PRESENTATION, SUMMARY AND CONCLUSIONS

✠ Inflation for 1999 as measured by the Consumer Price Index (CPI) stood at 9.2% in December, 0.1 percentage points lower than at the end of the third quarter. This reduction was produced after annual consumer inflation had risen in November by 0.4 percentage points. The annual inflation rate in December is the lowest since 1970, when it was 6.6%. It is also 7.5 percentage points lower than inflation for 1998 and 5.8 percentage points under the target for 1999. Producer inflation as measured by the Producer Price Index (PPI) was 12.7%, down by 0.8 percentage points on 1998. The annual change in PPI increased substantially between June (6.1%) and December (12.7%), largely because of the price behavior in farming, forestry and fishing, which burgeoned from a 6.0% shrinkage in July to an 11.7% expansion in December.

✠ December 1999 was the eighth month running with single-digit consumer inflation. Inflation decreased across the whole basket of goods and services, notably in housing (from 16.6% in December 1998 to 5.8% a year later), education (from 17.3% to 10.2%), and food (from 15.7% to 7.5%).

✠ Consumer price growth in 1999 was higher than average in transport (18.7%), sundry expenditures (16.1%), and health care (15.1%). Higher gasoline prices, the application of VAT to toiletries, and devaluation account for the price increases in these groups. Inflation was lower than average for clothing (3.1%), housing (5.8%), and food (7.5%), in the case of food thanks to an abundant supply of farm produce, especially in the first half of 1999. Under the alternate CPI classification, price increases were higher than average for tradables (10.0%) because of devaluation, and for indexed nontradables (10.2%) partly because of the gradual phasing out of public-service subsidies.

✠ The different measures of core inflation slowed in annual growth throughout the year except in November. In December their average (9.1%) fell by 0.9 percentage points relative to the third semester and by 0.5 percentage points relative to November. Two of the measures, CPI excluding food (10.0%) and the nucleus (9.8%), continued to run higher than observed inflation, as they had been doing since March.

✠ Data available to date on the various indicators of the real sector of the economy suggest that output continued to contract in the fourth quarter relative to the same period in 1998. However several developments point to its expansion relative to the third quarter of 1999, notably: increased power consumption and slightly higher credit-card sales in December, slower contraction in fourth-quarter imports, and growth of total and non-traditional exports in November. Satisfactory performance of industrial orders in the second half of 1999 through to November, and gradual reduction of inventories over the same period suggest an upturn in output in 2000. Given the magnitude of last year's accumulated contraction and the low levels of installed-capacity utilization, no inflationary pressures are expected to arise this year from excess demand.

✠ The 20-month moving average of the monetary base was above the indicative corridor's ceiling at the end of December because of increased demand for cash and reserves, caused by people's fears about the Y2K problem. It should be pointed out however that this large increase in the monetary base at the end of last year was quickly reversed in the first weeks of this year. The real value of outstanding debt continued to shrink during the fourth quarter at much the same rate as at the end of the third. Lastly, fourth-quarter nominal and real deposit rates were, on average, lower than the third quarter's, while nominal and real lending rates remained relatively stable.

✠ Structural and time-series models suggest that inflation will be running between 8% and 10% by the end of 2000 and may continue to fall in 2001, ending the year about 2 percentage points lower relative to that range. Forecasting by the item-projection methodology bears out the results obtained by statistical models for the year 2000. This suggests that the 10% target is very likely to be met and even that, barring negative supply shocks, the likelihood of reaching lower-than-target rates is not negligible.

✠ Higher unemployment during 1999 has prevented public opinion from fully appreciating the potential benefits of the successfully achieved one-digit inflation. The reduction in inflation will mean fewer distortions in the economy, greater efficiency in resource allocation, and a decrease in unjustified revenue transfers. This is expected to result in faster long-term growth of the economy and in improvement of the population's welfare. The country should understand the importance of gains of this kind and parlay the inflation decrease of 1999 into a low future inflation that remains steady at around developed-country levels.

In view of the foregoing and considering interest-rate trends in the market, the Board of Directors of Banco de la República has decided not to alter the current levels and structure of the Bank's intervention rates of interest.

The Board of Directors,

Chairman
Juan Camilo Restrepo Salazar
Minister of Finance and Public Credit

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