Minutes of the Banco de la Republica Board of Director's meeting on November 29, 2013

Detailed Explanation of the Macroeconomic Situation (only in Spanish) Must reads The Board of Directors of the Banco De La Republica Announces the Quantitative Inflation Target for 2014 and Keeps the Benchmark Interest Rate Unchanged Last modified Monday the 29th of April, 2024
A regular meeting of the Board of Directors of Banco de la República was held in the city of Bogotá D.C. on November 29, 2013. In attendance were Mr. Mauricio Cárdenas Santamaría, Minister of Finance and Public Credit, Mr. José Darío Uribe, Governor and Managing Director of Banco de la República, and the Board Members Carlos Gustavo Cano Sanz, Ana Fernanda Maiguashca Olano, Adolfo Enrique Meisel Roca, César Vallejo Mejía and Juan Pablo Zárate Perdomo. These minutes contain a summary of inflation, economic growth and their prospects for the future, which was prepared by the Bank's technical staff (Section 1), in addition to a review of the key deliberations and policy options considered by the Board of Directors (Section 2).

1. INFLATION AND ECONOMIC GROWTH a. Recent Developments in Inflation
There was a substantial decline in the annual consumer inflation in October and one that was significantly larger than expected. The result for this month was 1.84%, 43 basis points (bp) less than what was registered in September. So far this year the increase comes to 1.89% which is lower than the accumulated rise for the same period last year (2.48%). The decline of inflation in October was mainly concentrated in food and secondly in the regulated component.

In food, the annual variation slowed down significantly (139 bp compared to the record for September) and was at 0.7% at the close of the month. The decrease was concentrated in perishables where significant drops were seen in the prices for potatoes and a large variety of other products (tubers, vegetables, and fruit). A good supply of agricultural products together with limited rises in the costs of production and transportation are still the explanation for the small relative increases in these prices in October as well as in previous months. Another item that presented a decline during the month was that of meals away from home (from 3.7% to 3.3% annually). Last of all, the prices of processed goods did not show any relevant change last month and their annual variation remained at 0.0%. In recent months, the international prices of grain, oil, and other food have dropped which is part of the reason for the low upward pressure that has been seen for this group of goods.

The annual change in the CPI excluding food in October was at 2.31%, 5 bp lower than the month before. The 17 bp decline in the annual change in the CPI for regulated goods in October (1.1%) is noteworthy. This variable has seen decreases since July due to the limited rises or drops in the prices of fuel primarily and, to a lesser degree, the fees for various utilities. In the case of fuel, the recent reductions, which were -3.6% annually last month, are partly related to the few upswings that have been registered in international prices for several quarters and above all to the drops starting in August. Respecting the fees for utilities, there were small adjustments to gas and water and reductions for electricity in October. So far this year the rise in these items has been 2.5%, which is low compared to what was registered in previous years. This could be due to the decisions to lower the fee for water and garbage collection in some cities, the performance of the international prices for fuel, and the drop in the PPI, etc.

In October, the annual change in the CPI for non-tradables excluding food and regulated items remained almost unchanged at around 3.7%. The annual variation for rent declined slightly (3 bp) as it has been doing since the beginning of the year while no important changes in the other components of the basket were registered. At the

same time, the annual change in the CPI for tradables excluding food and regulated items stayed at 1.3% in October. In recent months, the depreciation of the peso has been reflected in a moderate upswing in this indicator and in rises (although slight) in the prices of some imported goods.

Core inflation declined again in October. The average of the four indicators monitored by the Bank was at 2.44% in comparison to 2.51% for the previous month. Since February of this year, this measurement has shown very few variations.

The annual change in the PPI went from -1.3% in September to -1.9% in October. The local component dropped with respect to the previous month (56 bp) in a wide range of goods. Imports rose 0.9% annually, a figure that is lower than what was registered the month before (1.6%).

With respect to inflation expectations, according to the Bank's monthly survey of financial market analysts, inflation expected for December of this year is 2.2% while the expectations for the coming 12 months are at 2.9%. This is lower than those for the previous month. At the same time, inflation expectations derived from the yield curve of the TES for different maturities are at levels below 3%. Compared to the month before, those derived from 2 and 3 year paper declined while the 5-year ones rose.

b. Growth

The latest information available indicates that some areas of domestic demand were expanding at a moderately positive rate in the third quarter. Household consumption continued to be strong while investment in machinery and equipment may have performed well over the period. Uncertainty with respect to information on the construction of buildings, public works projects, and public consumption persists.

According to the most recent information reported by DANE, the index of total commercial sales grew 4.9% in annual terms between July and September. This figure is similar to the one registered for the second quarter aggregate (5.1%). The balance of sales from the regional survey done by the Banco de la Republica (EMEE) also suggests that the expansion of household consumption continued at a positive rate during the third quarter.

With respect to investment other than investments in building construction and public works projects, both the balance of investment expectations from EMEE and the expansion in imports of capital goods in real pesos suggest that their performance may have been somewhat better than what was registered in the second quarter of 2013.

In the month of September, in turn, the total exports registered an annual drop of 1.2% in dollars due to the lower sales of mining products (-2.4%). This decline was slightly offset by the 10% growth in agricultural exports and 0.1% growth in industrial exports.

Total imports (CIF) in dollars climbed 10% compared to the same month last year. This performance is due to the larger purchases of capital goods (15%) and of raw materials (13%) since the purchases of consumer goods fell 1.1%.

In the area of supply, the most recent indicators for the third quarter suggest a mixed performance. In the case of industry, the annual change for the IPI excluding coffee bean threshing in September was -1.8%, which is in line with what was expected. With this, the third quarter registered a 1.9% decline and -2.7% for the year so far.

However, in September the number of construction licenses rose in comparison to the previous month (18.9%) and the accumulated growth for 12 months was at 10.6% (in June it was 7.3%). The production of cement and shipments, in turn, surged between the second and third quarters. Cement production went from growing 0.7% annually in June to 5.9% in September. The shipments grew at an annual rate of 6.9% in the third quarter compared to their 4.3% growth in the second quarter.

Thus, the strongest sectors in the third quarter are expected to be construction and agriculture. Others that may have contributed significantly to the growth are financial services, commerce, and mining. In contrast, the industrial sector (including coffee bean threshing) would be the one that contributed the least to the growth of output.

The above makes it possible to maintain a forecast range of 3.8% to 5.2% for the growth of the GDP in the third quarter. It should be pointed out that the uncertainty about investment in public works projects, public consumption, and housing construction remains high due to the lack of information.

There is still very little information on the fourth quarter. In the month of October, the recovery in the consumer confidence index (CCI) published by Fedesarrollo is notable as is the surge in vehicle sales. In the first case, the CCI was once again above the average it has held since 2001 after having overcome the shocks that significantly affected the perception and expectations of households in the month of August. Sales of vehicles, in turn, rose 10.2% in October in comparison to the same month last year. This indicates a surge with respect to what was registered on average for the third quarter (-0.6%).

For the fourth quarter, the most favorable news comes from the sectors of agriculture and energy. Specifically, according to the figures from the National Federation of Coffee Growers, coffee production showed a 62% expansion in October after having grown about 52% in the third quarter. In addition, the recovery in the annual variation of the total demand for energy stands out. This went from 1.2% in September to 3.5% in October.

Based on the information for October, the Fedesarrollo survey of business opinion (EOE) indicates an improvement in the indicators for confidence, orders, inventory, and expectations for industry for the coming three months. Furthermore, the demand for non-regulated electricity for industry, a variable that is highly correlated with the IPI, reported a 5.4% expansion in October (compared to -0.8% in September). The preceding may suggest a better performance for the sector for the month following it and a more favorable outlook for the end of the year.

With all of the above, the forecast range of 3.5% to 4.5% is maintained for all of 2013. Note that the performance of investment in public works projects, housing construction, and public consumption is a source of great uncertainty for these forecasts.

c. Financial Variables

Bank loans (N/C and F/C) in October registered an annual growth rate of 14.13% which is close to the average seen since March (14.02%). The loan portfolio in national currency climbed from 13.18% in September to 13.74% in October and the one in foreign currency went from 26.91% to 20.61% during the same period.

Broken down by market, the portfolio of loans granted to households registered an annual growth in October of 13.07%, which is higher than the growth in the previous month (12.81%). This was the result of the performance of consumer loans which went from 12.37% to 12.61% as well as mortgages where the annual growth of 14.05% in September went to 14.37% in October. Regarding the commercial loan portfolio, the annual growth rate in October (14.45%) was similar to the one for the previous month due to a surge in the component in national currency (from 13.13% in September to 13.99% in October) which offset the slowdown in the foreign currency component (from 27.02% to 18.85%).

The interest rates for the loans disbursed by credit institutions since the beginning of the cuts in the benchmark rate in July 2012 have accumulated reductions of: -222 bp for mortgages, -221 bp for consumer loans, and -185 bp for building loans.

The size of the decline in the real interest rates has been lower due to the effect of the lower rate of inflation. There have been reductions during this same period of: -171 bp for mortgages, -167 bp for consumer loans, and -

136 bp for construction loans.

The levels of the real interest rates for consumer loans, mortgages, preferential loans, ordinary commercial ones and commercial lines of credit, and loans for construction in September were below their historical averages as calculated since 2000. In contrast, the credit card loans are above their average.

d. Foreign Context

In the last few months, economic activity in the developed economies has continued to recover. In the emerging economies, in turn, growth rates have stabilized but, in some cases, at levels below their potential.

In the United States, the information from the third quarter shows that economic growth surged and was better than expected. In spite of that, the data show a slowdown in consumption and exports. The higher growth was mainly due to the increase in inventory which could affect growth in the last quarter of the year. The figures for the fourth quarter show that productive activity has continued to expand. Thus the main impact of the federal government shutdown in October was on consumer confidence and not on private activity as industry and the indicators of business opinion continued to rise.

In the euro zone, growth remained in positive territory during the third quarter. Nevertheless, the expansion was lower that what had been seen in the second. In both Germany and France growth rates that were lower than in the previous quarter were seen (in the case of France, there was a contraction). There are some symptoms of a recovery in some of the economies on the periphery although it is still at a very slow pace. In addition, the confidence indicators for both businesses and consumers as well as the business opinion indicators have continued to recover in the last few months. In spite of that, the economy remains vulnerable in terms of financial stability and economic activity.

In the emerging economies, growth was positive in the third quarter although lower than what has been seen in previous years. The growth in China was in line with what was expected and the preliminary figures for the fourth quarter show some stability. Growth in other Asian economies is remaining lower than what was seen in previous years.

In Latin America, in turn, there was a slight slowdown in the rate of growth in Peru while some stability can be seen in the growth rate for Chile. In both cases, the latest data shows levels that are lower than what their potential is estimated to be. A slowdown has been seen in Venezuela.

Regarding the international prices for petroleum, the lower geopolitical tensions and the lower expected growth in the emerging economies have allowed its price to decline since August. However, in the last few days there has been a slight uptick due to some law and order problems in Lybia. In the case of other goods exported by Colombia such as coal and nickel, the prices have remained relatively stable in the last few weeks. The prices of food, in turn, are staying below the levels seen in 2012 and, in some cases, they have decreased further in the last few weeks.

Due to all of the above, inflation in the main developed economies and in a considerable group of emerging ones has dropped in the last few months. This situation together with growth that is lower than the potential has given an incentive to several central banks to reduce their benchmark interest rates. The central banks of other economies that have higher inflationary pressures such as Brazil, India, and Indonesia have raised their rates in the last few months.

The country's terms of trade remain high but lower than those for previous years. Going forward, no rise in these terms is expected in a scenario of dilatory recovery of the global economy and better conditions expected in the global supply of petroleum.

With respect to the monetary policy announcements on the part of the Federal Reserve of the United States, it appears that the markets have discounted the fact that the termination of the stimulus program will be delayed more than was anticipated a few months ago. This has generated a degree of calm in the financial markets, which has been reflected in stability in the risk perception of the emerging economies. Some reactivation of capital flows has also been seen and this has contributed to reducing exchange rate pressures. Nevertheless, the uncertainty with respect to the beginning and speed of normalizing monetary policy in the United States as well as the effect that it could have on the financial markets remains high.

2. DISCUSSION AND POLICY OPTIONS

The board of directors took the following relevant aspects into consideration:

(i) The results of worldwide growth for the third quarter show a foreign global demand that is recovering slowly mainly fueled by the developed countries. Both the growth in the United States and the recovery of economic activity in the euro zone turned out to be somewhat better than projected. The growth of the large emerging economies in Asia and Latin America was heterogenous and the rates of growth in the majority were lower than their potential.

(ii) The interest rates for American Treasury bonds have been relatively stable but at levels that are higher than the ones seen before May, the month when a possible reduction in the monetary stimulus on the part of the Fed was announced. Nevertheless, the uncertainty with respect to the beginning and speed of normalizing monetary policy in the United States is high.

(iii) The country's terms of trade remain high but lower than those for previous years. Going forward, no rise in these terms is expected in a scenario of dilatory recovery of the global economy and better conditions expected in the global supply of petroleum.

(iv) In September, industrial production excluding coffee bean threshing showed a drop in annual terms again. The annual growth of retail sales was low although it registered a rate increase for the third quarter similar to the one seen in the second.

(v) The figures for October show a recovery in household confidence, an improvement in the sales performance of durable goods, and an improvement in the businessmen's perception of sales. The growth of the industrial demand for energy rose and the surveys suggest a recovery in shipping and in the production expectations of the manufacturing sector for the coming three months.

(vi) Due to the above, the technical team did not modify their growth estimate for the third quarter (between 3.8% and 5.4%) nor for all of 2013 (between 3.5% and 4.5%).

(vii) In October, the total growth of bank loans slowed down although it continued to be higher than the rise in the nominal GDP. The majority of the nominal interest rates for loans declined during the month. In real terms, they remained below their historical averages (except for the rates for credit cards) and drove economic growth.

(viii) Annual consumer inflation showed an unexpected, sharp drop as it went from 2.27% in September to 1.84% in October. This was mainly due to a transitory fall in the growth rate of food prices.

(ix) The economic analysts' inflation expectations for a year from now as well as those derived from the public debt papers with maturities of less than five years declined and were below 3%. To the degree in which supply shocks are diluted and the aggregate demand continues to be driven by an expansionary monetary policy, expectations are expected to converge on the long term target.

To summarize, economic growth in 2013 is expected to be similar to what was seen the year before. To the degree in which the supply shock for food dilutes, inflation and expectations for it should return to the target range and pick up their convergence again towards the long term target (3%). Interest rates are staying at levels that stimulate the economy's aggregate expenditures.

The members of the Board agreed that it would be appropriate to keep the benchmark interest rate unchanged. Some emphasized the fact that the information available as of the previous Board meeting had shown mixed signals with variables that performed better than expected and others that were below the expectations. They also thought that if the information available in the future suggests a consolidation of expectations of a downturn in inflation with a growth that is equally or less than expected, there would be room for a monetary boost that is greater than the current one. It will also be necessary to keep in mind the possible effects of a reduction in the purchase of assets on the part of the FED ("tapering") on the country's financial variables.

Other members also added that it is necessary to have a symmetrical response with respect to deviations from the forecast inflation compared to the target. This means that it is just as undesirable to go above the ceiling of the target range as it is to go below the range. Finally, the need to evaluate the signs that the potential GDP may be higher than what has been estimated as well as the permanence of this phenomenon and the effects that may occur in the policy realm was discussed. Due to that, it may be necessary to make adjustments in order to sped up the convergence of inflation with the goal and the closing the output gap.

3. POLICY DECISION

The Board of Directors agreed unanimously that it would be appropriate to keep the benchmark interest rate at 3.25%.

The Board confirmed their commitment to the long term inflation rate of 3% and reiterated that the actions taken by monetary policy will continue to be directed towards making inflation converge with said value. Thus, an inflation target of 3% was legally defined for 2014 with a range of +/- 1 pp. Low and stable inflation is the best contribution that monetary policy can make to sustainable growth of output and employment.

The Board will continue to monitor the performance and projections for economic activity and inflation in the country, the asset markets, and international situation carefully. Finally, they reiterate that the monetary policy will depend on the information available.

Fuente: https://www.banrep.gov.co/en/news/board-directors/minutes-november-2013