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LATAM FLASH

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Colombia—BanRep Held the Interest Rate at 13.25% in a Split Vote

- **Inflation remains the main concern, while GDP growth projections were revised up.**

The Board of Colombia's central bank (BanRep) kept the policy rate at 13.25%. Five members voted for holding and two for a 25bps cut, the same balance observed in September. The communique was similar to September's statement; they only included a new reference about increasing uncertainty in international financial markets. The central bank's board continued emphasizing that there is not enough confidence to start a sustainable easing cycle. During the press conference, Governor Villar said that the board is facing a challenging dilemma balancing inflation and economic activity outcome; however, concerns about high inflation dominate concerns about a deceleration in economic activity. Having said that, we think today's meeting is probably a non-event for markets. Options remain open; however, we still believe there is a close call between the possibility of having a rate cut in December or Q1-2024.

Interestingly, BanRep's staff revised their GDP projection for 2023 from 0.9% to 1.2%. Governor Villar said that despite growth decelerating, the level of economic activity remains above the long-term potential level (which means a positive output gap and excess demand). All in all, today's meeting continues pointing out that the majority of the board is waiting for further information before starting the easing cycle. Minister Bonilla continued being very vocal, calling for a rate cut, and we expect this disagreement will persist in the medium term.

The next monetary policy meeting will be on December 19th; we think that seeing further correction in core inflation and some better clarity about minimum wage negotiation could support some probability of having a rate cut. If information by then is not convincing, the easing cycle could be delayed to Q1-2024. In any case, our scenario favours a 50 bps rate cut if the easing cycle starts in December, or a stronger start with no less than a 100 bps cut if the easing cycle begins later in Q1-2024. Either way, we maintain our expectation of a monetary policy rate closing 2024 around 6.75%.

Key points about today's decision:

- Today's statement emphasized that inflation remains well above the 3% target. They said that services and regulated prices have shown persistence in recent months. In the same vein, the board is concerned because inflation expectations increased and remain well above the central bank target.

- On the economic activity front, the central bank's staff revised up their 2023 forecast to 1.2% GDP expansion from the previous estimate of 0.9%. During the press conference, Governor Villar said that although the activity is decelerating, the output gap is still positive. Villar repeated that the broad picture is mixed; some sectors are decelerating, but the unemployment rate remains historically low.

- During the press conference, Governor Villar said that credit growth deceleration is compatible with the context of higher rates. He also highlighted that non-performing loans are increasing but, for now, are not a big concern since the financial system in Colombia is robust and is prepared to support this kind of shock. The previous assessment indicates BanRep can tolerate further deceleration to pursue price stability.

- Governor Villar also said that despite having lower rates that could help economic activity, the cost of having persistent inflation is higher. In that sense, BanRep is still revealing that inflation signals are more relevant than economic activity signals in deciding the start of an easing cycle.

- Regarding uncertainty around inflation, Governor Villar said that not only does minimum wage negotiation matter but there are also many other factors such as regulated prices, El Niño weather phenomenon, etc, that could impact the convergence towards the 3% target.
- Minister Bonilla again voted for a rate cut. He said that despite inflation remaining high, the expectation of a further reduction in forthcoming months is a reason to consider a moderate start of the easing cycle. That said, we think Minister Bonilla will continue voting for rate cuts in coming meetings.
- The central bank staff is expected to provide further details about their economic projections in the Monetary Policy Report to be published on Thursday, November 2nd, and during the press conference on Tuesday, November 7th. Minutes will be released on Friday (5 pm local time).