Minutes of the Meeting of the Board of Directors of Banco de la República on Wednesday, June 24, 2015

Monetary Policy Report Last modified Monday the 29th of April, 2024
A regular meeting of the Board of Directors of *Banco de la República* took place in the city of Bogotá D.C. on Wednesday, June 24, 2015. In attendance were Mauricio Cárdenas Santamaría, Minister of Finance and Public Credit, José Darío Uribe Escobar, Governor of the Central Bank, and Board Members Carlos Gustavo Cano Sanz, Ana Fernanda Maiguashca Olano, Adolfo Meisel Roca, César Vallejo Mejía, and Juan Pablo Zárate Perdomo.

These minutes contain a summary of the outlook of the technical staff of the Central Bank on the macroeconomic situation (section 1), followed by a review of the main discussion regarding monetary policy by the Board of Directors (section 2).

A more detailed description of the macroeconomic situation prepared by the technical staff will be presented in the Inflation Report for the second quarter of 2015 and in the statistical annex.

1. MACROECONOMIC CONTEXT

1. The new data for global economic activity suggest that the average growth of Colombia's trade partners for 2015 could be somewhat lower than estimated in the previous quarterly report (1.3%). The economic recovery of the United States would be slower than estimated, while the euro zone and Japan continue exhibiting low growth rates. China's economy continues slowing down, while the data for economic activity of the major countries in the region suggest that their output will expand at low or negative rates. Accordingly, it is likely that in 2015 the average economic growth of our trade partners be less than the one observed a year ago.

2. The increase in the benchmark interest rate of the US Federal Reserve is expected to begin towards the end of this year. In turn, the European Central Bank continued issuing monetary stimuli, amidst high uncertainty upon the permanence of Greece in the euro zone.

3. In the US and the euro zone, interest rates for the long-term public debt bonds increased, but remain at levels lower than the average recorded in 2014. The US dollar resumed its trend towards appreciation, but with a lower slope than the one observed at the beginning of the year. So far this year, among the main countries of the region with an inflation targeting scheme, the Brazilian real and the Colombian peso have been the most depreciated currencies vis-à-vis the US dollar.

4. So far in June, the prices of oil exhibited levels higher than the projections for all of 2015, but they are still far lower than the average observed in the last five years. The average of the prices of goods imported by Colombia has descended, but at a slower pace that the fall of the prices of exports. This behavior indicates that in 2015 the level of the terms of trade will be low and similar to the one registered at the beginning of 2009, and that there will be a significant loss in the dynamics of national income.

5. The behaviors of external demand and the prices of commodities have impacted the results of foreign trade in US dollars. In annual terms, the value of exports descended again in April. This fall is mainly explained by mining exports, especially by the lower level in the price of oil in comparison to a year ago. In the same month, external sales of the main agricultural products and other sectors also descended. Within the accumulated value for the four first months of the year, total exports in US dollars have fallen

29%; mining exports have fallen 40.2%, and those of other sectors -9.4%; contrastingly, the external sales of agricultural products increased 16.9%.

6. In April, total imports in US dollars fell 18.2% on a yearly basis. The major fall was exhibited by those destined to capital goods (-23.2%), followed by raw materials (-17.5%) and consumer goods (-12.3%). With this, external total purchases accumulate a fall of 8.1% in the first four months of 2015, which is explained by the downturn of imports of raw materials (-16%), of consumer goods (-2.0%), and to a lesser degree, of capital goods (-1.0%).

7. The behavior of exports and imports and that of other items of the balance of payments indicate that in the first quarter of 2015 the current account deficit as a proportion of GDP would be greater than the one registered for all 2014.

8. As for the domestic context, growth in the first quarter of 2015 (2.8%) slowed down, in line with the estimations by the technical staff. Domestic demand grew at a slower pace than in the previous quarter, but at a rate greater than what had been projected due to the dynamics of investment. Net exports fell, and their negative contribution to growth resulted higher than had been estimated, as a result of the strong increase of real imports.

9. On the supply side, in the first quarter of 2015 the most dynamic sectors were civil works, retail, repairs, restaurants, and hotels, financial establishments, insurance, and real estate activity. In turn, the manufacturing industry and exploitation of mines and quarries were the only sectors that presented a downturn in their activity.

10. The new data for the second quarter of 2015 regarding retail trade, consumer confidence, and the survey of economic expectations by Banco de la República suggest that private consumption grows at a somewhat lower rate than the one registered at the beginning of the year. On the supply side, production of the manufacturing industry contracted again in April.

11. As for the labor market, the data to April of 2015 recorded a slight increase of the unemployment rate (seasonally adjusted), but its level is still historically low.

12. In May, total corporate debt grew at a somewhat higher rate than the one registered for the first quarter, while that of household debt continues slowing down. Both balances grow at a greater rate than the increase of the nominal GDP estimated for 2015. This has taken place together with interest rates (for trade and consumption), which in real terms continue at levels below their historic averages (excepting credit cards).

13. Regarding prices, inflation decreased in May, reaching 4.41%, a figure lower than had been forecast by the market average and the technical staff at the Central Bank. The slowdown of inflation is explained mainly by the lower pace of increase in the price of foodstuffs. The other groups of the family basket, (i.e., regulated goods, and tradable and non-tradable goods excluding food and regulated goods) accelerated, and their rates of increase are in the upper rank of the target range.

14. The average of core inflation completed eight months increasing, registering 3.99%. One and two-year inflation expectations by market analysts and those embedded in public debt bonds to 2, 3, and 5-year horizons are still between 3.0% and 3.5%.

In summary, the slowdown that began in late 2014 continues in 2015. Inflation decreased, and its expectations are still near 3.0%. Domestic expenditure continues its process of adjustment due to the slowdown in national income.

2. DISCUSSION AND POLICY OPTIONS

The Members of the Board consider that the new information available corroborates that the process of orderly adjustment referred to in previous meetings continues taking place, marked by a gradual reduction in the growth of domestic demand and output. All this is in line with the convergence of inflation to the long-term target and contributes to the reduction of the current account deficit of the balance of payments.

Regarding prices, the Board Members emphasized that annual inflation reduced, but core inflation indicators increased. The increase in the prices of some of goods and services has exhibited a greater-than-expected persistence, which has raised inflation forecasts for 2015. However, good anchorage of inflation expectations and the spare capacity that will be generated as a result of the slowdown of the output allow foreseeing that inflation will converge to the target in the policy horizon.

The Members of the Board also indicated that the current account deficit of the balance of payments poses vulnerability to the Colombian economy. The lower growth of domestic demand and the real depreciation of the peso are necessary elements to gradually reduce it.

Finally, the Board Members highlighted that flexibility of the foreign exchange rate is a fundamental element of the inflation targeting scheme, which allows for the exchange rate to absorb external shocks. This policy framework has enabled the Colombian economy to face the shocks in the terms of trade and the volatility of international financial markets.

3. POLICY DECISION

The Board of Directors unanimously decided to maintain the benchmark interest rate at 4.5%.

Bogotá, D. C.