Minutes of a Meeting of the Board of Directors of Banco de la República Held on March 22, 2013

Detailed Explanation of the Macroeconomic Situation (only in Spanish) Must reads Banco de la República Lowers the Benchmark Interest Rate by 50 Basis Points Last modified Monday the 29th of April, 2024
A regular meeting of the Board of Directors of Banco de la República was held in the city of Bogotá D.C. on March 22, 2013. In attendance were Mr. Mauricio Cárdenas Santamaría, Minister of Finance and Public Credit, Mr. José Darío Uribe, Governor and Managing Director of Banco de la República, and full-time co-directors Messrs. Carlos Gustavo Cano Sanz, Ana Fernanda Maiguashca Olano, Adolfo Enrique Meisel Roca, César Vallejo Mejía and Juan Pablo Zárate Perdomo. Inflation and the economic situation were discussed with respect to growth and prospects for the future, and monetary-policy decisions were reached.

1. BACKGROUNDa. Recent Developments in Inflation
In February the annual CPI inflation was 1.83%, 16 basis points (bp) less than the month before. As has been the case for several months, the minor adjustments in food prices are largely responsible for this result. However, the rest of the sub-baskets (regulated, tradables, and non-tradables) showed greater stability this month in comparison to what was seen in previous months.

The decline in the annual change in the CPI for food – from 1.7% in January to 1.2% in February – again covered a substantial number of products including perishables (from -5.0% in January to -5.6% in February), processed (from 2.2% in January to 1.6% in February), and eating away from home (from 3.9% in January to 3.6% in February). The different factors that could be the explanation for this performance in February and in previous months are: the few increases in international prices for imported food, the very limited exchange rate pressure, the low cost pressure (partly due to the reductions in tariffs associated with the trade agreements that have gone into effect), and climatic conditions that are favorable to the supply. It is also possible that the reduction in the IVA for eating away from home and some perishable food items since the beginning of the year is still in the process of being transmitted to prices in February. Furthermore, last month the lower demand form Venezuela would have begun to play a significant role and this could be translating into an upswing in the agricultural supply of products such as meat, eggs, and chicken that is available for domestic consumption. The adjustments in the prices for these products were low or even negative last month.

Within the CPI excluding food, there were no significant changes in the annual variations for regulated prices and tradables excluding food and regulated items. In the first case, the annual change in February remained at 0.7%. Even though there were increases in the fees for natural gas service, electricity, and fuel, these were offset by nullifying adjustments in the fees for water and sewer service and by a significant reduction in the ticket prices for intermunicipal buses. It is noteworthy that the annual change in the CPI for regulated prices showed significant drops in the second half of 2012 and in January of this year.

For tradables excluding food and regulated prices, the annual change in February was low (0.7%) and similar to what was registered in January. In this sub-basket, reductions or rare rises in the prices of imported goods such as cars, electrical appliances, electronic and communication devices, as well as airline tickets, etc. continued to be seen. The accumulated appreciation from previous months and the low pressure from international prices are the explanation for this situation.

Finally, the annual change in the CPI for non-tradables excluding food and regulated prices declined a little in February to 3.84% with respect to the 3.94% in January although it is still the sub-basket with the highest adjustments. A substantial part of the reduction was accounted for by the segment of entertainment, cultural and leisure activities. Other components that showed minor adjustments were enrollment fees, pensions and some health services. The annual change for rent, an item that has been highly indexed, remained at 3.8% and the declining trend it has been on for the last three months was broken.

In February, there was another decline in the indicators of core inflation but one that was less than what had been seen in the previous three months. The average for the four indicators that are monitored by the Banco de la República was 2.49% compared to 2.59% in January.

The annual change in the PPI remained in negative territory at -2.47% in February, which is 4 bp more that what was registered in January. This, as in previous months, is due to the accumulated appreciation and stability of international prices for the majority of raw materials and other goods.

nflation expectations for December 2013, which were gathered from market analysts through the Bank's monthly survey, declined in February although less than they had in previous months. At the beginning of March, this percentage was 2.55% compared to 2.65% in February. In spite of the above, expectations during both months for twelve months from now remained at close to 2.9%. In the case of the expectations that are estimated on the basis of the TES rate, no declines were seen there either in the four weeks prior to the closing date of March 14. The inflation expected for two, three, and five years from now was close to 2.6% which is slightly above the datum from the month before.

b. Growth

The latest information published by DANE shows a sharp revision in several of the components of the GDP for 2011 and 2012, especially investment in public works. With this, DANE corrected the figures for GDP growth in 2011 from 5.9% to 6.6%.

When the revisions are incorporated, the rates of annual expansion for the first three quarters of 2012 were 5.3%, 5.0%, and 2.7% respectively. The datum for the fourth quarter was 3.1% and that for the full year was 4.0%. Domestic demand grew 4.6% in 2012 which represents a slowdown in comparison to what was registered in 2011 (8.2%). The slowdown was mainly seen in the second half of the year.

Household consumption played an important role and actively contributed to the expansion of domestic demand. In the fourth quarter, private consumption grew 4.0%. However, this part of the GDP also showed a loss of strength in its annual rate of growth as it went from 5.9% in 2011 to 4.3% in 2012. Breaking it down by component, the most serious slowdowns were registered in expenditures allocated to the purchase of durable and semidurable goods. Services and the purchase of non-durable goods, in turn, also slowed down but to a lesser degree. With regards to government consumption, the annual expansion was 6.5% in the fourth quarter and 5.1% for the entire year.

With respect to fixed gross capital formation, this expenditure grew 6.0% in 2012 which is also lower than the growth in 2011 (18.7%). The component that contributed the most to the growth of expenditure on capital goods was what was allocated to investment in machinery and equipment. This grew 7.7% for the year as a whole. In the second half of 2012, all of the items that this aggregate is made up of showed a generalized slowdown, which complicates the interpretation of the shocks that this aggregate suffered in the second half of the year.

In 2012, significantly lower growth rates were registered for imports and exports. With respect to the first aggregate, its expansion was 8.0% last year, which is much lower than what was registered in 2011 when it grew 21.2%. Foreign sales also showed less strength as they grew 5.3% compared to 12.9% in 2011. In the fourth quarter, annual growth on the order of 3.3% and 1.4% respectively for the two areas was registered.

Regarding supply, the mining (5.9% annually), financial (5.5 annually), and community, social and personal services (4.9% annually) sectors are among the sectors that grew more than the overall economy did in 2012. In the case of the mining sector, a sharp slowdown in comparison to 2011 (14.4% annually) was seen. It was concentrated in the second half of the year and was due to the contraction in the production of coal and the slower rate of growth in petroleum production. In the financial sector, in spite of the slowdown in loans in the second half of the year, significant growth was reported that contributed positively to the total expansion of the economy given its large share of the GDP (19.6%). Last of all, in the area of services, the performance of the community services provided by the government stands out. With respect to the economic situation for the first quarter of 2013, the information available points to the growth of the economy being lower than what was seen at the end of 2012. This trend suggests a current economic growth that is below its potential.

In the area of expenditures, household consumption could show a slowdown at the beginning of the year as the latest information from survey of consumer confidence measured by Fedesarrollo suggests. In February, this indicator fell significantly and went to levels that were slightly below their historical average. Added to that, there was a slump in car sales on the order of 16.4% in February according to the Colombian Automobile Committee and the figures published by Econometria. The monthly survey of economic expectations done by the Banco de la Republica, in turn, suggests that the sales in January were significantly lower than those registered in the fourth quarter of 2012. Nevertheless, it should be noted that the figures in dollars for imports of consumer goods showed an annual growth of 19.9% in January.

Total exports, in contrast saw a change of -1.1% in January in comparison to the same month in 2012. This drop was due to the combined reduction of exports of mining (-2.2%) and agricultural (-15.3%) products. Exports of industrial products (along with others) registered an annual growth of 10.2%, an upsurge with respect to what was registered in December. This better performance was primarily due to the rise in sales of vehicles (109.5%), chemical products (13%), and rubber and plastics (43.7%).

In the area of supply, the variables associated with industry continue to show poor performance. In January, the order, inventory, and production expectation indicators continued to hold to the negative trend of previous months. Furthermore, the unregulated electricity demand fell 2.1% annually for industry in February after having grown a little more than 2% in January. This indicator, which is highly correlated with the growth of industry, suggests an additional deterioration in the sector for that month. The fact that part of this fall was because of one less working day in February this year (the year before was a leap year) should be kept in mind.

With regards to the area of mining, production of coal was affected in February and March by labor strikes in Cerrejon and the environmental problem Drummond had which caused a stop in production due to the restrictions on transportation of the product to the port (temporary suspension of the freight license). In the agricultural area, the fact that coffee production grew 36.7% annually on average between January and February should be emphasized.

Moreover, in addition to the unexpected shocks in the mining sector, there were fewer working days in the first quarter of the year (Easter week and one working day less in February) which have a negative impact, especially on the industrial sector.

The numbers from the labor market show that the unemployment rate continued to fall at the beginning of the year. Furthermore, as of January, the growth in the level of employment showed something of an upswing and the indicators of employment quality continued growing at significant rates. Wage-earning employment, in particular, surged substantially.

c. Financial Variables

The growth of bank loans (L/C and F/C) has stabilized in the last five months at an annual rate of growth of close to 15%. The slowdown in the loan portfolio denominated in local currency has been offset by a boost in

the loan portfolio denominated in foreign currency. Between October 2012 and February 2013, the rate of growth for the former slipped from 15.8% to 14.4% while the latter went from 6.0% to 24.8%.

Going by types of loans, the annual growth of the commercial loan portfolio went from 13.2% in October 2012 to 14.2% in February 2013. Loans allocated to households, in turn, saw a slight slowdown in February with 16.9% compared to the 18.6% seen in October 2012. The mortgage portfolio also saw a slowdown in the annual change during the same period (from 15.5% to 14.5%).

The nominal interest rates for all of the different types of loans granted marked a declining trend in comparison to their levels during the last part of July when the policy interest rate began to go down. However, in real terms, the decline in inflation and inflation expectations has neutralized a large part of that trend.

The real interest rate in February for disbursements allocated to consumption was 16.0%. Those for mortgages was 10.2%, for preferential loans, it was 5.9%, for regular commercial loans, 9.0%, all of which rates are below their respective historical averages calculated since 2000. However, the real interest rates for credit card loans and for the treasury loans were at 27.1% and 5.8% respectively. These are above their averages calculated since 2000.

d. The External Context

The new information suggests that the average economic growth our trading partners will have in 2013 could be somewhat less than what had been estimated in past reports and lower than what was registered in 2012. Furthermore, the uncertainty and risk perception in the financial market which had declined in the last few months could rise again due to the events in Europe last month.

In the euro zone, the recovery of productive activity has not materialized yet and everything indicates that the GDP for the region has continued shrinking in the first quarter of the year. In spite of that, the rate of deterioration in productive activity seems to be moderating since some indicators such as industrial activity and the opinion indices in the manufacturing and services sectors have paused in their downward trend. In addition, there has been a slight recovery in consumer and business confidence in the last few months. The most favorable news comes from Germany. In this country, a reactivation of productive activity was seen in the first few months of the year due to the exports to countries outside of the region and to the strength of domestic consumption. In this context, economic activity is expected begin to recover in the region by the second half of the year. However, the political climate and the decisions made by the European economic authorities could affect confidence in the region again as has occurred recently since the inconclusive elections in Italy and the conditions for rescuing the banking sector in Cyprus.

In the United States, the figures for the productive activity in the first few months of the year are relatively favorable and suggest that the economy has continued to expand. The real estate sector and labor market are still recovering slowly. However, since there was no agreement with respect to the budgetary cuts in health and education, the fiscal adjustment in the United States could be greater than expected. That could have a negative effect on the outlook for growth for this country in 2013. The drop in consumer confidence that was seen in the first weeks of March could already be reflecting this.

In China, although the indicators for January and February are not easy to interpret given the effects of the new year, it can be said that growth did not slow down during those months. Therefore, productive activity would have continued to expand at a favorable rate.

In the larger economies in Latin America, growth for 2012 was good with the exception of Brazil. Some economic indicators for the first quarter of the year show a favorable performance in Chile and Peru and to a lesser degree in Mexico. A recovery has been seen in Brazil but it is still at low levels. Low growth is estimated for Venezuela in 2013.

Regarding the international prices for petroleum, the upswings seen in February have reversed. The weakness of global demand and some favorable data on the supply of petroleum and its substitutes could explain the lower prices in the last few weeks. Other prices for goods exported by Colombia such as coal, nickel, and coffee have remained relatively stable at levels below those seen last year.

In the case of prices for food, although there have been some rises in soybeans, corn and palm oil, these still do not represent an inflationary risk and are not expected to continue given the expectations for a good worldwide supply.

That being the case, inflation in the main developed economies and in some of the emerging ones (mainly Latin American) is remaining at relatively low levels. This fact, together with the weak economic growth, has made it possible for the central banks in developed countries to maintain an expansionary monetary policy. In addition, it has allowed several central banks in emerging countries to reduce their policy rates recently.

In this context, if the risk premiums Colombia remains at the current levels, the cost of external financing for the country will continue to stay low.

In summary, the new information suggests that the average economic growth that our trading partners will have in 2013 could be somewhat lower than what had been estimated in past reports and below what was registered for 2012. If these predictions materialize, the contribution that foreign demand would make to Colombia's growth will remain low. Likewise, if the trend that has been seen in prices for the main export products continues, the average terms of trade in 2013 will be lower than those seen last year.

2. DISCUSSION AND POLICY OPTIONS

The board of directors took the following relevant aspects under consideration:

(i) The growth of our trading partners will probably be lower than expected and, as a result, the contribution of foreign demand to the growth of the country will remain low. Likewise, if the trends that were seen in the prices for our main export products should continue, the average terms of trade in 2013 will be lower than those from last year. As a consequence, the aggregate expenditure in 2013 will not have an additional boost from a larger national income.

(ii) The new data on economic growth for 2012 (4%) show a slowdown from the high levels in 2011 (6.6%). The largest loss of strength occurred in the second half of the year and was mainly due to a significant reduction in the growth of investment. The growth of private consumption moderated in 2012 and came to rates that were similar to their historical average. The growth of exports also registered a decline in comparison to 2011 with a significant fall in the fourth quarter.

(iii) Interpretation of the shocks that investment suffered in the second half of 2012 is complex and could be due to multiple factors as can be seen from the fact that all of the components of this aggregate showed a slowdown in the second half of the year.

(iv) In the first quarter of 2013, the deterioration in trade expectations as well as the fall in the consumer confidence index and sales of automobiles suggest a lower performance in private consumption. In January, the value of the exports in dollars was similar to what was registered a year before and industrial exports registered a positive annual growth. Nevertheless, the indicators of business confidence indicate that industrial activity will continue to shrink. This performance suggests that the current economic growth is below its potential and, therefore, the constraints on the use of the productive capacity are increasing.

(v) The drop in annual inflation from 2.0% in January to 1.8% in February was similar to what was predicted by the technical team. This slowdown was mainly due to the lower rate of increase in food prices, mainly processed

ones. All of the measurements of core inflation also declined. Both the average of those measurements and inflation expectations are below the target (3%). The recent reduction in the international prices for energy and other commodities imply lower pressure on local inflation.

(vi) The reductions in the Banco de la Republica's interest rates have been transmitted to the interest rates for deposits and loans in the financial system. However, the real interest rates have not fallen to the same degree due to the sharp drop in inflation and inflation expectations.

(vii) The growth of the loan portfolio is becoming more moderate. So far this year, there has been a slowdown in commercial loans denominated in pesos but a rise in financing through the issuance of bonds by firms together with greater foreign indebtedness. Loans to households (consumer loans and mortgages) continues to grow more slowly but at rates that are higher than the rise in the nominal GDP. The continuing moderation in the rate at which firms and households are using leverage is reducing the risk of generating financial excesses during the current expansionary phase of monetary policy.

In this context, an evaluation of the balance of risks indicates the usefulness of reducing the benchmark interest rate 50 bp. With this, the macroeconomic policy is expected to be consistent with a growth of the economy that is close to its potential.

3. POLICY DECISION

Based on the evaluation of the current balance of risks, the Board of Directors agreed unanimously to reduce the benchmark interest rate 50 basis points. The decision was based on the fact that the Colombian economy is growing at a rate that is below its potential and will probably be operating at below its productive capacity over the next few quarters. In addition, the inflation that has been seen and is being projected is below the target of 3%. This is in a context in which the reductions in interest rates are seemingly being transmitted into the economy more slowly than desired.

The Board will continue to monitor the performance and projections for economic activity and inflation in the country, the asset markets, and international situation carefully. Finally, they reiterate that the monetary policy will depend on the new information available.

Fuente: https://www.banrep.gov.co/en/news/board-directors/minutes-march-2013