

## Colombia: Monetary Policy

- **January monetary policy meeting preview: A non-event, but...**

BanRep will hold its first meeting of 2019 tomorrow. We (and market consensus) expect it to keep the monetary policy rate (MPR) at 4.25% in a unanimous decision. This will keep monetary policy in a slightly expansionary mode to help sustain the economic recovery, as GDP growth remains below potential and headline inflation and inflation expectations are under control.

Although we expect a rather neutral communication signaling no rush to start the hiking cycle, we will look to the communiqué and post-meeting press conference to shed light on the following concerns i) On one side, a more gradual economic activity recovery (dovish), would make market participants think of an even greater delay in MPR normalization process; ii) on the other side, stronger, than expected supply and FX shocks that would push inflation up (hawkish) that would lead to an earlier hike. Also worth noting, a dovish message could include a downgrade in 2019 GDP growth projections (currently at 3.5% y/y) and/or special emphasis on recent fall in consumption and industrial confidence. A hawkish message would see lack of unanimity on the decision, or showing concerns on current account financing or FX volatility and pass-through.

In regards to economic activity, Ana Fernanda Maiguashca (Board member) recently said that she is more optimistic than the signal coming from the confidence surveys (Consumption and industrial surveys). She said that November coincident indicators (Retail sales and manufacturing), as well as, energy demand and capital imports support the argument that the economic activity recovery continues. Having said that, the expansion continues to be gradual, still below potential, and employment indicators, although resilient to economic activity deceleration, are showing that informality increased last year, which is not good for productivity and contributes to a slower recovery than should be the case.

On inflation, December-2018 inflation ended below market and BanRep expectations, and inflation expectations, although in the upper side of the target range, have not changed much in the last three months. Additionally, core inflation measures are very close to 3% and non-tradable prices continue their convergence path to target.

Finally, although the COP has depreciated a bit more than 6% since September last year, tradable goods inflation remains 1.5% y/y, showing that recent depreciation has not affected, so far, Colombia headline inflation. Additionally, recently COP has stabilized, which should keep BanRep calm about possible FX pass-through in the near future. In other words, available data point to stable headline inflation around target this year.

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Bottom line, a gradual recovery in GDP continues, inflation and inflation expectations are under control and the COP has stabilized. Therefore, we do not see BanRep changing its flight plan soon. Additionally, a more dovish FED should depreciate, in the short-run, the dollar which, probably, will appreciate the COP. Under this scenario, we think BanRep will stay put at this meeting, keeping the rate at 4.25% in unanimous decision. We expect the first hike to take place in June. Having said that, the real news would be a less neutral communication that can affect first hike market expectations (currently in April).

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