Inflation Report - September 2012

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The Monetary Policy Report presents the Bank's technical staff's analysis of the economy and the inflationary situation and its medium and long-term outlook. Based on it, it makes a recommendation to the Board of Directors on the monetary policy stance. This report is published on the second business day following the Board of Directors' meetings in January, April, July, and October.

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In September 2012 annual change in the consumer price index (CPI), core inflation measures, expectations at different horizons and inflation forecast for December stood around the mid-point of the target range (3%).

At the end of the third quarter annual inflation stood at 3.08%, down by 12 basis points (bp) on June (Graph A), thanks to slower year-on-year growth in food CPI: 3.63% in September, down from 4.22% in June.

Non-food CPI and the other three measures of core inflation expanded year on year in the third quarter, at an overall average rate of 3.16%, up by 14bp on June.

The tradables component of non-food CPI remained relatively stable in the third quarter, rising year-on-year by 1.09% in September. Over the same period, nontradables accelerated from 3.62% to 4.02%, owing notably to rental CPI, which continued on the uptrend that started more than a year before, reaching an annual rate close to the targetrange ceiling. The price rise in regulated goods and services was 3.63% in September, making this the only group that lost pace in the third quarter (-61bp), because of lower increases in energy and gas. Oneyear-ahead inflation expectations obtained from the survey of analysts stood at 3.23% in October, down from 3.37% in July, whereas inflation expectations at 2, 3 and 5 years derived from public-debt securities rose to stand at rates close to 3%.

Second-quarter growth in gross domestic product (GDP) was 4.9% year on year, exceeding the technical staff’s estimated range of 3.3%-4.8%, as a result ofstronger than projected growth in domestic demand (6.4% year on year). This stronger growth was driven mainly by public consumption and investment in civil works.

Figures for third-quarter economic activity point to slower year-on-year growth, partly because of the high base of comparison recorded in the third quarter of 2011. Information on retail trade, vehicle purchases, business perception and household confidence points to deceleration in private consumption. However, the good performance of consumer imports, of credit for this spending and of the labor market indicates that the deceleration should not be too marked. In the case of investment, capital-goods imports and the increase in mortgage and commercial loans suggest that construction and other investment items will be rising at a good pace.

Although local-currency loans at September rose faster year on year than the nominal GDP growth estimated for 2012, their loss of pace went hand in hand with real interest rates on loans close to the average rates calculated since 2000 (except in the case of credit cards).

Externally, economic activity indicators for the third quarter confirm the global economy’s weakness. The economy of Europe continues to contract, while the US economy grows at a modest pace. The slowdown

observed in some of the larger emerging countries seems to be leveling off. In this context, with no inflationary pressures, external interest rates can be expected to remain low for a long time.

International financial conditions improved throughout the quarter, owing in part to policy action by the major central banks of the world. Volatility has decreased and some asset prices have risen. But there is still great uncertainty about some advanced economies' public finance and banking problems.

Despite slower global growth, international prices for oil and other commodities remain high, keeping Colombia's terms of trade elevated and boosting national income. However, in Colombia as in other countries, the world economy's weakness has been reflected in slower growth in exports and industrial production.

Based on the above domestic and external developments, the Bank's technical staff expects third-quarter GDP growth to have been in the range of 3.3% to 4.8%, year on year, with 3.9% as the most probable figure. Despite signs of a slowdown, growth in the coming quarters will still be driven by domestic demand. A sound financial system, household confidence and a dynamic labor market will continue to support higher consumption. For their part, commodity prices, confidence levels, the availability of domestic and external funding, and foreign direct investment will help to expand investment.

GDP growth for full-year 2012 is projected by the technical staff to be in the range of 3.7% to 4.9%, with the most probable figure standing at the mid-point of this range. For 2013, growth should be around 4.0%, but in a wider forecast range with a downward bias (2.%-5%), reflecting the possibility of a deep recession in the euro area that could have a significant impact on Colombia's economy.

The above price and growth developments reflect an economy in which inflation, and inflation expectations and projections are close to the long-term target (3%) and the output gap is close to zero. Interest rates on loans are around the average rates calculated since 2000, while housing prices are historically high. The greatest risk to the country's economic activity still relates to a deep recession in Europe, although this appears less likely to occur, given the actions taken by the European authorities and market reactions to them. In view of this macroeconomic setting, the Bank's Board of Directors decided to reduce the policy interest rate in July and August, from 5.25% to 4.75%, and then left it unchanged in September and October (Graph B).

To provide more and lasting liquidity to the economy, the Board decided on August 24 that through to September it would buy US$700 million by means of daily auctions of at least US$20m. On September 28 it decided that from October 1 to March 29, 2013 it would buy at least US$3 billion by the same mechanism.

The Board will continue to monitor carefully the international situation, inflation behavior and projections, growth, and asset-market behavior, and reaffirms that monetary policy will depend on new information that becomes available.

Fuente: https://www.banrep.gov.co/en/news-and-publications/inflation-report-september-2012