Monetary Policy Report
Contenidos relacionados
The Board of Directors of Banco de la República at today's meeting decided to maintain the benchmark interest rate at 4.25%

A regular meeting of the Board of Directors of *Banco de la República* took place in the city of Bogotá D.C. on Friday, July 27, 2018. In attendance were Mauricio Cárdenas Santamaría, Minister of Finance and Public Credit; Juan José Echavarría, Governor of the Central Bank; and Board Members Gerardo Hernández Correa, Ana Fernanda Maiguashca Olano, José Antonio Ocampo Gaviria, Carolina Soto Losada, and Juan Pablo Zárate Perdomo.

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

Further detail on the macroeconomic situation prepared by the technical staff from the Central Bank will be presented in the monthly Monetary Policy Report for July 2018 and in the statistical annex (Only Available in Spanish).

# 1. MACROECONOMIC CONTEXT

1. The average growth forecast for Colombia's main trading partners for 2018 was revised downwards in this report (2.4%). This, however, continues to reflect an acceleration *vis-à-vis* 2017. A very similar expansion of the country's trading partners to the one anticipated for 2018 is expected in 2019. This would allow the Colombian economy to receive an additional boost generated by a stronger external demand.
2. The prices of oil and other raw materials were revised upwards, which implies more favorable terms of trade than those considered in the previous quarter, and a stimulus for national income. Particularly, this report increased the forecast of the average price of oil, which stood at USD $71 per barrel for 2018. However, this forecast implies a reduction in the price for the rest of the year. For 2019, an average price of USD $67 per barrel is expected.
3. Although the perception of risk in emerging economies has increased, this has not yet compromised capital flows to most of these economies.
4. This report revised the current account deficit upwards, from 3.1% to 3.2% of GDP in 2018. This forecast implies a better dynamics of exports of goods and a good performance of current transfers.
5. The technical staff maintains the forecast for GDP growth at 2.7% for 2018. International financing conditions, prices of commodities, and demand from trading partners are expected to be favorable to the expansion of Colombia's GDP in 2018. Additionally, internal factors such as the decline in inflation, an expansive interest rate, and a labor market without many variations would strengthen the process of convergence towards the growth potential. However, there are risks that may affect the dynamics of GDP, such as the execution of investment on civil works, the price of oil, and the performance of the sector of buildings.
6. In terms of inflation, the results in the last four months show that the variation in prices has remained relatively stable after a major fall in the first two months of the year. Particularly, in June, the annual inflation rate stood at 3.20%, a figure somewhat higher than in March (3.14%).
7. In June, the average of core inflation indicators exhibited a slight descent, standing at 3.33%. Inflation expectations to December 2018 obtained from the monthly survey to financial analysts posted at 3.52%. Analysts' expectations and those embedded in public debt bonds to horizons greater than or equal to a year stand between 3.0% and 3.4%.

In all, inflation is expected to continue its process of convergence to the target, and economic growth is expected to exhibit a better dynamics in 2018 and 2019. The monetary policy actions carried out so far should consolidate the convergence of inflation to the target and maintain a favorable path for the expansion of the GDP. However, uncertainty about the external and domestic conditions and about the volatility of oil prices remains high, which could affect the dynamics of prices and economic activity.

# 2. DISCUSSION AND POLICY OPTIONS

The members of the Board continue to see a positive outlook in terms of the performance of headline inflation. The reading of the latest figure is favorable, particularly when observing the evolution of the different core inflation indicators as well as of inflation related to non-tradable goods and leases. Yet, the Board emphasized that the technical staff's projection for the end of the year was affected by the expected increase in food inflation and by inflation of regulated items, the latter due to the upward pressures of the international price of oil.

*Vis-à-vis* the previous meeting, the risk that persists on this front is due to the external context, in which the level of uncertainty is high. Until now, Colombia has not been negatively impacted, but it is essential to continue monitoring the external conditions and the domestic effects of possible shocks.

The Board Members perceive that the performance of economic activity for the remainder of the year will be better than the forecast by the technical staff, and agree that the latest indicators corroborate this hypothesis. There was general consensus on clear signs of recovery of economic activity, although there is still a negative output gap, which increased between 2017 and 2018, according to the forecast by the technical staff.

There were several mentions regarding the transmission mechanisms of monetary policy. Several Board Members emphasized that the commercial loans portfolio does not yet exhibit a strong evidence of recovery. Others mentioned that the transmission of the reduction in the benchmark interest rate has not yet ended, therefore the assessment of the evolution of all credit variables should continue.

The possible effects of narrower international financial conditions on the long-term real interest rate and on the assessment of the monetary policy stance were also discussed.

Within this context, despite a negative output gap, with stable inflation (albeit above the target), and a highly uncertain external context, there is an evident economic recovery. Therefore, the Board Members consider it prudent to maintain the current level of the benchmark interest rate.

## 3. POLICY DECISION

The Board of Directors unanimously decided to maintain the benchmark interest rate unaltered at 4.25%.

Bogotá, D. C.