

# Colombia Talking Points on the Economy I Semester 2003



*Banco de la República*  
*Bogotá D. C., Colombia*





## Standard and Poors improved Colombia's long-term perspective

Standard & Poors - international risk rating firm - improved Colombia's internal and external long-term debt perspective, from negative, to stable, on July 14th.

According to Richard Francis, Standard & Poors credit analyst, this improved perspective originates in three fundamental aspects: positive fiscal behavior - compliant with the guidelines of the International Monetary Fund's Agreement-, better economic growth expectations, and an outstanding improvement in the country's public order situation.

### Fiscal Behavior

On July 9th, most of the referendum was declared admissible by the Constitutional Court. This development draws the government closer to its objective of constitutionally freezing specific public administration operational expenses, that will lead to additional 0.6% and 1.2% of GDP savings, in 2003 and 2004, respectively.

Furthermore, three large state companies (Telecom; Ecopetrol; and the Social Security Institute, ISS) have undergone restructurings as part of the government's current State's efficiency program. This will lead to permanent savings and to the possibility of allocating these resources to greater social investment.

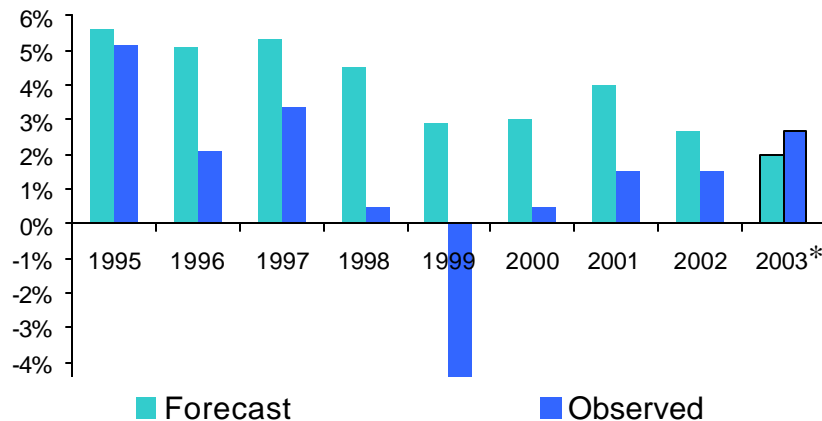
### Better economic growth expectations

The government is working on its 2003 economic growth projections, using a figure ranging between 2.5% and 2.7%, compared to its initial 2.0% cautious economic growth forecast.

The above is novel, given that negative differences between actual figures and original forecasts had been a constant from 1995 to 2002 (Graph 1).



**Graph 1**  
**Forecasted real economic growth rate versus observed**  
**1995-2003**



Source: CONPES, DANE

\* Forecast on Dec. 2002 vs Jun. 2003.

## Insurgency fighting results

Crimes with the strongest social impact have been reduced significantly, due to the different mechanisms implemented within the framework of the Democratic Security Policy and the Emergency Plan against insurgency.

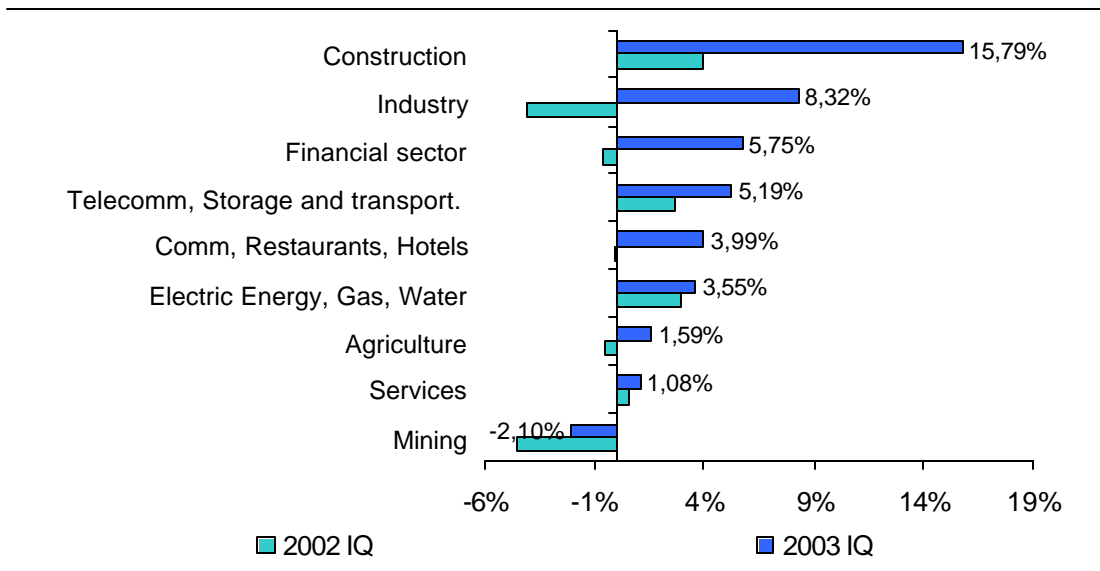
## GDP reached its highest level since 1998

According to data revised and disclosed in June by the National Statistics Administrative Department (DANE), the Colombian economy grew 3.82% during the first quarter of 2003. This exceeds both the growth observed the previous quarter (2.4%) and that of the same period of the previous year (-0.03%). It is also the highest growth since the first quarter of 1998, when GDP increased by 5.83%.

Economic activity was driven by the construction, manufacturing, and financial sectors with 15.8%, 8.3%, and 5.8% growths, respectively (Graph 2).



**Graph 2**  
**Gross domestic product by sector**  
**2002-2003- I Quarter**  
**Annual percentage variation**



Source: DANE

## Construction

The Construction sector results may be attributed mainly to the performance of civil engineering works (25.5%); and, to a lesser extent, to construction and building works (8.4%). During April 2003, construction permits increased 48.4%, compared to April 2002, and 19.5% in comparison to the last 12 months.

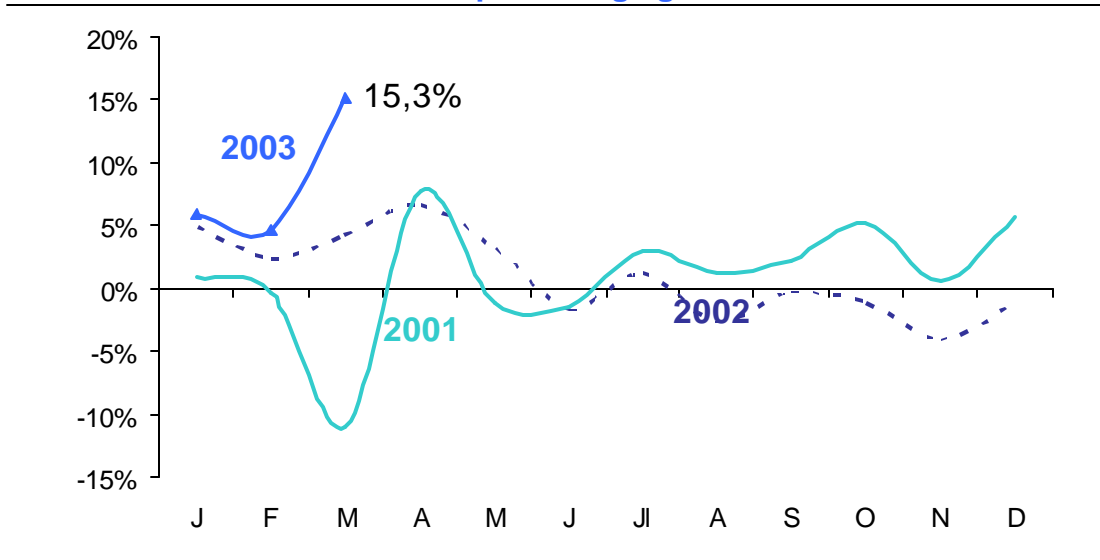
This dynamics result –at least in part– from government measures implemented in 2001 and still in force. The government encouraged social interest housing construction, by granting mortgage guarantees to informal workers, and a COP\$ 100,000 million allocation in subsidies. It also promoted higher social-level housing purchases by regulating construction promotion savings accounts (AFC), that provide substantial tax benefits to higher-income earners.

## Manufacturing Industry

Colombian industry's production is showing encouraging results, growing in excess of 15.28% in March 2003, vs. -11.00% for the same period of 2002 (Graph 3).



**Graph 3**  
**Real Industrial Production Index**  
**2001-2003**  
Annual percentage growth



Source: Dane. Calculation: DNP-Umacro

The National Association of Industrialists (Andi) ratified this information by announcing the sector's industrial production growth of 4.2% between January and April. During the first four months of the year, installed capacity reached 72%, inventories continued to fall, and 18 out of the 29 sectors analyzed, indicated higher growth levels with respect to the same period in 2002. Spinning and weaving, clothes, paper and related products, oil refining, iron and steel, chemical substances, glass and related products, and ceramics are some of the sectors with heavy activity.

Some of the causes leading to this significant entrepreneurial dynamism include the use of the advantages to access the US market, as defined in the Andean Preferences Act (Atpdea).

The growth experienced by capital goods imports for the industry, during the first quarter of 2003 (21.6%), predict that 2003 could be an excellent year for manufacturing industries. All items in this group showed positive results, in particular purchase of parts and fixtures for industrial equipment, office equipment and devices, other fixed equipment, etc.



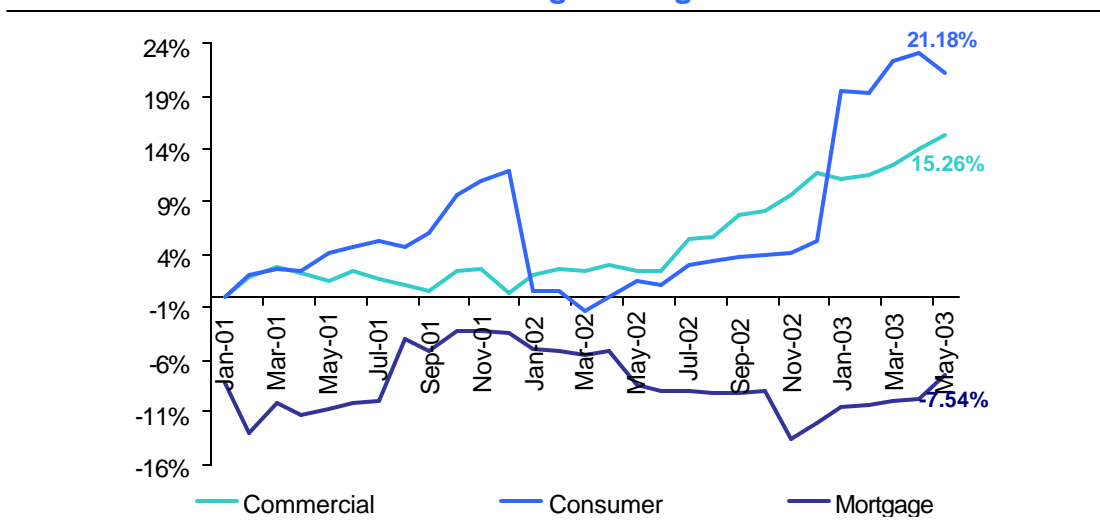
In addition, imports of intermediate goods for this sector contributed with 5.5 point of the 22.3 growth points of total imports. This contribution is mainly explained by the intermediate goods for the industry; in particular, by pharmaceutical products and non-food agribusiness goods. Growth is specifically observed in raw material purchases for chemical, animal foods, and plastics sectors.

## Financial intermediation

Growth in the financial sector is mainly due to the intermediation services sub-sector (15%). Credit recovery has been observed from the second half of 2002, reaching a 10.6% growth rate in 2003. In terms of types of credit, it is worth noticing the consumer portfolio's 21.18% accelerated growth, followed by a 15.26% increase in the commercial portfolio, while the mortgage slowdown process seems to have ended (Graph 4).

Provided that the economic recovery process becomes consolidated in the medium term, a more dynamic economic growth and an increased confidence will go hand in hand with an increased credit demand and a reduction on agents risk perception of contracting debts and providing credit.

**Graph 4**  
**Consumer, commercial and mortgage loan balances in the total financial system 2001-2003**  
**Percentage Change**



Source: Society Superintendence

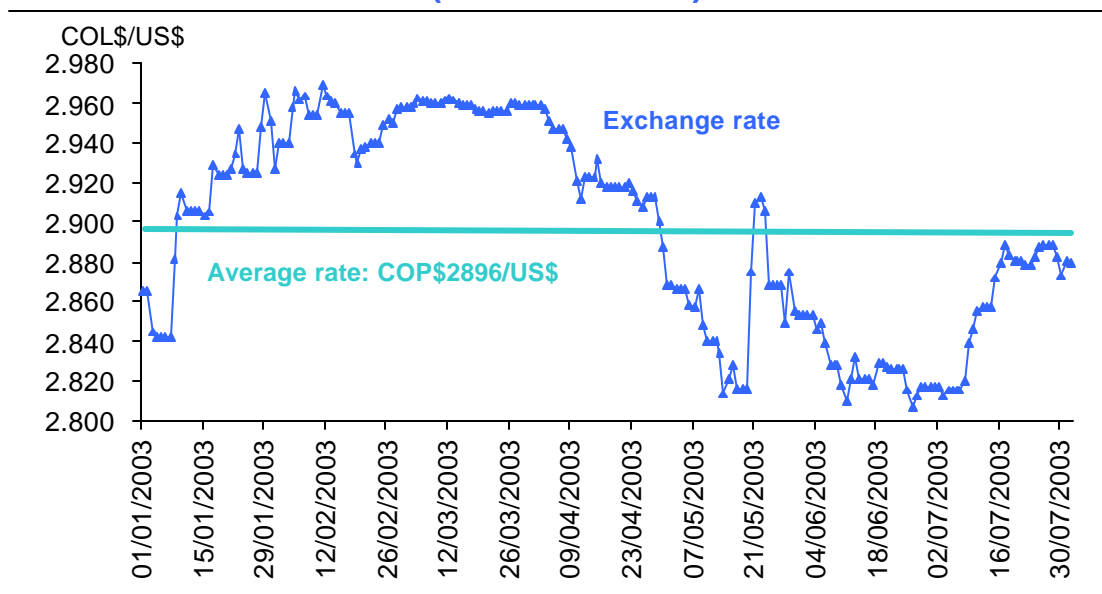


## The exchange rate stabilizes

During the first two months of 2003, the exchange market experienced a 3.19% devaluation, maintaining the trend observed for the previous year (25.04%). (Graph 5)

In order to control the exchange rate's high volatility and its effect already felt by the producer price index (PPI), Colombia's Central Bank announced auctions for the reduction of international reserves amounting to a total of up to US\$600 million, of which US\$344.5 million were fully exercised<sup>1</sup>.

**Graph 6**  
**Nominal Exchange Rate 2001-2003**  
**(vs. US\$ dollar)**



Source: Central Bank

<sup>1</sup> This was done on three different occasions (February 28, March 31 and April 30, 2003) Amounts approved for auctions may be exercised only if the market's representative exchange rate, TRM, is over the moving average for the last 20 days. The TRM is the weighed average of the dollar's price in accordance with the foreign exchange interbank market operations for the previous day.



This mechanism, along with the achievement of the fiscal goals with the International Monetary Fund, the full and certain funding by the government in 2003 and 2004, the support from multilaterals, and the recovery of the Colombian economy, improved the country's risk perception, consolidated confidence in Colombia, and stabilized the dollar exchange rate.

## Monetary policy

Colombia's monetary policy is based on an inflation targeting strategy. For this reason, it is seminal to identify the nature of expected inflation deviations from the original target. The monetary policy stance will be revised only if these deviations result from impacts identified as permanent. In this context, in recent years, the policy's stance has been to gradually reduce intervention interest rates in the monetary market.

However, since mid 2002, a change arose in domestic and foreign conditions, affecting price-increasing expectations, and compromising 2003's inflation target achievement, set to a 5% and 6% range. For these reasons, on January 17 and April 28, the Board of Directors of the Central Bank decided to increase intervention interest rates by one percentage point on each occasion. In the exchange front, on February 14th, the Board announced its intention to auction international reserves sales options up to US\$1,000 million, calling for individual US\$200 million auctions during March, April, and May.

These measures were aimed to cease expectations of a higher inflation, prevent differentials between the internal and external interest rates that promote negative capital flows, increase the probability of achieving the inflation target for this year, and securing the one for 2004.

As it was expected, the increase in the Bank's intervention interest rates was entirely transferred to the interbank interest rate (TIB), which increased from 5.07%, in December 2002, to 7.36% in June 2003.

The FTD nominal interest rate<sup>2</sup>, which continues at its all time low, reached 7.8% in June, slightly over the 7.7% observed in December. On the other hand, with increased inflation, the actual passive deposits rate registered in April a negative 0.12% level, in May barely over zero, 0.06%, and in June 0.52%. During 2003, interest rates for long term deposits (CDT 360 days) –decreased in June, in

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<sup>2</sup> Calculated as the weighed average of 90-day fixed term deposit rates.





nominal terms, by 29 basis points (bp)– fell in actual terms, almost by half a percentage point, 48 bp.

Credit interest rates in Colombia are classified in four groups: consumption, regular, preferential and treasury, according to the different risk levels faced by the financial intermediary upon granting a credit<sup>3</sup>. In June 2003, the nominal interest rate for consumer credits reached an average of 26.6%, regular credit 18.0%, preferential 11.2% and treasury 9.5%, registering variations vs December of -0.37 bp, 0.84 bp, 0.22 bp and 0.55 bp, respectively. In actual terms, consumer and preferential credit rates fell by 0.59 bp and 0.01 bp, respectively; regular and treasury credits increased by 0.56 bp and 0.31 bp, respectively.

Regarding monetary aggregates, an 18.6% monetary base annual average growth, for the first semester of the current year, represents a decrease with respect to the 23.9% growth of the prior year's second semester. The 19.8% cash annual growth rate, during the first half of the year, which was well below the rate registered between July-December 2002, (26.4%), determined this behavior.

Between January and June 2003, the expanded monetary aggregate (M3), registered a 10.3% annual nominal average growth, 3.3% in real terms, exceeding the observed rate of the same period during the previous year, 0.8%.

## Inflation and price growth expectations

Annual inflation, as of June 2003, was 7.2%, exceeding by one percentage point the rate registered the previous year for the same month; and by 0.2 percentage points that observed for December 2002. The consumer prices annual increase also exceeded 1.2 percentage points the target set by Colombia's Central Bank for the current year (between 5% and 6%).

The inflation increase, at the end of 2002, was due mainly to the low supply of perishable foods (mainly potato) and to the increase in international prices for some imported agricultural products. However, in early 2003, the pressures associated with the acceleration of the devaluation became evident through their impact on trading goods prices. Furthermore, VAT, public utilities, and fuel rates increased.

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<sup>3</sup> There is another credit type whose interest rate is indexed by inflation through the UVR. According to Resolution 14 of 2000 by the Board of Directors of the Central Bank, these credits are subject to a maximum 13.9% annual effective compensating rate. The treasury credit is defined as a preferential loan with a maximum 30-day term, in order to cover short-term liquidity requirements. On its turn, the market tends to charge higher interest rates to consumer credits vis-a-vis other reduced risk credit types like preferential or treasury credits.



For the second half of 2003, it is predictable that food will continue to contribute to reduce inflation, the same as in June. Inflation, not including food, continued to grow as of June, due to the readjustment of public utilities, fuel, and transport rates and pressures caused by the exchange rate. However, during this last month, exchange pressures started to yield, judging by the stability of the inflation of trading goods. A reduction seems possible for the second semester, provided that the exchange rate remains stable.

The above inflation-related results were reflected in the agents' price increase expectations. In fact, according to the two economic expectations surveys conducted by Colombia's Central Bank, on January and April 2003, credibility percentages for the inflation target were 42% and 16% respectively, the latter being the all time lowest credibility percentage.

## **Foreign Investment Cases and Announcements**

### **Comcel invests to meet demand**

Comcel, mobile telephony firm, owned by the Mexican América Móvil, will invest US\$ 30 million in order to meet the Atlantic Coast's demand, through its regional firm, Celcaribe. Resources will be destined to reinforce the TDMA and GSM networks, with US\$ 12 and US\$ 18 million respectively.

### **Esso and Mobil continue investing**

The US company will invest US\$ 10 million in Colombia to preserve its high market share (36%). The investment will be destined for its new lubricants' line, packaging renewal, market research and technification of commercial information channels.

### **Carrefour 100% French**

Carrefour, French hypermarkets chain, assumed total control of the firm's operations in Colombia, achieving separate agreements with Valores Bavaria and with the Spanish firm SIGLA, to obtain the 35% and 10% interests both companies owned in Grandes Superficies de Colombia, respectively, current operator of Carrefour hypermarkets. In the course of this year Carrefour plans to invest some US\$ 70 million for the construction of new points of sale.



## Colombia Key Data

**Table 2**

ITEM	Units	Latest data period	Data	Data One year before
<b>Total Foreign Investment</b>				
Direct	US\$ million	Jan.03 - Mar.03	241	872
Portfolio	US\$ million	Jan.03 - Mar.03	14	-675
<b>Demand and Unemployment</b>				
GDP	% variation year to year	Mar.03	3,82	-0,04
Production Rate (MMS) (*)	% variation year to year	Mar.03	15,30	-11,00
Retail Sales (**)	% variation year to year	Apr.03	3,88	-2,30
Investment a/	% variation year to year	Mar.03	33,16	-16,68
National Unemployment Rate	(%)	May.03	12,96	15,28
13 Main cities unemployment rate	(%)	May.03	16,72	17,51
<b>Prices and Interest Rates</b>				
Consumer Price Index	% variation year to year	Jun.03	7,22	6,25
Producer Price Index	% variation year to year	Jun.03	10,95	2,95
Resource gathering interest rate (90 days)	Monthly average (%)	Jun.03	7,77	8,41
Lending interest rate (Source: Central Bank)	Monthly average (%)	Jun.03	14,90	16,63
<b>Exchange Rate</b>				
Nominal Exchange Rate	Peso/dollar US\$	Jun.03	2826,95	2364,25
Nominal Devaluation	% annual variation to date	Jun.03	19,57	2,54
Actual Exchange Rate (ITCR)	1994=100	Jun.03	136,16	113,35
Actual Devaluation	% annual variation to date	Jun.03	20,12	-3,61
Peso/Yen Monetary Units	Peso/Yen	Jun.03	23,64	19,75
Peso/Euro Monetary Units	Peso/Euro	Jun.03	3229,79	2340,13
<b>Trade</b>				
Exports	US\$ million	Jan.03 - Apr.03	3.986,45	3.870,66
Traditional Exports b/	US\$ million	Jan.03 - Apr.03	2.054,86	1.743,84
Non-traditional Exports c/	US\$ million	Jan.03 - Apr.03	1.931,59	2.126,81
Imports	US\$ million	Jan.03 - Apr.03	4.462,13	3.915,65
<b>Other</b>				
M1	% variation year to year	Jun.03	13,71	22,49
M3	% variation year to year	Jun.03	13,02	7,88
Net International Reserves	US\$ million	Jun.03	10.499,79	10.816,98
Colombia General Stock Exchange Index	July 2001=1000	Jun.03	2.075,77	1.238,39
Financial Administration Deficit (Central Government)	% of GDP	2002	-5,58	-5,80
Financial Administration Deficit (Non-Financial Public Sector)	% of GDP	2002	-3,59	-4,21

Source: Central Bank, Statistics National Administration Department and Colombia Stock Exchange.

a/ Preliminary

b/ Coffee, coal, ferronickel, Oil and by-products, Gold, Emeralds

c/ Agribusiness, Production, Mining Industries

(\*) With Threshing

(\*\*) Excluding fuels



## Main Latin American Economic Indicators

**Table 3**

	COLOMBIA		ARGENTINA	BRAZIL	CHILE	ECUADOR	MEXICO	PERU	VENEZUELA
	2003*	2002	2002	2002	2002	2002	2002	2002	2002
Real GDP growth (%)	2,0	1,7	-10,9	1,5	2,1	3,4	0,9	5,2	-8,9
Population (millions)	44,7	43,85	37,5	174,7	15,1	13,1	100,1	26,7	25,6
GDP (US\$ billions)	-	81,2	86,1	451	68,2	26,3	636,1	56,9	99,5
GDP per capita (US\$)	-	1.819	2.294	2.585	4.394	2.004	6.352	2.128	3.451
GDP per capita growth (%)	-	-7,7	-66,2	-12,6	-3,9	1,6	0,5	3,5	-32,0
Consumer prices variance	6,0	7,0	41,0	12,5	2,8	9,4	5,7	1,5	31,2
Fiscal balance (% GDP)	-2,5	-3,6	-1,5	-10,3	-0,8	0	-1,3	-2,3	-3,3
Total External Debt/GDP (%)	48,4	45,9	155,9	50,4	60,8	54,8	21,6	49,2	33,1
Exchange Rate (LC/US\$ eop)**	-	2.865	3,35	3,53	712	-	10,4	3,5	1.401
Nominal Interest Rate (savings)	-	7,7	20,3	25,5	2,9	7	7	4,7	26
Current Account (% of GDP)	-2,7	-2,0	11,1	-1,7	-0,8	-4,5	-2,2	-2	7,8
Foreign Direct Investment (US\$ million)	1.468	1.974	1.500	13.402	858	1.335	13.500	1.943	1.200
Foreign Direct Investment (% of GDP)	1,90	2,44	1,39	2,48	1,36	6,36	2,14	3,41	0,13

Source: ECLAC (Preliminary Balance Latin American economies 2002), IMF, IDB and Central Bank

\* Forecast



## COINVERTIR

### Mission

**COINVERTIR** promotes, facilitates and consolidates foreign direct investment in Colombia.

**COINVERTIR** seeks to attract the attention of foreign investors, assists existing foreign investors, and works in the improvement of the country's investment climate.

### Characteristics

Autonomous, mixed entity, established under Colombian private law

Staffed by a small group of highly qualified professionals from different disciplines and managed with an entrepreneurial spirit

Acts as liaison between the public and the private sectors, and facilitates the exchange of views in order to achieve competitive and stable conditions for foreign investment.

### Activities

**COINVERTIR** works toward its objectives through three main activities:

#### Promotion

**COINVERTIR** promotes Colombia as an investment site

**COINVERTIR** provides accurate and up-to-date information about foreign investment conditions in Colombia, in order to attract foreign investors



## Investor Services

**COINVERTIR** identifies foreign investors and provides existing investment opportunities in Colombia

**COINVERTIR** advises foreign investors during and after the investment process, on legal, economic and procedural matters

**COINVERTIR** assists foreign investors already established in Colombia to overcome problems in their operations

## Investment Climate

**COINVERTIR** monitors and produces objective analysis on foreign direct investment conditions and on issues of interest and concern to foreign investors.

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- Colombia Outlook and Investment Potential Presentation
- Colombia: Foreign Investment Guide
- Colombia: Regional Investment Guides
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- Inflation reduction
- Monetary authority
- Foreign exchange authority
- Credit authority

### Colombian Central Bank Functions

- Currency issuer
- International reserves manager
- Lender of last resort
- Banker of banks and coordinator of the payments system
- Fiscal agent of the Government
- Researcher of Colombian economy

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