PUBLIC VERSION

Working Papers from the Board of Directors Banco de la República

Monetary Policy Report

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Board of Directors
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Monetary Policy Report

Economic Studies Division

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I. External Context and Balance of Payments

1. In April, Colombia´s terms of trade would have maintained the upward trend that began the previous month, thanks to the fact that international prices of oil and other commodities exported by the country continued to rise from the low levels recorded in mid-February. However, the current levels are lower than the ones registered last year.

2. The price of Brent oil increased 7.3% on average so far this month to April 26th, as compared to the observations from March. Compared to the average of December, the increase has been 10.8%. This increase is largely explained by the prospects of an agreement among some producer countries to freeze production at current levels, which in the end did was not reached, and by signs that production in the United States would have continued to decline slowly. Additionally, a temporary interruption in Kuwait's production, lower risk aversion in international financial markets, weakening of the US dollar and some economic figures for China which were better than had been forecast, would have also affected this increase. However, the value of oil is still below the average for 2015.

3. The prices of nickel and other metals exported by some countries of the region also exhibited increases compared to observations from the previous month, as a result of the reduction of risk aversion, weakening of the US dollar, and improvements in the economic figures for China. The international price of coffee also exhibited an increase compared with the low levels at the beginning of the year, due to some climate shocks.

4. The most recent records of economic activity of the country’s main trading partners suggest that growth for 2016 would be lower than forecast in the previous report.

5. In the United States, the first estimate for GDP in the first quarter recorded a 0.5% expansion (quarterly annualized rate), which represents a slowdown compared to what was observed three months ago (1.4%, q.a.r.). By disaggregating into items, the loss of dynamism of household consumption stands out, going from 2.5% q.a.r.to 1.9% q.a.r. Additionally, there were sharp declines in exports and residential investment.

6. In the American labor market, records of job creation in March were favorable, with which the unemployment rate stood at low levels (5.0%), and close to

what analysts and the Federal Reserve (Fed) estimate as long-term levels. Regarding the yearly variation in prices, there were some decreases in core inflation indicators (from 2.3% to 2.2%), and total inflation (from 1.0% to 0.9%).

7. The press release of the meeting of the Federal Open Market Committee (FOMC) in April indicated that the economy and the labor market would have continued recovering modestly; however, it expressed that it would continue to monitor carefully the risks arising from the strength of the US dollar, weakness in global demand, and uncertainty about the international economic and financial situation. Additionally, it suggested that the FOMC forecasts that inflation would converge more slowly to the target, and that normalization of the monetary policy would be more gradual than announced at the end of the last year.

8. In the euro zone, the indicators of retail sales and industrial production available for February and those of industrial and consumer confidence for April suggest that the economy would have continued to expand at a modest pace in the first quarter of 2016. Regarding the variation in prices, in March, the indicators of total annual inflation and core inflation did not exhibit significant changes and continue at low levels (0.0% and 1.0%, respectively). In this context, the European Central Bank (ECB) continued with a highly expansive monetary policy.

9. In China, GDP indicators for the first quarter of 2016 exhibited a slight deceleration *vis-à-vis* the figures observed three months ago, moving from 6.8% to 6.7%. Despite this, the records of fixed asset investment in March and those of industrial production showed some increases compared to the growth rates observed at the end of 2015. Yearly inflation in March remained low (2.3%).

10. As for Latin America, the figures of real activity for February exhibit a mixed behavior. Peru maintained the relatively high rates of expansion observed since the end of last year, while Chile and Mexico exhibited very low dynamism. For its part, the strong contraction that began in early 2014 in Brazil continues. Although there are no recent figures for Ecuador and Venezuela, the strong deterioration of their terms of trade and the tighter conditions of external financing should deepen the recession they are going through.

11. Inflation records to March in Latin American economies shows some decreases compared to observations from the first two months of the year, although they remain at high levels. In Brazil, Chile and Peru, inflation continued above their respective target ranges, while in Mexico it remains at the lower part.

12. So far in April, the low levels of risk aversion observed since the end of February continue, which was reflected on a reduction of financial volatility indicators. Additionally, the US dollar weakened *vis-à-vis* most currencies in the world, and recovery of the stock exchange indexes continued. The rates of long-term sovereign bonds of the main developed economies remained low.

13. In this environment, the risk premia for Latin America have presented strong decreases from the peaks reached at the beginning of the year. Similarly, the currencies of the region continued strengthening *vis-à-vis* the US dollar. The Colombian *peso* appreciated 3.9%, moving from an average value of COP $3,134 per US dollar in March to COP $3,011 per dollar to April 26.

a. Exports

14. In February, exports registered a yearly fall of 26.7%, due to setbacks in the external sales for all groups of goods. The strong fall in the group of mining goods stands out (-40.6%). So far this year, exports have registered a 31.2% decrease, also with a substantial decline in external sales of mining goods (**Table 1**).

15. According to the preview figure for foreign trade by DIAN, exports excluding oil fell 27.8% on a yearly basis in March.

Table 1: Behavior of Exports in US dollars

	Annual Variation	Main contributing items: Item	Annual variation of the item
February 2016			
Total	-36.2%		
Agricultural goods	-6.6%	Coffee	-26.9
Mining goods	-40.6%	Oil	-57.4%
		Coal	-18.5%
Other exports*	-8.3%	Chemical products	-16.2%
		Others	-33.4%
Accumulated value for January-February 2016			
Total	-31.2%		
Agricultural goods	-23.2%	Coffee	-36.1
		Banana	-11.3
Mining goods	-43.0%	Oil	-54.2%
		Coal	-30.8%
Other exports*	-10.7%	Chemical products	-19.3%
		Graphic and editorial arts	-34.4%

* By destinations, the 39.1% fall toward Ecuador stands out in this group. Contrastingly, external sales of this item towards the United States (28.4%) and the European Union (43.0%) increased. Source: DANE

b. Imports

16. In February, CIF imports in US dollars registered an annual fall of 24.5%, due to setbacks in the external purchases in all groups of goods. The contraction in imports of capital goods is remarkable: -43.8%. So far this year, imports have fallen 26.3% (**Table 2**).

17. According to the flash report of foreign trade by DIAN, in March, CIF imports recorded an annual 25.1% fall.

Table 2: Behavior of Imports in US dollars

February 2016			
	Annual Variation	Main contributing items:	
		Item	Annual variation of the item
Total	-24.5%		
Capital Goods	-43.8%	Transport equipment	-34.3%
		Industrial machinery	-34.8%
Raw materials	-5.4%	Chemical and Pharmaceutical products	-17.2%
		Mining Products	-24.5%
Consumer Goods	-24.0%	Private vehicles	-36.8%
		Domestic machinery and appliances	-34.3%
Accumulated Value for January-February 2016			
Total	-26.3%		
Capital Goods	-41.7%	Transport equipment	-78.5%
		Spare parts and accessories for transport equipment	-35.5%
Raw materials	-14.9%	Chemical and Pharmaceutical products	-17.7%
		Mining Products	-23.6%
Consumer Goods	-18.8%	Private vehicles	-27.3%
		Domestic machinery and appliances	-23.8%

Source: DANE

II. Projections of External Variables

a. External Growth Scenarios
Baseline or more likely scenario (Table 3)

18. Growth forecasts for 2016 for Colombia's main trading partners were revised downwards in the present report, compared to the ones published in the previous quarterly report. The forecast of the average GDP growth of Colombia's major trading partners (weighted by non-traditional trade) moved from 1.3% to 0.5%. For 2017, although some recovery is expected, the country's external demand would remain weak (1.1%).

19. This revision for 2016 was mainly due to the fact that the performance of some Latin American economies would be much weaker than expected in the December Inflation Report.

20. Such is the case of Venezuela, whose forecast was revised from -5.0% to -7.0% as a result of the adverse effect of the low prices of oil on its fiscal and external accounts, the signs that there is still shortage of several consumer goods and raw materials, and some problems with energy supply.

21. In Ecuador, the growth estimation for all 2016 was revised downwards by two percentage points (pp) to -2.5%. This is the result of the fiscal consolidation that this country would do in order to adjust to: the strong shock in its terms of trade; greater difficulty to find external financing after the fall of its external income; and the loss of competitiveness of its exports due to the strength of the

US dollar. Added to these factors is the negative impact of the earthquake that struck this country at the beginning of April.

22. In Brazil, the fiscal consolidation that the country must undertake, deterioration of employment and available income of households, and the deepening of the political uncertainty with its adverse effects on the confidence of entrepreneurs, investors and consumers would cause the contraction to be greater than foreseen in the previous quarterly report. Thus, the forecast for 2016 lowered from -2.5% to -3.5%.

23. As for Chile and Mexico, they are expected to maintain a low dynamism compared to the average of growth records from the last decade, since their economies continue adjusting to the strong shock to their terms of trade and to a lower external demand. In Peru, some recovery is expected, compared to the records of the past two years, thanks to a greater contribution of the mining sector and fisheries.

24. As for the United States, its growth forecast for all 2016 was revised downwards as a result of the slower-than-expected rate of expansion of private consumption in the first quarter. However, for the remainder of the year and for 2017, this item would register a greater dynamism and would consolidate as the main engine for economic growth since the fundamentals of household spending remain favorable. This would help to compensate for the moderation in non-residential investment and net exports, which have been affected by the weakness of external demand, the strength of the US dollar, and the global financial and economic uncertainty.

25. In this context, it is assumed that the Fed would continue to increase its benchmark reference rate throughout the year, although at a slower pace than foreseen in the previous report. These increases in the benchmark rate would be transmitted to market rates in an orderly fashion.

26. As for the euro zone, recovery of the economy would continue taking place slowly, as expected in the previous Inflation Report. The measures taken by the ECB have allowed for the recovery of confidence and have restored the credit channel to some extent, which would encourage private consumption and investment. However, the weakness in global demand would affect exports outside the European Union.

27. Inflationary pressures would remain contained during 2016 as a result of the low prices of fuels, scarce demand pressures, and modest inflation expectations.

In this context, it cannot be ruled out that the ECB increases the existing monetary stimulus measures.

28. As for China, its re-balancing process towards an economy supported by a greater dynamism of private consumption would continue. In this context, exports and investment are expected to continue moderating their growth rates from the high levels in previous years. However, this process is expected to be slow, and that stimulus measures taken by the government and the central bank would allow for soft landing.

Table 3

Economic Growth Forecasts for Colombia's main Trading Partners

Country or Region	2016			2017		
	Low	Baseline	High	Low	Baseline	High
USA	1.5	2.2	2.5	1.8	2.5	2.8
Euro Zone	0.8	1.6	2.0	0.4	1.6	2.0
China	5.8	6.4	6.8	5.6	6.2	6.6
Brazil	(4.7)	(3.5)	(2.3)	(1.0)	0.7	2.0
Ecuador	(5.0)	(2.5)	(0.5)	(4.0)	(2.0)	0.0
Venezuela	(10.0)	(7.0)	(4.0)	(7.0)	(4.0)	(1.0)
Peru	2.5	3.5	4.0	3.0	4.0	5.0
Mexico	2.2	2.4	2.6	2.0	2.8	3.3
Chile	0.8	1.8	2.4	1.5	2.5	3.5

b. Risks to the Baseline Scenario

29. A stronger slowdown in China associated with problems with its financial stability, to high debt levels, or to capital outflows facing a new scenario of risk aversion.

30. The high level of debt, together with deterioration of their economic situation, greater external interest rates, and depreciation of their currencies could result in a solvency problem in some of the economies that produce commodities. This situation could spread to international financial markets.

31. Political uncertainty in the United States and the euro zone.

32. The implicit fall in the prices of commodities in this report's baseline scenario could affect the economic performance of exporting countries and companies producing these goods more than expected.

33. Financial markets could overreact to the normalization of the monetary policy in the United States.

34. Problems of financial stability in the euro zone on account of the negative interest rates, with potential adverse effects on credit.

c. Projection of the Balance of Payments

35. For 2016, a lower current account deficit is foreseen, both in US dollars as well as relative to GDP (around 5.9%, USD $15,948 m). This forecast incorporates the effect of the additional fall in the price of oil on different accounts of the external balance, as well as the effects of a moderate deceleration of economic activity in Colombia. In this sense, it is estimated that the trade balance would continue to be widely in deficit, but less than the figures in 2014, in a scenario of contraction of exports, both traditional and non-traditional, offset by a significant reduction in imports (**Table 4**).

36. Regarding the projection for the external balance of 2016 presented a quarter ago, export growth excluding main products (others) was revised downwards due to the slowdown in the growth of external demand, explained mainly by the lower estimates for the economies of the region, particularly Venezuela and Ecuador. Additionally, the forecast of imports is lower than the one presented three months ago, given the behavior exhibited by external purchases in the first quarter and the greater slowdown of domestic demand for the whole year.

37. The performance of external sales will be affected by lower price forecasts for all major export products, partially offset by the recovery in exports of oil derivatives, with the entry into full operation of Reficar in the middle of the year. In the case of oil, an average price of USD $35 per barrel for Brent is estimated for the entire year. A reduction of about 5.0% is estimated for non-traditional exports, mainly due to the trading partners' slowdown in external demand, despite the positive impact that the depreciation of the *peso* could have on the demand for these goods. It should be noted that, for commodities, annual variations in the volumes exported are estimated which are consistent with the growth forecasts of their production (oil: -8.0%; coal: -1.0%; ferronickel: 5.0%, and coffee: 0%).

Table 4

BALANCE OF PAYMENTS - (Millons of US dollars)	2015	2016
		Baseline
CURRENT ACCOUNT (A+B+C+D)	**(18,925)**	**(15,948)**
Percentage of GDP	**(6.5)**	**(5.9)**
A. Goods	**(14,026)**	**(13,403)**
a. Exports	38,125	30,857
Main products	23,854	17,024
Other exports	14,271	13,833
b. Imports	52,151	44,260
B. Non-factor Services	**(3,981)**	**(2,581)**
C. Factor Income	**(5,989)**	**(5,084)**
D. Current Transfers	**5,071**	**5,119**

38. Consequently, in the baseline scenario, exports of commodities would fall about 29.0%, while total exports in US dollars would contract 19.1%. On the other hand, imports in US dollars would contract *vis-à-vis* observations from 2015 (-15,1% on a yearly basis), which is associated with: the significant reduction in external purchases of durable consumption goods and capital goods associated with the mining-energy industry; a less-dynamic domestic demand; and the substitution of part of the imports of fuels with the entrance into operation of Reficar and additional reductions in the prices of imported goods, particularly intermediate goods.

39. A lower deficit in the balance of services is projected versus the one observed in 2015, driven by the effects of depreciation on the net balance of some services such as business and tourism, and the reduction of prices of imported services such as cargo transport. A decrease in net outflows due to factor income is also expected, associated particularly with lower remittances of profits from the mining and energy sector as well as from the other sectors.

40. As for financing, capital flows are expected to be lower than those estimated for 2015, mainly due to the reduction in foreign portfolio investment, in a context of better conditions for advanced economies and the continuation of the monetary normalization in the United States. Particularly, lower resources derived from the placement of bonds are estimated for both the public and the private sectors in international markets, as well as lower investment flows by foreigners in the local public debt market. This would be partially offset by higher net inflows of direct investment and resources of external credit (**Table 5**).

Table 5

BALANCE OF PAYMENTS - (Millons of US$)	2015	2016 Baseline
CAPITAL AND FINANCIAL ACCOUNT (A+B+C+D+E)	**(19,201)**	**(15,948)**
A. Net Foreign Investment in Colombia	**(7,890)**	**(10,659)**
a. Foreign Investment in Colombia	12,108	13,659
b. Colombian Investment abroad	4,218	3,000
B. Portfolio Investment	**(9,686)**	**(1,534)**
a. Public sector	(6,213)	(2,256)
b. Private sector	(3,473)	722
C. Derivative Instruments	**1,526**	**0**
D. Other investment (loans and other credits)	**(3,567)**	**(4,328)**
a. Assets	(491)	(457)
b. Liabilities	3,076	3,871
E. Reserve Assets	**415**	**573**
ERRORS AND OMISSIONS	(276)	0
Financial Account without Reserve Assets	**(19,617)**	**(16,521)**

41. Thus, net foreign direct investment is projected to be lower than the previous year, as a result of lower resources from FDI in the oil and mining sectors facing the sharp declines in the prices of these commodities, which would be more than offset by an increase of flows towards other sectors resulting from the dynamism of infrastructure construction, resources from the sale of Isagen, and lower investment by Colombians abroad versus observations from 2015.

42. On its part, the greatest resources of external credit would be associated with a greater indebtedness of the National Government with the multilateral banks, and other credits from the rest of the non-financial public sector. The 4G infrastructure works would also require some additional resources from credit.

43. The projection exercise of the balance of payments for 2016 is consistent with a scenario of lower growth in domestic demand and a greater contribution of net exports to GDP. This would take place in a context of further declines in the terms of trade as a result of lower prices of exports, partly offset by a reduction of goods imported by the country.

44. Uncertainty about the conditions and availability of financing, as well as the sensitivity of some capital flows to the prospects of the mining-energy sector and economic activity in general, determine the forecast range for the current account deficit, which would stand between 5.3% and 6.4% of GDP.

III. Growth, Domestic Demand and Credit

45. According to the information available on the performance of real activity, during the first quarter of 2016, the pace of expansion of the Colombian economy would have been lower than the one recorded in the last three months of last year (3.1%).

46. GDP forecasts presented in this report consider adjustment in demand, which would have taken place above all by a lower level of spending on investment. Private consumption would have maintained its growth pace, while public consumption would have slowed compared to observations towards the end of 2015. Additionally, falls are projected for exports and imports, which is related with more recent figures for foreign trade in constant pesos.

47. By adjusting for seasonality, the series of the economic activity index (ISE) published by DANE rose 3.2% in January (compared to 3.2% of the aggregate of the fourth quarter of 2015).

48. The indicators of household consumption showed mixed signals in the first two months of the year. The monthly retail trade survey (EMCM) by DANE showed an annual growth of total sales in February of 5.4% (4.3% for the two-month period of January-February), which meant an acceleration *vis-a-vis* the record for the fourth quarter of 2015 (-0.4%).

49. Excluding vehicle sales, the remaining aggregate recorded a 6.9% expansion compared to the same month last year. For the two-month period, the growth was 6.1%. In both cases, the indicator suggests acceleration of the dynamics for this type of sales compared to the number at the end of 2015 (4.9%).

50. Motor-vehicle sales recorded declines, but lower than those recorded in previous months. In February, vehicle sales fell 2.6% annually, and 5.5% in the two-month period, which represents a recovery versus the -24.5% observed for the fourth quarter of last year. However, the series suggests stagnation at levels similar to those observed in 2011 and 2012.

51. The figures for license registers published by the Colombian Automotive Committee indicate something similar. To March, license registers fell 20.0% on a yearly basis. The aggregate of the first three months of the year did so by 17.5%, less than the figure of the fourth quarter of 2015 (-25.2%). This behavior took place both in the line of private use (consumption) as in commercial use (investment).

52. The information provided by other indicators with a high correlation with the growth rate of private consumption suggests a slowdown this component of GDP during the first quarter.

53. The Consumer Confidence Index (CCI) of *Fedesarrollo* reveals again historically low levels. The average of the quarter has been the lowest since it has been registered. It should be noted that the correlation between the series of consumption and consumer confidence has weakened in recent quarters.

54. Also, *Banco de la República*'s Monthly Economic Expectations Survey (EMEE) to February also suggests that in the first quarter of the year private consumption would have expanded at a rate somewhat lower than the one observed for the last quarter of 2015.

55. Additionally, the most recent employment indicators show that the labor market has been deteriorating. The seasonally adjusted series for the unemployment rate (UR) show an upward trend (more marked for the thirteen areas than for the national total), largely due to a decrease in the occupation rate (OR). The latter is due to a slowdown in non-salaried employment. Salaried and formal employment in the thirteen areas continues to grow in annual terms (1.6%), although less than the average for 2015 (4.1%).

56. Regarding gross capital formation, the figures for imports of capital goods in constant *pesos* and those for register of working vehicle licenses allow to foresee contractions in machinery investment and equipment and transport equipment during the first quarter of 2016. Civil works would have fallen partly as a result of a high base of comparison for the same period of 2015. In contrast, a good behavior of investment in construction of buildings is expected, driven especially by that in the residential sector.

57. As for foreign trade, the figures for January and February in real *pesos* show significant setbacks, higher for imports than for exports. The most important adjustments would have taken place in external purchases of capital goods and durable consumption goods, consistent with the behavior that the domestic demand for tradable goods would have shown during the first quarter.

58. On the supply side, the few indicators available for the third quarter of 2016 show uneven results. Figures related to sectors such as industry, retail, and coffee show a favorable behavior, while some indicators associated with branches of activities such as mining reported deterioration.

59. Industry presented an annual increase of 8.2% in February, which is partly explained by the opening of Reficar, which has driven the item of oil refining (21.7%). This result fell below the expectations of the technical staff at the Central Bank. So far this year, total industry grew 7.9%. Excluding oil refining, the industry expanded 5.7% in February and 5.0% in the year to date. It is important to note that when correcting by working days the increase in manufacturing excluding oil refining would have reached between 1.5% and 4.0%.

60. Additionally, sector disparities continue. While coking, oil refining, and mixture of fuels (21.7%), beverage manufacturing (21.1%), production of non-metallic mineral products (11.5%), clothing (10.7%), and manufacture of plastic products (7.0%) showed significant growth, on the contrary, other branches reported contractions, as is the case of manufacturing of other food products (-4.1%), production of machinery and equipment (-10.0%), processing of sugar and *panela* (-5.7%), and manufacturing of motor vehicles and their engines (-8.5%).

61. According to the March survey by *Fedesarrollo*, although the indicator for orders and the one for stock (countercyclical to production) deteriorated *vis-a-vis* the previous month, the trend components of each one of them point to a better performance of industry compared to previous quarters. Similarly, production expectations to three months continued to show an important recovery.

62. In the agricultural sector, according to the Federation of Coffee Growers, coffee production in March stood at 944 thousand bags, which meant an annual increase of 18.0%. Thus, during the first quarter of 2016, 3,174,000 bags were produced, which represents an 8.9% growth. On the other hand, although cattle slaughter showed an increase in February (around 3.5%), in the two-month period of January-February a significant slowdown was observed compared to the previous quarter (from 3.3% to 1.9%). It should be noted that there is high uncertainty on the cattle retention cycle and the impact of *El Niño* on slaughter.

63. With information to March, the mining sector exhibited a significant deterioration. Oil production was 916 thousand barrels per day (tbd), with which the first quarter closed with an average production of 951 tbd. March registered an annual 10.3% contraction (4.2% compared to February) and 7.4% for the quarter. With these results, the performance of the sector was below the forecast issued three months ago. In the case of coal, according to figures from the Colombian Mining Association (ACM), during the first quarter of 2016 production fell 8.0%.

64. In construction, the slowdown of production and cement shipments stands out, which posted at 4.1% and 5.7% in February, respectively, having reached 7.8% and 6.2% during the fourth quarter of 2015.

65. On its part, in March, total energy demand exhibited a yearly variation of 0.9% (the regulated component grew 3.0% and the non-regulated one fell 2.6%). The trend component reflects stagnation. It is important to note that this data would be influenced by the Holy Week and by the efforts of the country to save energy due to the significant impact of *El Niño* on the level of the reservoirs.

66. All of the above allows foreseeing a yearly expansion of GDP for the first quarter of 2016 lower than what was observed in the last quarter of 2015. Thus, the growth forecast would stand between 1.8% and 3.2%, with 2.5% as the most likely outcome.

67. For all 2016, the technical staff at *Banco de la República* foresees an annual GDP expansion of around 2.5%, somewhat below the 2.7% presented a quarter ago. The forecast range remained between 1.5% and 3.2%.

IV. Behavior of Inflation and Prices

68. Annual consumer inflation in March stood at 7.98%, a level 39 bp higher than the previous month (**Table 6**). For the year to date, the increase in the CPI amounted to 3.55%, higher than the 2.40% observed in the same period of 2015. The monthly variation of the CPI was 0.94%, a figure higher than the forecasts of the market (0.68%) and the technical staff at the Central Bank.

69. In March, the increase in annual inflation was once again explained by the tradable CPI excluding food and regulated items, processed foods, and regulated items. Both the pass-through of the depreciation of the *peso* and *El Niño* explain much of the upward pressures facing consumer prices in the first quarter of the year. Added to this are the effects of greater indexation.

70. Core inflation, measured as the average of the four indicators monitored by the Central Bank, also increased, reaching 6.29% in March *vis-a-vis* 6.07% in February. All the core inflation indicators increased: with the CPI excluding primary food, fuel and public services (6.57%) as the highest indicator, and the lowest that of the CPI excluding food or regulated items (5.91%). Core 20 stood at 6.48%, and the CPI excluding food in 6.20% (compared to 5.88% the previous month) (**Table 6**).

Table 6

Description	Weight	dic-14	jun-15	dic-15	jan-16	feb-16	mar-16	Participation percentage in monthly acceleration	Participation percentage in acceleration of the year to-date
Headline inflation	**100.00**	**3.66**	**4.42**	**6.77**	**7.45**	**7.59**	**7.98**	**100.00**	**100.00**
Non-food inflation	**71.79**	**3.26**	**3.72**	**5.17**	**5.54**	**5.88**	**6.20**	**57.48**	**58.64**
Tradables	26.00	2.03	4.17	7.09	7.39	6.97	7.38	**25.17**	5.29
Non-tradables	30.52	3.38	3.98	4.21	4.46	4.86	4.83	**(3.25)**	15.64
Regulated items	15.26	4.84	2.55	4.28	5.02	6.35	7.24	**35.56**	37.72
Food inflation	**28.21**	**4.69**	**6.20**	**10.85**	**12.26**	**11.86**	**12.35**	**42.52**	**41.36**
Perishables	3.88	16.74	10.73	26.03	31.31	27.42	27.09	9.55	12.56
Processed food	16.26	2.54	6.00	9.62	10.22	10.26	10.83	22.92	17.37
Eating out	8.07	3.51	4.45	5.95	6.78	7.09	7.53	10.05	11.43
Core inflation indicators									
Non-food inflation		3.26	3.72	5.17	5.54	5.88	6.20		
Core 20		3.42	4.24	5.22	5.56	6.25	6.48		
CPI excluding perishable foods, fuel and utilities		2.76	4.54	5.93	6.13	6.41	6.57		
CPI excluding food and regulated items		2.81	4.06	5.42	5.69	5.75	5.91		
Average of core inflation indicators		**3.06**	**4.14**	**5.43**	**5.73**	**6.07**	**6.29**		

Source: DANE. Calculations by *Banco de la República*.

71. Regarding the tradable CPI excluding food and regulated items, in March, its variation resumed a rising path, standing at 7.38% versus 6.97% in February. The depreciation of the *peso* that has built up from July 2014 to February this year continued passing-through to the prices of these items. One of the hikes that affected the most was that in the rates of telephone services.

72. During March, annual variation of non-tradables excluding food and regulated items exhibited no major changes. Within this group, that of goods and services that are more prone to indexation (health and education services, among others) recorded an increase, moving from 5.8% to 5.9%. This segment has been registering price increases which would be reflecting the activation of indexation mechanisms with the past inflation and/or increases in the minimum wage and other wages. On the other hand, the items affected by the exchange rate (5.8%) and leases (3.9%) did not exhibit significant changes *vis-a-vis* February.

73. As for food, after a pause in February, annual variation increased again in March and stood at 12.35% (compared to 11.86% in February). This time, the group of processed foods exerted upward pressures the most (from 10.26% in February to 10.83% in March, **Table 6**). At this level, the adjustments in the prices of oils and beverages stand out. An important part of these goods are intensive in imported agricultural products, for which increases can be attributed largely to the accumulated depreciation of the *peso*.

74. Annual CPI variation for perishable food remained at 27.0%. Anyway, price increases continue being considerable compared to the previous month, which suggests that the agricultural supply continues to be gravely affected by *El*

Niño, which, according to international meteorological agencies, is already weakening and would disappear by the middle of this year. However, it is expected that the lower planting and low productivity generated by this phenomenon maintain the annual variation of perishable foods at high levels.

75. Within the CPI excluding food, in March, the increase in the CPI for regulated and tradable items excluding food and regulated items exceeded the forecasts of the Central Bank. For the first sub group, annual variation moved from 6.35% in February to 7.24% in March, and the increases were observed in the main items. Particularly, among utilities (which went from 12.9% to 14.0%) the boost came from water and sewage rates, a case for which the indexation mechanism considered in the regulation formulas of the sector was activated. This mechanism operates every time three percentage points for inflation are accumulated since the immediately previous readjustment, which had taken place in November last year.

76. Similarly, significant increases in the rates of electrical energy and household gas took place again in March. The former were affected by the lack of rain, depreciation, indexation to the CPI and the PPI, and the closing of operations of the hydroelectric plant of Guatapé. The latter, by bottlenecks in transport that persist in the sector, and by the greater demand for thermal energy generation.

77. Annual CPI variation for public transport services increased from 4.3% to 4.5%, while fuel went from -6.1% to -4.7%. This last case is due to a very low base of statistical comparison in March of last year, when a much larger cut than this year's was decreed for the price of gasoline.

78. Yearly variation of meals outside the home in March was 7.53%, versus 7.09% the previous month. In recent months, this item would have incorporated the higher costs attributable to wage increases and to the increase in the prices of food and utilities.

79. On the side of non-labor costs, inflationary pressures on consumer goods did not increase in March judging by the behavior of the PPI for domestic supply (goods domestically produced and consumed plus imported goods), whose annual variation stood at 8.6% in this month *vis-a-vis* 11.0% in February. This reduction was led by imported items, which fell to 11.5% in March from 19.4% in February, hand in hand with the recent appreciation of the *peso*. Regarding goods locally produced and consumed, no major pressures would have been observed for costs, since their annual variation moved from 7.5% in February to 7.3% in March.

80. As for labor costs, with information to February and March, adjustments continued surpassing the inflation target significantly, although at rates lower than the adjustment to the minimum wage (except for industry). In the case of wages for heavy construction, adjustment to March remained at 4.7% on a yearly basis, and something similar is observed with the indicator for housing construction. On the other hand, the salary adjustment for trade rose from 5.6% in February to 5.9% in March, while that for industry moved from 6.1% to 8.9%.

81. Inflation expectations to December 2016, obtained from the monthly survey to financial analysts at the beginning of April, rose from 5.7% in March to 6.0% in April. Inflation expectations to twelve months obtained from the same survey moved from 4.41% to 4.54%, while expectations to twenty-four months stepped from 3.77% to 3.81%. On average, so far this year to April 26, with average data to March, break-even inflation (BEI) embedded in Colombian sovereign bonds (TES) in *pesos* and RVU have increased for 2, 3 and 5 years (2 bp, 8 bp, and 4 bp, respectively), while that for a 10-year term lowered (21 bp). Thus, average BEI so far in April to 2, 3, 5 and 10 years posted at 4.75%, 4.57%, 4.40%, and 4.41%, respectively.