

Economics Colombia

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Colombia: BanRep delivers a hawkish surprise amid persistent inflation pressures

At its September 30 meeting, the Board of Directors of Banco de la República surprised both market participants and our expectations by raising the policy rate by 25bps to 12.25%, after having remained on hold in the previous meeting. The decision was supported by four board members, including the Minister of Finance, while two members voted to keep rates unchanged and one favored a larger 50bps increase. According to both the policy statement and the press conference, the Board's focus shifted back toward inflation, reflecting growing concerns that a series of supply-side shocks could exert upward pressure on both inflation and inflation expectations. While policymakers acknowledged the resilience of economic activity during the second quarter, they also highlighted more recent indicators, including the July Monthly Economic Activity Index (ISE), manufacturing production and retail sales, which suggest that economic growth has begun to moderate.

The Board also emphasized the tightening of global financial conditions, noting higher observed and expected interest rates in advanced economies. In this regard, Colombia has diverged from other countries such as Mexico and the United Kingdom, whose central banks opted not to raise their interest rates after the Federal Reserve's 25bps rate increase in mid-September.

Among the key upside risks to inflation identified by policymakers were the ongoing El Niño phenomenon, particularly through its impact on agricultural production and food prices, the reconstruction process following the August 10 earthquake, and fiscal policy developments. On the latter, both Finance Minister Miguel Gómez and Governor Leonardo Villar viewed the government's fiscal adjustment efforts favorably. In their assessment, fiscal consolidation helps reduce pressure on domestic demand and inflation while improving the overall policy mix and strengthening coordination between fiscal and monetary authorities.

Making his first monetary policy decision as Finance Minister, Miguel Gómez stressed that reducing inflation is a central government objective given its disproportionate impact on lower-income households. He also underscored the inflationary implications of higher oil prices stemming from geopolitical tensions, arguing that these effects are transmitted not only directly through fuel prices but also indirectly through a broad range of goods that use petrochemical products as production inputs. The minister further noted that elevated inflation increases public expenditure, establishes a higher benchmark for minimum wage negotiations and complicates fiscal consolidation efforts. In this context, he publicly supported the 25bps

rate hike, arguing that it contributes to achieving the inflation target without prematurely discounting future inflation developments.

Governor Leonardo Villar noted that reconstruction efforts following the earthquake should support economic activity in the affected regions over the coming quarters. He also reiterated that interest rate cuts will become appropriate only once policymakers gain sufficient confidence that inflation is converging toward target.

According to the central bank's current projections, inflation is expected to return to the 3% target in 2028. Regarding exchange rate dynamics, Villar emphasized that pass-through effects to inflation remain relatively limited and occur with significant lags, although they could become more relevant if domestic demand conditions change.

One notable aspect of this meeting was the absence of discussion regarding the international reserve accumulation program announced in July. The Board also refrained from commenting on the appreciation of the Colombian peso, which had been an important consideration behind the decision to keep rates stable at the July meeting. Similarly, there was no reference to the widening current account deficit recorded during the second quarter, a variable that has historically received considerable attention given its close relationship with domestic demand dynamics.

With the information currently available, we continue to view this increase as the final rate hike of the tightening cycle. Our baseline scenario remains one in which policy rates stay at restrictive levels for an extended period before gradually declining. Assuming inflation peaks in December 2026 and resumes a sustained downward trajectory thereafter, we expect the Board to begin cutting rates around mid-2027, likely between June and July, when inflation expectations should once again fall within the central bank's tolerance range around the 3% target. Nevertheless, risks remain skewed toward a more hawkish outcome. The tone of the policy statement, the clear commitment of the new Finance Minister to restoring price stability, the stronger alignment between the government and the central bank, and Governor Villar's emphasis on securing clear evidence of inflation convergence before considering rate cuts all suggest that policymakers may be willing to maintain restrictive monetary conditions for longer.

The next key events for monetary policy will be the release of the meeting minutes on October 5th, the Federal Reserve's policy decision on October 28th, and Banco de la República's next rate-setting meeting on October 30th.

Macroeconomic forecast DAVIbank Economics Colombia

Forecast	2019	2020	2021	2022	2023	2024	2025pr	2026pr	2027 pr
National Accounts									
Real GDP growth (yearly %)	3.2	-7.2	11.1	7.6	0.9	1.5	2.6	2.5	2.3
Domestic demand (y/y. %)	4.0	-7.5	13.8	10.5	-2.3	1.6	3.9	3.9	2.8
Consumption (y/y. %)	4.3	-4.3	14.1	9.5	0.7	1.4	4.4	4.1	2.3
Private (y/y. %)	4.0	-5.0	15.3	11.1	0.6	1.6	3.5	3.2	2.5
Government (y/y. %)	5.5	-0.9	10.3	2.2	1.1	0.0	8.3	9.5	1.4
Gross capital formation (y/y. %)	3.2	-7.2	11.1	7.6	0.9	1.5	2.6	3.2	5.9
Exports (y/y. %)	3.3	-22.3	15.7	13.6	3.1	0.3	1.8	0.1	1.7
Imports (y/y. %)	7.7	-19.8	28.5	25.0	-9.8	1.3	8.8	3.0	3.7
Laboral Market									
Unemployment (%. Average)	10.9	16.7	13.8	11.2	10.2	10.2	8.9	9	9.4
Balance of Payments									
Trade Balance (USD\$. B)	-14.15	-13.10	-20.00	-16.10	-7.81	-9.77	-14.89	-16.61	-19.91
Exports (USD\$. B)	51.3	38.2	50.9	73.5	68.7	69.1	71.5	79.22	82.1
Imports (USD\$. B)	65.5	51.3	70.9	89.6	76.5	78.9	86.3	97.05	103.10
Current account (USD\$ Balance. B)	-14.81	-9.27	-17.95	-20.88	-8.32	-7.10	-11.02	-13.4	-16.18
Current account (% of GDP)	-4.6	-3.4	-5.6	-6.0	-2.3	-1.7	-2.4	-2.3	2.7
Prices. Rates & Exchange Rates									
CPI (y/y. %. End of period)	3.80	1.61	5.62	13.12	9.28	5.20	5.10	6.91	5.06
CPI (y/y. %. Average)	3.52	2.53	3.49	10.15	11.77	6.63	5.14	6.05	5.31
CPI without food (y/y. %. End of period)	3.45	1.03	3.44	9.99	10.33	5.60	5.11	6.21	4.43
COP (\$. End of period)	3297	3422	4077	4850	3902	4405	3780	3290	3487
COP (\$. Average)	3281	3694	3766	4254	4322	4153	4052	3422	3397
BanRep's rate (%. End of period)	4.25	1.75	3.00	12	13.0	9.50	9.25	12.25	11
Tax Codes*									
Net Debt of CNG (% of GDP)	48.4	60.7	60.1	57.6	53.4	59.3	58.5	59.7	66.2
Primary Balance of CNG (% of GDP)	0.4	-5.0	-3.6	-1.0	-0.3	-2.4	-3.5	-3.3	-4.5
Deficit of CNG (% of GDP)	-2.5	-7.8	-7.1	-5.3	-4.3	-6.8	-6.4	-7.2	-9.4

*Source: 2027 National Budget.

Source: DAVIbank Economics Colombia.

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