[Detailed Explanation of the Macroeconomic Situation]

Must reads

[Banco de la República keeps the Benchmark Interest Rate at 4.5%]

A regular meeting of the Board of Directors of Banco de la República was held in the city of Bogotá D.C. on October 30, 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 Board Members Carlos Gustavo Cano Sanz, Ana Fernanda Maiguashca Olano, Adolfo Meisel Roca, César Vallejo Mejía and Juan Pablo Zárate Perdomo.

These minutes contain a summary of how Banco de la República's technical team views the macroeconomic situation (Section 1), followed by a review of the key policy discussion points considered by the Board of Directors (Section 2).

A more detailed description of the macroeconomic situation prepared by the technical staff from the Central Bank is provided in the data section of the September 2014 edition of the Inflation Report, as well as in the statistical appendix.

1. MACROECONOMIC CONTEXT

Regarding the macroeconomic context, the technical staff highlights the following elements:

1. In the present report, the growth forecast for external demand was reduced for this and the [illegible] slowdown, while the majority of its partner countries in the region could recover in the following year, but would present lower growth rates than their respective potential.
2. The risk premium measures adopted by several countries of the euro zone, as well as by some [illegible] some of these economies export, chiefly that of oil, also contributed to increase the risk measures. With this, their currencies have depreciated against the US dollar.
3. In the United States, appreciation of the dollar and the fall in the international energy prices could [illegible] Nevertheless, the weaker rally of its commercial partners, together with the risks of a slowdown in the external demand, increased uncertainty upon the performance of its exportation sector.
4. Facing the prospect of a lower inflation in the United States, as well as the greater risks of a [illegible] year, as had been projected a quarter ago. This more distant horizon regarding this increment contributed to the downturn in the long-term interest rates.

5. The current levels in the international price of oil are situated way below the forecast produced [illegible] forecast, which is a situation that will be reflected on a lower national income if it continues to be sustained.
6. The weakness in the external demand as well as lower international prices of the basic mining [illegible] August, the agriculture and other sectors presented high annual growths, while the mining sector descended, but less intensely.
7. Until August, the imports in dollars have grown 6.8%, which is explained by the increase of those [illegible] of July-August, the external purchases addressed to consumption as well as to capital goods accelerated; those of raw materials presented a lower increase rhythm.
8. With the aforementioned external context and the new figures of foreign trade, the technical staff [illegible] sector due to the fall in the income from oil. Also, this supposes that the wide use of external savings by the remainder of sectors would have continued in the second half of the year.
9. As for internal growth, the new indicators of supply and demand for the third quarter of 2014 [illegible] product. The figures of foreign trade indicate that imports would increase more than exports, and with them the balance of trade would bring a negative contribution to growth.
10. In the third quarter, banking credit continued to slow down, recording annual rates over the [illegible] stabilized. All this takes place within a context of weak transfer of the increases in the benchmark interest rate to the interest rates of the loans.
11. Considering the aforesaid, the technical staff from Banco de la República estimates growth [illegible] estimations, in 2015 the economy would slow down, and the GDP would present a rate of increase of around 4.3%, within an interval between 3.0% and 5.3%.
12. The new product gap estimations for 2014 indicate that this would be slightly positive and more closed that the forecast performed in the last quarter. In 2015, the gap would continue to close, but could remain positive.
13. Regarding inflation, the result of 2.86% at September was aligned to the expectations of the [illegible] them from the CPI, their complement also slowed down in the latest month. The other three measures of basic inflation also decreased, and the average of the four indicators was 2.63%.
14. Along the year and until September, an inflation of 3.08% has stockpiled, a figure that already [illegible] analysts' inflation expectations to one year, as well as those for 2, 3, and 5 years derived from the public debt bonds, remain relatively stable and somewhat above 3%.

In summary, aggregate demand continues to show a strong growth in a context close to the full use of the productive capacity. At the same time, inflation expectations remain close to 3%. This takes place within an environment of deterioration of the terms of trade and a growing uncertainty regarding the recovery of the economic activity worldwide and the cost of external financing, which are factors that may impact aggregate demand and the exchange rate.

2. DISCUSSION AND POLICY OPTIONS

The Board of Directors unanimously decided to keep the benchmark interest rate at 4.5%.

The Board Members highlighted that the economy is showing a strong dynamic, but that there are risks of negative clashes in the traditional policy horizon which may result in a slowdown. Particularly, the external environment continues to show symptoms of weakness, and the terms of trade for Colombia have deteriorated. If this trend is maintained, the growth of national income as well as the aggregate expense will be affected.

On the other hand, inflation expectations are anchored at levels close to 3.0%. The average of the indicators of basic inflation and total inflation converges towards the goal.

Under these conditions, the Members of the Board agreed to maintain the benchmark interest rate unaltered, as well as to continue monitoring the performance of the economy.

3. POLICY DECISION

The Board of Directors of the Central Bank unanimously decided to maintain the benchmark interest rate at 4.5%.