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Decision-Making Process

and Communication Wednesday, 14 July 2021 - 12:00 Banco de la República establishes the benchmark interest rate based on an analysis of the current state of the economy, its outlook, and developments in the inflation forecast with respect to the target. If this assessment indicates there are risks of inflation persistently being above target during the timeline in which this policy operates, the Bank will increase the benchmark interest rate. Likewise, if the economy exceeds a sustainable growth rate, surplus spending may occur that could jeopardize price stability or lead to financial fragility. In such cases, the Bank will raise the benchmark interest rate to avoid a sharp drop in output and employment. For monetary policy decisions, the BDBR assesses the present and future state of the economy, as well as the forecast for inflation and its deviations from the target. This is because appropriate action with respect to monetary policy depends on the nature of any such deviations. If changes in consumer prices are caused by changes in demand (spending) in the economy, the risk of output exceeding its sustainable level coincides with the risk of inflation being above target, and vice versa. This happens because extremely strong aggregate demand places pressure on use of the economy's installed capacity and generates further increases in production costs. In these circumstances, monetary policy action to stabilize spending and output near their sustainable values also stabilizes inflation near its target. In this case, meeting the target for inflation is compatible with the objective of reaching the maximum sustainable level of output and employment. However, in the absence of surplus demand, upward pressure on inflation might be brought to bear by temporary supply constraints in the economy. In such cases, production costs rise, and companies reduce output and employment. In this type of scenario, deviations in inflation from the target run the risk of extending beyond the duration of a supply shock. However, if the inflation target is credible; that is, if markets expect the Bank will not allow a persistent gap between inflation and 3 percent, expectations will remain aligned with the target. Under these circumstances, the Bank can guarantee future compliance with the inflation target, without incurring major shortfalls or surpluses in output and employment.

Fuente: https://d1b4gd4m8561gs.cloudfront.net/en/monetary-policy/decision-making-process-and-communication