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## Colombia—BanRep Holds Interest Rate at 13.25% in a Split Vote

- **The central bank doesn't want to start an “unsustainable easing cycle.”**

The Board of Colombia's central bank (BanRep) kept the policy rate at 13.25%. Five members voted for holding and two for a rate cut. In the communique, the board highlighted that despite the progress on the inflation front, there are still risks that are slowing the speed of inflation convergence towards the target. On the other hand, the assessment of economic activity does not point to a significant concern yet. That said, in the last line of the communique they emphasized the need to be prudent and not start an easing cycle that could be unsustainable in the future. Additionally, they remarked that high inflation plays a negative role in terms of sustainable long-run growth and social equality.

Today's meeting demonstrated that BanRep is still very focused on inflation convergence, and despite some economic signals revealing weaknesses, the board didn't show a significant concern. In fact, they highlighted that the labour market remains strong and that a slowdown is necessary to bring inflation to more sustainable levels. All in all, it seems BanRep wants to see more significant progress in inflation before starting the easing cycle. Inflation by the end of 2023 is expected at 9.50% which could be insufficient evidence to start an easing cycle today. However, it is important to keep in mind that the last quarter of the year is critical due to the negotiation for minimum wage. If an increase is set well above inflation, it could trigger undesirable indexation effects in 2024. We think a rate cut in December 2023 or January 2024 is most likely.

### Key points about today's decision:

- During the press conference, Governor Villar emphasized that the economic activity slowdown has been aligned with the central bank's expectation and that this slowdown is necessary to achieve inflation convergence. Additionally, he said that despite the economic growth looking low, the level of activity remains strong and that some signals are revealing that the output gap is still positive. One signal of that could be the unemployment rate.
- Governor Villar said that Colombia has made significant progress in reducing the external deficit, which reflects the reduction of domestic demand.
- Regarding inflation, Governor Villar said that the progress in core inflation is key. Currently, inflation ex-food and regulated prices is at 9.9%, still more than three times the target. Villar emphasized that to make further progress on core inflation, it is important for economic growth to be aligned with the long-term trend.
- Minister Bonilla emphasized that his call for a rate cut was because the government wants to get support for the economy. He emphasized that despite the labour market remaining robust, the demand is showing significant weakness.
- Regarding the financial sector and credit deceleration, Governor Villar said that it was necessary to reduce the households' financial burden. He also said that the financial system is resilient, and that provision will help the banking system to surpass the recent surge of delinquencies and credit slowdown.
- Villar repeated that having a sustainable level of economic activity is important to achieve price stability and to ensure that an eventual easing cycle is sustainable.

All in all, today's meeting proves that inflation is the focus of the central bank. Governor Villar emphasized many times that economic activity deceleration is needed to achieve

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the inflation target. He also said that achieving a more reliable headline inflation convergence towards the target is important for having a sustainable easing cycle. That said, we maintain our call for a rate cut in December, which strongly depends on further inflation progress. In that sense we highlighted that minimum wage negotiation is critical for the board, the risk of having a minimum wage increase set well above inflation could make inflation reduction slower. That is why we think BanRep would prefer to wait and see what happens with the minimum wage before starting the easing cycle.

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