Colombia | Economic Analysis

Banco de la República maintained its policy rate stable at 9.5%

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Banrep's Board decided to keep the benchmark interest rate unchanged at 9.5% in March. The decision was split, with four members voting in favor of maintaining the rate and three members advocating for a 50bps cut. The decision was primarily based on concerns related to inflation and fiscal risks.

- **In its statement, the Board highlighted the recent increase in both observed and expected inflation. The annual inflation rate, at 5.3%,** reflected some temporary upward pressures, particularly from regulated prices and food. Inflation expectations, especially those from surveys, increased for both the 1- and 2-year horizons, while expectations implied by debt instruments remained above the 3.0% target. Nonetheless, they noted that core inflation—excluding food and regulated items, which is the reference measure for the Central Bank—declined marginally from 5.0% to 4.9%.

  Regarding the inflation outlook, the Board acknowledged the existence of risks in specific components. However, the Central Bank Governor expressed his personal expectation (not representing the Board's official stance) that inflation could decrease in March and end the year slightly below the Staff's current projections.
- **Fiscal risks were emphasized as a key factor in the decision to hold rates.** The Governor noted that their primary concern is the potential rise in risk premiums and interest rates, which could result in indirect inflationary pressures and additional pressures through the exchange rate.
- On the activity front, the Board emphasized January's GDP growth of approximately 2.5%, which they interpreted as continued gradual improvement compared to previous months. **Moreover, high-frequency indicators suggest that the economy likely continued to improve during the quarter.** The labor market has also shown favorable dynamics, with improvements in the employment rate and a decrease in the unemployment rate, alongside an increase in labor force participation. **As a result, the Central Bank's technical team revised their 2025 growth forecast upward from 2.6% to 2.8%.**.
- **On external conditions, the Board anticipates that global financial conditions will remain restrictive,** with a slow normalization of monetary policy in the U.S. They also highlighted that global uncertainty—particularly stemming from trade and migration policies in the US—is expected to persist and could affect the global economic outlook.
- **On the fiscal front, the Minister stated that the government is considering a new tax reform, though this would depend on its feasibility in Congress.** He also reiterated that while the government is exploring possibilities for some fiscal austerity, flagship programs under the national development plan will not be compromised. **Finally, the Minister noted that March tax collection figures indicate that revenue targets**

are being met, which would mark an improvement over the earlier months of the year. However, these figures have not yet been made public.

Our take:

- *The Board's decision to keep the policy rate unchanged was achieved through a split vote, with a slight majority (4 votes) in favor of maintaining the rate and 3 votes advocating for a cut. This position was primarily based on two concerns: (1) inflationary risks that may stem from various shocks, both domestic and external; and (2) fiscal vulnerabilities and the associated risks, particularly due to their potential to increase market interest rates and impact the exchange rate, thereby transmitting inflationary pressures.*

- *The minority stance focused on the need to support an economic recovery that is still considered weak. This group downplayed certain risks, such as the minimum wage hike, and conveyed a more optimistic view regarding fiscal performance, partially based on improved revenue figures as of March (which have not yet been disclosed). Notably, the proposed 50bps cut signals a clear preference for a faster pace of monetary easing. The fact that three members supported this stance—presumably including the two newly appointed Board members—suggests that the government bloc is aligned in advocating for a rate reduction, even though individual votes are not publicly disclosed.*

- *The balance within the Board remains divided and tighter compared to previous meetings. The minority stance in favor of rate cuts strengthened—while only two votes favored cuts in January (one of which was for a more modest 25bps cut), this time three votes supported a more aggressive 50bps cut. Based on our analysis, the two outgoing Board members likely voted for rate stability in January, while the two new members voted in favor of cuts in March. This most probably implies that one existing Board member may have shifted from supporting a 25bps cut in January to backing stability in March.*

- *We believe this change likely came from Co-Director Acosta, who had expressed concerns in public appearances about inflationary pressures, especially cost-related components such as PPI and energy prices. She also voiced concerns about fiscal vulnerabilities. These two factors have slightly deteriorated at the margin and could prove decisive in future policy decisions.*

- *Looking ahead, as the Governor emphasized, upcoming monetary policy decisions will depend on incoming data. Should tax revenues continue to improve and inflation moderate within a context of limited external shocks on the exchange rate, a renewed cycle of rate cuts could become feasible. The burden of proof will lie in the evolution of these variables. Therefore, our baseline scenario remains one of gradual rate cuts in the coming months, though a continued pause in the short term cannot be ruled out until more significant improvements are observed in key indicators.*

- *Nonetheless, the divergence between the current stance—rate stability—and a 50bps cut may represent the initial step toward a compromise in future meetings, where both sides might give ground to achieve consensus around more cautious rate reductions. This idea was hinted at by the Finance Minister during discussions at this meeting and could mark a pathway toward restarting the easing cycle, albeit with a prudent and measured approach.*

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