Box 3: Liquidity Provision by <em lang="es">Banco de la República Under the Inflation Targeting Scheme - Report of the Board of Directors to the Congress of Colombia, March 2026

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Pursuant to Article 5 of Law 31 of 1992, the Board of Directors of Banco de la República (the Central Bank of Colombia) submits a report to the Honorable Congress of Colombia, informing about the performance of the economy and its outlook. This report is submitted twice a year, in March and July, within ten business days following the start date of the sessions of the Congress.

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The 1991 Political Constitution assigned *Banco de la República* the mandate of maintaining low and stable inflation, in coordination with the general economic policy. To fulfill this mandate, since 1999, Colombia has adopted an inflation targeting scheme under a flexible exchange rate system, in which the main instrument for controlling inflation is the monetary policy interest rate (MPR) (also known as the intervention rate or benchmark rate). The Board of Directors of *Banco de la República* (BDBR) sets the MPR at a level consistent with achieving the inflation target over the monetary policy horizon. Subsequently, Banrep conducts monetary transactions to align the overnight money market interest rate with the MPR. To this end, it provides liquidity to financial institutions (which in turn transmit it to the rest of the economy) at a minimum cost equal to the MPR, or it absorbs excess liquidity, also using the MPR as a reference.

Consequently, the provision or withdrawal of liquidity is not aimed at fixing the money supply in the economy, but rather at ensuring the necessary liquidity conditions so that the shortterm interest rate is consistent with achieving the inflation target. The amount of money in circulation is thus determined by public demand, which depends on the MPR and other variables, such as economic activity and the price level. This scheme also operates under a flexible exchange rate regime, allowing the exchange rate to fluctuate freely in response to market conditions. By allowing the exchange rate and the money supply to adjust flexibly to changing economic conditions, interest rate volatility is reduced.

Operationally, the provision or withdrawal of liquidity to the economy is calibrated so that the supply of the monetary base matches the amount of money demanded by the public and financial institutions when the short-term interest rate equals the MPR set by the BDBR. The monetary base is the money issued by the central bank and is composed of currency in circulation held by the public and the bank reserves of financial institutions. It constitutes the economy’s primary liquidity and differs from broader monetary aggregates such as M1, M2, or M3, which include instruments like current accounts, savings deposits, and CDTs, among others, issued by financial institutions and which also perform the functions of money as a means of payment and store of value.

The objective of this box is to present the evolution of primary liquidity supply by *Banrep* over the course of the present century.