Minutes of the Banco de la República Board of Director's meeting on June 20, 2014

Detailed Explanation of the Macroeconomic Situation Must reads Banco de la República Raises the Benchmark Interest Rate by 25 Basis Points and Expands Its Foreign Currency Buying Program 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 June 20, 2014. In attendance were Mr. Mauricio Cárdenas Santamaría, Minister of Finance and Public Credit, Mr. José Darío Uribe Escobar, 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.

A synthesis is presented below of the view held by the Banco de la República's technical team with respect to the macroeconomic situation (section 1) and, afterwards, the main discussion points regarding policy considered by the Board of Directors are summed up (section 2).

A more detailed explanation of the macroeconomic situation written by the technical team at the Banco de la República is presented in the data section of the May 2014 Inflation Report and in the statistics appendix.

1. MACROECONOMIC CONTEXT
With respect to the macroeconomic context, the technical team would like to draw attention to the following points:

i.The information available indicates that the main developed countries continue to expand at a moderate rate. In the case of the United States, the recovery in manufacturing, retail sales, creation of employment, and consumer confidence seem to suggest a recovery of economic activity in comparison to the first quarter based on the indicators as of May. In spite of that, the World Bank and some analysts recently lowered their growth predictions for this economy for 2014. With respect to the economy in the euro zone, this has continued to grow at a modest pace in spite of the improvement in consumer and producer confidence. The growth of the emerging economies in Asia has stabilized while, with the exception of Colombia, a slowdown has predominated in several countries in Latin America.

ii. The performance of commodity prices has been mixed. The price for petroleum remains above what was forecast by the technical team at the Bank for 2014 and, in the last few weeks, it has rallied due to geopolitical factors. The price for coal remained stable and that for nickel has shown an upward trend so far this year in spite of a drop in the last four weeks. The price for coffee showed a decline. In the case of prices for imported food such as wheat and corn, decreases were seen in the last few weeks.

iii. In the euro zone, the risk of deflation persists. This has led the European Central Bank to announce new monetary stimulus measures. In Japan and the United States inflation has risen recently just as it has in several economies in Latin America. In Asia, there is stability.

iv. The global financial markets have shown a favorable performance in the last few weeks. The indices of stock market activity appreciated and the perception of risk declined. In Latin America, the risk premiums continued dropping while the exchange rates for the main currencies with respect to the dollar have shown different reactions. In the cases of Chile and Peru, there has been a certain amount of stability which contrasts with the

ups and downs that have been seen in Brazil and the downward trend in Colombia. In the latter case, this is the result of the inflow of capital related to the changes in the JP Morgan benchmark portfolios. Nevertheless, the signs of a better economic performance in the US and its effect on the expectations of an adjustment in the policy interest rates in that country make the future trend of the exchange rates in the region particularly uncertain.

v. In April, the value of Colombian exports in dollars declined in comparison to the same month last year. This was due to the general fall in the main items (mining and industrial products and the top agricultural goods). In the cumulative January-April period foreign sales of mining products were lower because of the lower prices while sales of agricultural products grew. For non-traditional exports, the contraction was largely the result of decreases registered in foreign sales of vehicles and of agricultural products other than coffee, bananas, and flowers.

vi. The annual growth of the GDP for the first quarter of 2014 was 6.4% and the growth for 2013 was revised upwards. In the area of supply, the positive strength of all branches of activity is noteworthy, especially the construction, social services, agricultural, and financial sectors. It should be noted that industry registered a growth of 3.3% after two years of negative rates.

vii. Although the GDP figures with respect to demand have not been published yet, the information available suggests that the surge in economic activity was due to the strength of domestic demand and due especially to the investment component (as shown by the growth of the construction sector and the data on imports of capital goods for industry and agriculture).

viii. For the second quarter, the indicators for sales and consumer confidence indicate that household consumption is remaining strong. Specifically, the figures for vehicle sales published by Fenalco and Econometria suggest that the consumption of durable consumer goods will have registered a favorable performance in the second quarter.

ix. The above is consistent with the behavior of the consumer loan portfolio in May which stopped slowing down and registered a slight rise in its growth rate. The labor market indicators, in turn, continue to suggest that there are improvements to labor conditions. The growth of employment has stayed at acceptable rates in the last few months and is mainly concentrated in wage-earning jobs.

x. To the above add the fact that the real interest rates are dropping for households as well as for commercial loans and both are below the average they have had since 2000 as a result of the rise in inflation and its effect on expectations. This could be a factor that might explain the rally that has been seen in the growth of the commercial and consumer loan portfolios. The positive trend for the mortgage portfolio has likewise been improving.

xi. In May, annual consumer inflation continued the upward trend it has been on since the beginning of the year. This upswing is mainly due to the behavior of food prices. So far this year, food has also been the item that has contributed the most to the increase in inflation.

xii. Two aspects of the recent performance of the variation in consumer prices should be noted: i) The CPI excluding food was the only indicator of core inflation that declined, and ii) the indicators of expectations are showing rises and some are beginning to surpass the midpoint of the target range.

xiii. The state of the economy as described by the growth data in the first quarter, the positive indicators for the second quarter that are known, and the possible upward revision of the forecast of the GDP for the full year that this could mean suggest that demand is growing at a pace that is higher than the potential GDP. The above combined with the record of some expectations of rising inflation increases the probability that inflationary

pressure may be spreading throughout the entire economy.

xiv. To summarize, it can be stated that the most recent data show an economy and inflation that are growing more rapidly than predicted as a result of which expectations have been pressured upwards. The real interest rate is still remaining at a low level (compared to its average since 2000) and could continue stimulating domestic demand.

2. DISCUSSION AND POLICY OPTIONS

The Board of Directors agreed that the economy grew more strongly than expected in the first quarter of the year and better than what had been considered in the models produced by the Bank's technical team. Furthermore, apart from the different opinions about the growth of the potential GDP, the gap is closing at a more accelerated pace than had been previously forecast or even, in the opinion of some members, has closed.

Regarding inflation, the members of the Board agreed that in spite of the fact that expectations had risen recently, they are still anchored to the target. They also agreed that a large part of the increase in the annual change in consumer prices was due to the expected reversal for some perishable foods as well as in the reduction of the increases in prices for some regulated goods and services. Several members of the Board stated that inflationary pressure could be emerging from the upsurge in demand. Another added that, in the recent past, the changes in the inflation rate have been fundamentally determined by the performance of food prices, especially for perishables, and that said performance, in turn, has been the result of climatic factors, i.e., the result of supply shocks instead of an excess of demand.

The Board indicated that a gradual adjustment in the benchmark interest rate was justified considering the following aspects: (i) the volatility and uncertainty of the data on public investment which has been the main unexpected outcome with respect to growth, (ii) the weakening of international trade, and (iii) the impacts of the monetary policy of the United States.

The members of the Board of Directors decided that, in the abovementioned context, it is necessary to continue the process of normalizing the monetary policy and closely monitoring the reaction of the financial system balances.

3. POLICY DECISION

The Board of Directors decided unanimously that it would be appropriate to raise the benchmark interest rate by 25 bp and set it at 4%.

Fuente: https://www.banrep.gov.co/en/news/board-directors/minutes-june-2014