

The determinants of liquidity in Colombia: an analysis of the spot FX market

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Publication Date: Wednesday, 22 of December 2021 **Abstract**

The objective of this paper is to study the evolution of liquidity in the spot foreign exchange market in Colombia and its main determinants from 2006 and 2020. First, we analyze different dimensions of liquidity such as transaction costs and resilience. We achieve our objective by measuring liquidity through different types of indicators using intraday data from the centralized interbank foreign exchange electronic market service. Second, we study the main determinants of liquidity considering supply-side, demand-side, and market conditions factors. The event study analysis evidence that transaction costs were higher during the recent crisis caused by the COVID-19, while the price impact of transactions in the FX market was higher during the 2008-2009 financial crisis. The empirical results highlight that local monetary conditions, Colombian peso volatility, the volatility of the Colombian debt market, foreign funding constraints, U.S. financial conditions and global risk perception are the main determinants of liquidity in the Colombian spot foreign exchange market.