PUBLIC VERSION

Working Papers from the Board of Directors
Banco de la República

Monetary Policy Report

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Board of Directors

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Monetary Policy Report

Economic Studies Division

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I. External Context and Balance of Payments

1. The international prices of oil recovered slightly in the last few weeks, after the fall that had been observed until March. In part, this is a consequence of the suggestion made by the main international specialized agencies that production in the United States would reduce in the next months, together with the most recent geopolitical events in the Middle East.

2. The international prices of some commodities have been lower on the average so far in April than the records for March. Thus, the prices of coal, nickel and some foodstuffs imported by Colombia have ranked below the levels of the prior month. In contrast, international prices of coffee and copper have shown a slight recovery in the last few weeks.

3. The figures of real activity in the United States to March suggest that their economic growth during the first quarter of the year would have been weaker than expected. This would have been affected by temporary supply (a very strong winter and strikes in ports on the Western Coast), by the appreciation of the US dollar, and by the fall of investment in the oil sector. Nevertheless, household confidence indicators remain at high levels, and suggest that the economy would take up its dynamism in the next months.

4. The data of the labor market for March show that employment creation was lower than expected. Despite this, the unemployment rate remained at 5.5% and the improvements of other indicators followed by the Federal Reserve continued, such as underemployment and long-term unemployment rates.

5. Annual inflation in the United States to March registered negatively (-0.1%), mainly due to the strong fall in the price of fuels. Meanwhile, inflation excluding energy and foodstuffs passed from 1.7% to 1.8% in February and March.

6. Given this evolution of the real activity and of prices, the forecasts by the members of the Federal Open Market Committee (FOMC) of the Federal Reserve (FED) suggest that the increase in the interest rate would be more gradual than had been announced in the previous quarter.

7. In the euro zone, the indicators of real activity in the first months of 2015 suggest a recovery of the economy. Thus, the data of retail sales to March and those of business and consumer confidence presented a positive trend, while the figures to February for exports and credit show recovery.

8. Regarding the prices in the zone in March, deflation remained: the annual mark was of -0.1%, mainly as a consequence of the lower prices of fuels. In turn, the annual change of the consumer price index (CPI) excluding foodstuffs and fuels increased marginally to 0.7%. In this context, the European Central Bank (ECB) continued with the financial assets purchase program.

9. On the other hand, the data for the first quarter in China show that the slowdown of this economy continued. Its gross domestic product (GDP) grew 7.0% in annual terms, which represents a moderation *vis-à-vis* 7.3% three months behind. Meanwhile, annual expansion of industrial production and of retail sales registered at the lowest levels since 2008, while investment in fixed assets clearly maintained a decreasing trend. On the other hand, the real estate market continues with a slowdown trend. In this context, the Central Bank reduced the rate of deposit for commercial banks in 100 basic points (bp).

10. In Latin America, the data of the economic activity index to February show that the growth of Chile, Mexico and Peru would have continued weak in the first quarter of the year, while in Brazil the contraction that started the year before would have continued.

11. Inflation in some emerging economies continued showing a heterogeneous panorama, although decreasing trends prevail. In most of the Asian countries inflation has registered low levels in recent months. The case of China stands out, where inflation remained low (1.4%). In turn, in Latin America, annual inflation of Chile has reduced slowly, while inflation in Peru and Mexico has remained relatively stable. In contrast, the annual variation of prices in Brazil displays a strong, growing trend.

12. As for the international financial markets, the rates for long-term bonds in the main countries of the euro zone continued lowering in the last few weeks, thanks to the sovereign bond purchase program by the ECB at the beginning of March. In turn, the rates for the US long-term bonds reduced and the US dollar depreciated *vis-à-vis* the main currencies of the world, as a result of the changes in the FED's forecasts.

13. In Latin America, the risk premia lowered in the last few weeks, although they remain at relatively high levels. In turn, the currencies of the region have reversed part of the strong depreciation observed at the beginning of the year. In the Colombian case, the average value so far in April is COP 2,521 per dollar, which represents an appreciation of 2.7% *vis-à-vis* the average of March.

a. Exports and imports

14. In February, the total exports in US dollars recorded an annual fall of 26.8%, explained mainly by a fall in prices. The only area that presented growth was that of agricultural goods (6.0%), while those of mining and other exports fell 38.6% and 4.0%, respectively. In the first case, coffee explains the growth due to its 23% increase. The fall in mining goods is associated to a great extent with the lower sales of oil (-40.4%) and of products derived of oil refining (-69.2%).

15. Regarding other exports (-4.0%) the most significant falls within the group are those of paper (-34.3%), meat (-52.5%), and machinery and equipment (-13.7%). Mainly, the first two showed falls in their sales towards Venezuela: in the case of paper, the fall was of 63.6%, while on the side of meat, no exports were registered in February. In turn, machinery and equipment fell 50.5% towards Ecuador, this being the destination of greater contribution to the abatement.

16. In the first two-month period of the year total exports fell 33.8%. This is the result of the falls in mining goods exports (-46.7%) and those of other products (-10.7%). Exports of agricultural goods grew 22.5% in said period.

17. In January, CIF imports in US dollars grew 0.8% in annual terms, as a product of the increase in the purchase of capital goods (21.3%), which compensates the falls registered in intermediate goods (-10.7%) and consumer goods (-6.6%).

18. The increase in the imports of capital goods was due to the increase in the area of transportation equipment (150%), which is explained by the 332% increase in transportation equipment, particularly planes. Excluding this, the imports of capital goods would have fallen 22.3%, and the total imports would have fallen 13.7%. Contraction in intermediate goods concentrated mainly in fuels and lubricants (-30.9%), with the purchase of fuels falling 31.0%. Imports of consumer goods fell due to the reduction of 13.9% in durable goods.

19. In February, total CIF imports fell 8.3% with regard to the same month of the previous year. This fall was due to the 25.8% fall in commodities and intermediate products, which was explained, to a greater extent, by the contraction of 71.4% in the imports of fuels and lubricants. In turn, capital and consumption goods grew 6.6% and 8.8%, respectively. In the first case, the main contribution was the 5.7%

increase in capital goods for the industry. On the side of consumer goods, increases were recorded in non-durable (10.9%) as well as in durable goods (6.7%).

20. So far this year, total imports accumulate a fall of 3.8%, due to the lower external purchases of intermediate goods (-18.4%). Within this area, the greatest contribution to such contraction occurred in fuels and lubricants (-53.3%), followed by the one registered in commodities for the industry (-1.7%). The purchases of capital goods increased 13.9%, and those of consumption grew 1.3%. The increase in capital goods can be explained by the 63.9% increase in transportation equipment and that of 4.1% in building materials. Finally, within consumer goods, there was a 3.2% fall in durables, which was compensated by the 6.2% increase in non-durable goods.

1. Projections of External Variables

a. External Growth Scenarios
Baseline or most probable scenario (Chart 1)

21. In the case of the United States, growth forecasts for 2015 were revised downward as a result of the low dynamism observed during the first quarter. Nevertheless, for the remainder of the year and for 2016 it is expected that the fundamentals of consumption remain in favorable conditions, with which household expenditure would consolidate as the main growth engine of the economic activity. Additionally, the positive impact of the fall in oil prices on consumption would be greater that the adverse effect that this shock would have on investment.

22. Exports as well as revenue of multinationals, would be affected by the strength of the US dollar *vis-à-vis* the main currencies and by the lower growth of their trading partners.

23. Fiscal discussions regarding the debt ceiling and the presidential elections in 2016 would not have a significant effect on the confidence of agents and on government expense.

24. The data for employment creation would be consistent with the good behavior expected of the economy, and hence the labor market would continue recovering. Thus, the existing excess capacity would continue being eliminated, and some upward pressures on salaries would start to appear.

25. During 2015, the inflationary pressures would be contained by the lower prices of commodities, especially oil, and by the greater strength of the US dollar. In 2016,

inflation would show a growing trend and would converge towards the long-term goal of the FED.

26. The FED would increase its benchmark rate towards the end of the third quarter, and would continue raising it very gradually during all of 2016. It is expected that this measure be transmitted correctly to market rates.

27. In the euro zone, the recovery of the economy would be stronger than it was expected in the previous quarter. The measures adopted by the ECB have allowed for the recovery of confidence, and have re-established, to a certain extent, the credit channel, which would favor private consumption and investment. Additionally, the weakening of the euro would continue propelling exports outside the European Union.

28. The reforms adopted in some peripheral countries would allow them to continue with their economic recovery. Additionally, it is expected that Germany will continue expanding at a favorable pace. Finally, the economies of France and Italy would show some improvement thanks to some more flexible conditions of the austerity plan, although they would continue facing competitiveness problems.

29. The situation of Greece would continue being a significant source of uncertainty for the region. Nevertheless, it has not been considered that this country leave the euro zone. Additionally, it is expected that the geopolitical conflict in East Europe would not affect financial markets and confidence.

30. In the case of China, growth would continue moderating as long as fixed-asset investment and the expansion of credit continue reducing from the high levels observed in prior years. Additionally, exports would provide a lower thrust to growth, given that the yuan has strengthened *vis-à-vis* the majority of world currencies, and that global demand remains weak. Nevertheless, the stimuli measures issued by the government and the Central Bank would allow for the slowdown to be less marked.

31. In Latin America, a heterogeneous behavior is expected among countries. On the one hand, Peru and Chile would exhibit some recovery as a result of the lower price of oil, of the stimulus by the public sector, and the reversion of some supply shocks. Similarly, Mexico would be favored by the greater dynamics of the US economy. In contrast, Brazil's economy would contract in 2015 as a result of the fiscal consolidation that would take place in this country and of the low levels of business and consumer confidence. In 2016, there would be some recovery.

Meanwhile, Venezuela's contraction would continue due to its structural problems, which have become more intense with the low international oil prices.

Risks to the Baseline Scenario (Table 1)

32. The financial markets could react in a disorderly manner to the monetary policy adjustments in the United States. In addition to the adverse effects on these markets, confidence worldwide could be affected negatively.

33. Greece would exit from the euro zone, which would result in a significant increase in financing costs for this economy, and contagion to other economies in the region.

34. A stronger slowdown could be observed in China and other emerging economies, which would happen mainly due to problems associated to their financial stability. In the case of Latin American economies, the reduction of international prices could affect their economic activity to a greater extent.

35. There would be a deflationary spiral in the euro zone or in Japan which would significantly affect growth in these economies.

36. An event that could compensate some of these biases would be that the government and the Central Bank of China would adopt far-reaching plans to stimulate the expansion of real activity, which would maintain growth rates for credit, investment and residential construction high.

Table 1

Economic growth forecasts for Colombia's major trading partners

Country or region	2015			2016		
	Low	Baseline	High	Low	Baseline	High
USA	2.2	2.8	3.4	2.0	2.8	3.6
Euro Zone	0.8	1.3	1.8	0.8	1.5	2.0
China	6.4	6.8	7.2	6.0	6.5	7.0
Brazil	-1.2	-0.6	-0.2	0.3	1.0	1.5
Ecuador	0.2	1.5	2.2	1.0	2.0	3.0
Venezu	-7.0	-5.0	-3.0	-2.0	0.0	2.0

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Peru	3.0	4.0	4.7	3.0	4.5	5.5
Mexico	2.0	3.0	3.5	2.5	3.5	4.0
Chile	2.5	3.0	3.5	2.5	3.5	4.5

b. Projection of the Balance of Payments

37. During 2014, the current account deficit was USD 19,780 m (5.2% of GDP), expanding with respect to that observed in 2013 USD 12,330 m (3.2% of GDP). The deterioration in the external balance of the country was the result of the sharp decline in the price of oil, the supply shocks for coal and refined oil products, and the dynamism of imports. Thus, the total exports in dollars fell 5.5% on a yearly basis in 2014, while total imports in US dollars registered an 8.0% growth.

38. Consistent with such expansion in the current account deficit, capital flows for 2014 were significantly higher than those recorded a year ago (USD 23,949 m in 2014 against USD18,782 m a year ago). This was associated particularly with the largest portfolio investment flows (USD 11,631 m) registered during the year both in the local public debt market (thanks to the re-balancing of the JP Morgan indexes) as well as the placement of bonds on international markets by the public sector. Similarly, in 2014, greater resources from higher net direct investment (USD 12,155 m) were registered. This resulted from foreign direct investment (FDI) at levels similar to those observed in 2013, and a reduction in investment flows by Colombians abroad. This was partially offset by lower resources from other investments (loans and deposits).

39. A slight expansion of the current account deficit as a share of GDP is expected for 2015 to 5.3% resulting from a reduction of -17,038 m US dollars, offset by a valuation effect of GDP in US dollars of 0.9 percentage points, given the average depreciation estimated for the year. This forecast incorporates the effect of the fall in oil prices in different external balance accounts. It is estimated that the goods trade deficit would expand with a strong contraction of the main mining and agricultural exports, partially offset by a moderate recovery of other exports and the reduction of imports; a reduction of the service trade deficit is projected, as well as a reduction in net outflows from primary income, associated to lower remittances of profits from the mining and energy sectors and the effect of the depreciation of the peso on other sectors' profit.

40. Performance of external sales would be affected by the lower price expected for oil (USD 55/b Brent) and coal, which would be partially offset with better prospects

for the agricultural products and the recovery of part of the exports of oil products with the beginning of operations of Reficar by the end of the year.

41. Moderate growth, around 2.0%, is estimated for the remaining exports, driven mainly by the effect of depreciation of the peso, despite the slowdown in external demand by the country's trading partners.

42. As for commodities, it should be noted that estimated expansions in export volumes for most products are consistent with growth projections of their production (oil, 3.2%; coal, 7.5%; and coffee, 5.0%).

43. Thus, in the central scenario, exports of the main products (in dollars) would fall by 34%, while the total would contract by 24%. On its part, imports in dollars would contract versus the data observed for 2014 (-15.5% on a yearly basis), a behavior associated to a sharp drop in imports of capital goods for the mining-energy industry, a less dynamic domestic demand, and the generalized reduction of international prices on imported goods, especially those of intermediate goods (fuels and derived goods).

44. Regarding financing of the deficit, it is expected that capital flows in dollars be lower than those observed in 2014, affected by lower resources of FDI and the lower foreign portfolio investment flows. This would be partially offset by greater resources from other investment (loans and deposits), and by the end of the international reserves purchase program by the Central Bank, which in 2014 recorded USD 4,058 m.

45. Net foreign direct investment is projected to be lower than in the previous year (USD 11,226 m in 2015, as compared to USD 12,155 m in 2014), especially as a result of lower flows towards the oil and mining sectors (particularly, a 25% fall in oil investment is assumed). Similarly, a moderation of the flows to other sectors is expected, which is explained by the estimated slowdown of domestic demand and a lower valuation in dollars of resources from the reinvestment of profit in some sectors due to the projected depreciation.

46. On the other hand, a lower net financing with resources from portfolio investment (USD 4,064 m) is expected, as compared to the previous year (11,631 m), given the reduced flow of foreign capital into the local public debt market and a lower placement of bonds in the international markets by the non-financial public sector.

II. Growth, Domestic Demand, and Credit

47. The information available for the first quarter of 2015 suggests that the Colombian economy's pace of expansion would have slowed down compared to the data towards the end of last year. Lower growth of private consumption is expected, particularly that of durable goods. Investment would also exhibit a mediocre performance. Lower domestic demand and the depreciation of the nominal exchange rate would restrain the dynamism of imports, in contrast with the better performance expected for exports.

48. According to the latest publication of the *Encuesta mensual de comercio al por menor (Monthly survey of retail trade*) by DANE (National Bureau of Statistics), retail sales expanded 4.8% in February, compared to the same month in 2014. For the January-February two-month period, retail sales growth was 6.2% on an annual basis, a figure lower than for the fourth quarter of 2014 (11.1%). Excepting vehicle sales, the increase in the indicator was 8.5% and 9.3% on a yearly basis for February and the first two months, respectively.

49. In the case of vehicle sales, an 11.3% fall was recorded during February (-8.7% for the two-month period). On its part, according to the data on car sales published by ANDI, *Fenalco* and *Econometría* to March, the fall in this segment of the market was 7.1% during the first quarter. This allows to forecast a poor performance of the consumption of durable goods during this period.

50. Additionally, the results of the *Encuesta mensual de expectativas económicas (Monthly Survey of Economic Expectations*, EMEE) by Banco de la República, allow to forecast that household consumption would have expanded at a slower pace than what had been observed during the fourth quarter last year: in February, the balance of sales expectations fell importantly for a second, consecutive month.

51. In turn, the consumer confidence index published by Fedesarrollo showed an important monthly setback in March, which placed the series significantly below its average since 2001 and at levels comparable to those recorded in mid-2009. Within the components of this index, the greater deterioration was observed in consumer expectations.

52. Also, in March, annual growth of consumer credit to households in nominal terms (13.1%) was slightly lower than the one observed in December (13.4%). In spite of the aforesaid, household real interest rates remain stable.

53. The recent performance of the labor market indicators have been good, and it is still not possible to forecast moderation in the future pace of household expenditure by this channel. To February, the unemployment rate continued its decline, explained

mainly by the growth of salaried and formal employment. However, in order to identify the emergence of possible inflationary pressures from the labor market in a timely manner, wage adjustments, NAIRU estimates, and unemployment forecasts must be carefully monitored.

54. With respect to gross capital formation, the balance of investment expectations by the EMEE to February also suggests a slowdown in the pace of expansion of that item (without construction of buildings and civil works). Additionally, the data for capital goods imports in US dollars (other than aircraft) also showed setbacks.

55. In the field of foreign trade, the numbers observed for exports until the month of February suggest that during the first quarter of 2015 this item could register an annual increase in real terms, driven by growth in the sales of oil, coal, and coffee, primarily. Besides, in the first two months of the year, exports of other products have grown (1.1% in volumes).

56. Finally, the records of imports observed in February suggest that this item of the GDP would have fallen in real terms during the first quarter, as was expected one quarter before.

57. On the supply side, the indicators available for the first quarter of 2015 exhibit uneven behaviors. Figures relating to sectors such as industry and the slaughter of cattle show a weak performance with respect to what was observed in the last quarter of 2014, while some indicators associated with branches of activity such as construction, mining, energy demand, and coffee reported some important accelerations.

58. Industry exhibited a contraction of 1.3% in February, explained mainly by the fall of oil refining (-17.6%), whose participation is high (18.6%). This result is ranked below the expectations of the SGEE. So far this year, total industry has fallen 2.9%. It should be noted that the figure for January was revised downward (from -2.5% to -4.4%). Excluding oil refining, the industry would have grown 2.4% in February and -0.7% so far this year. Additionally, disparities among sectors remain: beverage industries (7.9%), meat and fish processing and preservation (14.7%), and manufacture of chemicals and basic chemicals products (11.1%) exhibited significant growth, contrary to the branches of coking, oil refining, and fuel mixing (-17.6%) and textile spinning, weaving and finishing, and others (-11.5%).

59. According to a survey by *Fedesarrollo* to February, although the indicator for orders and that of inventories (countercyclical to production) improved as compared to the previous month, the trend components of each one of them point to

a deterioration of the industry. Production expectations to three months showed a significant recovery in levels as compared to the previous month. However, the trend component continues to suggest a weak behavior.

60. On its part, cattle slaughter continues to exhibit contraction in February of around -5.4%. The trend component also reported significant deterioration, indicating that such behavior could last for the rest of the year. It should be noted that uncertainty about the cattle retention cycle is high, given that changes in trade patterns with Venezuela and other shocks affect its duration.

61. In contrast, other indicators had a good behavior in the first months of 2015: construction stands out due to its acceleration of production and cement shippings, which grew 13.3% and 6.1%, respectively, in February of this year. In the January-February period, these indicators expanded 10.8% and 10.3%, then 6.0% and 6.8% during the fourth quarter of 2014.

62. In March, oil production was 1,021,000 barrels per day, with which the first quarter closed with an average production of 1,027,000. In terms of annual expansions, March saw a 4.5% increase, and 3.0% during the first quarter of 2015. It should be noted that the results observed to date are above the average production of the central growth scenario and balance of payments (1,020,000 barrels per day).

63. According to the *Federación Nacional de Cafeteros* (National Federation of Coffee Growers), coffee production reached 2,917,000 bags during the first quarter of 2015, expanding 7.9%. On its part, in March total energy demand reported an annual variation of 4.1%, while the regulated component did so by 4.7%, and the unregulated component by 2.2%. The trend component reflects a positive slope.

III. Behavior of Inflation and Prices

64. Once more, annual consumer inflation accelerated in March, completing six months of consecutive increases, closing at 4.56% and surpassing the register for February by 20 pb (**Table 4**). On its part, the monthly variation stood at 0.59%, higher than the level expected by the market (0.51%) and by the SGEE (0.53%). As has been happening over the last few months, the increase in inflation is associated with higher food prices and secondly, by the widespread increase in the CPI for tradable items.

65. So far this year, accumulated inflation has been 2.4%, compared to 1.52% during the same period the year before. The acceleration of inflation between December

last year (3.66%) and March 2015 (4.56%) is explained in 84.3% by the increase in food prices, especially processed foods. Prices of tradable goods excepting food and regulated goods explain this acceleration in 37.3%, while the non-tradable excepting food and regulated goods only contributed 6.3%. The segment of regulated goods was the only one that contributed negatively (-27,9%) to the acceleration of inflation.

66. In March, the average of core inflation indicators also rose for the sixth consecutive month. This average stood at 3.65%, 12 bp higher than the register for February, this being the highest level observed since October 2009. As it happened in the previous month, the four indicators increased again, with the CPI excepting primary food, fuel and public utilities the one exhibiting the highest acceleration, reaching the highest level (4.0%). Non-food inflation, with the lowest level, increased by only 5 bp to 3.5% (**Table 4**).

Table 4
Inflation to March 2015

Description	**DEC 2013**	**MAR 2014**	**JUN 2014**	**SEPT 2014**	**DEC 2014**	**JAN 2015**	**FEB 2015**	**MAR 2015**	**Participation in monthly acceleration (%)**	**Participation in acceleration so far this year (%)**
Total	**1.94**	**2.51**	**2.79**	**2.86**	**3.66**	**3.82**	**4.36**	**4.56**	**100.00**	**100.00**
Non-food Inflation	**2.36**	**2.62**	**2.66**	**2.70**	**3.26**	**3.20**	**3.41**	**3.46**	**14.42**	**15.66**
Tradables	1.40	1.65	1.94	1.59	2.03	2.28	3.26	3.46	23.68	37.25
Non-tradables	3.76	3.55	3.45	3.26	3.38	3.47	3.50	3.56	7.96	6.34
Regulated items	1.05	2.21	2.14	3.25	4.84	4.01	3.47	3.25	(17.21)	(27.93)
Food Inflation	**0.86**	**2.23**	**3.11**	**3.25**	**4.69**	**5.41**	**6.77**	**7.37**	**85.58**	**84.34**
Perishables	(0.16)	3.17	8.92	7.61	16.74	16.78	19.68	21.57	47.58	25.06

Processed food	(0.24)	0.92	1.44	2.14	2.54	3.70	5.62	5.99	26.85	58.27
Eating out	3.26	4.13	3.52	3.23	3.51	3.60	3.34	3.59	11.15	1.01
Core Inflation Indicators										
Non-food Inflation	2.36	2.62	2.66	2.70	3.26	3.20	3.41	3.46		
Core 20	2.72	2.86	3.04	2.89	3.42	3.58	3.62	3.70		
CPI excluding perishable foods, fuels and utilities	2.19	2.53	2.53	2.39	2.76	3.12	3.69	3.95		
Inflation excluding foods and regulated items	2.74	2.74	2.81	2.55	2.81	2.97	3.40	3.52		
Average of Core Inflation Indicators	**2.51**	**2.69**	**2.76**	**2.63**	**3.06**	**3.22**	**3.53**	**3.65**		

Source: DANE. Calculations by BANCO DE LA REPÚBLICA.

67. Within the basket of the CPI excluding food and regulated goods, the tradable component increased again, reaching 3.5% in March, a figure not seen since December 2004 and about 20 bp more than what had been observed a month before. Until last January, the pass-through of the depreciation of the peso to inflation had been relatively low, but in the past two months it has shown an increasing trend. According to the most recent estimate by the SGEE, the magnitude of this transmission would be close to 4.0% (i.e., an additional 10.0% nominal depreciation increases total consumer price inflation by 0.4%).

68. Again, the dissemination of the increases in the tradable component without food and regulated goods in March was high. The monthly adjustment of the CPI for vehicles was high again (1.02%), accumulating a variation of 7.3% from the month of October last year. This category, with a weight of 4.4%, is the third most important of the family basket, after rent and food outside the home. Other tradables with significant monthly increases were: cellular phone sales (13.1%), stoves (2.1%) and watches (1.8%).

69. On its part, the CPI for non tradables excepting food and regulated goods increased slightly from 3.5% in February to 3.56% in March. Annual variation of rents accelerated by 4 bp, closing at 2.90% in March. So far this year, increases have

been observed in education and health services fees greater than those observed last year. Despite the slight increase in the non-tradable segment of the CPI, at present there are no significant inflationary pressures on the demand side.

70. As was expected by the technical staff, the annual CPI variation for regulated goods slowed down from 3.47% in February to 3.25% in March. This lower growth is attributable to a decrease in the price of gasoline (the most recent adjustment was less than 300 pesos, decreed by the national government at the end of February). So far this year, the CPI for gasoline has fallen a little more than 6.0%. The subgroup of public utilities rose from 5.7% in February to 6.3% in March, a behavior explained especially by the 2.9% increase in gasoline prices during the last month.

71. Once again, the annual variation of food was higher in March than expected by the SGEE and the market. In this month, the increase was 60 bp, raeching 7.37%. As has happened since December, the segment of processed foods propelled the annual variation of food strongly, basically rice, whose monthly increase was 4.4% in March, 35.6% so far this year, and 36.6% in the past twelve months. These increases are explained mainly by the fall in production due to the uncertainty caused by El Niño and the low prices in the recent past. Added to this, the retention of inventories by some millers and more expensive imports due to the depreciation of the exchange rate.

72. On its part, perishable foods increased from 19.7% in February to 21.6% in March. Potato continues explaining this increase, moving forward 14.4% during the month and 71.8% in the last twelve months. Other foods such as some fruits and vegetables also fueled inflation. On its part, the prices of imported foods such as cereals and oils in March registered some hikes again, which would be affected more by the depreciation of the peso than by the international prices of these goods. These records are lower than those observed in the same month last year. Finally, meals outside the home increased by 25 bp in March, reaching an annual rate of 3.6%.

73. Regarding the pressures by non-labor costs, the variation of the prices of domestic supply to producers (produced and consumed plus imported) slightly picked up from 5.0% in February to 5.1% in March. This behavior is caused by the fact that depreciation is still propelling the PPI. Wholesale prices for food, on the contrary, relented, although they are still very high. Imported goods drove producer inflation in March, moving from 6.1% in February to 10.3% in March. The local component fell from 4.7% to 3.5%, particularly by the slowdown in the annual adjustment of food from 17.5% to 11.1%.

74. So far this year, wages have exhibited adjustments which are compatible to the inflation target. Those of industry had been adjusting to an annual rate of 2.6% until January. (After this date, this information has no longer been produced due to a methodological change). On its part, those of construction border 5.0%, which is a slowdown given that in previous months it stood at much higher levels (7.5% in September). Those of housing and heavy construction fell as compared to February, posting at 3.7% and 3.6%, respectively.

75. Inflation expectations to December of this year obtained from the monthly survey to financial analysts, with information to the second week of April, grew by 11 bp, compared to the previous month, standing at 3.76%. Inflation expectations to twelve months, obtained from the same survey, fell slightly from 3.17% in March to 3.13% in April. In turn, the average inflation expectations for 2, 3, 5, and 10 year horizons, inferred from *break-even inflation*, fell so far in April to 28 bp, 26 bp, 22 bp and 14 bp, compared to the average data for March, reaching 3.64%, 3.49%, 3.41% and 3.76%, respectively.