Minutes for the Meeting of the Board of Directors of Banco de la República on 17 December 2021

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The Board of Directors of *Banco de la República* raised the policy rate by 50 basis points (bp) thus putting it at 3.0% in a 4-3 majority decision at its December 17 session. Three members voted for a 75 bp increase.

The decision took the following aspects into account:

Annual inflation in November increased 68 bp with respect to what was registered in October, reaching 5.26%. This increase was above the expectations of the technical staff and the market. Annual core inflation (excluding food and regulated items) also showed an upward trend as it stood at 2.54%, 52 bp above the October figure. While the main upward pressure came from the increase in food prices, other CPI groups also registered increases. As a result, the inflation forecast was revised to 5.3% for 2021 and 3.7% for 2022.

GDP continued to grow strongly in the fourth quarter, as shown by leading indicators such as energy consumption, mobility, banking transactions, and air and land transportation. Industrial, commercial, and consumer confidence indicators also remain at favorable levels. Economic activity is still driven by domestic demand, particularly by private and public consumption. Taking this into consideration, the technical staff ratified its 9.8% GDP growth projection for 2021, which would place economic output at levels higher than before the pandemic.

The current account deficit is likely to reach 5.6% of the GDP in 2021, two percentage points higher than in 2020. The widening of this imbalance is partly due to the impact of domestic demand on imports, which has only been partially offset by the rebound in exports. In addition, the net factor income imbalance has increased, thus reflecting an improvement in the profits of companies with foreign capital. These are higher due to the improved pace of economic activity. For 2022, the current account deficit is expected to drop to 4.9% of GDP. The external imbalance has been financed with greater foreign direct investment resources and public sector capital flows in an international financial context that is beginning to become tighter with widespread increases in interest rates in emerging economies and the expected tightening of monetary policy in the United States.

Inflation expectations, both those obtained from surveys and those inferred from the difference between fixed and indexed yields on public debt instruments, have been rising and are currently above the 3.0% target even for the medium term. This increases the risk of inducing indexation processes at higher inflation levels.

All the Board Members agreed that the increases in inflation and inflation expectations and the high rate of economic activity, which has been reducing spare capacity, warranted the continued withdrawal of monetary stimulus. In this context, four members of the Board voted for a 50 bp and three for a 75 bp increase in the policy rate.

The Board members who voted for the 50 bp increase believed that while these factors justify the continued withdrawal of monetary stimulus, they did not think it would be advisable to fast-track an interest rate adjustment. In support of this, they expressed doubts about the sustainability of the pace at which domestic demand is picking up due to the reduction in household savings, the sluggishness of investment, the employment recovery lag, and the limits to consumption of durable and semi-durable goods. They also underlined the fact that economic recovery has not been uniform, as shown by investment items that have been slow to recover and

are still at considerably lower levels than in the pre-pandemic period. Finally, they believe it is advisable to, as far as possible, gradually increase interest rates in order to avoid the financial tensions that sharp and sudden changes could cause in the markets.

The group that advocated a 75 bp increase stated that the surge in inflation and the increase in inflation expectations were of concern not only because of the level they had reached, but also because the factors that generated them were beginning to take on a structural nature given the inability of supply to meet the needs of the market's increased demand. They added that the recent raise in the minimum wage well over the usual practice of basing it on actual inflation and productivity gains creates a perception in public opinion that nominal increases well-above the inflation target are normal. This could contribute to de-anchoring inflation expectations and make *Banco de la República's* task of controlling inflation more demanding. This, together with the notable increase in the different current and expected inflation indicators since the previous Board meeting, makes it advisable for this group to quicken the pace of monetary policy tightening.

Finally, the Board of Directors as a whole reiterated its commitment to the 3.0% annual inflation target and reaffirmed that it will continue to adopt the decisions required to ensure the convergence of inflation towards this target.

Fuente: https://www.banrep.gov.co/en/minutes-meeting-board-directors-banco-republica-17-december-2021