

## Contributors

**Jackeline Piraján**

Head Economist, Colombia

+57.1.745.6300 Ext. 9400 (Colombia)

[jackeline.pirajan@scotiabankcolpatria.com](mailto:jackeline.pirajan@scotiabankcolpatria.com)

## Colombia—BanRep Holds on Inflation Convergence Worries

**The board of Colombia's central bank (BanRep) maintained its monetary policy rate at 9.25% in a split vote:** four members voted to keep the rate unchanged, one voted for a 25bps cut, and two voted for a 50bps cut. This was against the market consensus and our official expectation for a rate cut.

**In both the communiqué and the press conference, the board cited three key reasons for maintaining a cautious stance.** First, the Colombian economy is performing better than expected, with robust household consumption. Second, there is significant uncertainty regarding the ability to meet the inflation target within the monetary policy horizon. Third, volatile international conditions could tighten financing conditions for the country.

**In today's statement there was no explicit mention of fiscal risks.** However, Governor Villar emphasized that fiscal policy in Colombia was one of the topics considered in the discussion.

**Following today's vote we do not anticipate further interest rate cuts for the remainder of 2025.** According to our projections, inflation may rebound starting with the August reading (to be released in September) and fluctuate erratically, ending 2025 above 5%. Additionally, in the second half of the year, a potentially contentious debate on tax reform and the government's budget could trigger volatility in local assets, further supporting a cautious approach by the central bank.

**The main reason for our expectation that the central bank will maintain a cautious stance is the uncertainty surrounding next year's minimum wage increase,** which is critical to the inflation outlook for 2026 and will not be known until December 2025. All in all, we see the earliest possible resumption of an easing cycle in March 2026, firmly determined by the impact of the minimum wage hike on inflation next year—an effect that will be observed in the January and February inflation readings.

### Highlights from the decision:

- **During the press conference, Governor Villar emphasized that the central bank's main concern is that inflation expectations are not responding to recent declines in headline inflation.** Instead, analysts anticipate that inflation will remain steady around ~4.7% y/y for the rest of the year. At Scotiabank, our expectation is for ~5.2% at year-end.
- **Villar also stressed that uncertainty surrounding the 2026 minimum wage increase is critical to the inflation path.** In our view, the board's discussion revealed some tension, as the Minister of Finance repeatedly argued that wage increases are not detrimental to inflation or employment dynamics—contrary to Governor Villar's concerns.
- **Governor Villar was reluctant to speak explicitly about Colombia's fiscal situation but noted that it was a factor in maintaining a cautious stance,** especially given the high uncertainty in global markets. In relation to this point, he stated that the board is not currently discussing a program to increase international reserves.
- **Finance Minister Avila argued that the economy needs more support from the central bank.** In his remarks during the press conference, he repeatedly stated that while service-related sectors are performing well, investment-related sectors such as manufacturing and construction are lagging in the recovery, which is a reason for having a less restrictive monetary policy.

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- **Regarding fiscal matters, Governor Villar was very prudent in sharing his perspective.** However, in our opinion, the decision to maintain rate stability may also reflect a situation of fiscal dominance. It will be interesting to see whether this assessment is addressed in the Monetary Policy Report to be released next week.
- **Minister Avila's comments on the release of the 2026 Budget suggest that the government sees significant inflexibilities in reducing fiscal spending, which in turn shifts the focus to discussions around fiscal reform.** In our view, these remarks also indicate a low willingness to make efforts to reduce spending pressures. Eventually, this situation could lead to higher financing needs and increased volatility in domestic assets.
- **Next week, the central bank staff will likely face difficult questions regarding the current macroeconomic outlook.** Our attention will focus on how a weaker fiscal situation influences the assessment of a higher real interest rate for Colombia. The central bank will release the Monetary Policy Report on Monday, followed by a press conference on Wednesday. Minutes from today's meeting will be published on Tuesday, August 5<sup>th</sup>.

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