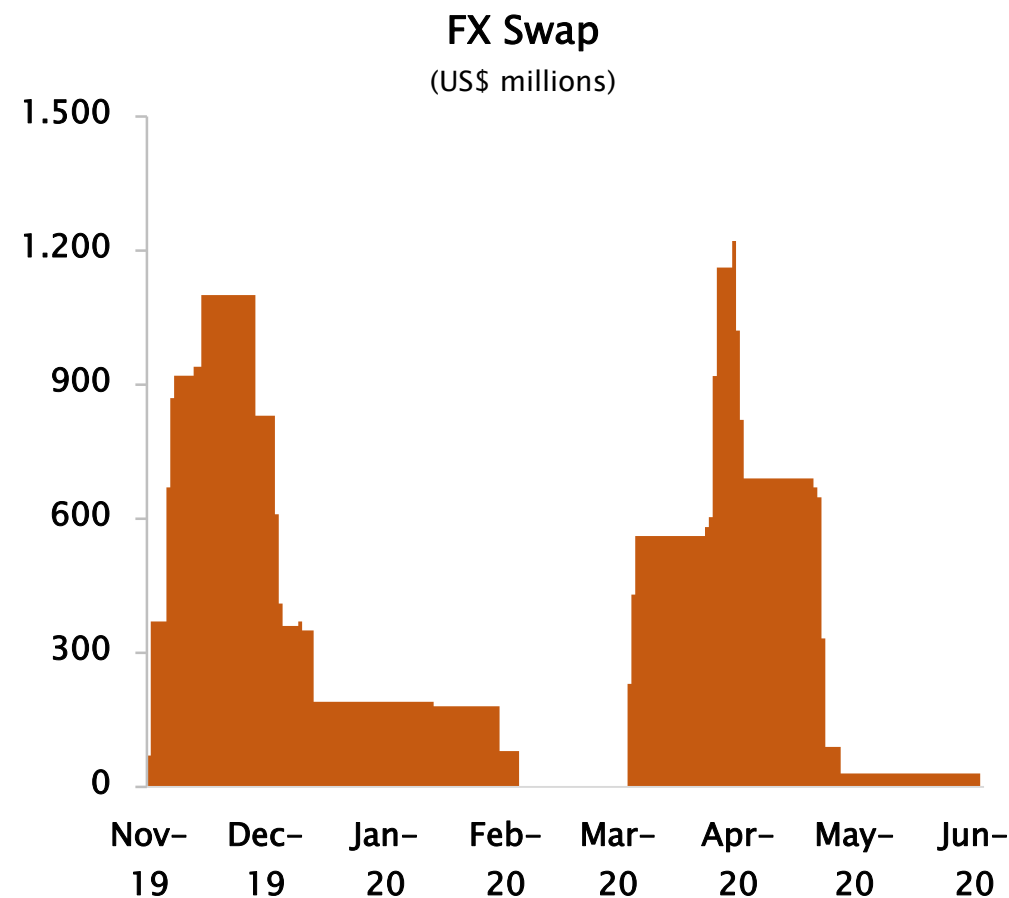
1. Mitigate the volatility of the CLP in order to allow adequate price formation

- On March 16th, the Board extended the exchange intervention program to January 9th, 2021, as a result of impacts of COVID-19.
- On June 3rd, the CB announced that it will let the stock of US\$ forwards expire at a rate of US\$250 million per week, due to decreased volatility of the exchange market. However, it conditions the behavior of volatility in this market and reiterates that the exchange intervention program will continue until January 2021.
- If the differential between the forward's trading price and the observed exchange rate is positive, the banks pay the CB, implying less liquidity without affecting the balance sheet



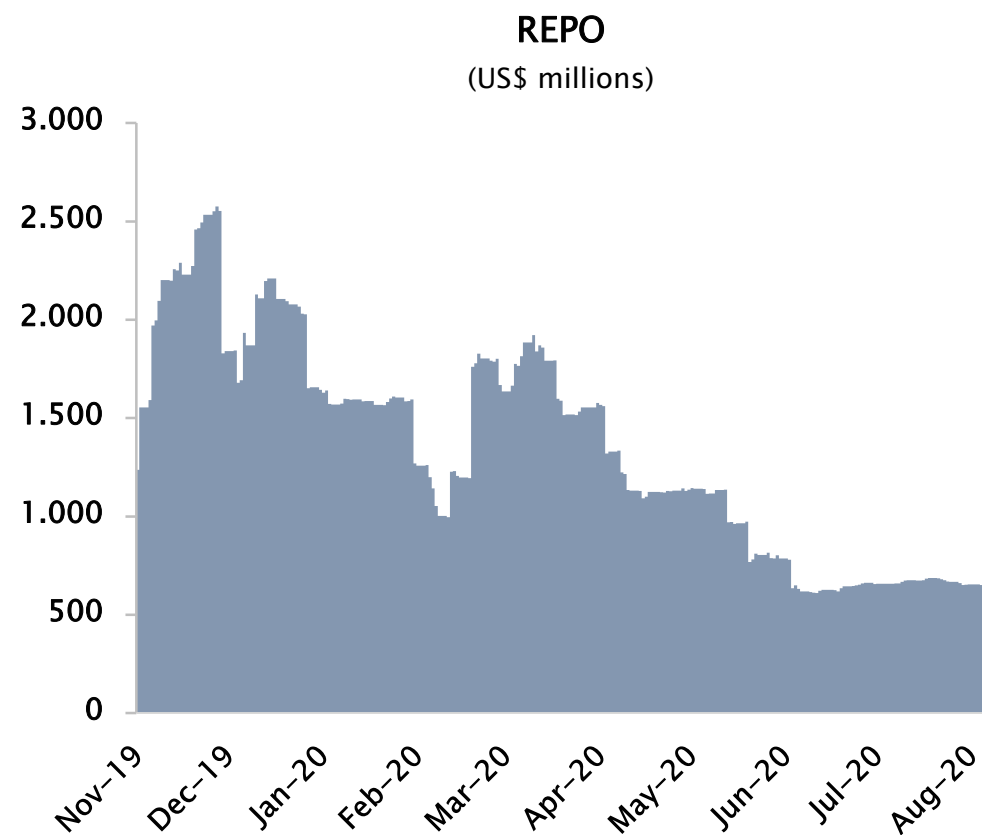
2. Facilitate the management of liquidity in US\$ in order to mitigate eventual tensions in the financial markets

- **FX swaps** have been implemented since November 2019.
- These are temporary operations of term loans in US\$ at a LIBOR + 200 bp, and are guaranteed with liquidity in pesos.
- Maturities were extended in March 2020: 30, 90 and 180 days, all at a LIBOR + 200 bp



3. Facilitate the management of liquidity in CLP

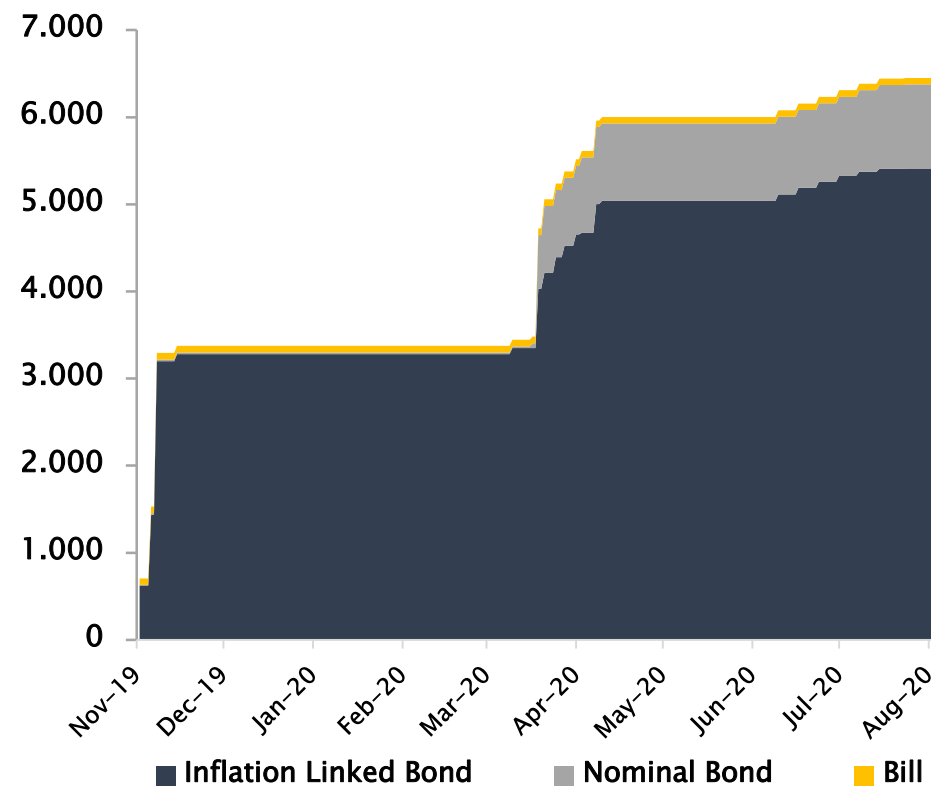
- **REPOs** have been implemented since November 2019.
- These are temporary operations of term loans in pesos at a MPR, which are guaranteed with financial instruments
- Maturities were extended in March 2020: 7, 30, 90 and 180 days, as were the universe of collaterals: instruments issued by CB, Government, banks and corporate entities.



3. Facilitate the management of liquidity in CLP

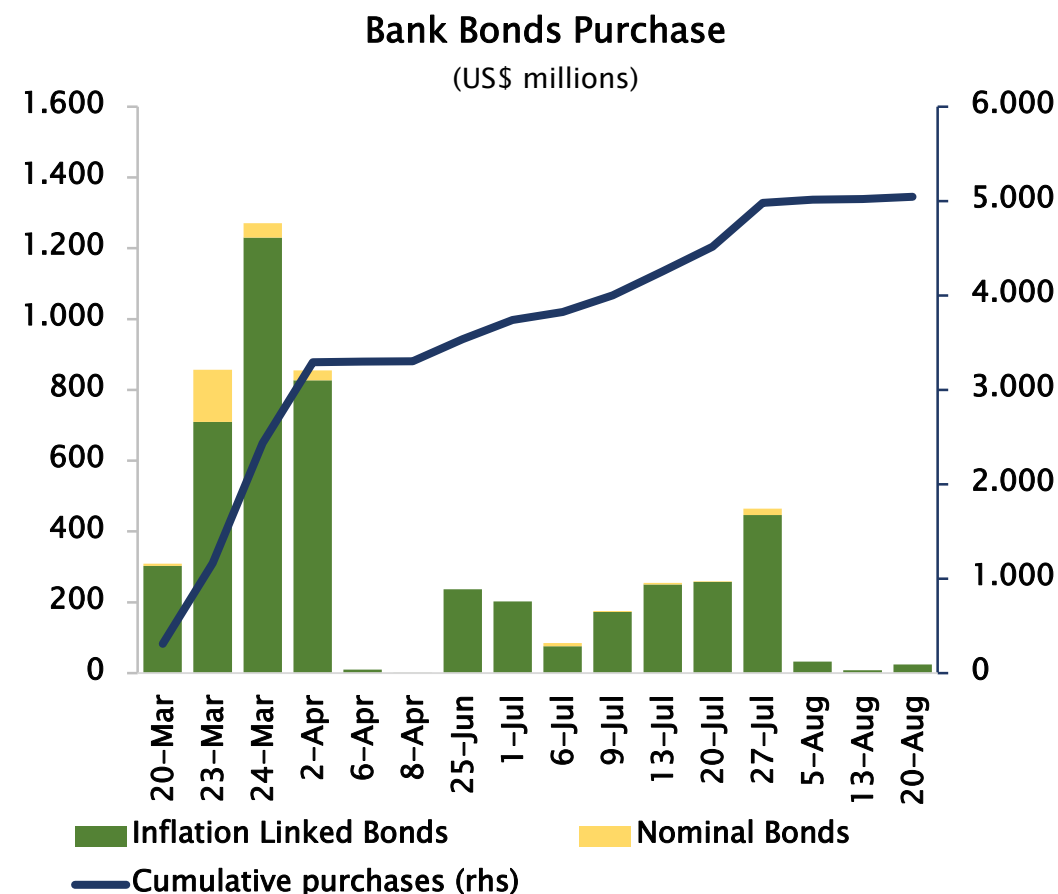
- The CB has been buying back **its instruments** at market prices since November 2019. The total buyback amount has reached US\$3,300 million.
- The program was modified in March, to buying back all instruments with maturities below 3 years at MPR of 0.5%. The goal was improve the transmission of monetary policy.

Cumulative Buyback by Instrument Type
(US\$ millions)

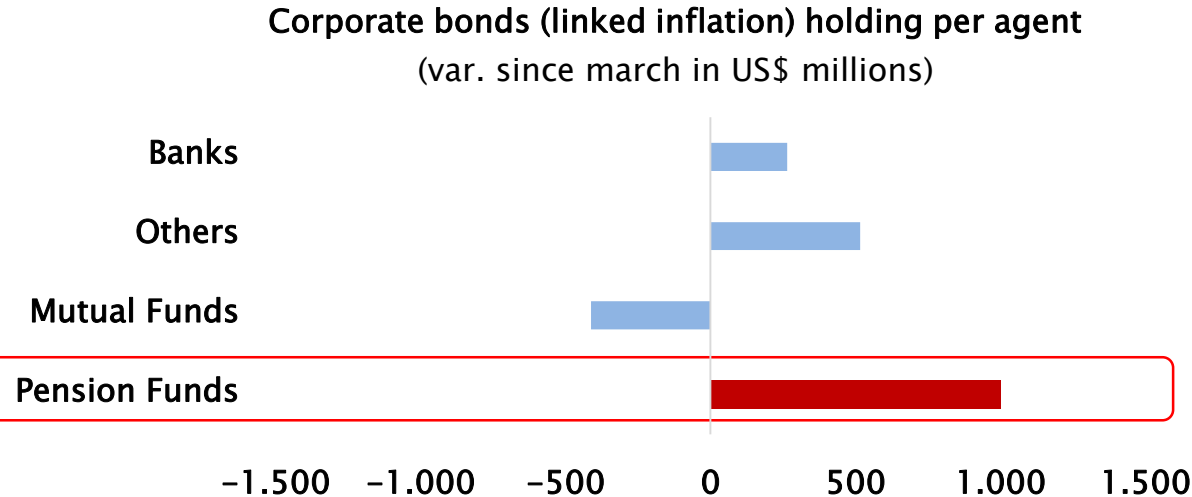
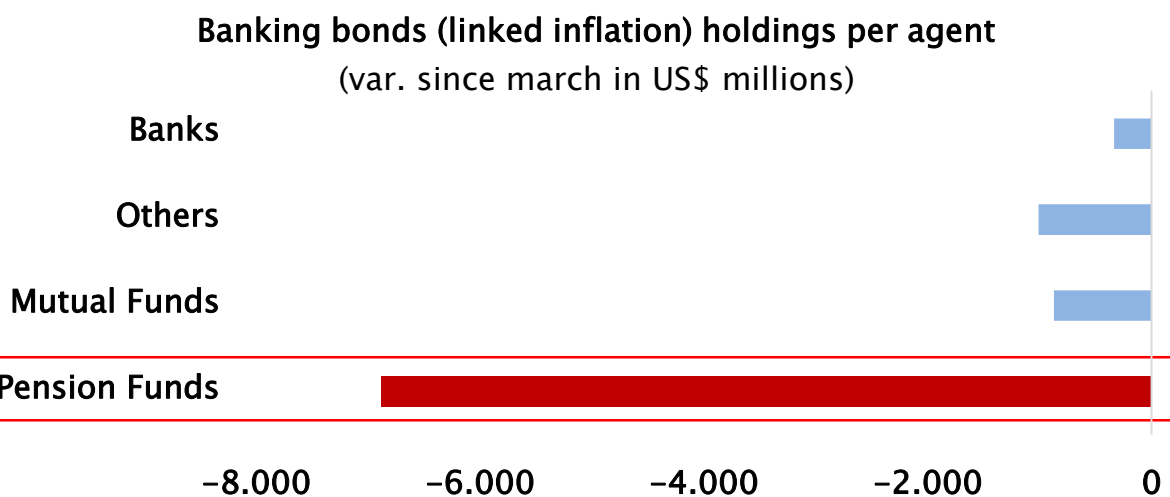
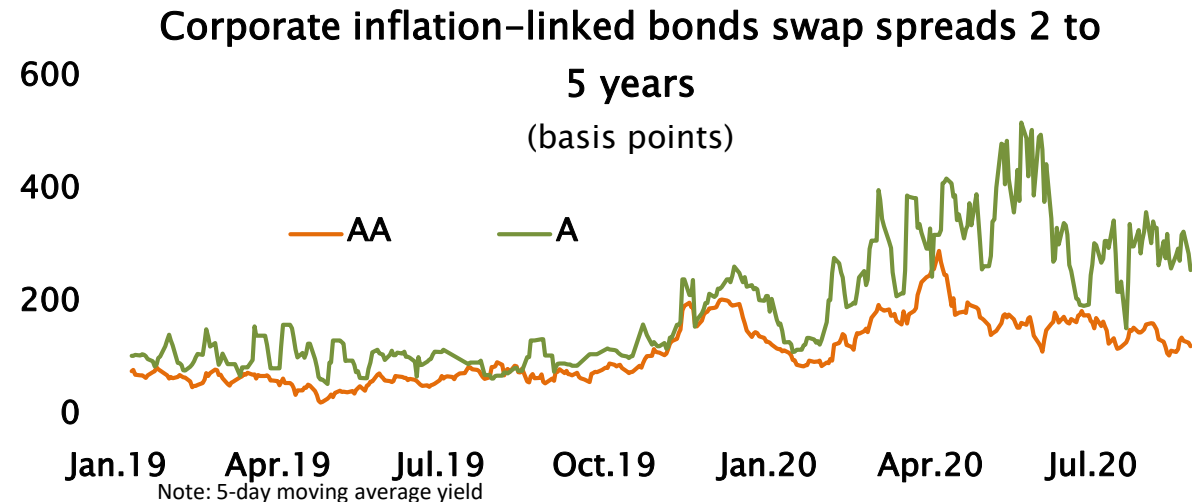
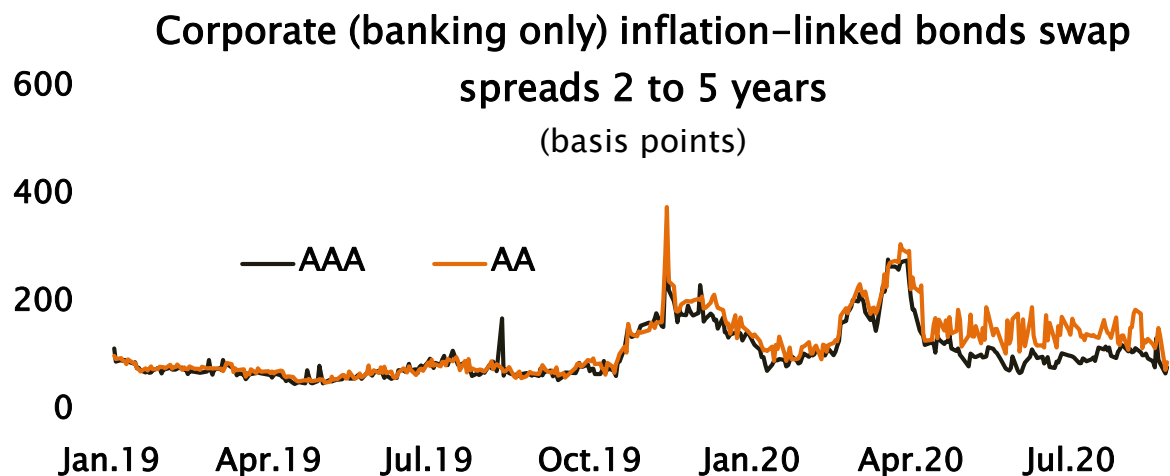


4. Contain volatility in the fixed income market

- **Bank Bonds Purchase (BBP):** this program was announced in the MPM of March 16th, to purchase a total of US\$4,000 million.
- Purchases were made at swap promedio camara (SPC) premium rates, differentiated by the issuer's risk rating:
 - AAA = SPC+250 bp
 - AA = SPC+260 bp
 - A = SPC+280 bp
- Last March, the total amount of the purchases was increased to US\$8,000 million.



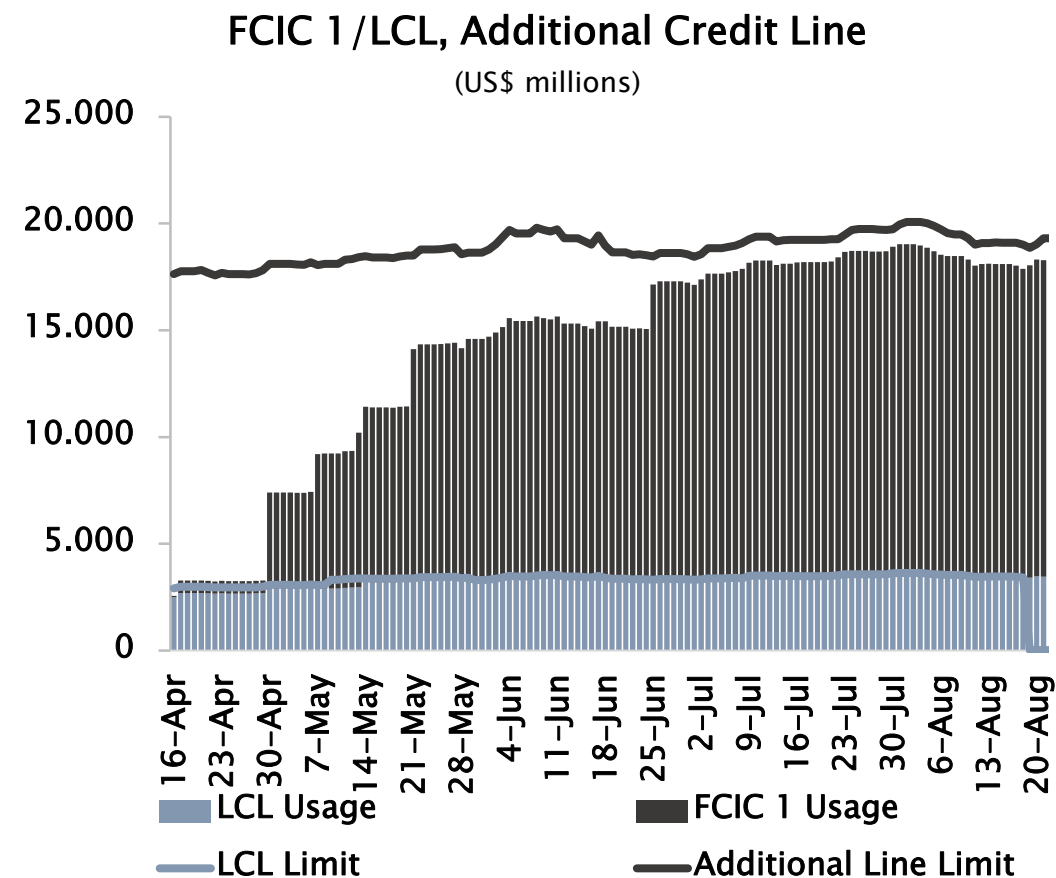
In fact, BBP program had an intended crowding-in effect on corporate bonds (which are not permitted for CB purchases). We also saw some additional contraction in most spreads for both markets since our last call



5. Provide liquidity, support the flow of credit and the transmission of monetary policy

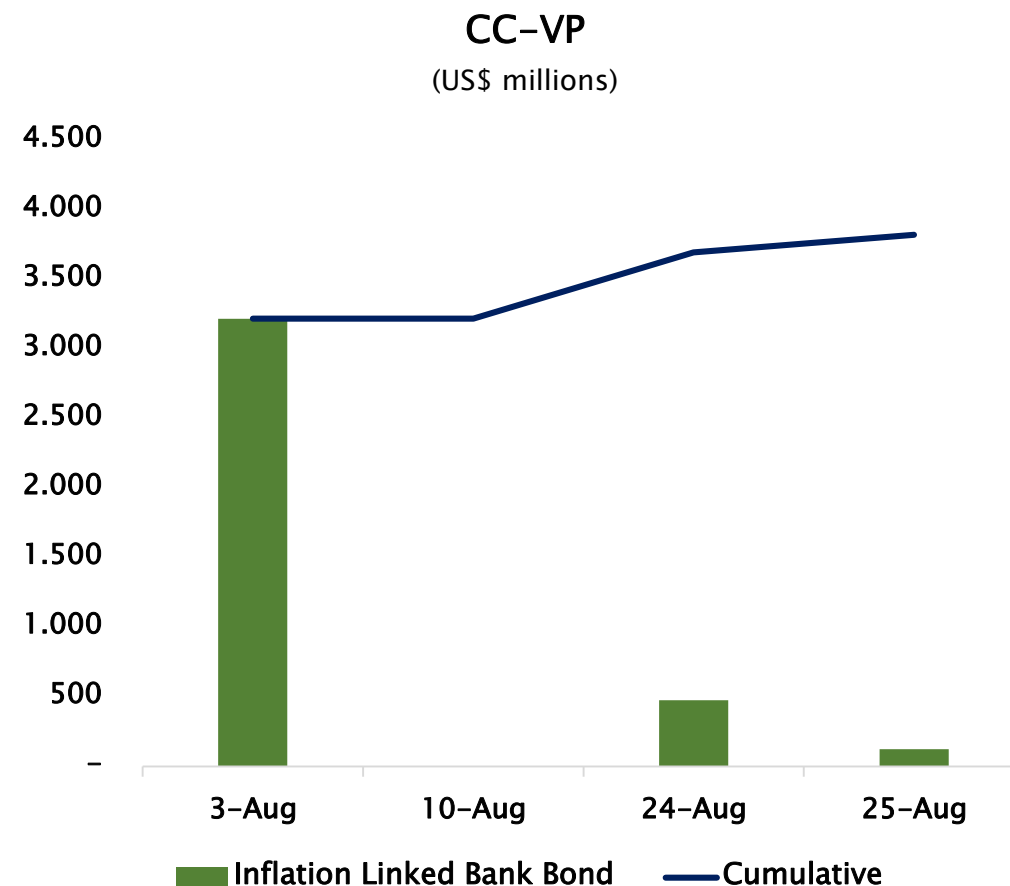
- The **Condition Funding Facility (FCIC)** is a special financial line used to promote the financing and refinancing of loans for households and small and medium size companies.
- This measure has a limit of 15% of the total bank's portfolio, equivalent to US\$24,000 million. The maturity is 4 years, at minimum MPR. The instruments for the guarantees include instruments issued by CB, the Government, banks, corporates and banks' credit portfolio.
- A 2 year **Credit Liquidity Line (LCL)** was also offered at a minimum MPR, backed by the constitution of reserve requirements in pesos.

In June an **FCIC2** was approved, for up to an additional US\$16,000 million.



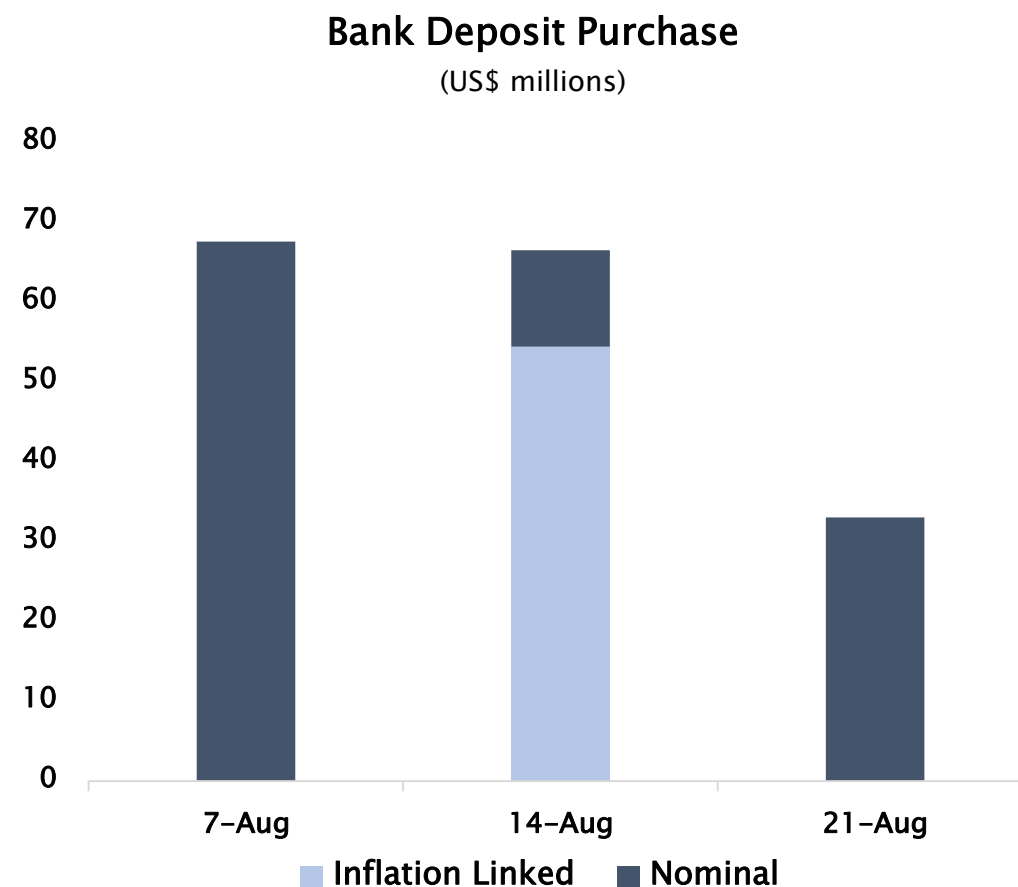
6. Mitigate volatility resulting from the change in the Pension Fund portfolio

- On July 8th, the withdrawal of 10% of the pension funds was approved, which would cause a liquidation of asset by PF. Two additional measures were implemented:
- **CC-VP**: cash purchase of bank bonds with joint and simultaneous sale in terms of 1 or 3 months, for up to US\$10,000 million.
- Until now, the total amount reached is US\$3,837 million.



6. Mitigate volatility resulting from the change in the Pension Fund portfolio

- **Bank Deposit Purchase:** direct purchase over discount window of bank deposits, for a total amount of US\$8,000 million.



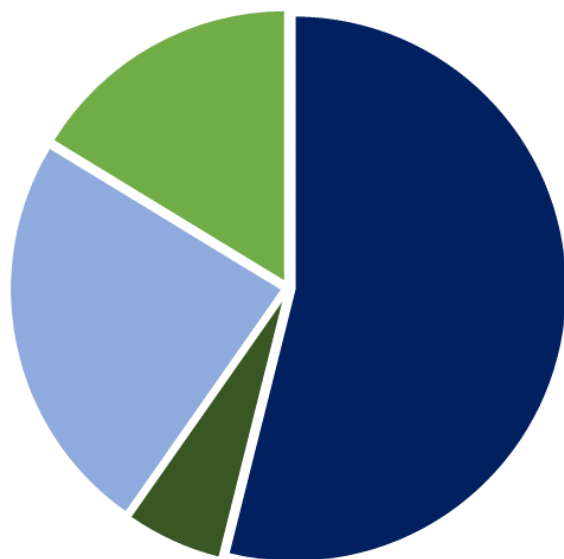
So far the FCIC has been the most effective tool to provide liquidity. The purchase of bank bonds and the CB's debt buy-back program have also played an important role. Special programs liquidity injection account for around 20% of GDP.

Central Bank of Chile Special Operations				Impact on CB's Balance Sheet		
	Amount of the program	Current amount	Total amount since announcement	Assets	Liabilities	Balance Sheet
FX Spot	10,000	2,550		↓ RIN	↓ Liquidity, Bill	↓
NDF	10,000	1,650	35,540	↑→↓	↑→↓	↑→↓
FX Swap	4,000		2,422	↓ RIN ↑ US\$ credit	Unchanged	Unchanged
REPO		621	6,214	↑ REPO	↑ Liquidity, Bill	↑
Purchase of bank bonds	16,000	5,385		↑ BB	↑ Liquidity, Bill	↑
CC VP Program	10,000	3,837		↑ BB pledge	↑ Liquidity, Bill	↑
Deposit Program	8,000	167		↑ BD	↑ Liquidity, Bill	↑
Bond buyback of CBC	8,514*	6,190		Unchanged	↓ BCP, BCU ↑ Liquidity, Bill	Unchanged
Facility of Conditional Financing to the Increase of Placements fo Banking Companies (FCFI) and Liquidity Line of Credit (LLC)						
Use of LLC	Use FCFI 1 + LLC	Use FCFI 1 + LLC (%)	Use FCFI (FCFI1 + FCFI2)	↑ LCL, REPO pledge (FCIC)	↑ Liquidity, Bill	↑
7,077	22,978	95	19,889			

On August 6, a law was approved that allows the CB to buy Government Bonds. So far this measure hasn't been used, however it allows the CB to have another mechanism for providing liquidity if necessary.

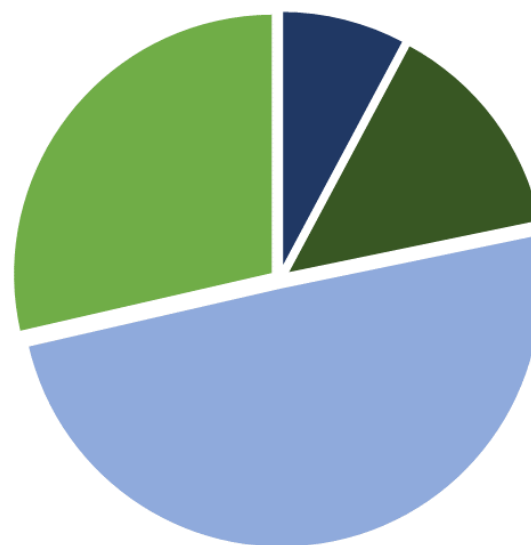
Stock of US\$ 64,244 millions

Holding Government Bonds (%)



Stock of US\$ 1,708 millions

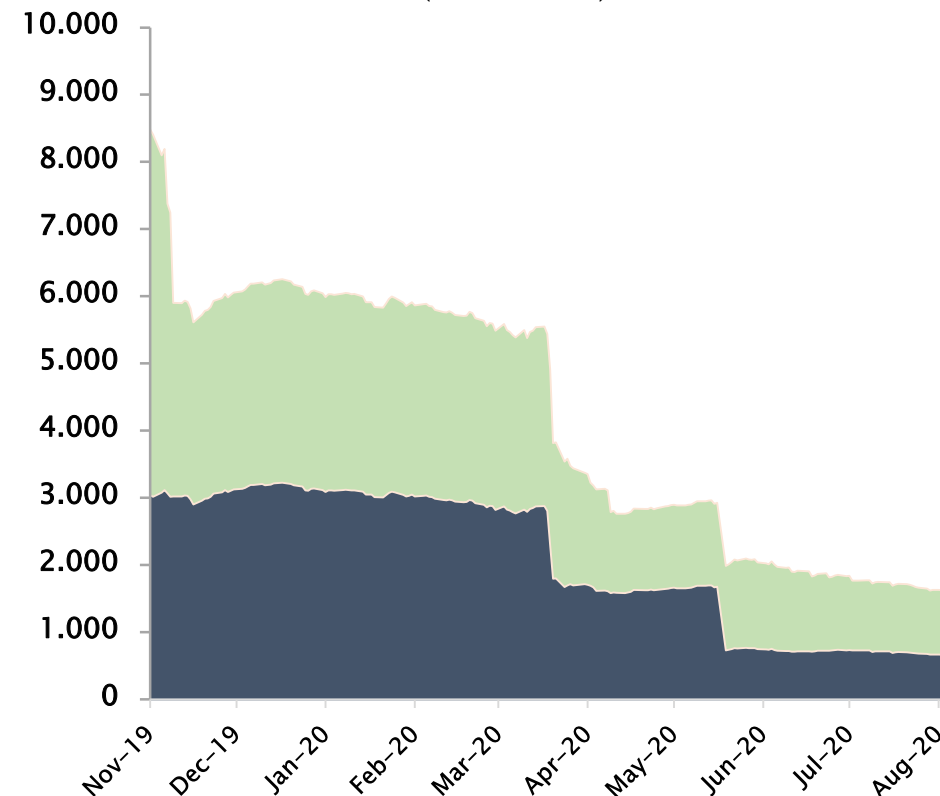
Holding Central Bank Bonds (%)



■ Pension Fund ■ Mutual Fund ■ Banks ■ Others

Central Bank Debt Stock (BCP-BCU)

(US\$ millions)

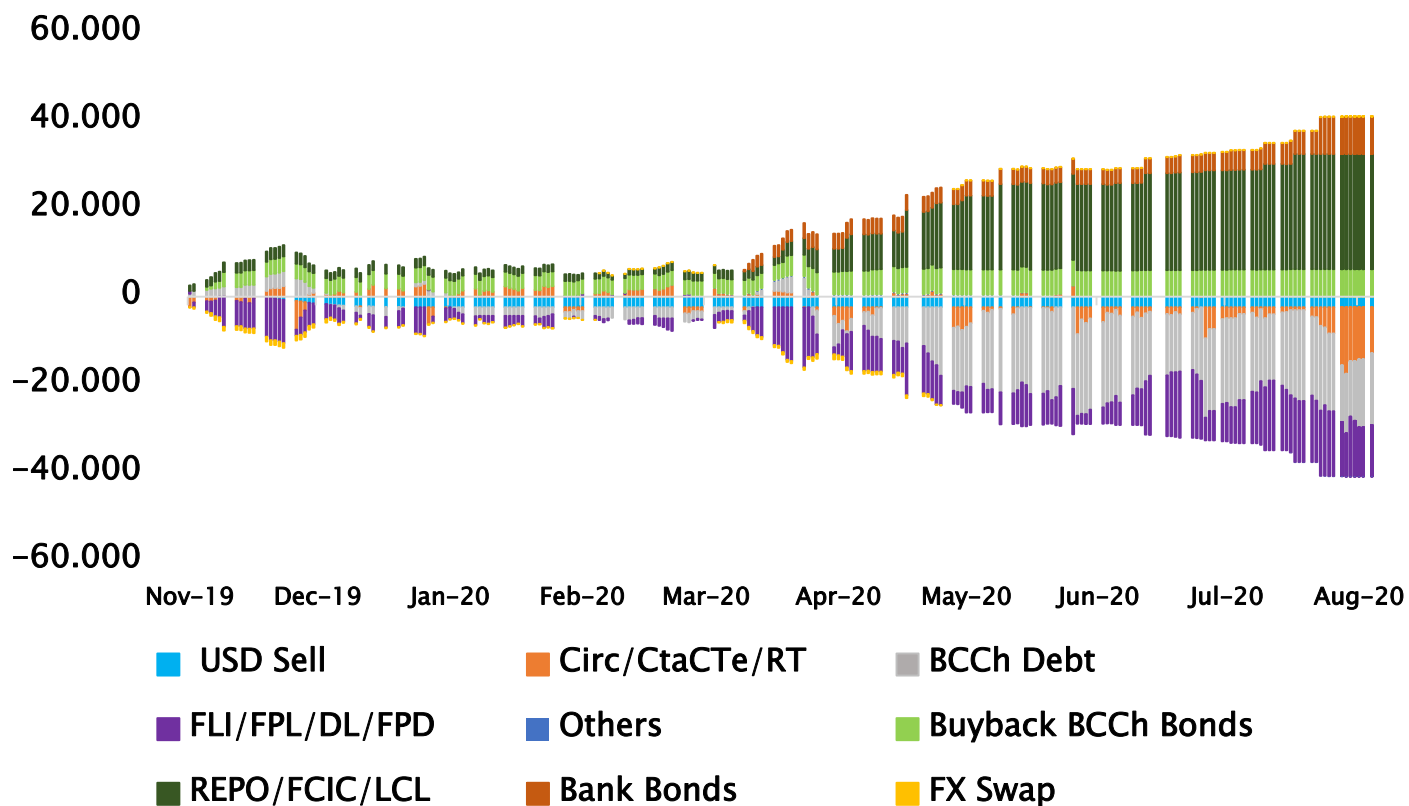


■ BCP (Nominal Bond) ■ BCU (Inflation Linked Bond)

All these operations have implied an increase in local assets on the Balance sheet, which now represent 17% of GDP, as compared to the RIN which are equivalent to 15% of GDP.

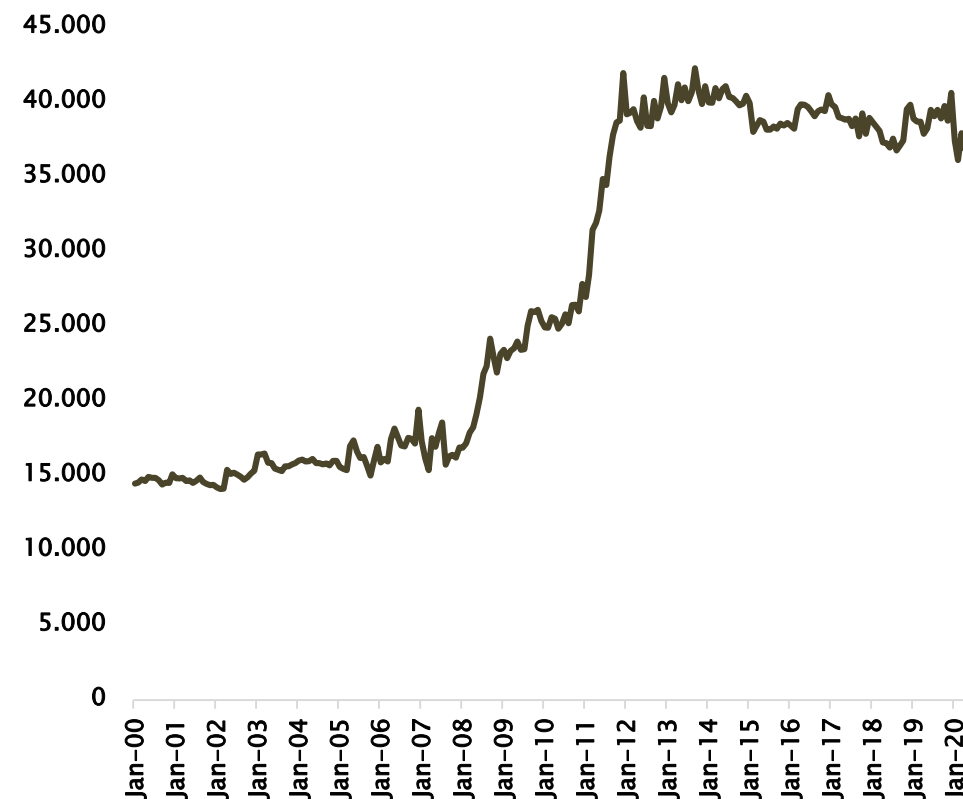
Central Bank Balance Sheet

(mill. US\$)



International Reserves

(US\$ millions)



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