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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Economic Studies Division

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I. International Context and Balance of Payments

1. The recent dynamics of the prices of goods exported and imported by the country suggest that Colombia' terms of trade in July would have been lower than in the previous month, thus remaining at levels similar to those observed at the beginning of 2009. This will continue affecting national income adversely.
2. The international price of oil (Brent) decreased on average 8.4% as to July 29, compared to the observations from the previous month. This reduction would be explained, to a great extent, by the high levels of inventories, a weak global demand, the appreciation of the US dollar, and the prospects that supply would continue high (due to the reintegration of Iran to world markets, a historically high production in the major OPEC countries, and because oil extraction in the United States continues to expand).
3. Similarly, the prices of coffee, nickel and other metals exported by the country have also fallen. In contrast, the prices of some foods imported by Colombia exhibited some increases as a result of supply shocks in North America.
4. The most recent figures of global economic activity confirm that growth of Colombia's main trading partners for 2015 would be lower than that for the previous year and than the forecasts presented by the technical staff from *Banco de la República* in the March edition of the Inflation Report. The figures available for the second quarter suggest that reactivation in the United States would have been weaker than expected, while the euro zone would have continued expanding at very modest rates. Meanwhile, the economies of China and Latin America would be growing at lower rates than the averages observed over the past few years.
5. The most recent data for growth in the United States show recovery after the weakness observed between January and March. Thus, the expansion of GDP rose from 0.6% quarterly annualized (q.a.) (revised from -0.2% q.a.) in the first quarter to 2.3% q.a. three months later. This better behavior was explained largely by a reactivation of private consumption and exports, which offset the lower dynamism of investment. However, it is worth mentioning that the performance of US economy during the first semester of the year was lower than expected by the technical staff at *Banco de la República*, as presented in the March edition of the Inflation Report.
6. As for the labor market, employment generation continues at a favorable pace, therefore the unemployment rate in June lowered to 5.3%. Regarding the annual variation in prices, modest increases in the total and core inflation indicators were observed in June.
7. In this context, the press release of the meeting of the FOMC (Federal Open Market Committee) of the Federal Reserve (Fed) in July suggests that the benchmark interest rate would be raised towards the end of the year, and that it would continue increasing gradually in the future.

8. As for the euro zone, data for real activity and industrial surveys for the second quarter suggest that the economy would have continued reactivating slowly. On the other hand, according to the most recent indicators of household and business confidence, the events in Greece would not have generated much additional uncertainty. Regarding the variation in prices, mild reductions were observed in the annual indicators of total and core inflation.

9. China's GDP grew at a yearly rate of 7.0% during the second quarter, the same as had been registered three months before, but less than 7.4% for all 2014. Meanwhile, the indicators of industrial production, fixed asset investment and retail sales are still pointing at a low dynamism of real activity. Annual inflation in June remained low (1.4%).

10. In Latin America, the data for economic activity in May suggest that the economies of Chile, Mexico and Peru continued to expand at modest rates during the second quarter. For its part, data in Brazil shows that the contraction that began last year would be deepening.

11. As for Latin American economies, inflation data as of June continued exhibiting a heterogeneous behavior among countries. In Mexico it fell and continued within the target range of its central bank, while in Chile and Peru inflation increased, mainly as a result of the depreciation of their currencies. In contrast, annual variation of prices in Brazil remains high and with a marked growing trend.

12. In terms of international financial markets, the agreement between Greece and its major creditors helped to reduce global risk aversion. In this context, the movements of the major global financial variables during July would be explained, to a large extent, by the Fed's prospects of increasing the benchmark rate towards the end of the year. Thus, the interest rates for long-term bonds of the United States and of the major countries of the euro zone remained higher than those recorded in previous months, while the US dollar exhibited a strong appreciation.

13. In Latin America, an increase in the risk premia was observed so far in July, while the currencies of the region have depreciated. This behavior has been particularly marked in the case of the Colombian peso, which stepped from an average value of COP 2,562 per dollar in June to an average value of COP 2,737 per dollar one month later (with data to July 29), which represents a monthly depreciation of 6.8%.

a. Exports and Imports

14. In May, total exports in US dollars fell 38.9% due to the general decline in the value of the main items exported, caused by the effect of quantities and prices. The decline in the value of mining goods exported was 49%. External sales of agricultural goods and other exports exhibited variations of -19.9% and -9.5%, respectively. The fall in mining goods is associated to the lower exports of oil (-40.7%) and coal (-68.6%). In turn, exports of agricultural goods recorded joint falls in bananas (-46.2%), flowers (-14.9%) and coffee (-8.6%).

15. Within other exports, reductions were recorded in food and beverages (-18.7%), vehicles (-52.7%), and other agricultural goods (-37.2%). By destinations, the declines of 23.5 % to Ecuador, of 24.3% to Venezuela, and of 12.4% to the United States stand out.

16. So far this year to May, total exports fell 31.3%. Exports of mining goods (-42.3%) and those of other products (-9.4%) contributed to this fall. Exports of agricultural goods increased 7.6% in this period. The decrease in exports of mining goods was due to the general decline in the items belonging to this group, whose major falls were oil (-45.7%) and refined goods (-59,8%). Within other exports, the falls in food and beverages (-11.2%), vehicles (-22.0%), and paper (-15.3%) stand out. Exports of agricultural goods increased thanks to the 20.4% increase in coffee.

17. In May, total CIF imports fell 18.1% in annual terms. This behavior is explained by the decrease in imports of intermediate goods (-20.2%), capital goods (-20.2%) and consumer goods (-10.9%). As for imports of intermediate products, the result is explained by the reductions registered in raw materials for industry (-16.3%) and fuels and lubricants (-36%). Imports of capital goods were greatly affected by the falls registered for transportation equipment (-33.8%) and capital goods for the industry (-12.6%). Regarding consumer goods, there were falls in both durable (-12.2%) and non-durable goods (-9.3%).

18. In the accumulated value from January to May, CIF imports have fallen 10.2%. This fall is explained by the reduction of imports of intermediate goods (-16.9%), capital goods (-4.8%), and consumption goods (-4.0%). To a larger extent the fall in intermediate goods is associated to the 38.8% reduction in fuels and lubricants. Within capital goods, the main fall was recorded in capital goods for industry (-9.7%), while imports of consumer goods were affected by the 8.0% reduction in durable goods.

II. Projections of External Variables

a. Scenarios for External Growth

Baseline or more likely scenario (Chart 1)

19. Growth forecasts for the country’s main trading partners were revised in the present report. The projection of the average annual growth of GDP of Colombia’s major trading partners (weighted by non-traditional trade) fell from 1.3% to 0.9% in 2015, and from 2.4% to 2.2% for 2016.

20. As for the United States, the growth forecast for all of 2015 was revised downward. For the remainder of 2015 and for 2016, it is expected that the determinants of consumption continue at favorable levels, so household expenditure would be the main engine of growth of economic activity.

21. Exports would be affected negatively by the strength of the US dollar *vis-à-vis* major currencies in the world and by the lower growth of its trading partners.

22. The excess of existing capacity would continue being eliminated, and some upward pressures on wages would begin to appear.

23. The Fed would increase its benchmark rate by the end of the third quarter and would continue increasing it very gradually throughout 2016. It is expected that this measure is transmitted to market rates in an orderly manner.

24. In the euro zone, recovery of the economy would continue slowly, as was expected in the previous Inflation Report. The measures taken by the ECB have resulted in the recovery of confidence and have restored, to some extent, the credit channel, which would encourage private consumption and investment. Additionally, weakening of the euro would continue propelling exports outside the European Union.

25. The situation in Greece would continue to be a source of political uncertainty for the region, although it is expected that the impact on household and business confidence would continue to be limited.

26. In China, growth would continue moderating inasmuch as fixed asset investment and the expansion of credit continue reducing from the high levels recorded in previous years. Exports would give less impulse to growth due to the strengthening of the Chinese yuan and because global demand remains weak. However, stimulus measures by the government and the central bank would allow for a soft landing.

27. In Latin America, a heterogeneous behavior among countries is expected. Peru, Chile and Mexico would exhibit some signs of recovery. In contrast, Brazil's economy would shrink in 2015 as a result of the fiscal consolidation that is taking place in this country and the low levels of business and consumer confidence. Some recovery would take place in 2016. Meanwhile, Venezuela would continue contracting due to the structural problems it is facing and the fall in international oil prices.

Risks to the Baseline Scenario

28. This report considers that global economy continues facing mainly downward risks. Among the most important, the following can be noted: potentially destabilizing effects on financial markets due to the increase in the policy rate of the Fed; a deeper slowdown in China; and increased political uncertainty in Europe.

Chart 1

Economic growth forecasts for Colombia's major trading partners						
Country or region	**2015**			**2016**		
	Low	**Baseline**	**High**	**Low**	**Baseline**	**High**
United States	2.0	2.4	2.8	2.0	2.8	3.6
Euro zone	0.8	1.3	1.8	0.0	1.4	1.8
China	6.4	6.7	7.0	6.0	6.5	7.0
Brazil	-2.0	-1.5	-1.0	0.2	1.0	1.8
Ecuador	0.2	1.2	2.2	1.0	2.0	3.0
Venezuela	-8.0	-6.0	-4.0	-4.0	-1.0	2.0
Peru	2.5	3.5	4.0	3.0	4.5	5.5
Mexico	2.3	2.7	3.3	2.5	3.2	4.0
Chile	2.3	2.8	3.3	2.5	3.5	4.5

b. Projection of the Balance of Payments

29. During the first quarter of 2015, the current account deficit was 7.0% of GDP (USD 5,136 m), greater than the one observed in the first quarter of the previous year (4.6%, USD 4,032 M). This increase as a percentage of GDP is explained in 1.1 percentage points (p.p.) due to the larger deficit in US dollars, and in 1.3 p.p. due to the effect of the depreciation of the peso on the measurement of nominal GDP in US dollars.

30. In terms of US dollars, the expansion of the deficit is mainly associated to the significant deterioration of the trade balance, reflecting a situation of low prices in the country's major export products and lower external demand for the rest of the products. Quarterly exports were 26% lower than those recorded a year ago, while imports fell slightly (-4.3%), despite the depreciation of the currency that has been taking place since the third quarter of 2014. This was partly offset by a significant reduction of outflows due to profit remittances in the oil sector as well as in other sectors.

31. Compared to the fourth quarter, the deficit of the current account in US dollars was lower by USD 1,213 m, as a result of a reduction of net outflows due to non-factor services and factor income; the trade balance remained at levels similar to those registered in the previous quarter.

32. Capital inflows for the first three months of the year added a net inflow of USD $4,796 m, which is USD $558 m higher than the one registered in the same period last year. In net terms, this result reflects a reduction in direct and portfolio investment, which was offset by an increase in the resources of other investments (loans), particularly those addressed to the public sector.

33. The estimation of the current account deficit for 2015 is slightly higher than the forecast issued three months ago. As a percentage of GDP, it remains above the rate recorded in 2014. In the

most likely scenario, the current account deficit would be around 5.6% of GDP (**Chart 2**). This result reflects a reduction of the deficit to USD $17,214 m (from USD $19.549 m in 2014).

34. The income from exports of goods will continue being affected by the low level of the prices of the main export products *vis-à-vis* the data observed in 2014. However, given the behavior of prices in the second quarter of the year, estimates of the average export price for oil and coal were revised upward. Thus, the drop in exports of mining goods decreased slightly from the estimations presented in the previous quarter.

35. On the contrary, the poor performance of external demand for industrial products led to a downward revision of the forecast for these exports; hence, a contraction of the exported value is expected.

36. It should be noted that expansions in export volumes for most commodities are expected, which are consistent with the projections of growth of their production, although lower than those expected three months ago for oil and coal, and greater for coffee (1.2% oil; 3.0% coal, and 6.7% coffee). Thus, in the baseline scenario, exports (in dollars) of the main products would fall around 31%.

Chart 2

BALANCE OF PAYMENTS - (US$ million)	2014	2015
		Baseline
CURRENT ACCOUNT (A+B+C+D)	**-19,549**	**-17,214**
Percentage of GDP	**-5.2**	**-5.6**
Percentage of GDP (TRM 2014)		**-4.3**
A. Goods	**-4,583**	**-8,448**
a. Exports	57,027	43,441
Main Products	41,019	28,229
Other Exports	16,008	15,213
b. Imports	61,610	51,889
B. Non-factor Services	**-6,638**	**-5,076**
C. Factor Income	**-12,685**	**-8,213**
D. Current Transfers	**4,358**	**4,523**

37. This projection assumes that the adjustment of the external balance would continue henceforth as a response to the shocks to the terms of trade and the consequent reduction of external income. A significant reduction of imports is forecast, which is associated with a strong fall in imports of capital goods for the mining -energy industry, a less-dynamic domestic demand, and the generalized reduction of international prices on imported goods, especially those of intermediate goods (fuels and derivatives). A lower deficit in the balance of services is projected as a result of the positive effects of the exchange rate on exports of this type and the reduction in imports associated with freight services and tourism; also due to lower net outflows

of the net factor income, as a reflection of the fall in the profits of the mining-energy sector, as well as the effects of depreciation and the economic slowdown on the rest of the sectors.

38. As for the financial account, it is estimated that moderation of funding resources from direct and portfolio investment would continue during the rest of the year, in an environment of slowdown of domestic economic activity and the possible normalization of the monetary policy in the United States towards the end of the year (**Chart 3**).

39. A greater reduction in net foreign direct investment is foreseen for 2015, given the confirmation in the first quarter of the cut in funding flows to the oil sector and the greatest reduction in resources to other sectors, associated to a greater effect of depreciation on the reinvestment of profits and lower growth prospects for the economy. For the whole year, USD $10,543 m resources of net direct investment are estimated.

40. Funding with resources from portfolio investment would also be lower in 2015 *vis-à-vis* the previous year, as a consequence of the reduced flow of foreign capital into the local public debt market, despite more placements of foreign bonds in the first semester by *Ecopetrol* and the private sector. This will be partially offset by greater resources coming from other investment, particularly credits obtained by the non-financial public sector.

Chart 3

BALANCE OF PAYMENTS - (US$ million)	2014	2015 Baseline
CAPITAL AND FINANCIAL ACCOUNT (A+B+C+D+E)	**-19,745**	**-16,874**
A. Net Foreign Investment in Colombia	**-12,358**	**-10,543**
a. Foreign Investment in Colombia	16,257	12,042
b. Colombian Investment Abroad	3,899	1,500
B. Portfolio Investment	**-11,654**	**-3,546**
a. Public Sector	-15,428	-6,893
b. Private Sector	3,774	3,347
C. Derivative Instruments	**268**	**493**
D. Other Investment (loans and other credits)	**-439**	**-3,050**
a. Assets	1,820	1,207
b. Liabilities	2,258	4,258
E. Reserve Assets	**4,437**	**-228**
ERRORS AND OMISSIONS	-196	340

41. Additionally, alternate scenarios to the baseline projection of the balance of payments for 2015 were considered, with different assumptions about the conditions of international financing and internal growth. In a scenario in which financing conditions remain positive, with economic growth of around 3.4%, the current account deficit would be 6.4% of GDP. Lower international

financing along with lower growth of the economy (for example, 1.8%) would result in a GDP deficit of 4.8%.

42. A lower current-account deficit in dollars and as a proportion of GDP (about 5%) is projected for 2016. This would be associated mainly with a lower negative result of the trade balance, with a better picture for the prices of the main export products, recovery in the major trading partners, and the effect that the beginning of operations of *Reficar* would have on exports and imports of fuels.

III. Growth, Domestic Demand, and Credit

43. Data available for the second quarter suggest that the growth rate of the Colombian economy would have remained at levels close to those registered during the first three months of the year. Household consumption would have moderated (particularly consumption of durable goods), while government consumption would have contributed to a greater extent to GDP growth. For its part, investment in capital goods would have also exhibited a setback. Lower dynamism of domestic demand, together with the depreciation of the nominal exchange rate, led to a major correction of imports. On the other hand, according to data to May, real exports would have grown at a slightly higher pace than the one recorded at the beginning of the year.

44. According to the most recent publication of the Monthly Survey of retail trade (EMCM) by DANE, retail sales expanded 2.7% in May as compared to the same month in 2014 (1.1% April-May), which represented a slowdown with regard to registers of the first quarter (5.5% on a yearly basis). Excluding vehicle sales, the increase in sales was 6.1% and 4.7% on a yearly basis for May and the first two months, respectively (*vis-à-vis* 8.1% in the first quarter).

45. For its part, vehicle and motorcycle sales continue exhibiting a poor performance. In May, they fell 12.9% as compared to the same month a year before. The fall deepened during April-May with respect to the first quarter of the year (-14.7% in the two months *vis-à-vis* -6.7% in the first quarter of 2015). Additionally, according to data of new license plates for vehicles issued by the *Comité Automotor Colombiano* (Colombian Automotive Committee) in the second quarter of the year a fall of 12.0% on a yearly basis was observed (*vis-à-vis* 1.3% in the first quarter).

46. Other indicators not used by DANE as input for calculating private consumption, but which evidence a high historical correlation to their growth rate, suggest that consumption would have expanded at a pace similar to that of the first quarter. This is the case of the sales balance of the Monthly Survey of Economic Expectations (EMEE) by *Banco de la República* and *Fedesarrollo*'s Consumer Confidence Index (CCI).

47. In the first case, the results from EMEE to May showed no significant changes *vis-à-vis* the data of April. As for the second, the ICC improved slightly in June with respect to the data of May. The average for this index in the second quarter is similar to that of the first, and continues

below the one calculated since 2001. Upon disaggregating this index into its components, it is noted that the perception about current economic conditions is better than consumer expectations toward the future.

48. Regarding the labor market, to May some annual increases of the unemployment rate were observed in some geographic domains. Forecasts suggest that the gap in the labor market would be positive for the remainder of 2015 and during 2016.

49. Employment to May grows at a slower pace, especially in the 13 major metropolitan areas. Salaried employment continues to grow at favorable annual rates.

50. With respect to Gross Capital Formation, the balance of investment expectations of the EMEE to May suggests that during the second quarter investment in capital goods other than construction of buildings and civil works would have slowed down again with regard to the data of the first three months of the year. Additionally, the data for imports of capital goods in US dollars showed significant reductions.

51. Exports in real pesos should have grown somewhat more in the second quarter than in the first, while imports decreased significantly. This is stated considering the data on foreign trade provided by DANE, the evolution of the prices of exports and imports, and the expected behavior of the domestic demand.

52. On the supply side, available indicators show that the GDP of the industry in the second quarter would not have grown on a yearly basis. In May, the industrial production index (IPI) excluding coffee threshing fell by 3.9%, with which the April-May period showed a fall of 3.6%. So far this year, the fall reported by the industry is around 2.6%. After seasonally adjusting the series, a contraction of the trend component is observed. Heterogeneity in the results remains, but the number of industries falling is greater than those which exhibit expansions. Excluding oil refining, the rest of the industry also fell (-3.6% in May and -0.3% so far this year).

53. This takes place within a context in which manufacturing exports fell 9.4% in US dollars so far this year, despite the fact that the depreciation of the peso observed should contribute to improve profitability of exports and competitiveness of locally produced industrial goods over imported ones in the domestic market. The weak growth of Colombia' trading partners, particularly those in the region (to which a significant percentage of these exports are headed), may be countering the effect of depreciation of the exchange rate.

54. It should be noted that in the last few months the companies that traditionally exported to Ecuador (one of our main destinations for industrial trade), have faced the effects of the trade restrictions imposed by that country, which imply paying a tariff (5% to 45% increases depending on the product type).

55. According to the survey of business opinion by ANDI, the use of the installed capacity is at levels slightly below the historical average, and the business climate shows slight improvements.

56. In spite of this, other industry indicators for the month of June showed some improvements. According to the survey by Fedesarrollo, the indicator of orders picked up slightly compared to the previous month, while the one for inventories reduced; trend components suggest a slight improvement. On the other hand, expectations of the industrial sector regarding production to three months increased slightly *vis-à-vis* those of the previous month. However, its trend is descending. As a result of this, the confidence index of the industrial sector improved, but its trend component remained flat.

57. With data to June, the demand for industrial energy (an indicator that shows some contemporary relationship to the IPI) grew by 0.1% per year after a 4.1% contraction in May. This would suggest an acceleration of the indicator for that month.

58. Regarding the production of the mining and quarrying sector, a better performance is expected for the second quarter, after four consecutive quarters contracting. This is explained mainly by oil production, which stood above one million barrels (1,019 mbd) in that quarter and exhibited an annual growth of 5.8%. This result could be offset by the recent behavior of coal, which shows a significant decline in the volume exported in the April-May period (-34,4%).

59. As for the agricultural sector, the National Federation of Coffee Growers reported an expansion of coffee production of around 17%. So far this year, production is around 6,246,000 60-kg bags, which implies a 12.8% growth *vis-à-vis* the previous year. On the contrary, cattle slaughter in April-May fell at a slower pace than in the first three months of the year (-2.9% vs. -4.8%), which is a consequence of the retention phase that the activity currently exhibits within its production cycle.

60. According to the *Índice de Seguimiento a la Economía* (ISE) published by DANE, the index of the seasonally adjusted series grew by 3.6% in April, higher than the records from March (2.9%) and than the aggregate value for the first quarter of the year (2.8%). In spite of this, information is still scarce so as to define a specific trend of GDP growth for the second quarter.

IV. Behavior of Inflation and Prices

61. In June, annual consumer inflation remained relatively stable at 4.42%. This level is higher than the one registered last December (3.66%), but less than the data for April (4.64%), which is the highest value observed in the past few years (**Chart 4**). The decrease in the last two months has been concentrated on the CPI for food and has offset the increase observed in the CPI excluding food.

62. For the whole semester, acceleration of annual inflation is largely explained by the rise in the prices of tradables, excluding food and regulated goods from the CPI, by the increase in food prices, and, to a lesser extent, by increases in non-tradable goods, excluding food and regulated items, and in meals outside the home. In contrast, the prices of regulated goods and perishable

food exerted downward pressures on annual inflation in this period (**Chart 4**). It should be noted that the variation in the CPI so far this year amounts to 3.33%, which is above the midpoint of the range and higher than the cumulative change for the first six months of 2014 (2.57%).

Chart 4

Inflation to June 2015

Description	**DEC 2014**	**JAN 2015**	**FEB 2015**	**MAR 2015**	**APR 2015**	**MAY 2015**	**JUNE 2015**	**Participation in monthly acceleration (%)**	**Participation in acceleration so far this year (%)**
Total	**3.66**	**3.82**	**4.36**	**4.56**	**4.64**	**4.42**	**4.42**	**100.00**	**100.00**
Non-food Inflation	**3.26**	**3.20**	**3.41**	**3.46**	**3.44**	**3.72**	**3.72**	**0.01**	**42.53**
Tradables	2.03	2.28	3.26	3.46	3.64	3.74	4.17	**0.01**	65.10
Non-tradables	3.38	3.47	3.50	3.56	3.67	3.83	3.98	**0.10**	25.00
Regulated items	4.84	4.01	3.47	3.25	2.68	3.45	2.55	**0.05**	(47.57)
Food Inflation	**4.69**	**5.41**	**6.77**	**7.37**	**7.70**	**6.16**	**6.20**	**36.58**	**57.47**
Perishables	16.74	16.78	19.68	21.57	16.99	8.34	10.73	694.21	(22.60)
Processed food	2.54	3.70	5.62	5.99	7.00	6.55	6.00	(660.26)	69.14
Eating out	3.51	3.60	3.34	3.59	4.68	4.45	4.45	2.63	10.93
Core Inflation Indicators									
Non-food Inflation	3.26	3.20	3.41	3.46	3.44	3.72	3.72		
Core 20	3.42	3.58	3.62	3.70	3.97	4.06	4.24		
CPI excluding perishable foods, fuels and utilities	2.76	3.12	3.69	3.95	4.29	4.39	4.54		
Inflation excluding foods and regulated items	2.81	2.97	3.40	3.52	3.65	3.79	4.06		
Average of Core Inflation Indicators	**3.06**	**3.22**	**3.53**	**3.65**	**3.84**	**3.99**	**4.14**		

Source: DANE. Calculations by BANCO DE LA REPÚBLICA

63. The monthly variation for the last month observed stood at 0.10%, a level that is lower than expected by the market (0.12%) and by the SGEE (0.18%).

64. In June, the average of the four core inflation indicators increased for the ninth month in a row and stood at 4.1%, i.e., 15 bp above the record of May and 108 bp more than the data of last December. This average is the largest one observed since October 2009. All the indicators increased in June as compared to May, except the CPI excluding food, which remained stable at 3.72% and recorded the lowest level. The CPI excluding primary food, fuels and utilities exhibits the highest level of all the indicators, standing at 4.54%, while the CPI excluding food and regulated items closed at 4.06%, and the Core-20 at 4.24% (**Chart 4**).

65. Within the subset of the CPI excluding food and regulated items, the tradable component continued increasing, as it has done since August last year without interruption. The data to June was 4.17%, surpassing by 33 bp the one observed a month ago, and 214 bp higher than in December. The acceleration of this indicator is still closely related to the depreciation of the peso. As mentioned in the previous report, as of January, the pass-through of depreciation to inflation had been low this year, but it accelerated in the rest of the first semester of 2015.

66. In June, once again, there were widespread increases in the items of the tradable component of the CPI excluding food and regulated items. In this segment of the basket, monthly increases in vehicles, newspapers and some household appliances stand out. As for vehicles (whose weight in the CPI is 4.4%), an 8.5% increase was accumulated in the first six months of the year.

67. The annual variation of the non-tradable CPI excluding food and regulated items rose again in June, standing at 4.0% (i.e., 15 bp more than in May). This item has also increased gradually throughout the year (in December, its record was 3.4%). The upward trend of this aggregate is attributed to an increase in import costs, depreciation, a greater indexing, and to specific increases in entertainment services (soccer tickets), the latter transitory, in part. To date, it is unclear if there are inflationary upward pressures arising from demand, among other reasons because the estimates of the output gap indicate that it would be in negative terrain, and because aggregate demand would be slowing down.

68. Specifically in June, acceleration of non-tradable goods is explained by the increases in soccer tickets (according to information provided by DANE), rent (which went from 3.2% in May to 3.3% this month), and the items most directly affected by the exchange rate such as furniture and household items, whose annual variation increased from 3.9% to 4.1%.

69. For its part, annual variation of the CPI for regulated goods stood at 2.55% in June, reducing 90 bp as compared to the results of May. This item has reduced along the first semester, a trend attributed to the decrease in the price of gasoline mainly at the beginning of the year (considering that it increased in June). In the last month, decrease in the annual variation was caused by a specific reduction in tariffs for energy and household gas. It should be noted that these two variables have been highly volatile in the past; considering what happened in June, this does not necessarily correspond to a trend that will continue in the coming months.

70. In June, annual food inflation (6.2%) remained stable with respect to May, but fell *vis-à-vis* the maximum value of the last quarters registered in April (7.7%). Per components, it was observed that processed foods fell from 6.6% in May to 6.0% in June thanks to a recovery in the supply of rice and a decline in its price (from 3.4% in June). In contrast, perishable goods went from 8.3% in May to 10.7% in June, after the falls observed in the two previous months. The decrease in the price of potato this month could not offset the increase in prices of several vegetables and legumes. The annual variation in meals outside the home remained stable at 4.5%.

71. As for non-labor cost pressures, increases were perceived in June. This is suggested by indicators such as the annual variation in producer prices for domestic supply (produced and consumed plus imported) whose annual variation rose from 3.7% in May to 5.0% in June, having declined in March and April. This new increase, as in previous months, has been closely linked to the depreciation of the peso: the PPI for imported goods stood at 12% in June compared to a 9.3% annual variation a month before. Additionally, the local component increased from 2.4% to 3.2% in the last month.

72. So far this year, wages have been showing adjustments which are compatible with the target range for inflation. Those for construction remained at yearly rates of around 4.0% in June. Yearly adjustment of the salaries for trade amounted to 3.3% in June, lower than in previous months.

73. Inflation expectations to December 2015, based on the monthly survey addressed to financial analysts with information to the second week of July, were stable between May and June, standing at 3.89%. Inflation expected to twelve months, based on the same survey, fell slightly from 3.17% in May to 3.11% in June. Inflation expectations for 2, 3, and 5 years inferred from the break-even inflation (BEI) in the course of July have fallen 28 bp, 23 bp and 14 bp, respectively, as compared to the average data of June, although they increased 10 bp for a 10-year period. Thus, BEI to 2, 3, 5 and 10 years registered 2.95%, 2.88%, 3.04%, and 3.92%, respectively.