



Macroeconomic Conditions and Outlook for 2021

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Member of the Board
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*Opinions presented herein do not represent the position of the Board of Directors of the Central Bank of Colombia.



Content

CONTEXT

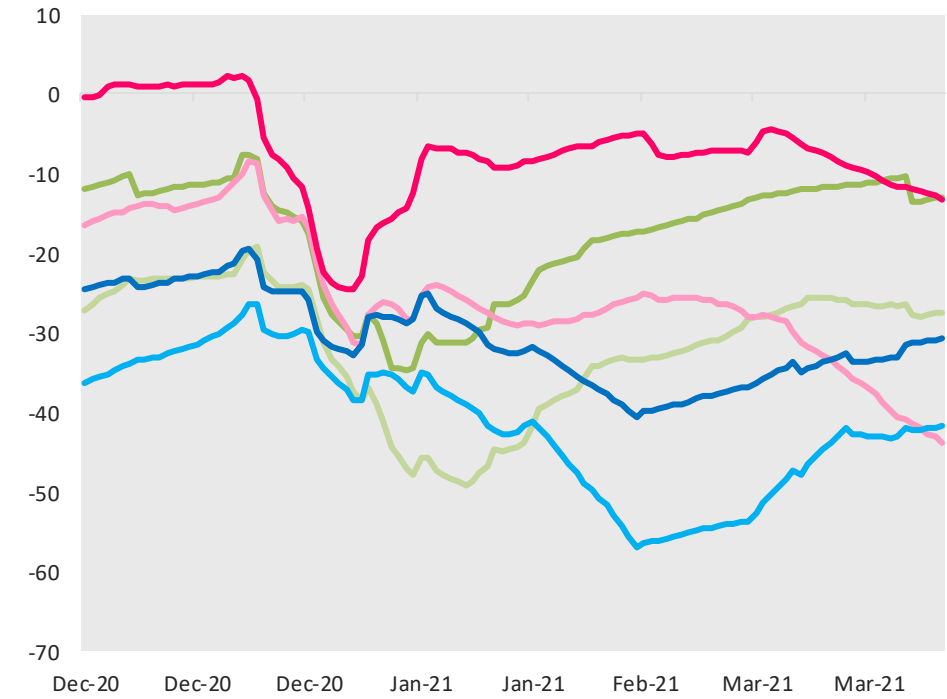
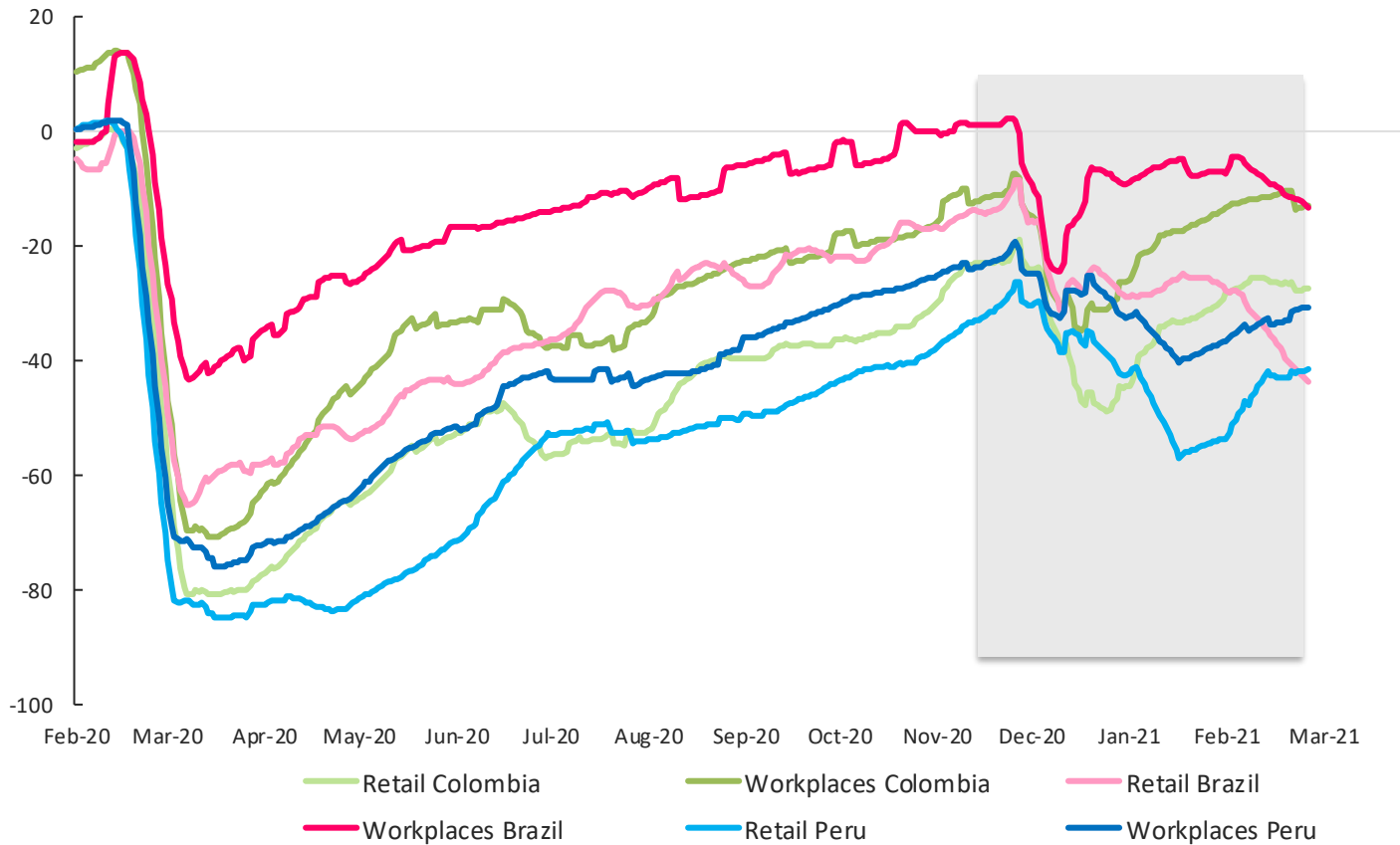
CONDITIONS THAT SUPPORT THE POLICY RESPONSE

ECONOMIC FORECASTS

POLICY CHALLENGES

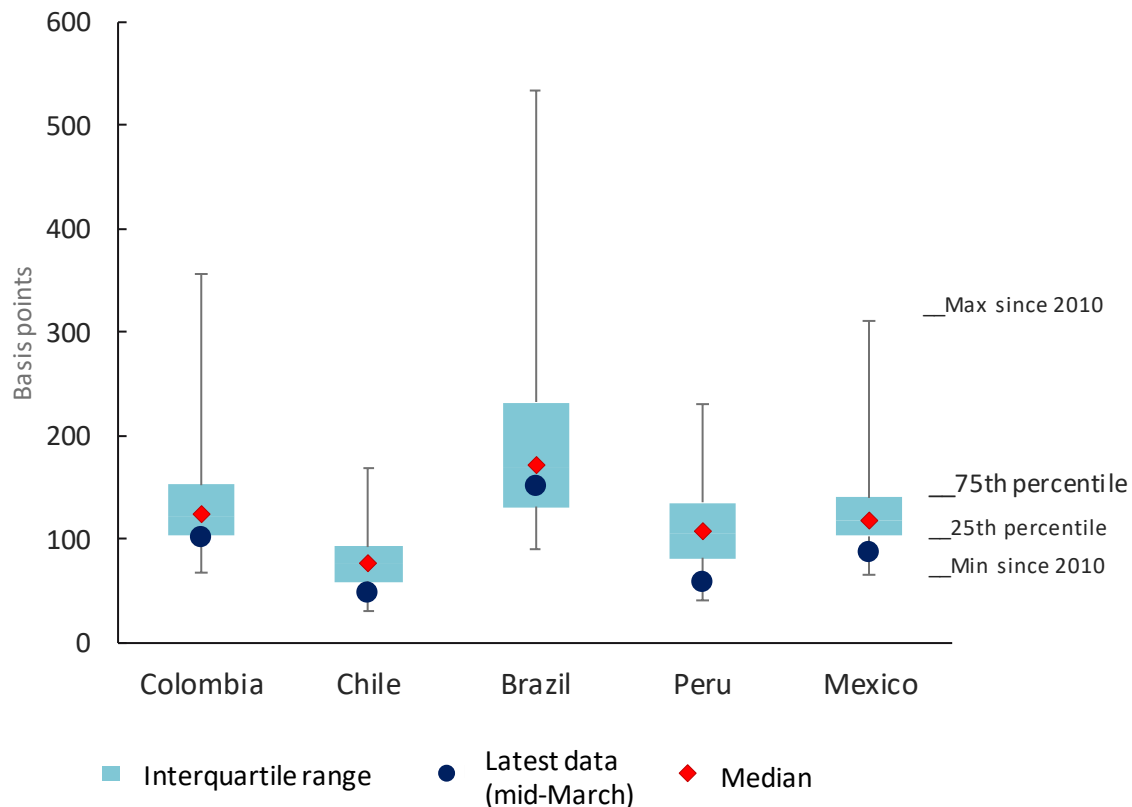
- **The Colombian economy is facing an unprecedented shock** because of the pandemic. There is uncertainty about its evolution, while further outbreaks and the ensuing public and private responses might hinder economic recovery.

Mobility Trends

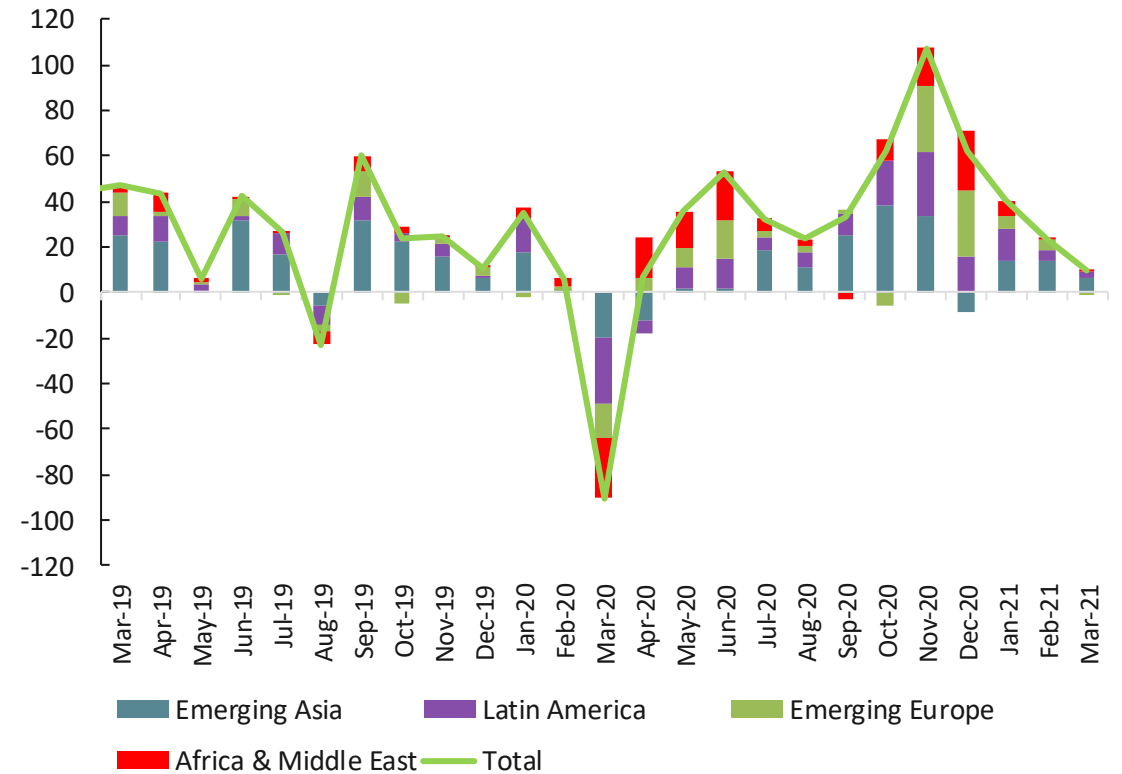


- **External liquidity is abundant, and sovereign risk premia are still at historically low levels.** There are risks stemming from the recent steepening of the yield curve in the U.S.
- **Portfolio flows to emerging markets remain positive but have decreased.**

Historical distribution of the 5-year CDS
(daily data since 2010)

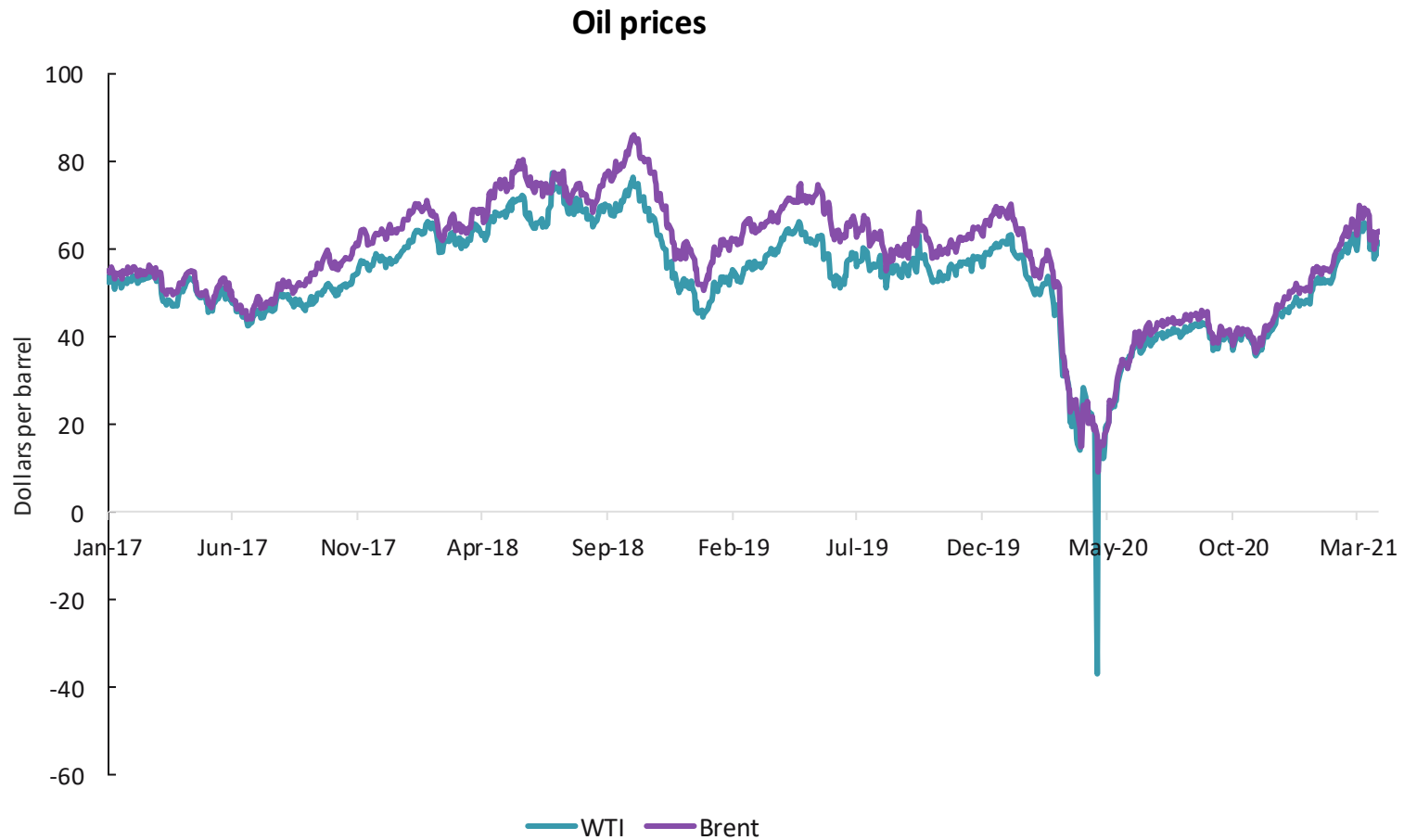


Portfolio flows to Emerging Markets
(USD billion)

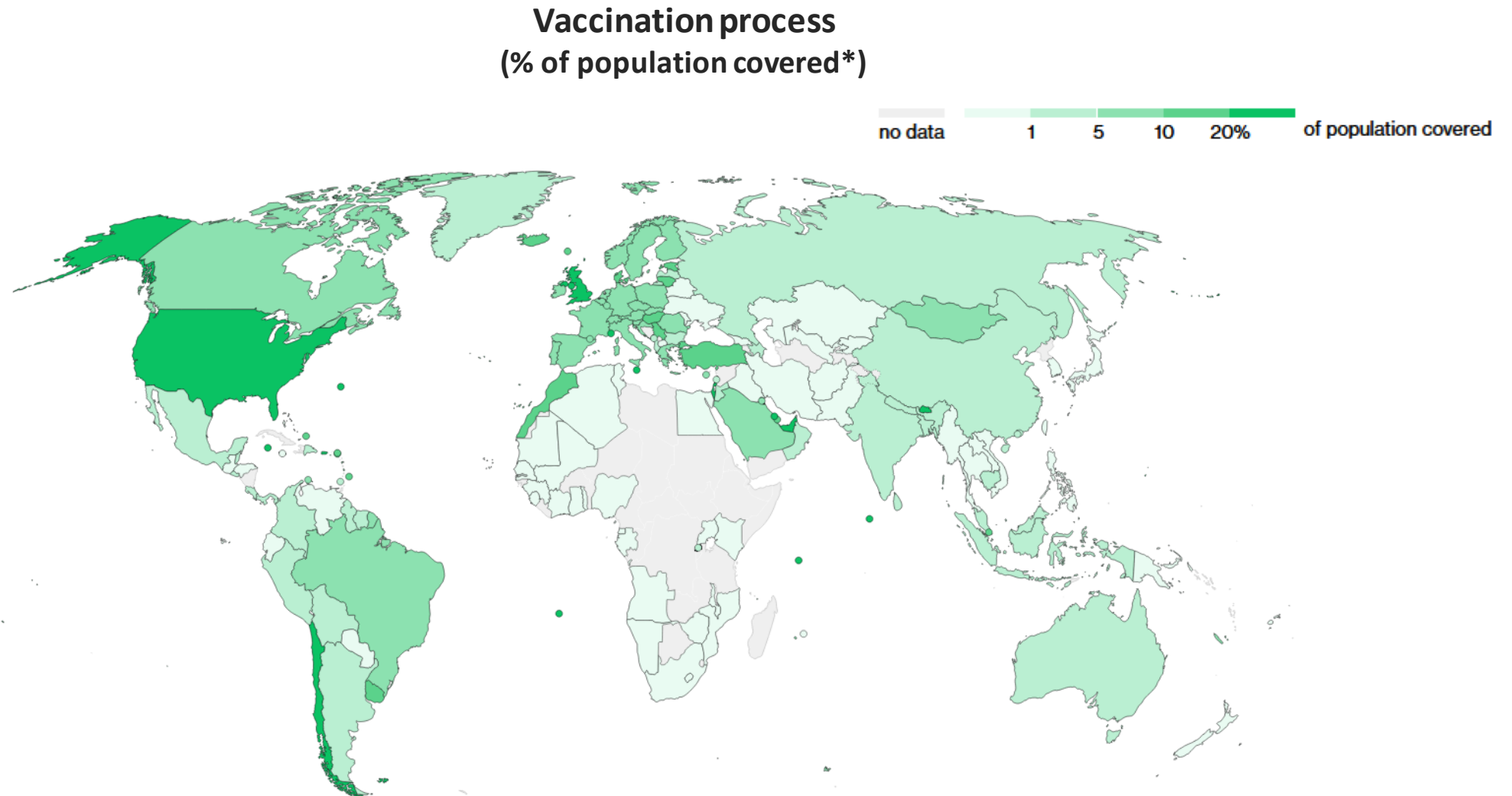


Sources: Bloomberg, IIF; calculations by Banco de la República.

- Commodity prices have increased. The oil price has risen above previous expectations



- **The vaccination process will support growth in 2021.** The recovery path is likely to be heterogeneous across countries.



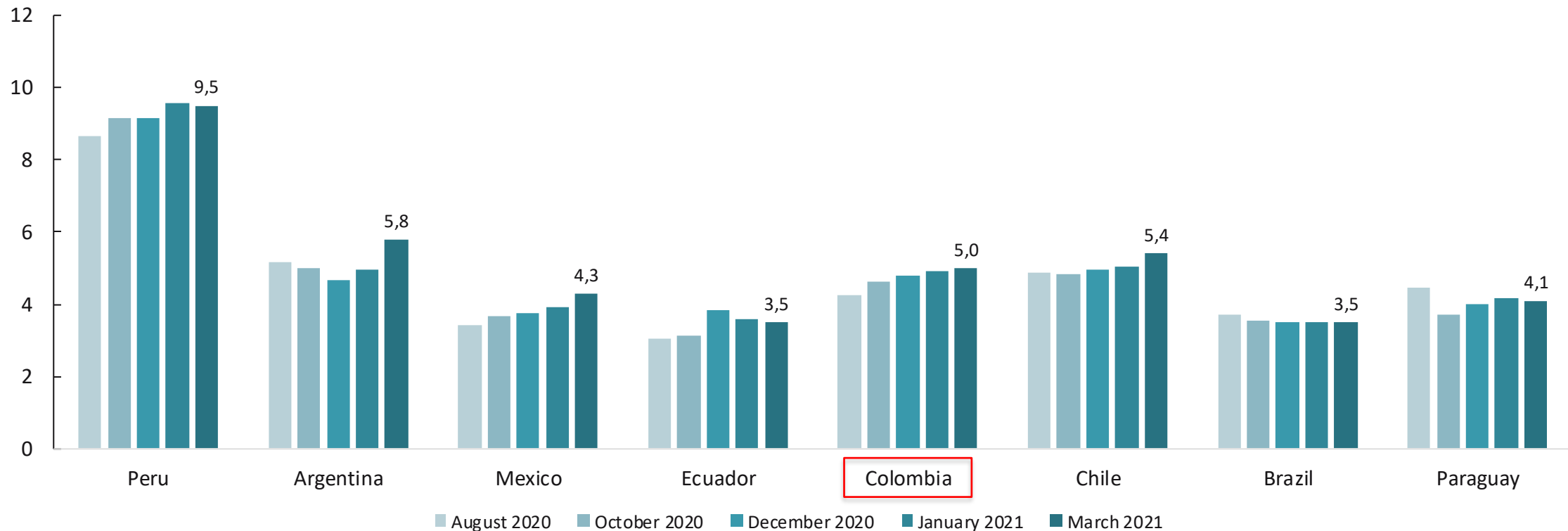
- Progress in the vaccination programs and the impulse of fiscal and monetary policies in advanced economies have improved the outlook for global growth

IMF Economic Growth Projections
(% change)

	2021 Projection	Difference from January 2020 WEO update Projections
World Output	6,0	0,5
Advanced Economies	5,1	0,8
United States	6,4	1,3
Euro Area	4,4	0,2
Japan	3,3	0,2
China	8,1	0

- **Analysts estimate that the region will grow 4.5% in 2021.** Forecasts have improved after positive news regarding global demand and the vaccines.

Growth Forecasts for 2021
(Analysts' estimates)



Source: Latin American Consensus Forecast. Forecasts for the region do not include Venezuela.



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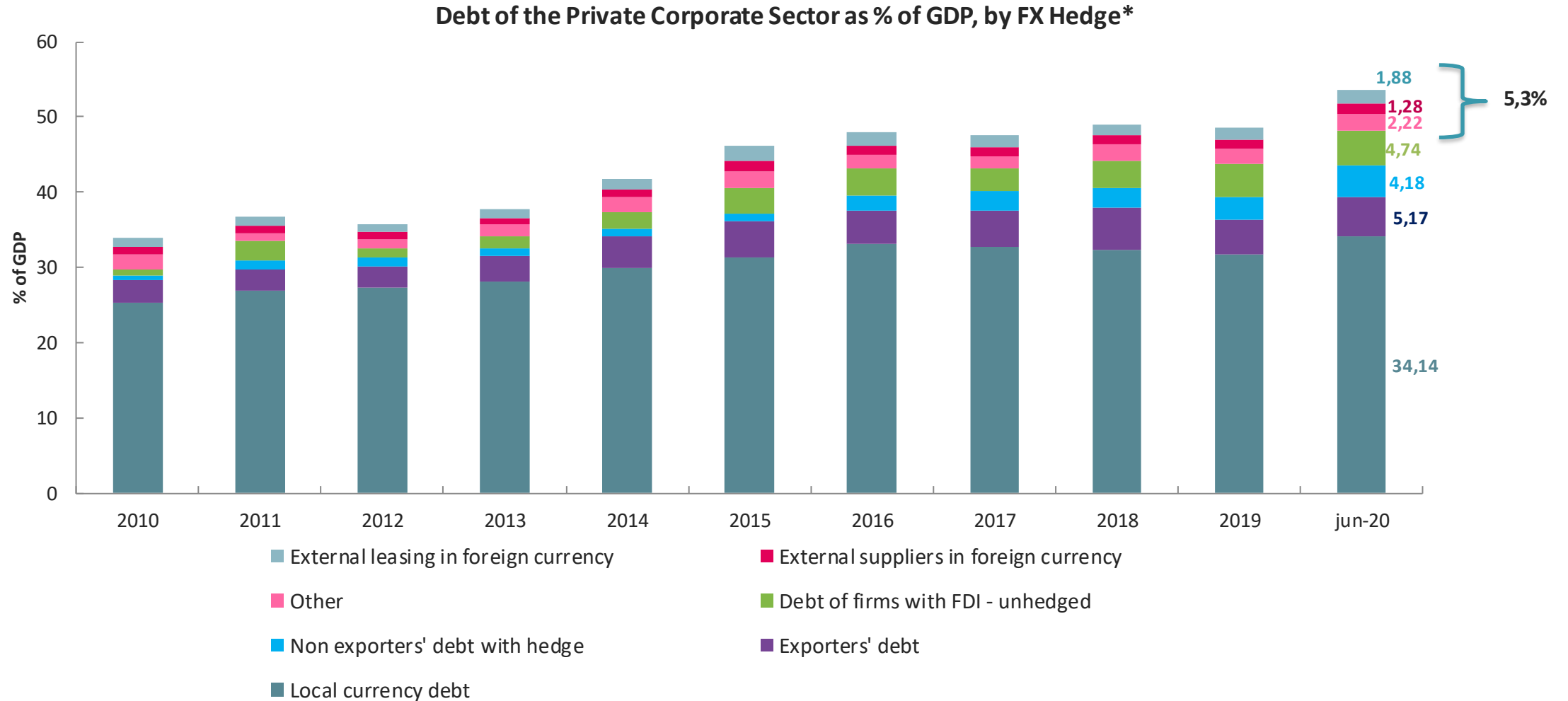
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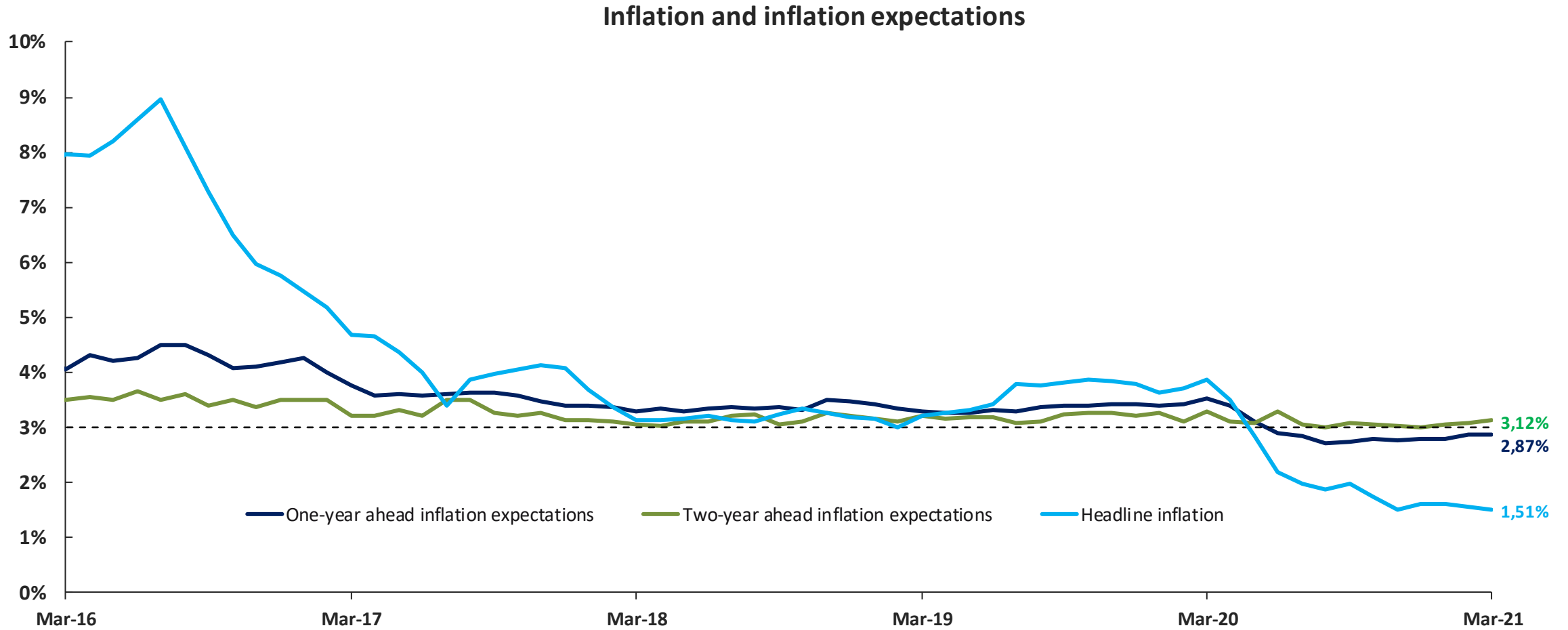
- The monetary policy framework and other characteristics of the Colombian economy allowed for a quick response against the shocks and provide space to react in the future:
 1. The Colombian economy has a fully-fledged inflation targeting regime with exchange-rate flexibility, and the Central Bank has high credibility.
 2. Adequate levels of external buffers.
 3. Adequate financial supervision and regulation.
 4. There is a Medium-Term Fiscal Framework that seeks to achieve a sustainable path for public debt.

- **Currency mismatches are low**, allowing the exchange rate to become the first line of defense against external shocks without creating financial stability concerns. Unhedged FX denominated debt of the corporate sector has not changed substantially and nowadays represents only 5.3% of GDP



Source: Banco de la República – Financial Stability Report 2020-II. *Fx debt from suppliers and leasing is not available by ID, and it is not possible to identify if this debt has an FX hedge.

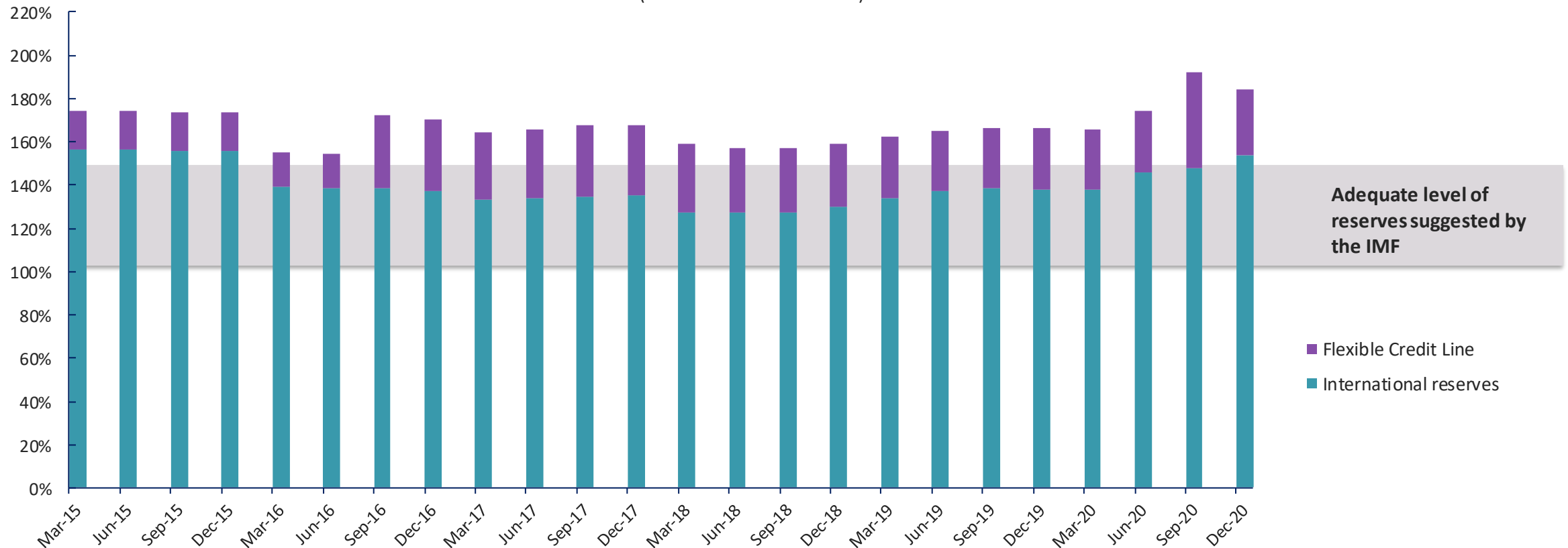
- **The high credibility of the Central Bank** maintains inflation expectations close to the target despite the size of the shocks.



Source: Banco de la República (monthly expectations survey) and DANE.

- **External liquidity levels are adequate** and were reinforced mostly through the direct purchase of USD 3.5 billion from the National Government and the augmentation of the Flexible Credit Line with the IMF to USD 17.2 billion.

Foreign Reserves and Flexible Credit Line (precautionary)*
(% of the IMF's ARA metric)



Source: Banco de la República and IMF. *The reduction observed in December is explained by the disbursement of USD 5.4 billion from the FCL to the government.

The Central Bank has used its toolbox to support the economy by:

- **Providing liquidity** to avoid disruptions in the payment systems and contribute to the credit supply by financial institutions.
- **Helping stabilize key financial markets** that have suffered liquidity problems.
- **Maintaining external buffers** to facilitate external payments of the economy.
- **Supporting the economy** through **lower interest rates**.

Central Bank Response

Objectives	To protect the payments system	To preserve the supply of credit	To stabilize key financial markets	To provide an economic stimulus
Actions				
Temporary liquidity (repo operations): Increase in the allotment counterparties, collaterals and maturities	X	X	X	
Outright purchases of public and private securities	X	X	X	
Reduction of banks' reserve requirements	X	X		X
Auction of FX Non-delivery Forwards			X	
Auction of FX Swaps	X	X	X	
Reduction of interest rates		X		X



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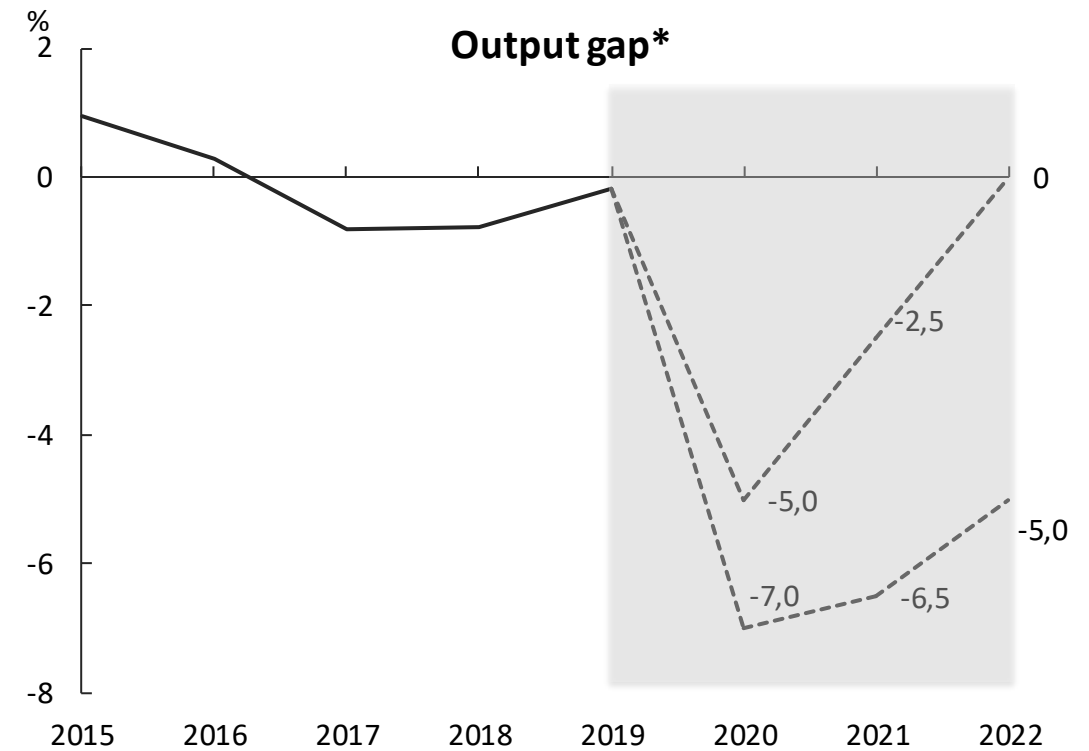
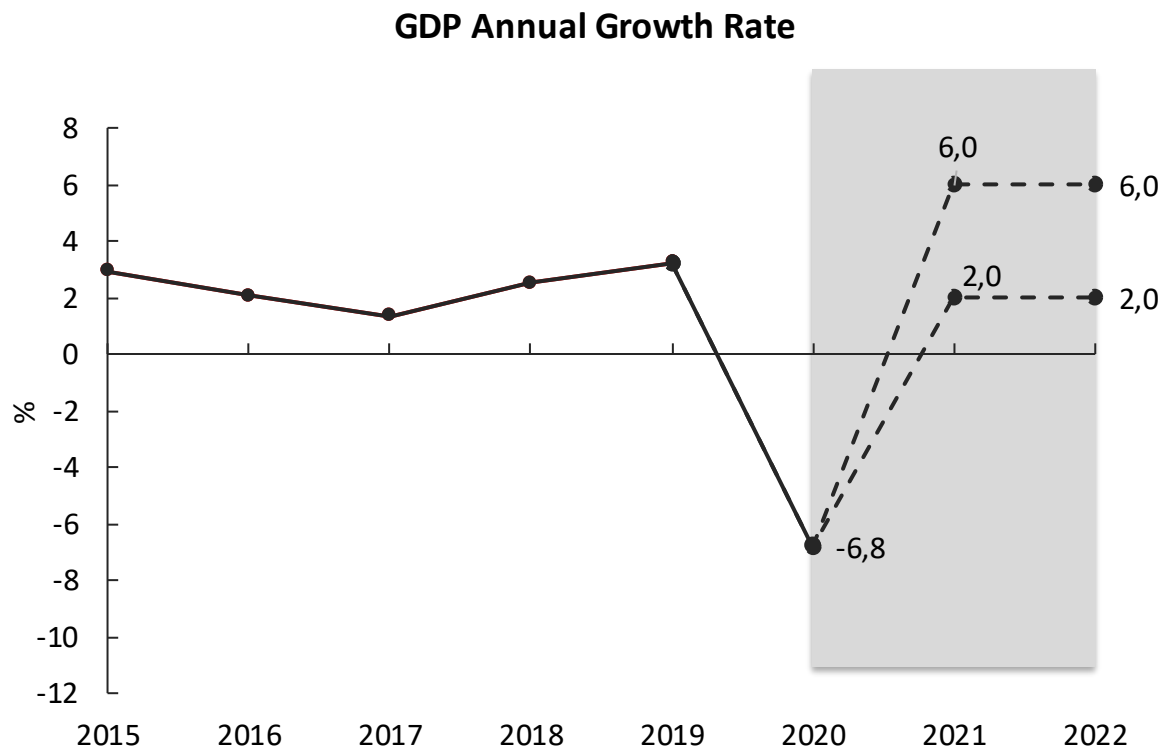
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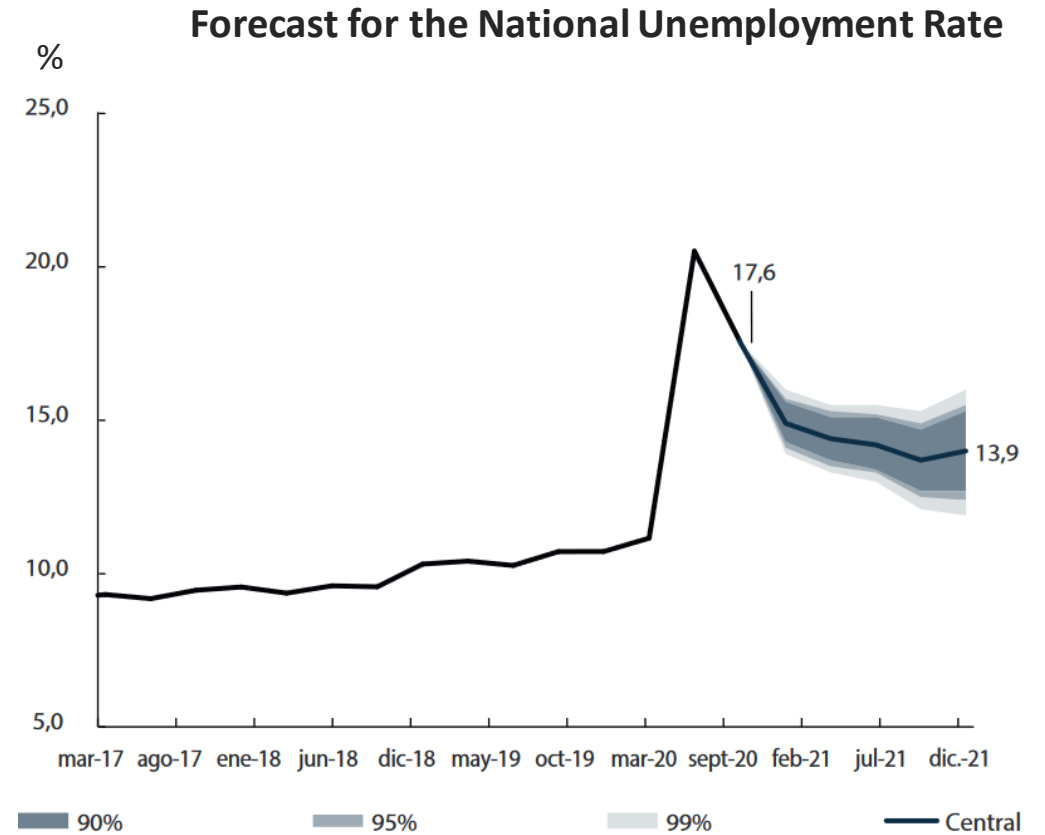
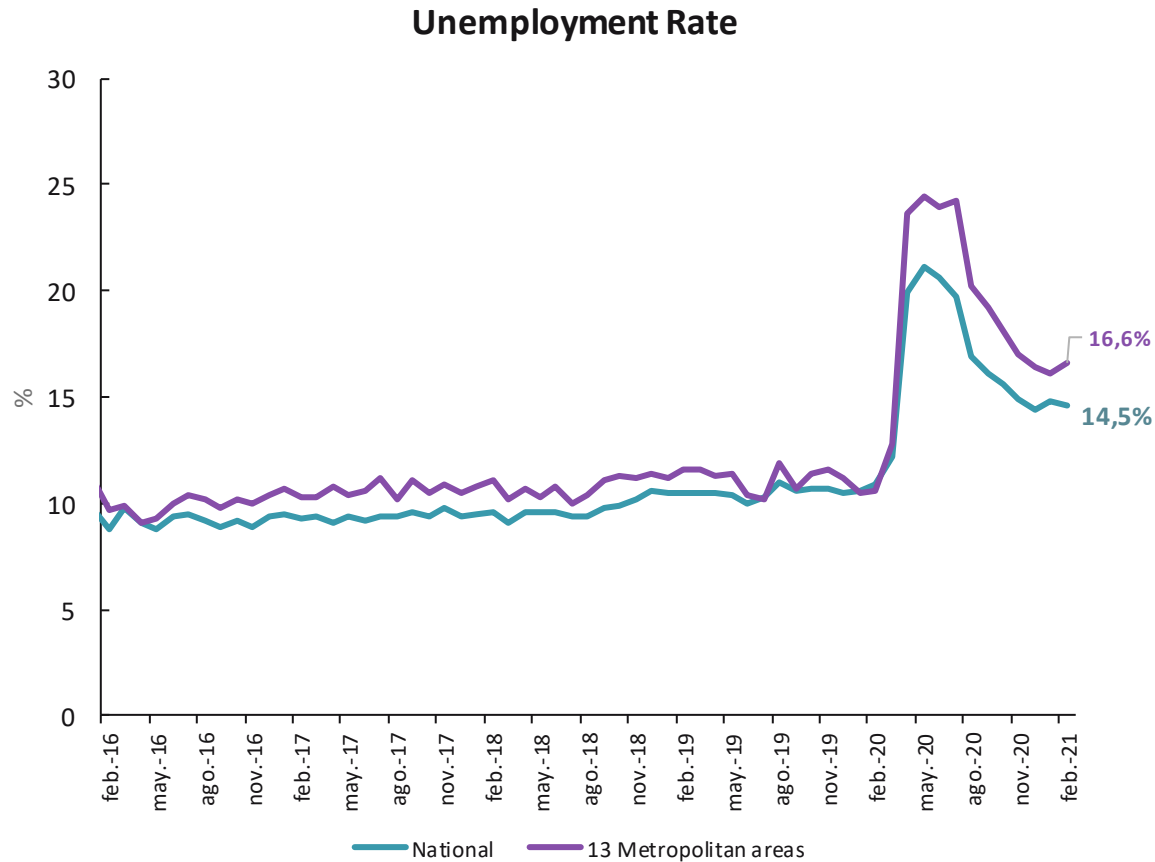
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POLICY CHALLENGES

- The Central Bank's staff estimates a growth rate between 2.0% and 6.0% for 2021. **The latest point estimate for growth in 2021 is 5.2%**
- **The shock has both supply and demand effects.** The impacts on the latter have prevailed, which can be seen in the large negative output gap.
- **Gradual convergence of economic activity toward pre-pandemic levels is expected.** Output is estimated to reach pre-pandemic levels in 2022.

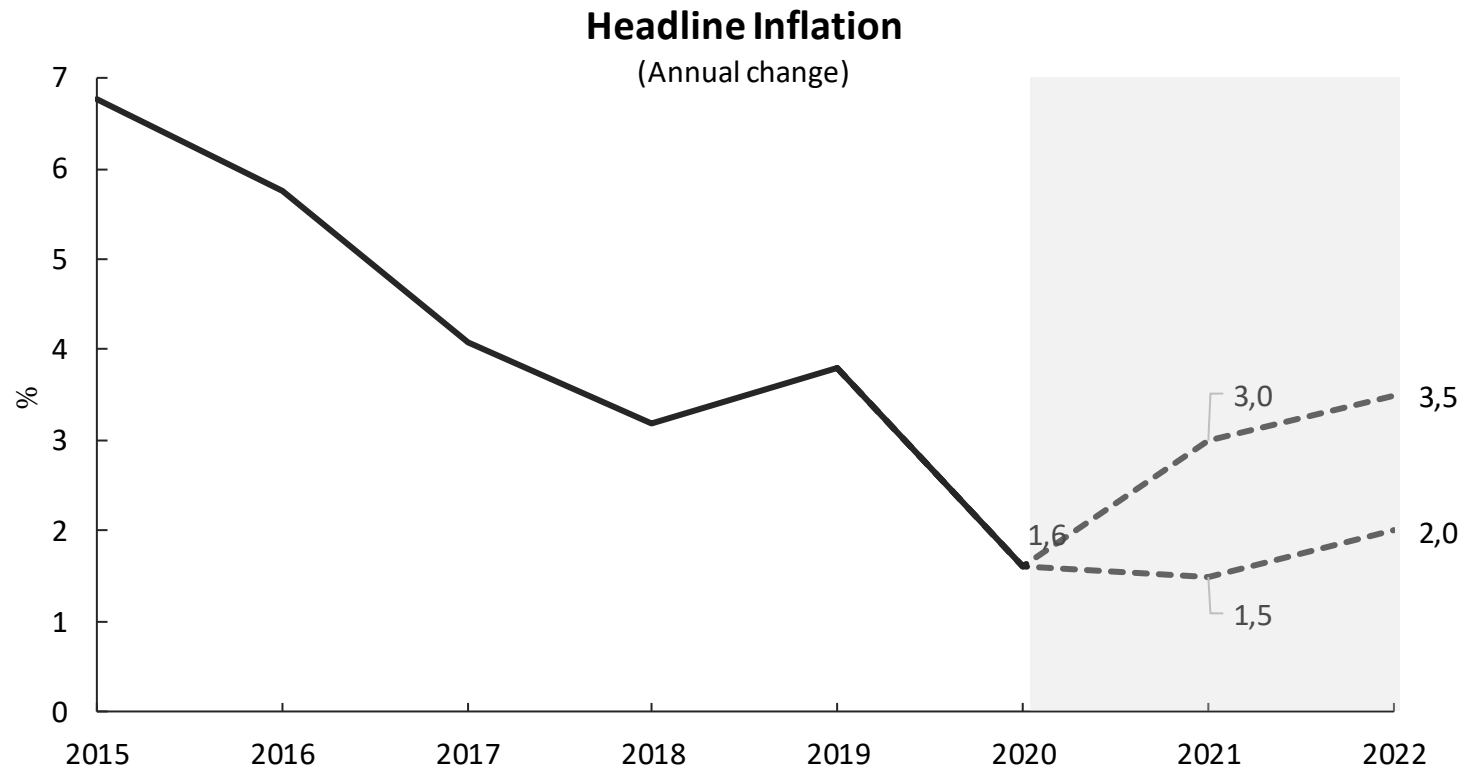


- **The labor market has partially recovered**, but it keeps showing significant slack.
- Forecasts from the Central Bank's staff suggest that the unemployment rate will continue falling at a moderate pace throughout 2021.



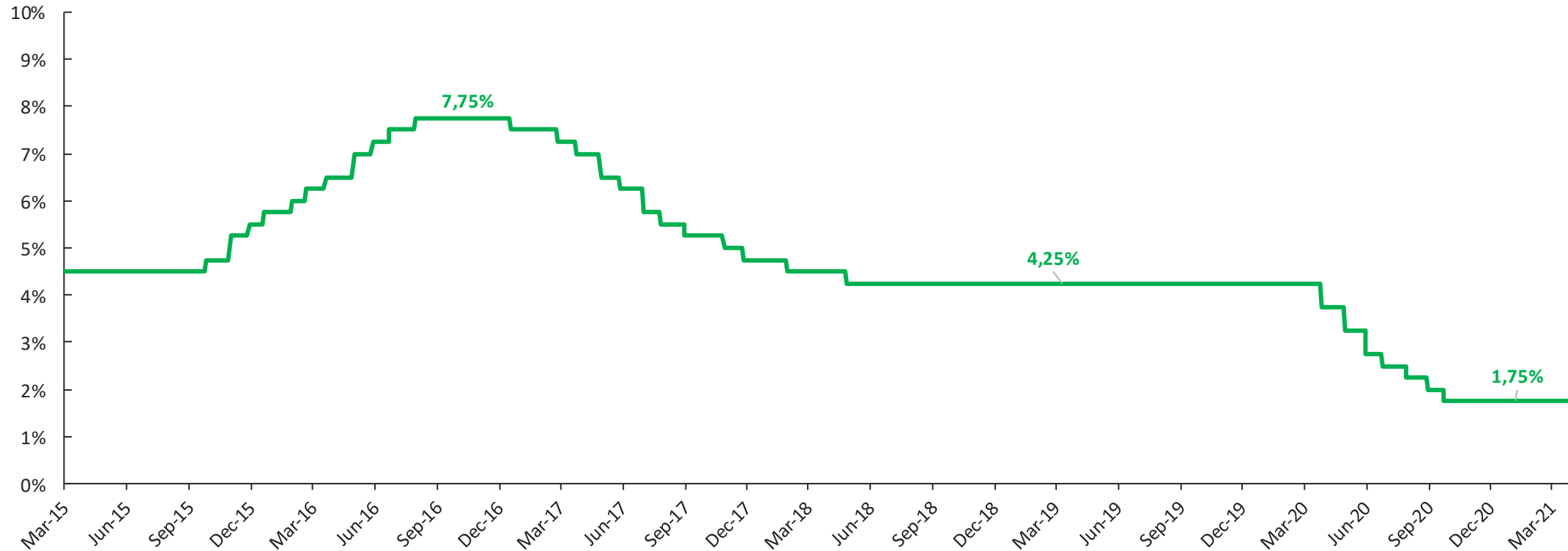
Note: seasonally adjusted series.
 Source: DANE; calculations by *Banco de la República*.

- Because of the demand shock and price relief measures, in 2020 inflation was below the Central Bank's target. **Inflation should converge to the 3.0% target in the next two years**

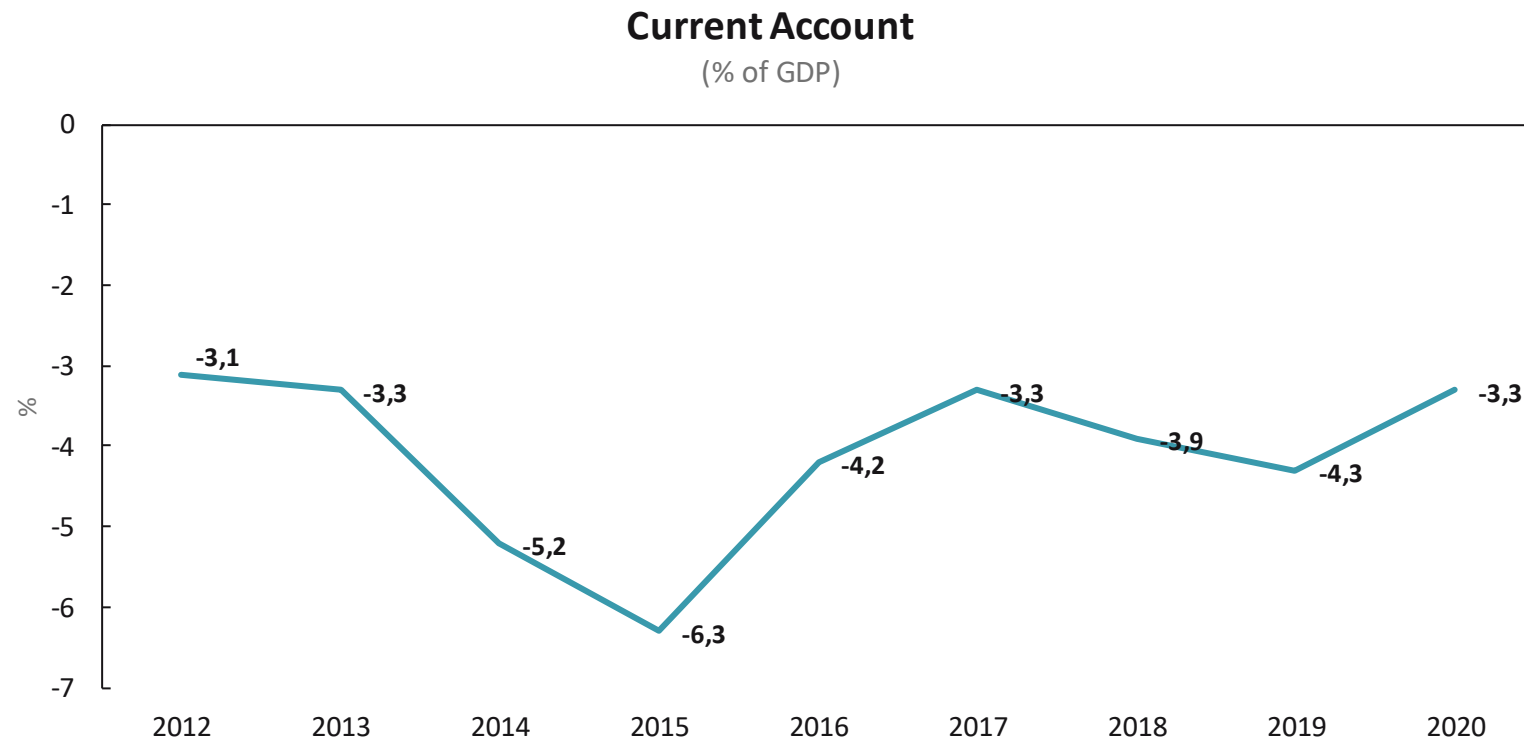


- Given the sizeable excess capacity and projected core inflation below target, **the central bank has set an expansionary monetary policy stance.**
- Due to the unprecedented nature of the shock and the variable external context, the macroeconomic forecast and monetary policy response are very uncertain.

Monetary Policy Rate



- **In 2020, the external deficit contracted**, in line with a lower domestic demand.
- Domestic demand is expected to recover in 2021...
- ... Hence, although in 2021 global recovery will support a higher external demand and better terms of trade, **the current account deficit is expected to increase slightly**.





Content

CONTEXT

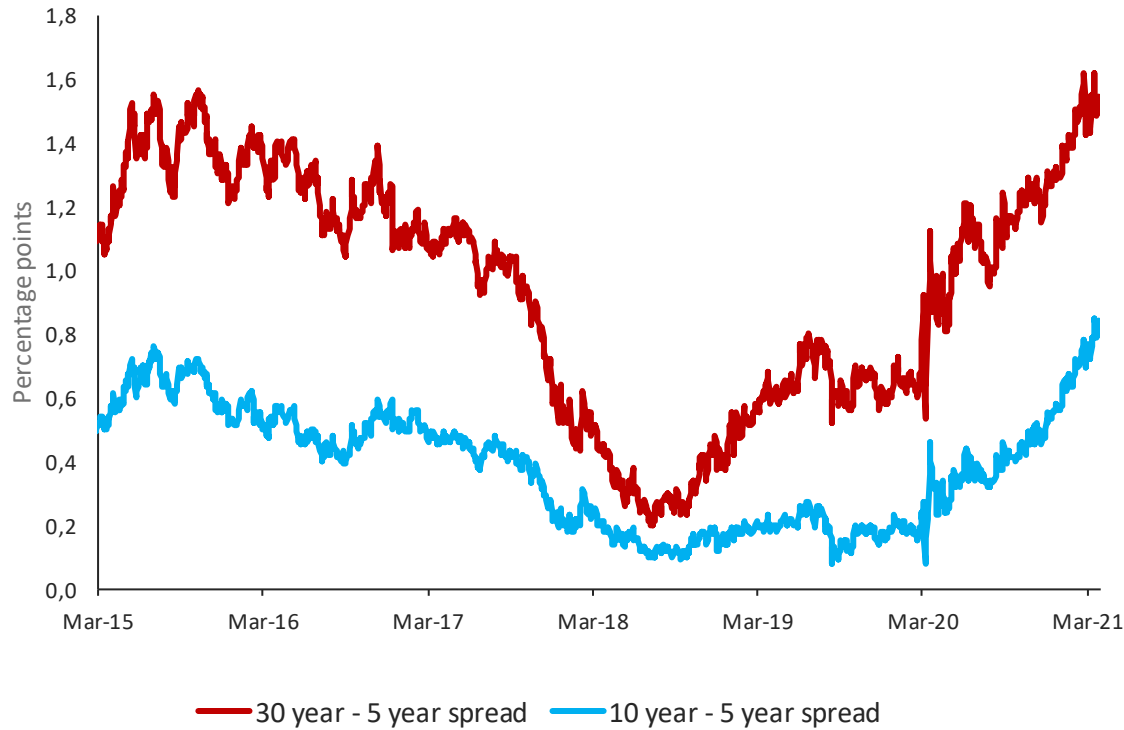
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POLICY CHALLENGES

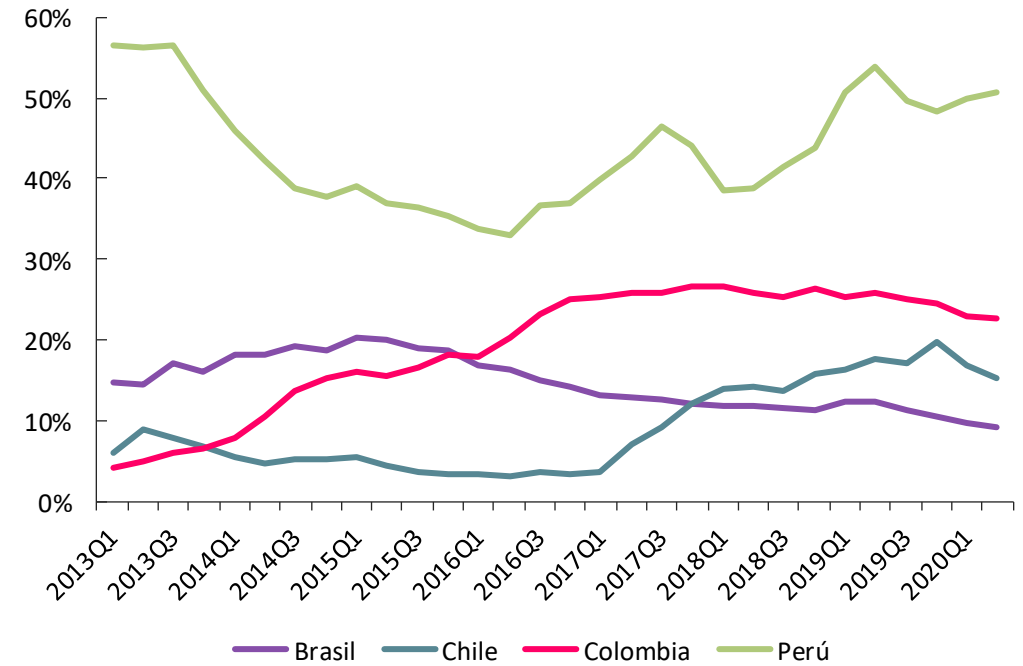
- **The Central Bank of Colombia has adopted a gradual approach in its monetary easing,** providing a sustainable level of stimulus to support the recovery. There is high uncertainty regarding:
 - **The relative size and evolution of aggregate supply and demand effects** caused by the pandemic.
 - **External financial conditions.** Expected inflation and the effects of fiscal policy in the U.S. may alter financial conditions.

Slope of the U.S. Treasuries Curve

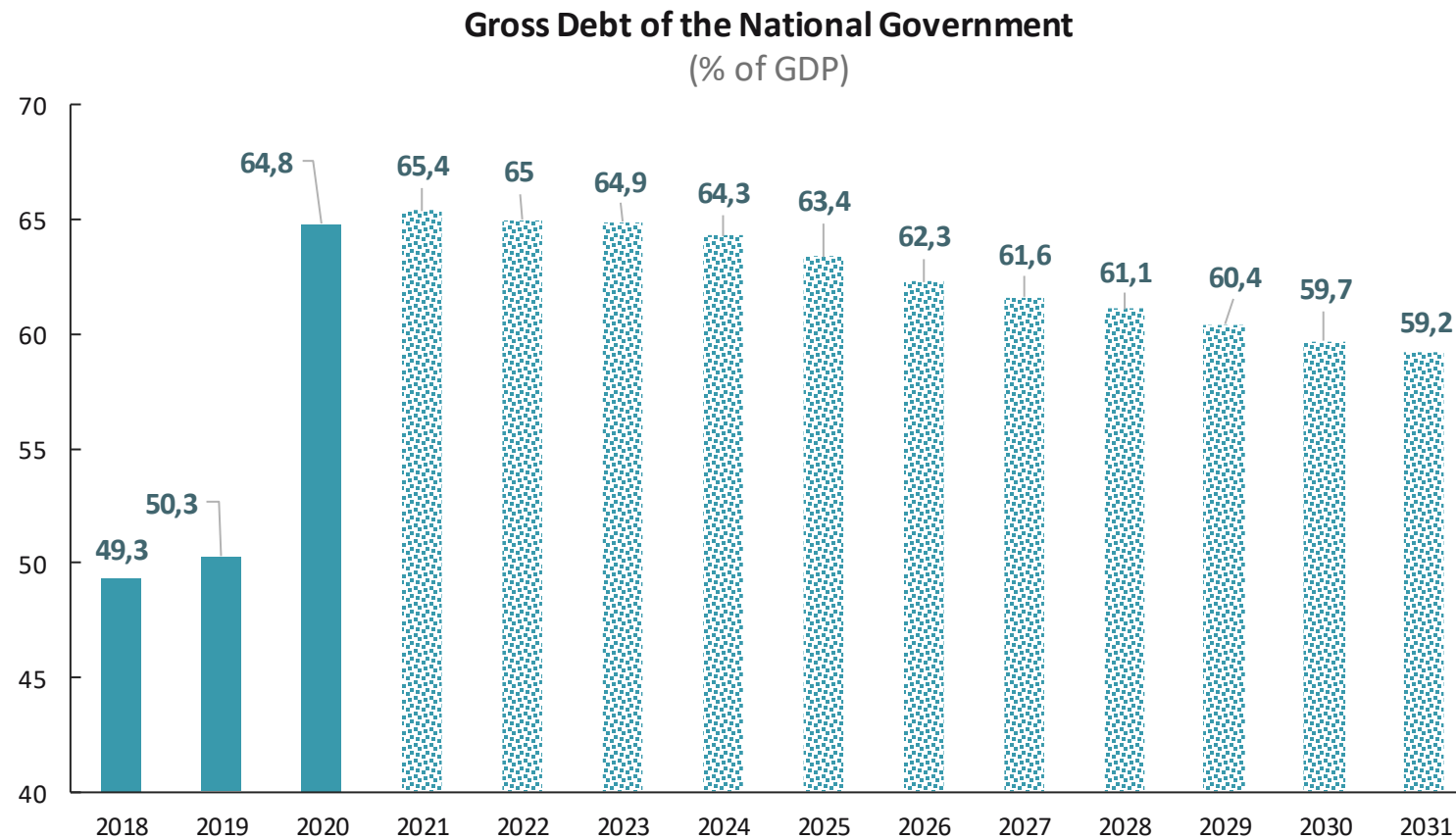


Foreign Participation in the local Currency Bond Markets

(Foreign holdings as a percentage of outstanding)



- **The pandemic caused a significant increase in the level of public debt.** The government has announced a fiscal adjustment equivalent to 1,5 % of GDP.
- According to the Financial Plan, this adjustment, together with better tax collection, should bring public debt below 60% of GDP by 2030.



- The gradual reduction of public debt ratios is important for the operation of countercyclical monetary policy.

			Inflation Expectations**		Public Debt (% of GDP)		Real Ex-ante Interest Rate	
Country*	Monetary Policy Rate	Inflation Rate	One-year Ahead	Two-year Ahead	2019	2020	One-year Ahead	Two-year Ahead
Chile	0.5	2.8	3.0	3.0	27.91	32.81	-2.5	-2.5
Peru	0.25	2.68	2.3	2.5	27.12	39.48	-2.05	-2.25
Mexico	4.0	3.76	3.51	3.50	53.75	65.54	0.49	0.5
Colombia	1.75	1.51	2.87	3.12	50.30	64.80	-1.12	-1.37
Indonesia	3.5	1.38	2.3	3.0	30.49	38.48	1.2	0.5
Hungary	0.6	3.1	3.2	3.2	66.34	77.42	-2.6	-2.6
South Africa	3.5	2.9	4.2	4.4	62.15	78.82	-0.7	-0.9
Brazil	2.75	5.2	4.81	3.51	89.47	101.4	-1.96	-0.76
Turkey	19	15.6	10.5	9.05	32.99	41.67	8.5	9.95

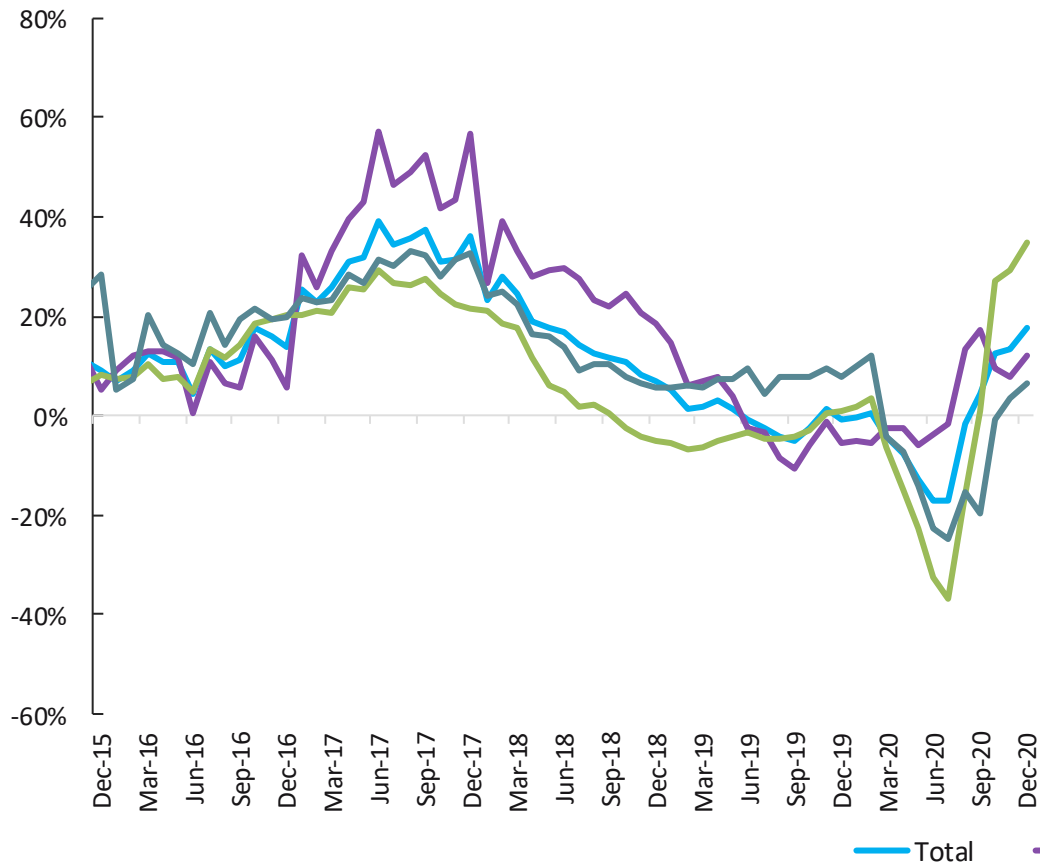
Source: central Banks, IMF and Fitch Ratings.

*Countries are ordered according to their credit rating. Green are all A-rated countries (A+, A and A-), Pink are all BBB countries, purple are all BB and red are B-rated'.

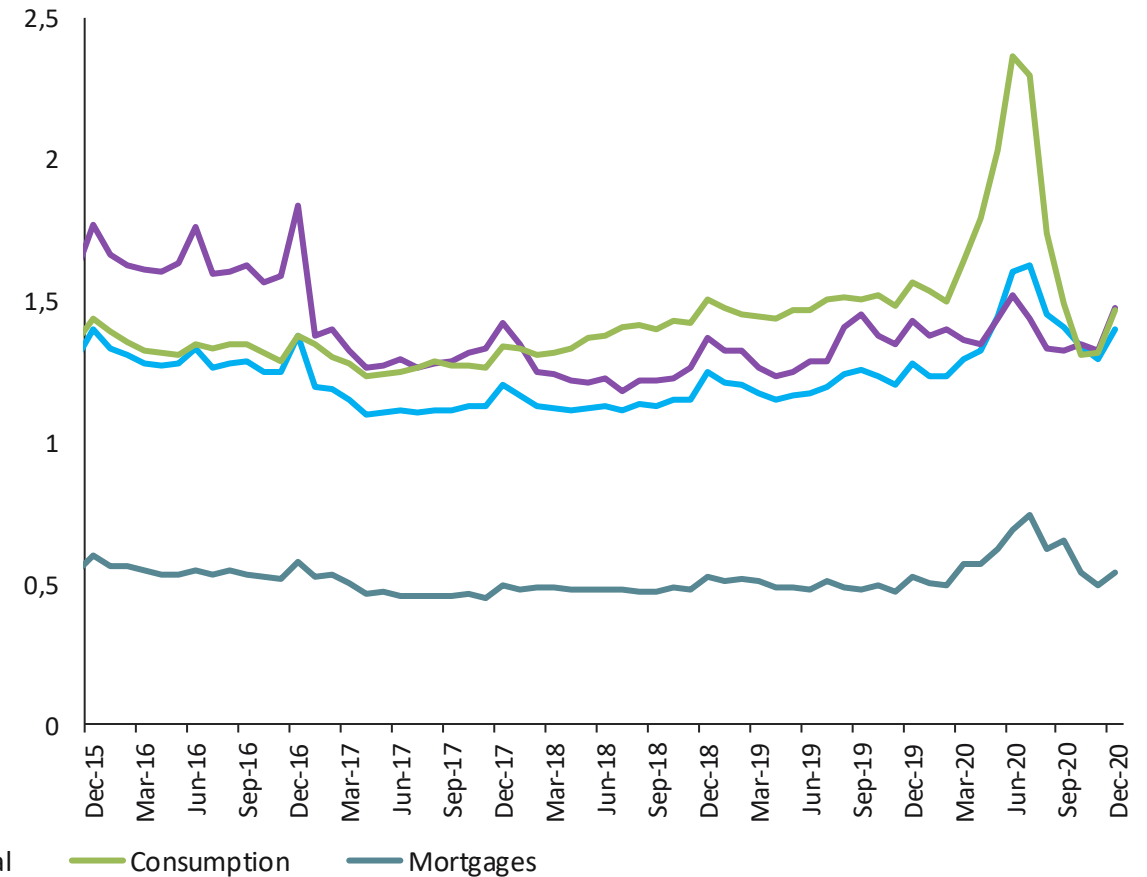
** Inflation expectations are based on surveys. Inflation expectations: México, Brasil, Chile, Perú, Turquía, Sudáfrica, Hungría, Colombia). Inflation expectations for Indonesia are for year-end 2021 and year-end 2022, they are taken from FocusEconomics' consensus forecast.

- In line with the economic slowdown, **deterioration of the loan portfolio is expected.**
- **Banking institutions have increased their provisions** in order to manage this risk.

Non-performing loans - Annual Growth Rate

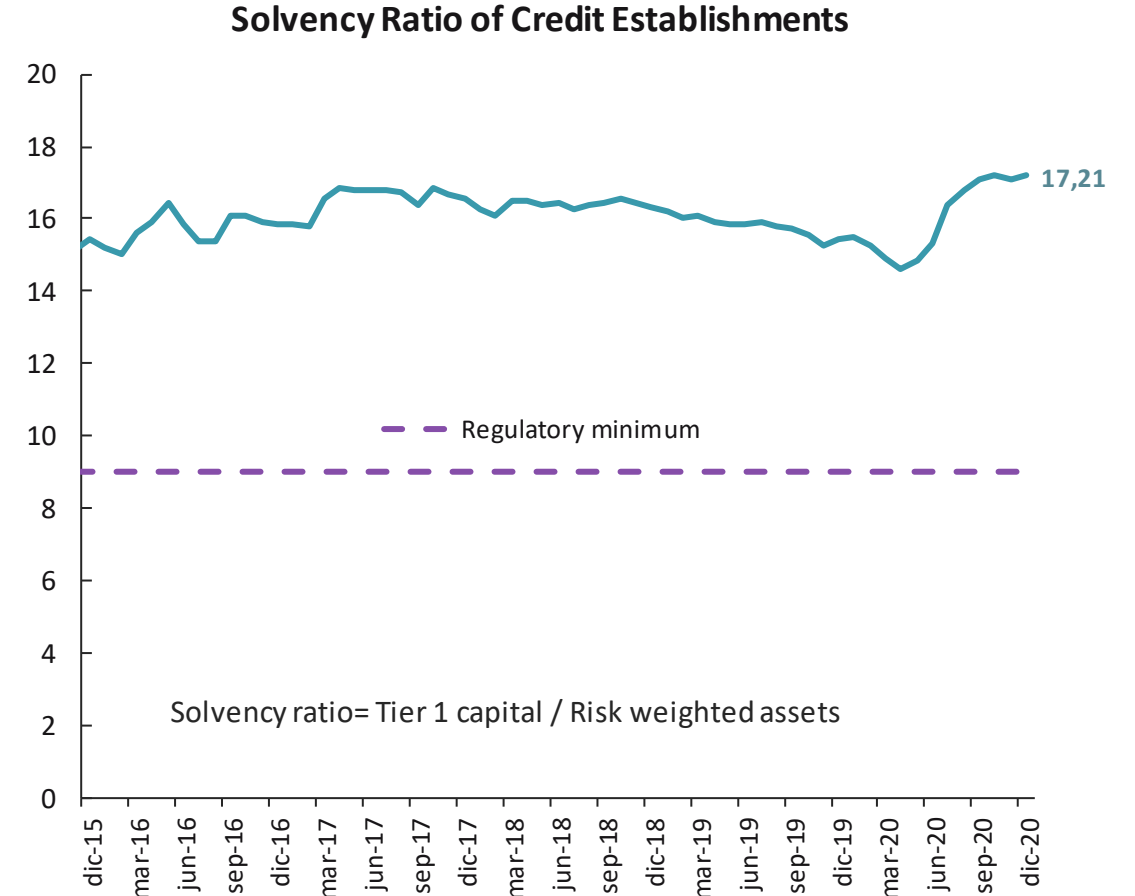
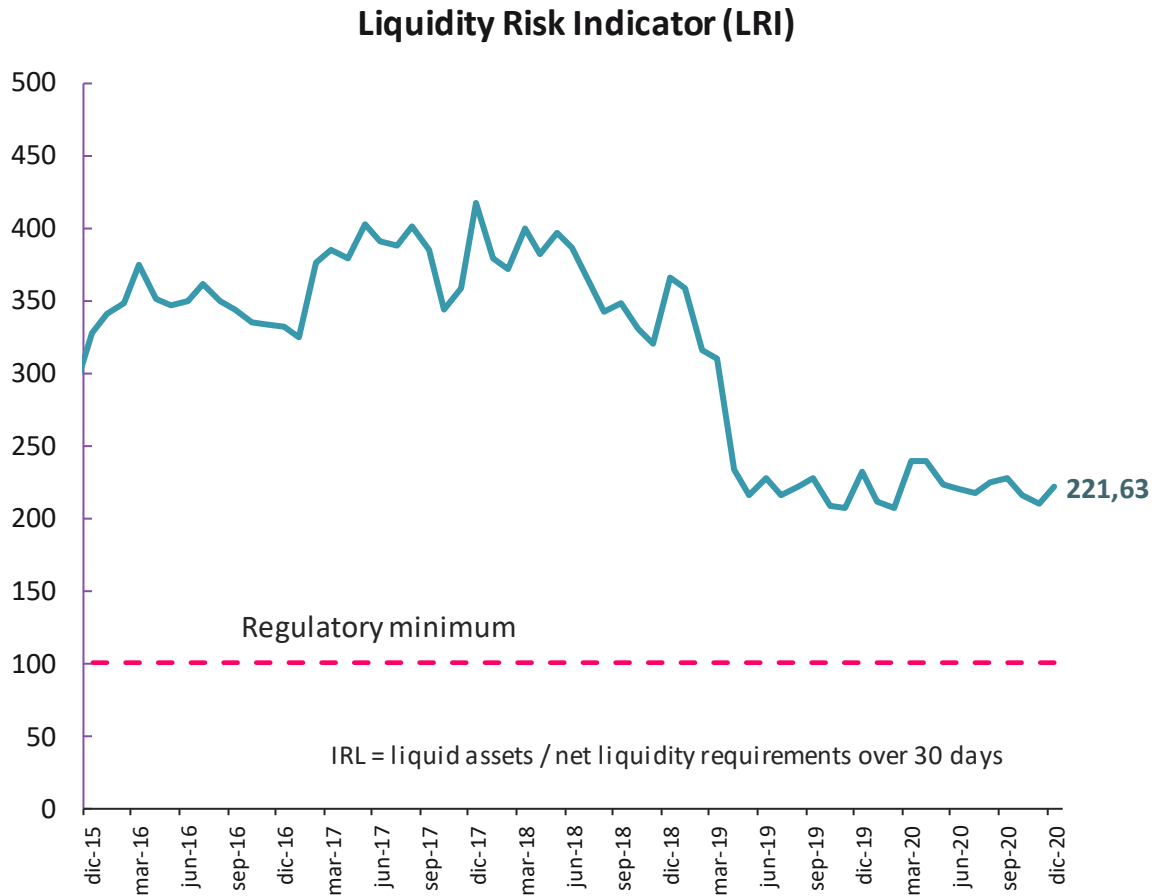


Provisions over non-performing loans



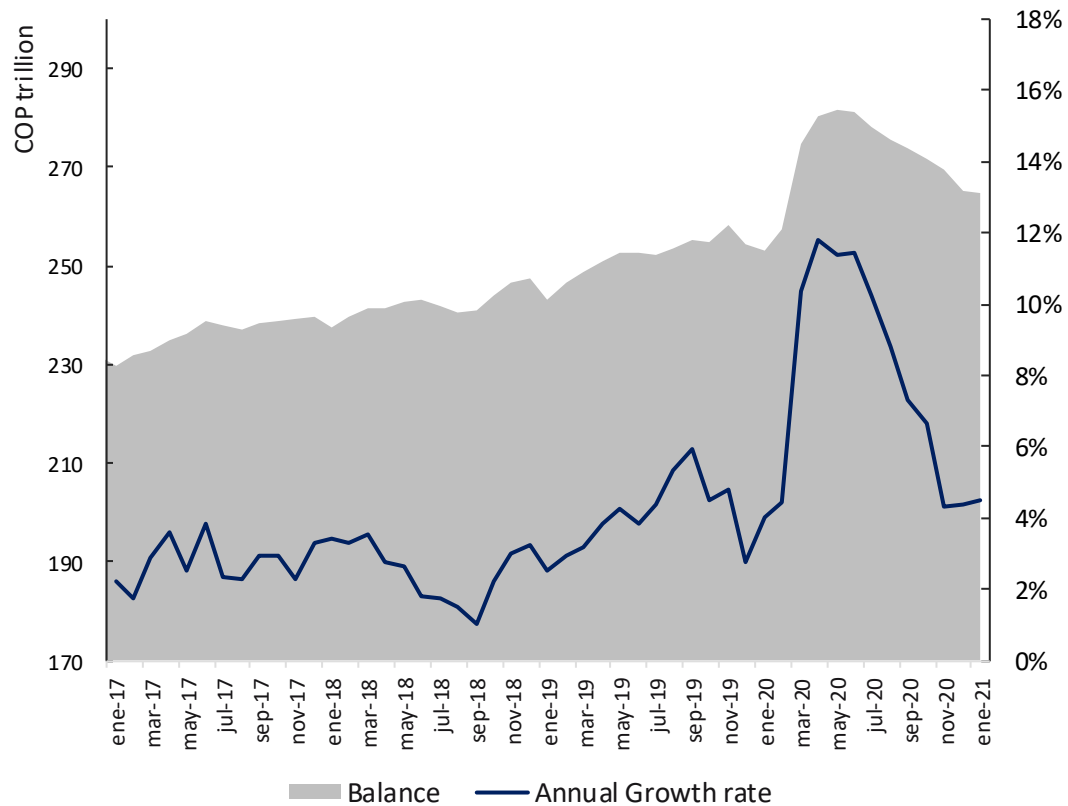
Source: Office of the Financial Superintendent. Calculations by Banco de la República.

- Despite of this, solvency and liquidity levels of financial intermediaries remain above regulatory limits.

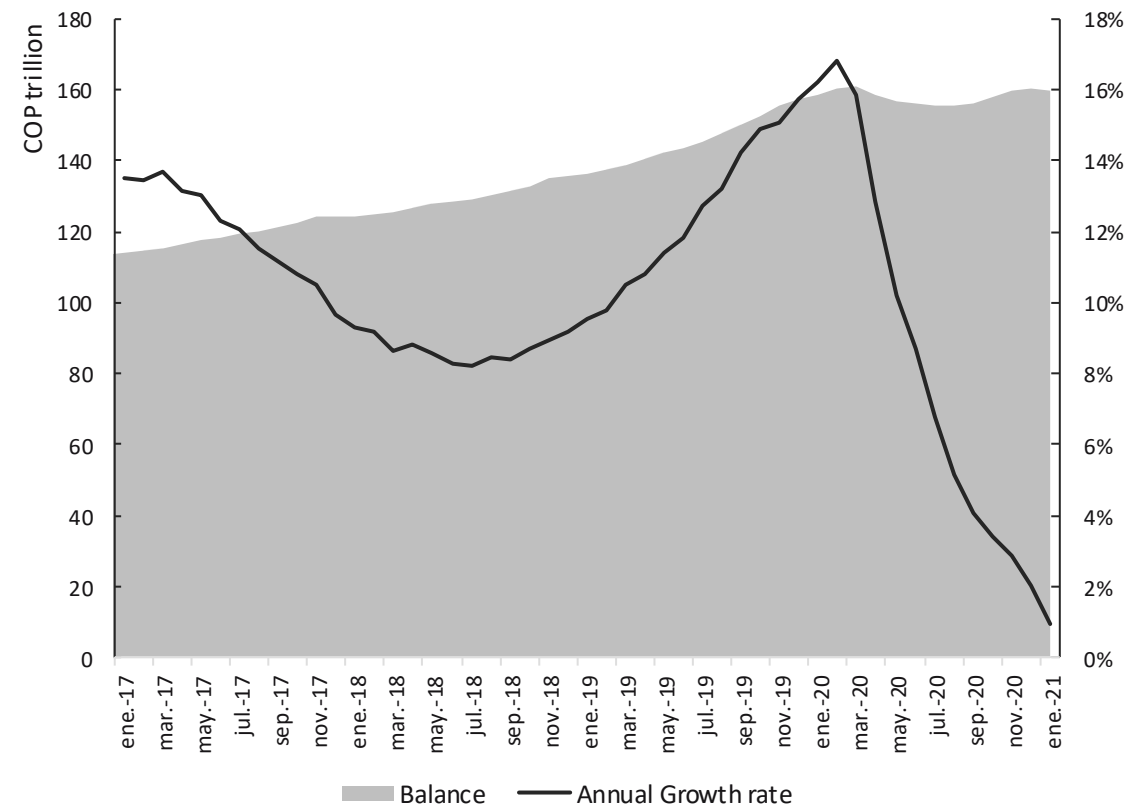


- **And, despite the size of the macroeconomic shock, financial intermediation has continued smoothly.**
- The growth of the loan portfolio has decelerated but remains positive in nominal and real terms.

Commercial Loan Portfolio



Consumption Loan Portfolio



Source: Office of the Financial Superintendent. Calculations by Banco de la República.