

Economics Colombia

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Colombia Monetary Policy Preview: BanRep expected to keep rates unchanged amid a more complex risk balance

On Wednesday, September 30th, the central bank will hold a new monetary policy meeting to set the interest rate. After delivering a surprising 75 bps hike in April, economists and market participants broadly anticipated an additional 50bp increase in July. Instead, the Board opted to keep the policy rate unchanged at 12.0%, marking another deviation from consensus expectations. **According to the minutes, the decision was largely influenced by concerns regarding the strength of the Colombian peso and its implications for export competitiveness and financial stability. The Board simultaneously announced a new international reserve accumulation program of up to USD 4 billion through FX put options.** Under the program, options can only be exercised when the daily exchange rate reference (TRM) is below its 20-day moving average. The central bank sought to accumulate USD 400 million per month in both August and September. While the August target was fully achieved, appreciation pressures eased during September, causing the exercise condition to remain non-binding for much of the month. As of the latest available data, reserve accumulation through the program totals USD 296.3 million in September. July's meeting was also the last attended by former Finance Minister Germán Ávila.

The July vote split was 4 to 3 in favor of keeping rates unchanged, breaking the pattern observed in previous meetings. Nevertheless, the minutes suggest that at least one board member who voted for unchanged rates remained open to supporting further hikes should inflationary pressures intensify.

Several developments since July's meeting could alter the Board's assessment of risks ahead of this month's decision. **First, this will be the first interest rate decision under the participation of the new Finance Minister, Miguel Gómez.** Historically, finance ministers have tended to occupy the more dovish side of the Board. Consequently, investors will closely monitor the minister's first policy signals regarding his assessment of economic conditions, inflation risks, and the appropriate degree of monetary restraint. **Second, Colombia has faced a series of adverse supply shocks in recent months.** The August 10 earthquake, widespread wildfires across several regions, and the initial effects of El Niño on the energy and agricultural sectors have increased uncertainty regarding both inflation dynamics and economic activity in the coming quarters. **Third, second quarter GDP and balance of payments data highlighted the resilience of domestic demand during the first half of the year.** Both annual GDP growth and the current account deficit reached 3.5% of GDP in the second quarter. Strong public expenditure associated with the presidential elections, higher government payroll spending, and temporary consumption effects linked to the FIFA World Cup contributed to this performance.

While these data portray an economy that remained robust through mid-year, some signs of moderation have begun to emerge. August's Economic Monitoring Indicator (ISE) expanded by only 1.1% y/y, suggesting a gradual fading of the temporary factors that boosted growth earlier in the year.

Inflation developments have also strengthened the case for maintaining a restrictive monetary policy stance. Annual inflation accelerated from 6.03% in July to 6.24% in August, exceeding market expectations. The upside surprise was driven primarily by food and regulated prices, while services' inflation remained highly persistent, particularly in housing related components. Inflation expectations have also moved higher since the July meeting. Consensus forecasts now place year end inflation at 6.77%, while one- and two-year ahead expectations stand at 5.43% and 4.13%, respectively, remaining above the central bank's 2% to 4% target range.

The external backdrop has become less supportive as well. US Treasury yields have risen sharply, with the 10 year Treasury yield surpassing 5%. Oil prices have returned above USD 100 per barrel, and the Federal Reserve resumed its tightening cycle with a 25bp increase, bringing the federal funds rate to 3.75%-4.00%. Meanwhile, Colombia's sovereign risk premium continues to reflect investor confidence in the fiscal adjustment plans of the new administration, although volatility increased following the publication of the 2027 National Budget, which projects a fiscal deficit equivalent to 9.4% of GDP. Despite the initial market reaction, investors have largely interpreted the budget as a realistic recognition of fiscal constraints rather than a signal of materially looser fiscal policy.

While recent supply shocks and the inflation outlook would ordinarily support additional monetary tightening, we believe the economic and social consequences of the August earthquake, as well as the still strong exchange rate could lead the Board to adopt a more cautious approach. Consequently, we expect Banrep to leave the policy rate unchanged at 12.0% at its September meeting. This view is consistent with the latest survey of economic analysts conducted by the central bank, which points to rate stability this month, although respondents continue to anticipate an additional 25bp hike before year end.

Over the medium term, we believe the current 12.0% policy rate provides an appropriate balance between upside inflation risks and downside risks to economic activity. Under our baseline scenario, the policy rate would remain unchanged until July 2027, when inflation expectations should display a clearer convergence toward the 2% to 4% target range. As a result, we expect the policy rate to end 2026 at 12.0% and gradually decline to 11.0% by the end of 2027.

Key points to consider ahead of Septembers' meeting:

- **The technical staff of the Banco de la República revised its inflation forecasts upward relative to the April Monetary Policy Report, raising the end-2026 projection to 6.9% from 6.4% and the end-2027 projection to 4.3% from 3.7%.** The revision was driven mainly by higher projected food inflation, which increased to 9.0% from 7.1% for 2026, and regulated-price inflation, which rose to 7.1% from 6.1%, reflecting supply shocks, the incorporation of a strong El Niño scenario, and higher projected utility tariffs. Core inflation was revised slightly lower for 2026, to 6.2% from 6.3%, but higher for 2027, to 4.2% from 3.8%. On activity, GDP growth forecasts were revised to 2.5% for 2026, from 2.4%, and to 1.9% for 2027, from 2.1%, while the estimated output gap for 2026 increased to 0.4% from 0.3%.
- **Economic activity remained resilient in Q2, with GDP expanding 3.5% y/y, above expectations, supported mainly by temporary demand factors including election-related public spending, public wage increases and FIFA World Cup effects.** From the production side, public administration was the largest contributor, growing 10.0% y/y and adding 1.7pp to GDP growth, while leisure expanded 9.5%, financial services 8.7%, mining 4.2% and commerce 2.2%. Construction returned to positive territory for the first time since 2024, increasing 2.2%, although agriculture contracted by 2.1%. On the demand side, final domestic demand accelerated to 4.9% y/y, driven by a 12.2% increase in government consumption, 2.8% growth in household spending and a 7.0% expansion in fixed investment, while imports rose 7.5% and exports declined 1.0%, reflecting strong domestic demand and a stronger peso. **Consistent with this, the current account deficit widened sharply to USD 4.7bn in Q2, equivalent to 3.5% of GDP, from 1.0% of GDP in Q1, largely driven by a wider goods trade deficit and a return to a services deficit.** Goods imports increased 14.2% y/y, led by consumer goods (+30.0% y/y), while exports rose 13.6% y/y, supported by stronger gold and oil shipments. The strength of domestic demand was also reflected in the external accounts, as the peso appreciated 14% y/y during the quarter, boosting import demand, while net FDI inflows reached USD 3.2bn and continued to finance the current account deficit despite a deterioration in financing quality relative to earlier in the year.
- **August inflation surprised to the upside, with headline CPI rising 0.39% m/m, above market expectations of 0.27%, driven mainly by food and housing prices, which together accounted for roughly 40% of the monthly increase.** As a result, annual inflation resumed its upward trend, increasing from 6.03% in July to 6.24% in August, while core measures also accelerated, with inflation excluding food reaching 6.27% y/y and inflation excluding both food and regulated items

rising to 6.19% y/y. Food prices were the main source of the upside surprise, reflecting higher prices for perishable items, particularly fruits, while regulated inflation continued to increase on the back of higher electricity and water tariffs amid expectations of a stronger and longer-lasting El Niño event. Services inflation also remained elevated, supported by indexation mechanisms and labor cost pass-through in housing and restaurant-related services. Looking ahead, inflation is expected to continue rising in the coming months, with DAVIbank Economics forecasting year-end inflation at 6.9% in 2026 before moderating to 5.1% in 2027.

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	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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