Minutes of the Banco de la Republica Board of Director's meeting on March 21, 2014

Must reads Banco de la Republica keeps the benchmark interest rate at 3.25% and extends the international reserve purchase program Last modified Monday the 29th of April, 2024
On March 21, 2014, the regular meeting of the Board of Directors of the Banco de la República was held in the city of Bogota, D.C. In attendance were Mauricio Cardenas Santamaría, Minister of the Treasury and Public Credit, Jose Dario Uribe Escobar, the General Director, full-time Board members present: Carlos Gustavo Cano Sanz, Ana Fernanda Maiguashca Olano, Adolfo Meisel Roca, Cesar Vallejo Mejia and Juan Pablo Zárate Perdomo. A summary of the inflationary and economic growth situations as well as the outlook for both drawn up by the technical team (section 1) is presented and the main discussion points and policy options considered by the Board of Directors have been summed up (section 2).

1. INFLATIONARY AND ECONOMIC GROWTH SITUATION

a. Recent developments in inflation

In February, annual consumer inflation (2.32%) registered a surge of 19 basis points (bp) compared to what was registered in January. The surge resulted primarily from the baskets of food and regulated items.

In the basket for food, the annual variation was 1.78% at the end of the month or 58 bp higher than in January. The surge occurred in the three main components of the subbasket: perishables (from 2.1% to 2.6% annually), processed foods (from -0.2% to 0.4% annually), and the meals away from home (from 3.3% to 3.9% annually).

Within the CPI excluding food (2.53% annually), the main upward pressure came from the groups of regulated prices and tradables. In regulated prices (1.8% annually), a rise of 10 bp was registered in the annual change compared to the previous month which was primarily due to increases in the price for natural gas. The annual change in the CPI for tradables excluding food and regulated items (1.6% annually), in turn, rose 4 bp with respect to the previous month. The depreciation since the beginning of last year would explain the rising trend of the CPI for tradables, which had a cumulative annual variation of 90 bp in the last twelve months. The annual variation for non-tradables excluding food and regulated items remained at 3.6% with a notable rise of 10 bp in the annual change in the CPI for rent that interrupted the downward trend that has been seen for two quarters.

The average of the four indicators of core inflation monitored by the Banco de la Republica was at 2.63% in February, 8 bp higher than the previous month. Thus, there have been slight rises in that variable for a full period of four consecutive months.

The annual change in the PPI climbed 104 bp in February (1.3% annually). A significant portion of these rises is related to the accumulated depreciation in the exchange rate and is mostly reflected in an upswing in the imported PPI (from 2.95% to 4.28% annually). However, major growth in the PPI for locally produced and consumed goods (from -0.35% to 0.63% annually) has also been seen in the last few months. This has been concentrated in goods from the agricultural and mining sector.

With respect to inflation expectations, these tended to rise in February although they remained close to the midpoint of the target range. The percentage derived from the monthly survey of the expectations of financial market analysts was 2.85% and 2.90% for the end of the year and for a horizon of 12 months from now

respectively. The measurements derived from the TES curve yield for 2-, 3-, and 5-year maturities remained at around 3.0%.

b. Growth

According to DANE, the Colombian economy grew 4.9% in annual terms during the fourth quarter of 2013. Thus, the annual expansion of the Colombian economy for 2013 was 4.3%. In addition, the economic growth for 2012 was revised downwards (this went from 4.2% to 4.0%).
With respect to demand, the significant rise in household and government consumption towards the end of the year is noteworthy. Household consumption grew 4.5% thus maintaining the pace that was seen 2012. Regarding governmental consumption, annual expansion was 6.0% for the entire year.

In the case of investment, this grew 5.7% annually in 2013. This percentage is higher than the one (4.6%) in 2012. The items that contributed the most to the expansion of investment were those related to construction of public works and building. Expenditures for investing machinery and equipment slowed down significantly while those for transportation equipment shrank.

That being the case, domestic demand contributed actively to the growth of economic activity, especially in the last few months of 2013 (6.2% in the fourth quarter vs. 3.4% in the first half of the year).

The categories in foreign trade showed slowdowns between 2012 and 2013 which were greater for imports than for exports. For the former, growth went from 8.9% in 2012 to 2.1% in 2013 while in the case of the latter, it went from 6.1% to 5.3% respectively.

With respect to supply, the sectors that showed growth that was greater than the economy as a whole in 2013 were construction (9.8%), social services (5.3%), and agriculture (5.2%). In the first case, both the subgroup of building construction and that of public works were very strong. In the last sector, the expansion was primarily due to the significant boost that coffee production received. Mining (4.9%) showed an uneven performance: while the production of petroleum grew annually at a rate that was higher than that of the other sectors (7.8%), production of coal shrank (-4.0%) as a result of various supply shocks that occurred over the course of the year. Last of all, industry showed a decline in aggregate value for the second consecutive year (-1.2%).

For the first quarter of 2014, the information available shows mixed results for the performance of the economy. The figures for retail and automobile sales point to a positive performance in private consumption. According to the figures from the Monthly Retail Sample index (MMCM in Spanish) published by DANE, sales grew 6.5% annually in January, which implies an upswing with respect to what was registered in the fourth quarter of 2013 (5.3% annually). The strongest component was that of vehicle sales which grew 19.9% annually. When the latter are excluded from the total, the annual growth was 4.0%. However, the Fedesarrollo Consumer Confidence Index (CCI) showed a significant setback in February after having shown a substantial rise during the previous month. Declines were registered in the components of both expectations and economic conditions, declines that were higher in the former than in the latter case. In spite of the above, the average for the first two months of the year was close to the average it has had since 2001.

In the area of exports, the total exports in dollars fell 1.5% in January 2014 due to the combined drop in mining (-1.6%), industrial and others (-1.1%), and agricultural (-2.1%) exports. The performance of mining exports is largely due to the lower foreign sales of gold, petroleum derivatives, and coal. In the case of agricultural exports, the drop is due to the lower exports of coffee. The fall off in the exports of industrial goods and others is primarily because of the reductions in vehicles, rubber and plastic, and chemical products. These declines were partly offset by the increase in exports of food and beverages.

Total imports in dollars (CIF) also registered a 6.6% drop in January 2014 with respect to the same month last year. This performance was caused by a generalized fall in the main categories with declines of 12.6% in capital goods, of 6.3% in consumer goods, and 1.9% in raw materials.

In the area of supply, the indicators available for the first quarter of the year also gave mixed signals. The performance of the total demand for energy and of coffee production in February are noteworthy. Respecting the former, demand grew 6.4% annually and the level it reached surpassed the records for the last six months. In the latter, based on the figures provided by the Coffee Growers Federation production surged 39.8% compared to the same month last year. In contrast, industrial performance remained weak. According to DANE, the index of manufacturing production grew 0.1% in January. The trend for the series is still demonstrating stagnation. Note that the sector performance is quite disparate. While subbranches such as mills, milling and starches, apparel as well as other food and metal products showed high growth, other subbranches registered significant drops such as was the case with automotive vehicles, other chemical products, and publishing.

Last of all, although the production of petroleum stayed at levels above one million barrels per day (1.002 mbd), it has slowed down considerably in the last four months. The annual change was at 0.5%.

Thus, the technical team at the Bank holds to a forecast of economic growth that is within a range of 3.3% to 5.3% with 4.3% being the most probable figure.

c. Financial variables

Bank loans (N/C and F/C) registered an annual growth rate of 12.4% in February, which is slightly higher than the level seen the previous month (12.2%). The loan portfolio in national currency showed a growth rate of 13.2%, which is up slightly from that of last month, while the one in foreign currency surged as it went from an annual growth rate of 0.4% to one of 1.9%.

Broken down by market, the portfolio of loans granted to households had an annual growth of 13.2% in February, which is slightly lower than the growth the previous month (13.5%). This was due to the performance of consumer loans, which moderated between January and February (from 12.1% to 11.6%). Loans for housing, in turn, rose as they went from growing at a rate of 15.6% to 16.1% during the same period. Regarding the commercial loan portfolio, the annual growth rate in February (12.0%) was higher than the rate for the previous month (11.5%). This was due to the upsurge in the national currency component (from 12.9% in January to 13.3% in February) and in the foreign currency component (from -0.04% to 1.7%).

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: -209 bp for mortgages, -199 bp for consumer loans, and -215 bp for construction loans.

The size of the decline in the real interest rates has been lower due to the effect of the lower inflation rate. There have been reductions during this same period of: -182 bp for mortgage loans, -171 bp for consumer loans, and -188 bp for construction loans.

The levels of real interest rates for consumer loans, mortgages, preferential loans, ordinary commercial ones and commercial lines of credit as well as 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

The latest information shows that the recovery in the Euro zone has continued at a modest pace as expected. In February, the activity indicators in the manufacturing and service sectors showed they were still growing.

Meanwhile, the confidence of businessmen and consumers remained at favorable levels although there was a slight deterioration in the latter case.

In the United States during the first two months of the year, some indicators showed evidence of lower than expected performance. This was the case of retail sales which had dropped in monthly terms and when compared annually, they showed a slow down. The former could be partly the result of the severe winter that country is experiencing. In contrast, industry expanded in February and the job market continued to show signs of improvement as the hiring rate rose with respect to what has been seen in the last few months.

For the emerging economies, the information available indicates a slowdown in various ones. In China, the indicators for retail sales, industry, investment in fixed assets, and international trade showed a performance that was below what the market expected. Even if these figures were affected by the festivals marking the Chinese New Year, the trend is in the direction of a moderation in their economic growth.

Something similar is occurring in Latin America where the latest figures on economic activity also show a greater than expected deterioration in the region's growth. In Chile, the index of monthly economic activity showed that it had been slowing down for several full months as of January while, in Brazil, industry contracted again in annual terms. Furthermore, exports for the region remained weak and consumer confidence in several countries declined.

With respect to international prices for commodities exported by Colombia, the prices for petroleum referenced to the Brent index remained close to 108 dollars per barrel in February, a level that is higher than was anticipated (105 dollars/barrel on average). The price for coal fell slightly while that for nickel showed a slight rise. The droughts in Brazil have fueled coffee prices again and these are well above what had been forecast. In the case of imported food, recoveries in the prices for soybeans, corn, and wheat have been seen in the last few weeks.

Inflation in the main developed economies, in turn, remained at a relatively low level. In February, in particular, the change in the general level of prices in the Euro zone continued to decline and has been below 1% for several full months now. In the United States, the indicators showed stability. In the emerging economies, inflation started to climb again in several Latin American countries and this could be associated with the depreciation of their currencies. In contrast, there was a slight slowdown in Asia.

In terms of monetary policy, the central banks in the major advanced economies, excluding the United States, continued their stimulus policies and did not announce any new measures. In the case of the Fed, the decision was made to continue cutting back on their asset purchases by an additional ten billion dollars in their March meeting. In addition, they announced that it would be appropriate to maintain the stimulus policy given the current economic conditions. Likewise, the Fed ruled out a fixed target for the unemployment rate and conditioned their policy to a broader range of indicators for the labor market, inflation, and the financial markets. In the opinion of many analysts, the likelihood of earlier increases in the rates has risen.

Among the emerging economies, some countries such as Chile, Hungary, and Romania reduced their benchmark rates as a reaction to the slowdown in their productive activity indicators. Other countries that face higher inflationary pressures, such as Brazil and India, increased their rates.

Finally, so far this year, the measures of country risk and the exchange rate have remained at levels above the averages registered in 2013. If the monetary policy conditions in the United States are normalized and this is confirmed, it is likely that the exchange and the risk rate levels will remain stable or rise slightly. However, the recent announcement by JP Morgan with respect to the increase in the share of TES in its benchmark portfolio for emerging markets (in local currencies) may significantly offset these effects.

2. DISCUSSION AND POLICY OPTIONS

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

(i) The recent data on economic activity from various parts of the world suggest that the growth recovery will continue in 2014 but at a slightly slower pace in comparison to previous predictions. The recovery in the Euro zone has continued at a modest rate while, at the same time, the slowdown in some emerging economies has accentuated.

(ii) Foreign interest rates and the price of the dollar are surpassing the averages seen in 2013. It is probable that a significant part of those rises will be permanent to the extent that they are due to less expansionary levels of global liquidity. The recent decision by the Federal Reserve and forecasts made by its members for the benchmark interest rate reaffirm this trend.

(iii) The increased weight Colombian public debt securities have in the benchmark portfolios of some international investors could offset to some degree the effects that the adjustment in global liquidity has on the exchange rate and market interest rates in Colombia.

(iv) In the fourth quarter of 2013, the annual growth of output was 4.9%. For the entire year it was 4.3% which is above the revised rate of 4% for 2012. Growth surged in the second half of the year driven especially by investment. Household consumption remained at growth rates that are close to their historical average over the course of the year while public consumption grew more than the output every quarter. With respect to supply, the sectors with the highest growth for the quarter were in mining, agriculture, construction, and personal and social services. Industry showed a poor performance. Similar trends were seen for the entire year.

(v) Recent information on the growth of retail sales, coffee production, energy consumption, and the continued decline of unemployment suggests a strongly dynamic economy over the course of the year. Nevertheless, the drop off in consumer confidence in February as well as the weakness in exports and in manufacturing point in the opposite direction. For 2014, the Bank's technical team still forecasts that economic growth will be between 3.3% and 5.3% with 4.3% as the most probable figure.

(vi) In February, the growth of credit as a whole stabilized at rates that were higher than the rise in the nominal GDP. The growth of consumer loans has moderated, but mortgage loans have surged. The real interest rates for loans remain at levels that drive economic growth.

(vii) Annual inflation rose in February for the third consecutive month and was at 2.32% which is within the target range. The average for the measures of core inflation also continued to rise and came to 2.63%. The inflation expectations of economic analysts for a year from now as well as those derived from public debt paper with maturities of less than five years remain at around 3%. To summarize, economic growth surged in the second half of 2013 and inflation continued rising in February. Interest rates remain at levels that stimulate aggregate expenditure, and they are expected to contribute to making output approach the economy's productive capacity and inflation converge with the goal of 3% in 2014.

The members of the Board of Directors emphasized the strength of domestic demand with respect to both consumption and investment that was seen in the second half of 2013 and beginning of this year. Inflation has also risen as expected. The above could indicate that the output gap and the current deviation of observed inflation from the target (inflation gap) will continue closing over the course of 2014.

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 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-march-2014