Monetary Policy Report

A regular meeting of the Board of Directors of *Banco de la República* took place in the city of Bogotá D.C. on Thursday, December 14, 2017. In attendance were Mauricio Cárdenas Santamaría, Minister of Finance and Public Credit; Juan José Echavarría, Governor of the Central Bank; and Board Members Gerardo Hernández Correa, Ana Fernanda Maiguashca Olano, Adolfo Meisel Roca, José Antonio Ocampo Gaviria, and Juan Pablo Zárate Perdomo.

These minutes contain a summary of the outlook on the macroeconomic situation by the technical staff of the Central Bank (section 1), followed by a review of the main discussion regarding monetary policy by the Board of Directors (section 2).

Further detail on the macroeconomic situation prepared by the technical staff from the Central Bank will be presented in the monthly **Monetary Policy Report for November 2017** and in the statistical annex (Only Available in Spanish).

1. MACROECONOMIC CONTEXT

1. There were no changes in the external context compared to what was presented in the previous report: advanced economies continue to drive the recovery of the global economy, particularly, with more favorable than expected indicators for the United States and the Euro zone.
2. The Federal Reserve of the United States increased its reference rate by 25 bp in its December meeting, as was expected.
3. In recent weeks, the price of oil has remained relatively high following the better outlook for global demand and the extension of the OPEC agreement until mid-2018.
4. The exchange rates in the region have been relatively stable in recent weeks. For the moment, S&P’s decision to reduce Colombia´s credit rating has had moderate effects on the country´s risk measurements, on the price of TES, and on the price of the peso against the dollar.
5. The information on the current account deficit to September of 2017 shows that the external imbalance continues to adjust vis-à-vis the same period last year. This continues being a result of the better performance of external revenues, particularly the exports of goods favored by the better terms of trade, and to a lesser extent, by a better behavior of net exports.
6. Given the information observed to the third quarter, the GDP growth of 1.6% expected by the technical staff for all of 2017, would imply an annual expansion of 1.8% in the last quarter. However, available activity and perception indicators for the fourth quarter continue to show a

low dynamism in the economy and reveal that several of the downside risks in growth would be materializing.

7. The credit slowdown continued in the last month, explained mainly by the moderation in household indebtedness, particularly in the consumer modality. -The commercial credit also slowed down in November and registered an annual growth of 5.1%.
8. In November, annual consumer inflation increased for the fourth consecutive month and stood at 4.12%, above that expected by the technical staff and by the market. This is mainly explained by the rebound in the annual adjustment of perishable foods, tradables and, to a lesser extent, non-tradables. Core inflation interrupted the downward trend that it had been presenting and stood at 4.54% in the last month.
9. Inflation expectations for December of 2017, obtained from the monthly survey to financial analysts, increased, and stood at 4.01%. The expectations calculated from the public debt bonds, with horizons of 2 and 3 years, had some increases vis-à-vis the previous month and stand above 3.0%.

In summary, to December 2017, inflation is expected to finish slightly below 4.0% and decline in the first quarter next year, partly as a result of the reversal of the transitory shocks that have diverted it from its target. This takes place in an environment of economic activity that continues to be weak. Monetary policy actions undertaken so far, which consider these effects, should strengthen convergence of inflation to its target.

2. DISCUSSION AND POLICY OPTIONS

The Board of Directors decided unanimously to maintain the benchmark interest rate unchanged at 4.75%. In making this decision, they considered that inflation for November was above that forecast by *Banco de la República*´s technical staff, that the average of the core inflation indicators stopped falling, that the inflation forecasts continue showing a decrease for the first quarter of 2018, and that this trend is expected to strengthen. Although the inflation figure for November was not good, there is a high probability that inflation will be close to 4.0%, or even slightly below, by the end of 2017.

They also referenced the weakness of demand, which is reflected both in the GDP data for the third quarter and in the industry, commerce and consumption surveys available for the third quarter. On the external front, the good performance of total exports is highlighted, driven mainly by oil and carbon, as well as by non-traditional exports.

The Board Members also agreed that the space to decrease the benchmark interest rate has been reduced. For this reason, they considered it appropriate to wait for more information on the behavior of inflation, output and the exchange rate before reducing the policy rate.

As for the credit rating reduction announced by S&P, the Board observed that the market has had no significant reaction that may alter in a relevant way the inflation and product forecasts.

3. POLICY DECISION

The Board of Directors of the Central Bank of Colombia unanimously decided to maintain the benchmark interest rate unchanged at 4.75%.

Bogotá, D. C.