Minutes of the Banco de la República Board of Director's meeting on September 27, 2013

Detailed Explanation of the Macroeconomic Situation (only in Spanish) Must reads Banco Republica Holds the Benchmark Interest Rate at 3.25% and Adjusts the International Reserves Purchase Program 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 September 27, 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 the Board Members Carlos Gustavo Cano Sanz, Ana Fernanda Maiguashca Olano, Adolfo Enrique Meisel Roca, César Vallejo Mejía and Juan Pablo Zárate Perdomo. These minutes contain a summary of inflation, economic growth and their prospects for the future, which was prepared by the Bank's technical staff (Section 1), in addition to a review of the key deliberations and policy options considered by the Board of Directors (Section 2).

1. INFLATION AND ECONOMIC GROWTHa. Recent Developments in Inflation

Annual consumer inflation in August was 2.27%, which is 5 basis points (bp) above what was registered the month before. In the first eight months, the accumulated change in the CPI came to 1.86%, which is less than the aggregate variation for the same length of time in 2012 (2.03%).

The annual change in the CPI for food in August was 1.8%, 13 bp higher with respect to July. The upswing was concentrated in the basket of perishables (5.5% in comparison to 4.0% in July). This may be due to the decline in the supply of these products because of the blockades experienced that month. The change in the prices for eating away from home saw a slight rise as they went from 3.5% in July to 3.6% in August. The annual change in the prices for processed foods (-0.1%) dipped in comparison to July (0.1%).

In the CPI excluding food, the annual variation in August (2.45%) did not change with respect to what had been seen the previous month. The rises in the annual changes in the prices for tradables and regulated items were registered in this basket. In the case of the first one, the uptick (from 1.3% to 1.4% in August) is added to the ones seen during previous months and is partly related to the depreciation of the peso that has been registered over the course of the year. With respect to the regulated items, the annual change (1.5%) meant an increase of 9 bp compared to the month before. This upswing was concentrated in public transportation fees which went from growing 1.7% annually in July to 2.5% in August (the rise was partly the result of the effect of the statistical basis of comparison on the annual variation which captured the drop in Transmilenio fees ordered in August 2012). The other two components of regulated items –utilities and fuel– fell.

A decline of 12 bp in the annual change in the basket of non-tradables excluding food and regulated items (3.8%) occurred during the month. This level is similar to the one in June. In July, there had been an upswing of 12 bp. This volatility is essentially due to the segment of entertainment, cultural and leisure activities (specifically soccer tickets). The annual rental adjustment (3.7%), in turn, remained stable.

The average for the four core inflation indicators that are monitored by the Banco de la República was at 2.54% in August, a figure that is the same as the one for the month before. This indicator has been extremely stable at around 2.5% since February of this year.

The annual variation of the PPI stayed in negative territory in August (-0.5%). Both the local and imported components dropped in comparison to last month (52 bp in the former and 33 bp for the latter).

Inflation expectations did not register significant changes last month. According to the Bank's monthly survey of financial market analysts, expected inflation for December of this year remained at 2.6% while the inflation expectations for the coming 12 months were at 3.0%, 7 bp lower than the previous month. At the same time, inflation expectations derived from the yield curve of the TES at horizons of 2, 3, and 5 years have remained between 2.3% and 2.8%. These levels are slightly lower than the ones seen the month before.

b. Growth

In the second quarter of 2013, the Colombian economy grew 4.2% in comparison to the same period in 2012. This record was higher than the one for the first three months of the year (2.7%). Although part of this surge was expected, the result was higher than the range anticipated by the technical team (2.5% to 4.0%).

Broken down by expenditure components, private consumption (4.4% annually), public consumption (5.0% annually) and net exports gave rise to the higher rate of growth. The contribution of the latter to the growth of the GDP was positive, something that has not occurred since the fourth quarter of 2009. This was due to the significant upswing seen in exports, which went from falling 2.7% annually in the first three months of the year to growing 7.6%. Meanwhile, imports grew at a slower pace (from -0.2% to 1.3% respectively).

Broken down by branches of activity, all of the economic sectors with the exception of construction showed a better annual growth rate in the second quarter than in the previous one. The sectors that grew the most were agriculture (7.6%) and construction (6.4%). The performance of the mining sector was favorable (4.3%) but remained below the average for the last five years (10.3%). Industry, which includes coffee threshing, registered positive growth (1.2%) after having contracted for the last three quarters.

For the third quarter, some of the indicators from July suggest that economic activity is still recovering.

Private consumption may continue registering rates of growth similar to those seen in the first half of the year. According to the DANE Monthly Retail-trade Survey (MMCM in Spanish), the retail sales for commercial establishments grew 5.4% in annual terms during July (compared to 5.2% registered in the second quarter of the year). When the effect of the sales of vehicles (cars and motorcycles) is discounted, sales grew 3.2% in the same period and their growth trend is continuing. Another indicator that points to the favorable performance of private consumption is the Banco de la Republica's Monthly Survey of Economic Expectations (EMEE in Spanish). This showed that in July, the conditions and sales expectations of businessmen were favorable since the outcome was above the second quarter average. The variables in the labor market also give a perspective of a better performance for private consumption in the third quarter. Wage-earning employment, which has shown a high correlation with private consumption, is growing at a positive rate (5.8% annually). Last of all, consumer credit has maintained a respectable rate of expansion (12.9% annually in August) and also points to a positive performance on the part of this expenditure in the third quarter.

With respect to investment and with the information from July, stability in the outcome of the short and medium term investment expectations in the EMEE could indicate that those investments other than the ones intended for building construction and public works projects may be stabilizing in the third quarter. Furthermore, investment in buildings and public works projects are expected to grow at a favorable rate in the second half of the year. This is partly due to the statistical effect of a low base of comparison in 2012.

There was also an annual decline of 6.6% in the value of the total exports in dollars during the month of July. The drop was due, in large part, to the -7.4% change in the exports of mining products (mainly coal and gold). Likewise, the foreign sales of agricultural products registered an annual fall of 8.8%. In the case of exports of industrial and other goods, there was a 3.2% reduction in July.

In July, total imports in dollars declined 1.6% annually. These reduced purchases from abroad are because of the 11.5% drop in purchases of capital goods since the purchases of consumer goods and raw materials grew

4.2% and 3.9% respectively. The decline in imports of capital goods is associated to a large degree with those of transportation equipment (-35.1%). The drop in this item is primarily due to the -50.5% change in rolling stock.

With respect to supply, the few indicators available for the third quarter of 2013 suggest improvements in commerce, construction, and industry. In the case of commerce, in addition to the abovementioned strength of retail sales in July, the better outlook for the present and future that the Fedesarrollo survey arrived at should be noted. In the case of construction, although there was an 11.4% drop in licences in July, the aggregate figure for twelve months continues to show growth (around 6.2%). Production and sales of cement, in turn, grew 6.2% and 11.5% respectively in July.

In the case of industry, the annual growth of production was slightly positive (0.2%) in July. It is noteworthy that for the first time this year, the trend component of the series is on a rising slope. Growth for the year up to July is still in negative territory (it went from -3.4% in June to -2.9% in July). Other variables related to the sector, such as indicators of orders, inventory, production expectations at three months and industrial confidence expectations published by Fedesarrollo based on information as of July, confirm the change in the trend and show an improvement with respect to previous months.

That is how the latest information increased the probability that the GDP would grow this year at a rate similar to the rate in 2012. The economic activity indicators and their projections show that the output level is moving towards its potential. The monetary and fiscal policy actions taken so far are expected to contribute to strengthening this trend.

c. Financial Variables

Bank loans (N/C and F/C) in August registered an annual growth rate of 13.9%, which is slightly higher than what was seen the month before (13.8%). The annual growth of the portfolio in national currency went from 12.45% to 12.91% between July and August while the foreign currency portfolio dropped from 37.07% to 30.66% during the same period.

Broken down by market, the portfolio of loans granted to households saw an annual growth rate of 13.21% which is 6 bp lower than the previous month. This was due to the stability in consumer loans (12.90% in both July and August) and the slight dip in the portfolio for housing purchases which went from 14.28% in July to 14.06% in August. With respect to the portfolio of loans granted to companies, the annual growth rate increased 26 bp between July and August (14.05%).

The interest rates for the loans disbursed by credit institutions since the beginning of the cuts in the benchmark rate in July 2012 have accumulated reductions of: -224 bp for mortgages, -210 bp for consumer loans, and -194 bp for building loans.

The levels of the real interest rates for consumer loans, mortgages, preferential loans, ordinary commercial ones and commercial lines of credit in August were below their historical averages as calculated since 2000. In contrast, the real rates for credit card loans are above their average.

The size of the decline in the real interest rates since the beginning of the cuts in the benchmark interest rate has been lower due to the lower rate of inflation. There have been reductions during the same period of: -190 bp in mortgages, -174 bp in consumer loans, and -160 bp in loans for construction.

d. The External Environment

The world economy has continued to recover mainly due to the developed countries. In the euro zone, the figures for economic activity have been better than expected while growth has remained modest in the U.S. As was forecast, the large emerging economies are registering a weaker rate of economic activity compared to 2012 and, in some of them, the economy has slowed down more than expected.

In the euro zone, the recent indicators of productive activity and confidence show that the economic recovery that took place in the first part of the year is still in progress. In spite of this, the expansion rate across the region remains very low (-0.7% annually in the second quarter of 2013) and the weakness persists since the labor markets are still vulnerable and credit has not shown signs of recovery yet.

In the United States, the economic expansion continues at a modest rate. During the second quarter, the economy expanded at an annual rate of 1.6% which showed a slight uptick compared to what was registered in the first quarter (1.3%). The recent figures on retail sales and industrial activity showed a positive trend. In addition, although the unemployment rate is still on a downward trend, the creation of jobs remains low. The recent increases in the long term interest rates have been transmitted to the interest rates of mortgage loans. This phenomenon has occurred simultaneously with a slight slowdown in some figures for the housing market (construction start ups and permits, housing prices). These facts have generated warnings about the sensitivity of the housing market recovery to a lower expansion of the monetary policy in that country.

With respect to the emerging economies, the growth in the first half of the year was lower than what was registered last year. However, this growth is still favorable. In China, the industrial output, retail sales, and some international trade indicators rebounded again in August which would indicate that productive activity could become stronger in the third quarter.

The results of the first half of the year were mixed for the countries in Latin America. Productive activity slowed down sharply in Mexico as it went from an annual expansion rate of 2.6% in the first quarter to 0.3% in the second quarter. Chile also saw a lower rate of expansion in the second quarter (4.0% annually) compared to the results for the first quarter (5.1% annually). In contrast, economic activity rebounded in Brazil during the second quarter with an annual growth rate of 3.3% in comparison to the 1.9% registered in the first quarter. In Peru, better annual growth in the second quarter was also registered (5.6% vs. 4.5% in the first). For the third quarter, the latest information shows that economic activity in Mexico could grow at a moderate pace while in Chile and Peru, the economy should continue expanding at a favorable rate.

Regarding the international prices for commodities, the geopolitical tensions in the Mid-East raised the foreign price quotes for petroleum again. Recent announcements helped to partially reduce these surges. In this context, the prices of crude oil will be at the upper limit of the forecast range established in the last Inflation Report (110USD/barrel).

The foreign prices of other goods exported by Colombia such as coal and nickel have shown some stability in the last few weeks. Coffee prices declined again. In the case of some imported food such as wheat and corn, the favorable supply conditions have lowered international prices. As a result, the country's terms of trade stopped falling and stayed at historically elevated levels.

Inflation in the main developed countries is remaining at relatively stable levels. However, the price trend in Japan, a country in which the expansionary economic policies are causing a rise in price levels, deserves mention. For emerging economies the situation is less homogenous inasmuch as countries such as Brazil, India and Indonesia continue to experience high inflation while economies such as Chile, Colombia, and Peru have seen a moderate rise in their inflation although the level is still low.

It should be noted that the economies with strong inflationary and exchange rate pressures such as India and Indonesia raised their benchmark interest rates in the last few weeks. Other countries with fewer changes in prices and concerns about productive activity lowered them (Mexico and Hungary).

With respect to global financial markets, the Fed's decision to not start phasing out the monetary stimulus yet contributed to the appreciation of public and private bonds and to that of the currencies of the majority of the emerging countries. In spite of that, this correction has been partial and the prices of these assets are still higher

than those seen before May. Moreover, it is likely that the uncertainty about when, how, and how soon the monetary stimulus program will be discontinued will continue to put pressure on the capital markets for the coming weeks.

Note that the budget for the next fiscal year and the government's debt limit are supposed to be negotiated in the US Congress in the next few days. In the last few years, these discussions between Democrats and Republicans have been very complex and polarized. This has generated a high level of uncertainty that has affected the confidence of American consumers and businessmen and has produced an increase in the volatility of the international financial markets.

2. DISCUSSION AND POLICY OPTIONS

The Board of Directors considered the following relative aspects.

(i) The figures for the third quarter indicate that the growth of a significant number of advanced economies has improved at the same time as the emerging economies are growing slower than the year before. The average growth of Colombia's trading partners will probably be lower in 2013 than in 2012.

(ii) The international price of petroleum remains at high levels and the prices for some of the commodities that Colombia imports have fallen. As a result, the country's terms of trade are staying at high levels.

(iii) The US Federal Reserve's decision to keep the monthly purchase asset program unaltered contributed to the appreciation of international financial assets and the appreciation of the majority of the emerging countries' currencies.

(iv) The growth of Colombia's GDP in the second quarter was higher than what had been projected. With respect to domestic demand, both investment and consumption on the part of households and the government showed greater strength. Likewise, the real growth of exports surpassed that of imports. This is something that has not been seen since the second quarter of 2009. In the area of supply, all of the economic sectors with the exception of construction expanded at a faster pace than in the previous quarter with the agricultural sector showing the best performance. Industry, including coffee bean threshing, grew at a positive rate after having contracted for three consecutive quarters.

(v) The indicators for the third quarter suggest that the GDP will grow at annual rates that are higher than those seen in the first half of the year. Investment, especially investment in buildings, should grow at high rates while consumption will probably grow at about the same rate as it did in the first half of the year. That is what the retail figures, the monthly surveys of economic expectations for commerce, consumer credit, and wage-earning employment data suggest.

(vi) Bank loans are growing at stable rates that are higher than those of the nominal GDP. In real terms, the interest rates for the different types of loans are below their historical averages (except for credit cards). The general financial conditions, however, may have adjusted to the rising price of foreign financing.

(vii) The new information increased the likelihood that, this year, the GDP will grow at a rate that is similar to the rate in 2012. Nevertheless, although it is probable that the risks from advanced economies are now lower than before, those from some of the emerging economies may be rising.

(viii) In August, annual inflation (2.27%) was in line with what had been estimated by the technical team and the core inflation average remained stable at 2.5%. The average of the analysts' inflation expectations and those calculated on the basis of the rates for public debt securities is similar to the inflation target of 3%.

The members of the Board highlighted the growth of output in the second quarter of the year, which was higher than the estimate, as a reflection of the greater strength of domestic demand and, for the first time since 2009, positive data for net exports. Likewise, the data on the labor market and the growth of wage-earning employment (5.8%) was favorable. Furthermore, although the consumer confidence index (CCI) published by Fedesarrollo in the month of August showed a drop, this is expected to be temporary. Economic growth is also expected to continue becoming stronger partly driven by the investment in construction of buildings and public works. Nevertheless, there are still elements of uncertainty in the foreign context in both the advanced and some emerging economies.

3. POLICY DECISION

Based on the evaluation of the balance of risks, the Board of Directors agreed unanimously that it would be appropriate to keep the benchmark interest rate at 3.25%.

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-september-2013