INTERNATIONAL MONETARY FUND

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STAFF REPORT FOR THE 2022 ARTICLE IV CONSULTATION—SUPPLEMENTARY INFORMATION

Prepared By Western Hemisphere Department

This supplement provides an update to the Staff Report (SM/22/59) based on an initial assessment of the effects of the Russia-Ukraine war. The update does not alter the thrust of the staff appraisal and recommendations.

1. **Global conditions have changed in the wake of Russia-Ukraine war, which affects Colombia's macroeconomic outlook**. International commodity prices for both fuel and food have been revised upward with respect to assumptions underpinning the macroeconomic projections in the Staff Report. For 2022, the average price for Brent oil has been revised by 30 percent in the baseline (from USD 82 per barrel to USD 107 per barrel) given changes in spot and futures prices for oil. In the case of coal, the baseline price has been revised by 300 percent (from USD 235 per metric ton to USD 558 per metric ton). In addition, international agricultural commodity (food) prices have been revised up by 7 percent. These price revisions have important implications for GDP growth, external and fiscal accounts, and inflation.

2. **Colombia's growth outlook has improved reflecting stronger terms of trade**. GDP growth projection for 2022 has been revised up by 0.4 percentage points to 5.8 percent of GDP. As a net oil exporter, higher oil prices will have a positive effect on growth through the channels of higher consumption and investment. Oil production continues its gradual recovery process from the effects of last year's social demonstrations with limited spare capacity to ramp up production in a shorter period of time. With respect to stronger domestic demand, a positive output gap would open in the second half of the year, after closing fast since the last part of 2021.

3. **External and fiscal accounts are set to improve**. With oil and coal representing around half of Colombia's exports, stronger export revenues through higher prices would improve the external position noticeably. Specifically, the expected large increase in the price of these key commodities alone would lead to a significant reduction in the current account deficit from 5.7 percent of GDP in 2021 to 3.3 and 3.4 percent of GDP in 2022 and 2023, respectively. Similarly, external financing needs are expected to decline

significantly from 18 percent of GDP in 2021 to around 14 percent in 2022 and 2023. Higher oil prices will also boost fiscal revenues, mainly in 2023 in the form of higher corporate taxes and dividends received from Ecopetrol (with the state as its largest shareholder).[1] Consequently, the consolidated public sector deficit is now projected to be 4.4 and 2.1 percent of GDP in 2022 and 2023, respectively, down sharply from 7.2 percent of GDP in 2021. Due to lingering domestic supply bottlenecks, higher oil and coal prices are expected to have a limited and lagged effect on boosting production volumes over time.

4. Domestic inflationary pressures will intensify due to upward pressures on global food and energy prices. Amid strong domestic demand, elevated commodity prices, and persistent supply shocks, inflation continues exceeding the central banks' upper limit of its tolerance range (4 percent), as inflation climbed to 8 percent in February. Higher global inflation and possible supply disruptions will place additional pressure on domestic prices, especially food prices as energy subsidies are in place through the fuel price stabilization fund (FEPC). On the other hand, currency appreciation in recent weeks will modestly contribute to mitigate these inflationary effects. Staff's inflation forecast has been revised up to 6.9 percent from 5.7 percent for end-2022. While the lion's share of the inflation increase is associated with supply shocks, domestic factors related to a lower excess capacity and indexation effects will continue having an impact on underlying inflation. The balance of inflation risks continues to be on the upside from higher international prices of commodities and raw materials; more persistent disruptions in global supply chains; more stringent external financial conditions; and second-round effects from higher inflation.

5. Risks to Colombia's growth remain tilted to the downside but their nature has changed. While uncertainty remains about the course of the pandemic, other risks have also become prominent, including (i) uncertainty surrounding the ongoing conflict in Ukraine and its effects on global growth, financial markets, and commodity prices and (ii) risks arising from elevated inflation in many countries and uncertainty about the degree of monetary tightening in these countries. Realization of these risks, such as faster-than-expected monetary tightening in major economies, could dampen global growth and commodity prices and prompt capital outflows from emerging markets. With high external financing needs, Colombia remains vulnerable to a decline in global growth, to a sharp rise in global risk premia, and to other external shocks in a context of elevated global uncertainty and geopolitical conflict.

6. The thrust of the staff appraisal remains unchanged. Higher global and domestic inflation pressures reinforce staff's advice on the need for accelerated monetary policy tightening in Colombia. Amid rising inflationary pressures, low real rates, limited spare capacity, and an already high inflation rate, the central bank would need to continue raising interest rates on a

[1] The oil price assumption for 2022 in the 2022 Financial Plan is 70 USD/bl. It is estimated that each dollar increase in the price of oil could increase government revenues by 0.05 percent of GDP. The lion share of oil-related revenues occur as a result of dividends and income tax, which are based on the previous year earnings. Hence higher oil prices in 2022 will have a delayed effect on fiscal revenue (e.g., higher Ecopetrol dividends in 2023).

frontloaded basis in order to safeguard its credibility, ensure that inflation expectations remain well-anchored, and insure against upside inflation risks. In line with staff's fiscal policy recommendation, saving additional fiscal revenues, especially in 2023, related to higher GDP growth and hydrocarbon prices due to higher income tax collections and dividends from Ecopetrol, would help further reduce the fiscal deficit relative to the previous baseline. This would allow the authorities to achieve smoothly or to overperform their fiscal targets over a transition path anchored by the new fiscal rule as provided by the Social Investment Law.

Table 1. Colombia: Selected Economic and Financial Indicators

						Projections					
	2017	2018	2019	2020	2021 1/	2022	2023	2024	2025	2026	2027
					(In percentage change, unless otherwise indicated)						
National Income and Prices											
Real GDP	1.4	2.6	3.2	-7.0	10.6	5.8	3.6	3.4	3.4	3.4	3.4
Potential GDP	2.9	3.0	3.1	-2.0	5.0	4.4	3.8	3.4	3.4	3.4	3.4
Output Gap	-0.8	-1.2	-1.1	-6.2	-1.2	0.1	-0.1	0.0	0.0	0.0	0.0
GDP deflator	5.1	4.6	4.0	1.4	6.6	7.5	3.4	3.1	3.1	3.1	3.1
Consumer prices (average)	4.3	3.2	3.5	2.5	3.5	7.7	4.2	3.5	3.0	3.0	3.0
Consumer prices, end of period (eop)	4.1	3.1	3.8	1.6	5.6	6.9	3.8	3.0	3.0	3.0	3.0
External Sector											
Exports (f.o.b.)	16.8	8.1	-5.4	-20.5	32.3	47.0	1.8	-3.4	-0.3	2.6	2.2
Imports (f.o.b.)	1.9	12.1	2.3	-18.5	37.7	16.3	3.7	2.9	1.9	3.4	3.4
Export volume	2.6	0.6	3.1	-9.1	-0.8	4.1	14.7	4.2	1.2	3.6	2.4
Import volume	1.0	5.8	7.3	-15.9	17.8	6.1	3.8	2.5	1.1	2.8	2.6
Terms of trade (deterioration -)	9.9	3.5	-2.3	-12.2	13.4	26.6	-11.1	-6.3	-1.8	-1.4	-0.7
Real exchange rate (depreciation -) 2/	5.6	0.7	-9.1	-11.1	-1.9	...	...	...	...	...	...
Money and Credit											
Broad money	6.4	5.7	10.0	10.3	12.3	12.2	8.5	7.8	7.6	7.5	7.5
Credit to the private sector	12.8	6.8	11.6	-0.8	11.5	12.5	8.5	7.9	7.8	7.6	7.5
Policy rate, eop	4.8	4.3	4.3	1.8	3.0	...	...	...	...	...	...
					(In percent of GDP)						
Central government balance 3/	-3.6	-4.8	-2.5	-7.8	-8.2	-6.1	-3.7	-3.6	-2.6	-2.5	-2.5
Central government structural balance 4/	-2.6	-2.2	-2.1	-6.1	-7.3	-5.8	-3.9	-3.9	-2.7	-2.5	-2.5
Consolidated public sector (CPS) balance 5/	-2.4	-4.5	-2.9	-6.9	-7.2	-4.4	-2.1	-1.3	-0.8	-0.9	-1.0
CPS non-oil structural primary balance	-0.1	-1.2	-1.7	-4.3	-4.9	-3.3	-2.4	-2.0	-0.7	-0.2	-0.3
CPS fiscal impulse	0.1	1.0	0.6	2.6	0.5	-1.6	-0.9	-0.4	-1.2	-0.5	0.1
Public sector gross debt 6/	49.4	53.6	52.4	65.7	64.6	60.6	59.2	57.5	56.3	54.5	52.9
Gross domestic investment	21.6	21.2	21.4	19.2	19.7	19.0	19.2	18.9	18.9	19.0	19.3
Gross national savings	18.4	17.0	16.8	15.8	14.1	15.6	15.9	15.1	15.0	15.2	15.4
Current account (deficit -)	-3.2	-4.2	-4.6	-3.4	-5.7	-3.3	-3.4	-3.8	-3.9	-3.9	-3.9
External Financing Needs	13.5	14.3	15.3	17.9	17.8	13.9	14.1	15.3	15.0	14.8	14.6
External debt 7/	47.3	46.7	50.1	65.6	60.3	58.1	58.4	59.1	59.0	58.6	58.2
					(In percent of exports of goods and services)						
External debt service	73.7	70.8	77.8	113.0	87.0	59.5	62.6	72.1	73.1	72.8	73.7
Interest payments	10.7	10.7	14.7	16.4	12.9	10.2	11.2	12.6	13.2	12.9	13.1
					(In billion of U.S. dollars; unless otherwise indicated)						
Exports (f.o.b.)	39.8	43.0	40.7	32.3	42.7	62.8	64.0	61.8	61.6	63.2	64.6
Of which: Petroleum products	13.3	16.8	16.0	8.8	13.5	21.4	23.5	22.4	19.9	19.3	18.5
Gross international reserves 8/	47.1	47.9	52.7	58.5	59.1	60.2	61.5	62.9	64.2	65.1	65.9
Share of ST debt at remaining maturity + CA deficit	102	99	113	106	125	119	106	104	103	99.7	102.6

Sources: Colombian authorities; UNDP Human Development Report; World Development Indicators; and IMF staff estimates.

1/ Estimate for monetary sector variables (except for policy rate) and fiscal sector variables.

2/ Based on bilateral COL Peso/USD exchange rate.

3/ Includes one-off recognition of previously unrecognized accounts payable worth 1.9 percent of GDP in 2018 and central bank profits. For 2021 includes privatization receipts worth 1.2 percent of GDP that, under GFSM 1986 which is used by the authorities, produces a headline deficit of -7.0 percent of GDP.

4/ IMF staff estimate, excludes one-off recognition of arrears.

5/ Includes the quasi-fiscal balance of Banco de la República, sales of assets, phone licenses, and statistical discrepancy. For 2021 includes privatization receipts, see 3/ above.

6/ Includes Ecopetrol, Fogafin, and Finagro.

7/ Current account deficit plus amortization due including holdings of locally issued public debt (TES).

8/ Excludes Colombia's contribution to FLAR; includes valuation changes of reserves denominated in currencies other than U.S. dollars.