



## *Colombia's Resilient Economy...*

Colombia's economy performed moderately during the past year, despite the economic climate worldwide. Like most Latin American countries, Colombia was able to withstand the economic slump of 2009, surpassing many analysts' expectations. Its performance however was not on par with some of its neighbors like Brazil and Chile, who out-performed expectations.

Colombia is located in South America and has a population of approximately 46 million. Its capital city is Bogota, native language is Spanish and the currency is the Colombian peso (COP). Its key trading partners include the United States, the European Union, Venezuela, Ecuador and Peru. Colombia is rich in natural resources and this has contributed to the composition of its exports which comprises mainly petroleum, coal, coffee and other agricultural products.

With the collapse of the world financial markets in the fourth quarter of 2008, the world economy was subsequently drawn into a recession and Colombia was no exception. Initial speculation that the depressed financial markets would not filter into the real economy were quickly dispelled by the end of 2008/ early 2009, when many countries began to see contractions in growth rates and increased levels of unemployment. By November 2008, Colombia recorded a contraction in industrial production of 13%, which contributed to a notable slow down in Gross Domestic Product (GDP) of 1.1% at the end of December 2008, compared to growth of 8.2% a year ago. The marked deterioration in key economic data from Colombia, together with U.S. economic downturn enabled analysts to conclude that the Colombian economy would contract by 1.5% for 2009. Inflation levels for the 12 months to November 2008 stood at 7.7% which was higher than the central bank's desired range of 3.5% to 4%. The South American economy suffered considerably from a double whammy. First, constrained commodity demand as well as depressed prices reduced the value of Colombia's petroleum exports. Secondly, the slowdown in the U.S. economy, its main trading partner, translated into reduced demand from that market for Colombian exports, as well as reduced imports due to lower production levels in the domestic economy.

As Colombia entered 2009, the prospects for its economy remained pessimistic. GDP for the first quarter contracted 0.4%, registering the second consecutive quarter of negative growth, sending the Colombian economy into recession. This was the first since 1998 and 1999 when insurgent violence and a banking crisis triggered a similar slowdown. A key contributor to the current decline in GDP was a fall in industrial production of 7.9% in the first quarter from a year earlier. The contraction in GDP could have been much worse had there not been growth of 4.7% and 2.1% (year-on-year) in the finance and construction sectors respectively. As the economy slowed, inflation continued its downward trend and as at the end of June 2009 it stood at 3.81%, which was well within the Central Banks threshold.

Colombia's trade balance also continued to deteriorate in the early months of 2009. A key factor here was the country's heavy reliance on the U.S. economy as its main export market. The U.S. economy continued to grapple with its own economic downturn, and consequently its capacity to import was constrained. Another issue negatively impacting Colombia's trade balance was its dependence on its neighbor Venezuela. Venezuela is Colombia's second largest trading export market, accounting for 16.8% of total exports in 2008. The expectation of a devaluation of the Venezuelan bolivar meant that the Colombian peso will now become more expensive in relation to the bolivar, thus making Colombia's exports more expensive. Additionally, diplomatic relations between the two countries deteriorated, adding to the grim outlook for Colombia's trade balance. Trade between the two countries last year totaled about USD7 billion, and in September, Colombian exports to Venezuela fell 50% from the same period a year earlier.

Towards the second half of 2009, Colombia's economy continued to shrink as the global credit crunch cut exports while domestic demand fell. The unemployment rate was recorded at 11.5% in October, up from 10.1% in October last year. The inflation rate continued to fall throughout the year and stood at 2.7% in October, down from 3.21% in the previous month. Exports and imports for the month of September were USD2.8 billion and USD2.6 billion respectively. For the same period a year earlier exports totaled USD3.1 billion and imports USD3.6 billion. Although there was an improvement in the trade balance, the decline in imports was indicative to a fall in private consumption. In an effort to enhance growth, policy makers slashed policy interest rates from a record 10% in November last year to 3.5 % in November 2009. In September, the central government announced an additional COP2.2 trillion domestic bond issuance aimed at helping the government fund the projected COP4.4 trillion fiscal shortfall for 2009. The government was forced to maintain and in some instances increase its level of spending to offset the reduction of private consumption in order to keep its economy buoyant.

Despite the slowdown in the Colombian economy throughout 2009, the impact of the global recession was not as bad as had been anticipated at the close of 2008. Analysts revised the forecasted growth rate from a decline of 1.5% to 0% growth in 2009, while the Finance Ministry forecasts 2009 growth at 0.5% to 1.5%. A key contributor to this optimistic outlook was the Colombian government's combined policy of lower interest rates and increased government spending. Additionally, the recovery of the global economy was faster than previously anticipated, with economic activity in many of the developed economies recording positive economic growth in the latter half of 2009. For the year 2010, prospects are for growth between 2% and 3%.

There are however, some determining factors that can set the Colombian economy back. As mentioned before Colombia's main export partners are the U.S. and Venezuela. This is inherently threatening to the economy since unfavorable events in those economies will directly impact Colombia's balance of payments, a vital macroeconomic indicator. This was evident when the U.S. was in recession, causing Colombia's exports to vastly decrease. By extension, imports from the U.S. in 2008 consisted of raw resources, industrial machinery and food. These products are used as inputs in domestic production, thus illustrating the importance of U.S. imports to Colombia's domestic economy. In the case of Venezuela, strained diplomatic relations between the two countries can affect the level of exports to that market. Trading restrictions can be imposed by Venezuela, and its sometimes erratic governance can leave Colombia vulnerable to a trading partner that historically contributed to a significant portion of its international trade. Additionally, Colombia's over-dependence on oil exports leaves its economy susceptible to commodity price movements which adversely contributed to the negative

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growth rates experienced in late 2008 to mid 2009.

Another area of concern is that of the government's ability to spend its way out of the recession. As Colombia entered the recession, it was fortunate enough to have solid macroeconomic conditions and more importantly a relatively light debt burden, which allowed the government some fiscal flexibility to issue debt to increase its infrastructural spending in an effort to enhance growth and help alleviate the unemployment situation. The question that arises is: How long can the Colombian government maintain this level of spending? Signs of the end of the global recession are promising, meaning that private consumption may begin to pick up, thus easing the government's need to maintain spending. However, this may begin to surface later rather than sooner given the lag that developing countries are expected to face on the road to recovery. If the government seeks to maintain its level of spending it runs the risk of issuing more debt than it can comfortably manage, possibly causing a downgrade in its sovereign credit rating, creating further implication for the economy.

2009 has indeed been a challenging year for Colombia as it has been for most countries. However, what differentiated Colombia were its sound economic policies and stable levels of debt. On the downside, Colombia is heavily dependent on two main trading partners and on commodity products. If the global economy remains on stream for recovery next year, barring any unforeseen circumstances, Colombia will begin to steadily recover and experience economic activity levels that made it one of the strongest Latin American economies.

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## FINANCIAL & ECONOMIC INDICATORS

As at 3 December, 2009

Exchange Rate/US\$	Closing Value	Previous Week
Yen	88.26	86.59
Euro	1.51	1.50
Jamaica	89.54	88.98
Guyana	204.90	202.70

Commodity Prices	Closing Value	Previous Week
Crude oil (US\$/bbl)	76.46	N/A
Natural Gas (US\$/mmbtu)	4.55	N/A
Gold (US\$/Troy Ounce)	1,207.60	1,188.38

### Eurobond Indices (As at 03-12-09)

Lehman Brothers Global Aggregate Index (Return % YTD)	10.68
JP Morgan EMBI+ (Basis points)	312
JP Morgan Central America and Caribbean Index (CACI) (YTD return %)	34.30

Policy Interest Rates (%)	Closing Value	Previous Week
United States	0.12	N/A
Euro Zone	1.00	1.00
Japan	0.10	0.10
Brazil	8.75	8.75
Trinidad	5.75	5.75
Jamaica	12.50	12.50
Barbados	2.50	2.50

Market Interest Rates (%)	Closing Value	Previous Week
US 90-day T-Bill	0.04	0.04
US 10-Yr Treasury	3.39	3.28
3-month UK Libor	0.61	0.61
Japan 90-day T-Bill	0.28	0.11
Brazil 90-day T-Bill	8.68	8.65
TT 90-day T-Bill	1.44	1.46
Jamaica 90-day T-Bill	15.99	16.21
Barbados 90-day T-Bill	3.48	3.48

Sources: Bloomberg, J.P. Morgan, CMMB, Central Bank of Trinidad and Tobago, Bank of Jamaica, Central Bank of Barbados, [www.lehman.com](http://www.lehman.com)

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