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Colombia Business Forecast Report Q2 2014

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Abstracts

Core Views

We believe that Colombia's economy will expand at robust growth rates in the coming years, characterised by improved macroeconomic conditions and an increasingly friendly business environment. Stronger private consumption will drive the majority of growth, although gross fixed capital formation (GFCF) will play an increasingly important role over the coming quarters.

The infrastructure, mining and hydrocarbons sectors are particularly well positioned for growth.

We expect President Juan Manuel Santos to win re-election in May, and anticipate broad policy continuity throughout the next administration.

Major Forecast Changes

We have revised our real 2014 real GDP growth forecast from 4.4% to 4.3%, following a downward adjustment to our 2013 growth estimate, from 4.3% to 4.1%, due to weaker-than-expected economic activity in Q413.

The Colombian peso weakened more than we expected this year, prompting us to revise our 2014 average exchange rate forecast from COP1,880/US$ to COP1,980/US$, implying a 5.9% depreciation from last year's average exchange rate of COP1,869/US$.

Key Risks To Outlook

Upside Risks: Elevated foreign investment inflows into the country following Colombia's upgrade to ‘investment grade’ by all three major ratings agencies could drive growth even faster than expected. In addition, a successful agreement during the ongoing peace negotiations between the government and the country’s main left-wing insurgent group, the Fuerzas Armadas Revolucionarias de Colombia (Farc), would likely result in even greater foreign investment as risk perception improves.

Downside Risks: Another wave of labour strikes would pose significant downside risks to our export and real GDP growth outlook. Indeed, workers demanding higher wages and greater government support disrupted key exports such as coal throughout 2013, and another episode of industrial activity cannot be ruled out at this moment.

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recovery in exports, after strike activity last year disrupted production in key-export oriented sectors, such as coal. In addition, we expect foreign direct investment to remain robust, especially into the infrastructure and oil and gas sectors, which will continue to result in strong financial account surpluses in the coming years.

Table: CURRENT ACCOUNT, % of GDP

Monetary Policy

Rate Hiking Cycle To Begin This Year As Inflation Heads Higher

We believe Colombia's Banco Central de la República (BanRep) will begin hiking rates this year, as domestic demand growth accelerates and consumer price inflation ticks up. We forecast BanRep to increase its policy rate by 50 basis points (bps) from 3.25% to 3.7 5% by end-2014 and then by another 75bps to 4.50% by end-2015.

Table: MONETARY POLICY

Fiscal Policy

Fiscal Consolidation To Regain Traction This Year

After Colombia's government budget deficit widened slightly in 2013, we expect fiscal consolidation to regain traction in 2014 and 2015. Rising revenue growth, in large part due to greater income tax intake, will be a main driver of a stronger fiscal position. In addition, we expect the next administration to maintain fiscal prudence in terms of spending, given the composition of the newly-elected congress, which is dominated by fiscally conservative parties.

Table: FISCAL POLICY

COP: Weakness To Persist In H114, Modest Strength In H214

Table: CURRENCY FORECAST

Regional Economic Activity

Regional Inflation Update: Divergence Continuing To Play Out

Consumer price data from January suggest that our forecast for inflation to remain within central bank target bands in most of Latin America's largest economies is on track. That said, divergent real GDP growth trajectories will produce greater variation in monetary policy than was the case in 2013, when the trend was toward easier policy. Additionally, we expect inflation will remain quite high in Argentina and Venezuela, in light of a January currency devaluation in the former and our expectation of another devaluation in the latter.

Table: LATIN AMERICA - CONSUMER PRICE INFLATION & MONETARY POLICY RATES

CHAPTER 3: 10-YEAR FORECAST

The Colombian Economy to 2023

Sustainable And Sturdy Growth

Business-friendly policies and an improving security situation will help Colombia achieve sustainable levels of strong real GDP growth, which we forecast will average 4.5% in 2014-23. A surge in fixed investment will catalyse such growth over the coming years and we expect consumption to follow suit and remain the main driver of the Colombian growth story.

CHAPTER 4: BUSINESS ENVIRONMENT

CHAPTER 5: KEY SECTORS

CHAPTER 6: BMI GLOBAL ASSUMPTIONS

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