INTERNATIONAL MONETARY FUND

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COLOMBIA

May 2018

2018 ARTICLE IV CONSULTATION—PRESS RELEASE; STAFF REPORT; AND STATEMENT BY THE EXECUTIVE DIRECTOR FOR COLOMBIA

Under Article IV of the IMF's Articles of Agreement, the IMF holds bilateral discussions with members, usually every year. In the context of the 2018 Article IV consultation with Colombia, the following documents have been released and are included in this package:

- A **Press Release** summarizing the views of the Executive Board as expressed during its April 27, 2018 consideration of the staff report that concluded the Article IV consultation with Colombia.
- The **Staff Report** prepared by a staff team of the IMF for the Executive Board's consideration on April 27, 2018, following discussions that ended on March 2, 2018, with the officials of Colombia on economic developments and policies. Based on information available at the time of these discussions, the staff report was completed on April 16, 2018.
- An **Informational Annex** prepared by the IMF staff.
- A **Statement by the Executive Director** for Colombia.

The documents listed below will be separately released.

Selected Issues

The IMF's transparency policy allows for the deletion of market-sensitive information and premature disclosure of the authorities' policy intentions in published staff reports and other documents.

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April 30, 2018

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700 19th Street, NW
Washington, D. C. 20431 USA

IMF Executive Board Concludes 2018 Article IV Consultation with Colombia

On April 27, 2018, the Executive Board of the International Monetary Fund (IMF) concluded the Article IV consultation[1] with Colombia.

In 2017, adequate policy management brought Colombia near completion of its adjustment to large external shocks while further advancing inclusive growth. Economic growth moderated as private investment and consumption weakened in line with lower national income. Some delays in the infrastructure agenda also contributed to the decline in private investment.

Fiscal consolidation continued guided by the fiscal rule and contributed to the narrowing of the current account deficit which was also buttressed by some recovery in oil and non-oil exports. The proceeds of the structural tax reform helped protect public investment and social expenditure. As past shocks dissipated, inflation rapidly declined toward the target and the central bank's easing cycle supported the recovery observed in the second part of the year while protecting the anchoring of inflation expectations. Despite the growth moderation, social indicators improved with both poverty and income inequality decreasing in 2017.

The current account deficit declined to 3.4 percent of GDP and continued to be financed by FDI to a large extent. Portfolio inflows moderated somewhat but remained ample with further increases in foreign participation in the local government debt market. The banking system has weathered the economic slowdown well and the planned implementation of the conglomerates law this year will improved the regulatory and supervisory framework including the management of corporate and overseas risks.

Colombia's outlook is favorable as continued efforts to advance the structural reforms will foster economic diversification and productivity growth. Economic growth is expected to rebound strongly in 2018 and further over the medium-term, led by strengthening investment and exports. The combined impact of the structural tax reform, a brighter outlook for oil prices and the authorities 4G infrastructure agenda will underpin investment while reducing Colombia's relatively large infrastructure gap.

[1] Under Article IV of the IMF's Articles of Agreement, the IMF holds bilateral discussions with members, usually every year. A staff team visits the country, collects economic and financial information, and discusses with officials the country's economic developments and policies. On return to headquarters, the staff prepares a report, which forms the basis for discussion by the Executive Board.

Continued efforts to reduce trade barriers and some recovery in global growth will help sustain strong export growth. The implementation of the peace agreement will promote regional development and reduce inequality. Risks to this outlook remain to the downside and stem in part from still sizeable external financing needs. Colombia remains exposed to a sharp tightening of global financial conditions.

Executive Board Assessment[2]

Executive Directors commended the authorities for their strong macroeconomic management and improvements to the policy framework, which have secured the needed adjustment, strengthened recovery, and reduced poverty and income inequality. While the outlook is positive, the economy remains vulnerable to uncertainties from a sudden tightening of global financial conditions and escalation of trade or geopolitical tensions. Directors welcomed the authorities' commitment to maintain very strong policies and ambitious structural reforms to address remaining vulnerabilities, ensure macroeconomic stability, and foster sustainable and inclusive growth.

Directors highlighted that structural reforms should focus on raising productivity and potential growth. They noted that implementation of the Fourth Generation infrastructure projects and the peace agreement offer an opportunity to advance priorities, including, improving the business environment, tackling labor market informality, providing high quality education, and promoting infrastructure investment. Lowering barriers to international trade would also be important.

Directors concurred that placing public debt on a declining path is an appropriate fiscal target which would also leave room to fine tune the consolidation pace as guided by the fiscal rule. They welcomed the achievement of the 2017 deficit target despite the weaker than expected growth outturn. Directors encouraged the authorities to focus on improving tax administration, as associated revenue gains will create space for public investment. They highlighted the need for a comprehensive pension reform to increase coverage and progressivity.

Directors welcomed improvements in the monetary policy framework which will help further refine the central bank's decision making process and, combined with clear communications, will preserve the anchoring of inflation expectations. They noted that the current monetary policy stance should be conducive to a recovery in activity and that reducing the rate further in line with inflation expectations could be warranted if the recovery faltered. Directors agreed that the flexible exchange rate regime has served Colombia well and should remain the first line of defense against global shocks as well as help accumulate adequate buffers.

Directors noted that the banking system has been resilient amid the economic slowdown, reflecting partly effective financial supervision and ample capital and liquidity. They welcomed recent regulatory measures to homogenize banks' loan restructuring practices and to bring regulation closer to Basel III standards, including through the implementation of the conglomerates law.

[2] At the conclusion of the discussion, the Managing Director, as Chairman of the Board, summarizes the views of Executive Directors, and this summary is transmitted to the country's authorities. An explanation of any qualifiers used in summings up can be found here: http://www.imf.org/external/np/sec/misc/qualifiers.htm.

Colombia: Selected Economic Indicators

	2016	2017	Proj. 2018
	(Annual percentage changes, unless otherwise indicated)		
National Income and Prices			
Real GDP	2.0	1.8	2.7
Consumer price index (period average)	7.5	4.3	3.5
Consumer price index (end of period)	5.8	4.1	3.4
GDP deflator	4.9	4.8	3.3
Terms of trade (deterioration -)	-3.0	7.9	1.7
Real effective exchange rate (depreciation -)	-4.7	2.8	0.6
	(In percent of GDP, unless otherwise indicated)		
Public finances			
Central government balance	-4.0	-3.6	-3.1
Combined public sector	-2.8	-2.9	-2.5
Public debt 1/	50.4	50.2	49.9
External Sector			
Current account (deficit -)	-4.3	-3.4	-2.6
External debt	49.6	47.5	46.6
Of which: Public sector	32.1	30.5	30.0
GIR in percent of short-term debt	115.3	135.3	126.4
Savings and Investment			
Gross domestic investment	24.7	23.4	23.6
Gross national saving	20.4	20.0	21.0
	(12-month percentage changes, unless otherwise indicated)		
Money and credit			
Broad money (M2)	11.5	4.2	9.8
Credit to the private sector	7.7	11.0	7.5
Interest rate (90-day time deposits; percent per year)			
Nominal	6.9	5.3	...

Sources: Colombian authorities; and Fund staff estimates and projections.
1/ Includes Ecopetrol and Banco de la Republica's outstanding external debt.

INTERNATIONAL MONETARY FUND

COLOMBIA

STAFF REPORT FOR THE 2018 ARTICLE IV CONSULTATION

April 16, 2018

KEY ISSUES

Context. The Colombian economy is at a turning point, recovering from the large oil price shock of 2015–16 that put a break on high growth, pushed up inflation, and widened the current account deficit. A very strong policy framework and well-executed policies, including a tax reform, narrowed external imbalances and laid the foundations for an economic recovery. Growth picked up in 2017H2 and inflation has been hovering around the top of the target band.

Outlook and risks. The outlook is positive but risks remain. Increased infrastructure investment, easier demand policies, and improving global conditions will lift growth to 2.7 percent in 2018. Inflation will remain within the target band as the effects of past shocks dissipate and indexation pressures moderate. The current account deficit will continue to narrow on the back of higher oil prices and increasing nontraditional exports. While the ongoing recovery in global growth has reduced some external risks, global financial markets are vulnerable to a sudden, sharp tightening in financial conditions as a result of an unexpected increase in inflation and/or an escalation of trade or geopolitical tensions. Moreover, Colombia's exposure to tighter global financial conditions has increased with higher foreign participation in local bond markets.

Policy advice. Fiscal consolidation should continue, while there is some room to cut policy rates further—if inflation expectations continue to converge to the 3 percent target and growth underperforms. It will be important to communicate monetary policy decisions more clearly. The medium-term agenda is centered on lifting inclusive growth and productivity through structural reforms, while preserving macroeconomic stability. Top structural priorities include promoting infrastructure investment, lowering barriers to international trade, and tackling labor-market informality.

Elections. Presidential elections scheduled for May-June 2018 are widely-expected to ensure policy continuity and a strengthening of the reform agenda. Center-right parties gained strength in the Congressional elections that took place in March 11; rating agencies noted that this outcome should be conducive to a continued strong policy framework.

Approved By
Robert Rennhack (WHD) and Mary Goodman (SPR)

The team comprising Jorge Roldós (Head), Sergi Lanau, José Daniel Rodríguez-Delgado and Frederik Toscani (all WHD), Alina Iancu (SPR), Farid Jimmy Boumediene (MCM) visited Colombia during February 19–March 2. Tomás Gonzalez (OED, Senior Advisor) also participated in the policy discussions.

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ANNEX

BACKGROUND

1. **Colombia's very strong policies and structural reform agenda—including the implementation of the peace agreement—have contributed to a broadly stable economic environment.** Strong policies led to a successful adjustment and structural reforms have improved the business climate. Colombia's accession to the OECD is almost complete and 23 out of 26 committees have granted their clearance. The implementation of the 2014–18 Development Plan has rightly focused on improving access to education and infrastructure. The peace agreement's emphasis on rural development stands to further reduce inequality. Despite the economic slowdown since 2014, key social indicators have improved with poverty declining from 21.9 percent in 2014 to 17 percent in 2017, and inequality improving (Gini coefficient falling from 53.8 percent in 2014 to 50.8 percent in 2017). The government's efforts to improve transparency and access to information, and to strengthen the legal framework and government structure should contribute to lower corruption.

2. **Presidential elections scheduled for May-June 2018 are widely-expected to ensure policy continuity and a strengthening of the reform agenda**. Center right parties gained strength in the Congressional elections that took place in March 11; rating agencies noted that this outcome should be conducive to a continued strong policy framework. The campaign platforms of the three leading center candidates, Ivan Duque (center-right), German Vargas Lleras (center-right) and Sergio Fajardo (center-left), who latest estimates suggest will combined capture about 2/3 of total votes, share central elements of the current administration's agenda including explicit commitments to macro-fiscal sustainability and plans to promote economic diversification and formalization including through further reduction of firms' tax burden. They all consider important to align the pace of public debt reduction with the country's growth outlook, in line with the constitutional mandate for fiscal sustainability. Mr. Vargas Lleras calls for further lowering corporate tax rates financed by reducing tax evasion. At the same time, the left-leaning candidate Gustavo Petro, endorses a larger role for the public sector including on health, education and pensions, financed with higher taxes. He also calls for expanding the public development bank to fund an agro/industrial transformation. All candidates include reducing corruption and pension reform as priorities.[1]

3. **Past Fund Advice.** Policy measures taken since the 2017 Article IV consultation have been broadly aligned with past Fund advice. The central bank continued its data-dependent easing cycle to support the recovery. The proceeds of the tax 2016 reform helped protect social spending while achieving the structural deficit target. Regulatory changes to banks' risk management and loan restructuring practices have improved the monitoring of NPLs and the implementation of the conglomerate laws has continued. Efforts to improve trade logistics, access to education and infrastructure are rightly targeted to improve productivity and economic diversification.

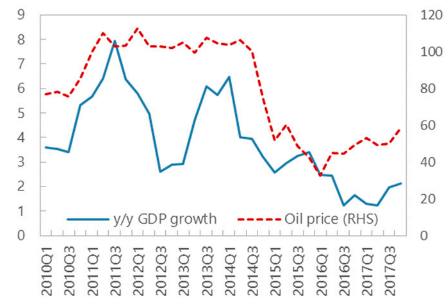
[1] Obtained from each candidates' published platform and recent public statements as of April 9, 2018.

CONTEXT: THE COLOMBIAN ECONOMY AT A TURNING POINT

4. Growth is beginning to recover with inflation declining to target, as Colombia completes the adjustment to the large oil price shock of 2015–16.

- The economy showed signs of revival in 2017H2, growing at 1.9 percent y/y, after reaching a trough in 2017H1. This turnaround follows four years of reductions in growth since it reached 4.9 percent in 2013. Exports contracted early on, followed by a decline in domestic demand as the drop in national income was internalized (Figure 1 and Box 1).

GDP Growth and Oil Prices



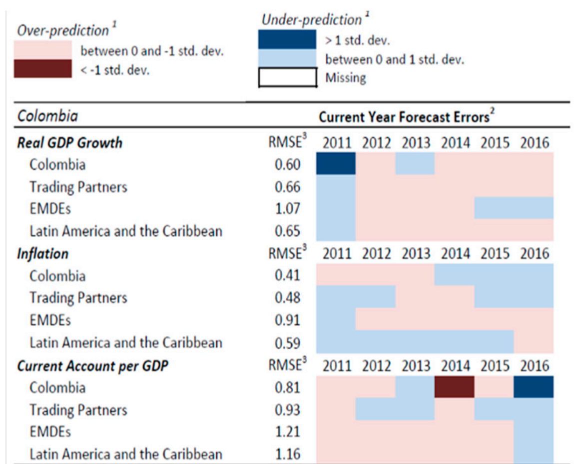
Sources: Banrep; and GAS.

Box 1. Macroeconomic Forecast Errors

In recent years the forecast errors of projections included in WEO for Colombia have been smaller than for its peers. For GDP growth, during 2011–16, the square error (RMSFE) of the outturn vis-à-vis the projection made in the previous Spring WEO, has been 0.60, smaller than the average for Latin America (0.65) and all emerging markets (1.07). Similarly, the forecast for inflation and current account has been more precise than for its peers.

Both external and domestic factors contributed to optimistic growth forecast since 2014. On average, GDP growth forecasts have been 0.4 percentage point higher than the outturn.

- On the external front, except for 2016, the forecast for oil prices has been between 3 and 15 percent optimistic. Trading partner growth has also underperformed previous forecast especially in 2016.
- On the domestic front, a truck-driver strike contributed to a deeper-than-expected slowdown in 2016, while delays in 4G projects are behind the 2017 forecast error.



Source: WEO Historical databases.
1. Standard deviation of the actual series in question.
2. Forecast Error(FE) = Actual-Forecast; Refer to Figure 1 footnotes for difference between two FEs.
3. RMSE refers to forecast root mean square error normalized by standard deviation of actual series in question.
4. Additional descriptions on interpretation of heatmap and RMSE can be found in appendix.

Colombia: Real GDP Forecast Error

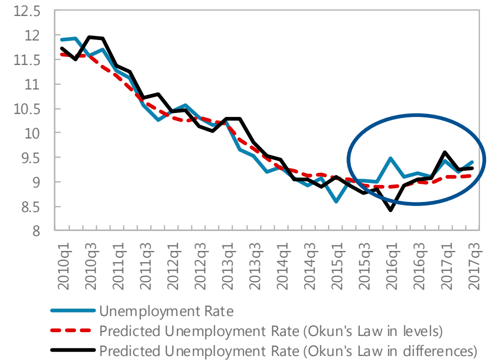
Vintages	2014	2015	2016	2017
Colombia Real GDP Growth (in percent)				
Outturn	4.4	3.1	2.0	1.8
Forecast April of each year	4.5	3.4	2.5	2.3
Current year error (pp)	-0.1	-0.3	-0.5	-0.5
Brent Oil Prices (US$ per barrel)				
Outturn	98.9	52.4	44.0	54.4
Forecast April of each year	108.0	61.5	36.1	56.3
Current year error (percent)	-8.42	-14.86	21.91	-3.40
Trading partner GDP Growth (in percent)				
Outturn	2.9	2.8	1.8	2.6
Forecast April of each year	3.0	2.8	2.3	2.5
Current year error (percent)	-0.1	0.0	-0.4	0.1

Source: WEO and Fund staff calculations

- Unemployment increased to 9.7 percent in 2017Q4, up from 8.6 percent in 2015, in line with standard Okun's Law predictions, and employment creation slowed markedly.

- Inflation fell steadily after peaking at 9 percent y/y in July 2016, as the effects of weather shocks and large nominal depreciation faded. Headline inflation fell below 4 percent in 2017H2 but remained slightly above the target band of 2–4 percent in December 2017. Inflation expectations remained anchored throughout.

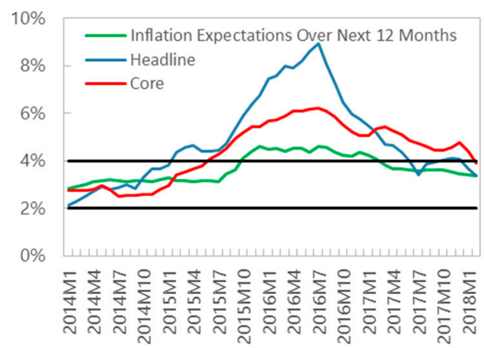
Unemployment Rate



Source: IMF staff estimates based on data from DANE.

5. Significant external adjustment occurred as policies were tightened in response to the oil-driven loss of national income. The current account deficit initially widened to 6.4 percent of GDP in 2015. Currency depreciation and policy adjustment compressed domestic demand and imports in 2016−17, while non-traditional exports started to pick up pace by late 2017—but are still below the 2015 level. The decline in the trade deficit, lower repatriation of profits by oil companies and lower deficits in services narrowed the CA deficit to 3.4 percent of GDP in 2017 (Figure 2).

Inflation
(Y/Y percent)



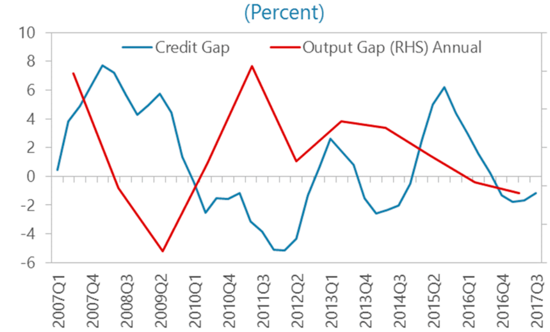
Sources: Banrep; and Haver.

6. As the adjustment process advanced and the output gap widened, the policy focus has shifted to support the recovery. Tightening monetary and fiscal policies in 2015–16 in response to the oil price shock was fully appropriate (Figure 3). In 2017, policies moved to a more neutral stance, following a 300 bp reduction in policy rates and no fiscal impulse.

7. Real credit growth remained broadly stable and the credit gap closed, suggesting the credit cycle is aligned with the business cycle. Consumer credit growth decelerated with the slowdown in demand (Figure 4). Commercial credit growth remained negative but contracted more slowly towards end-2017, suggesting a better outlook for corporate investment. NPLs increased to 4.2 percent in December 2017 from 3 percent in 2016, while banks remain sound.

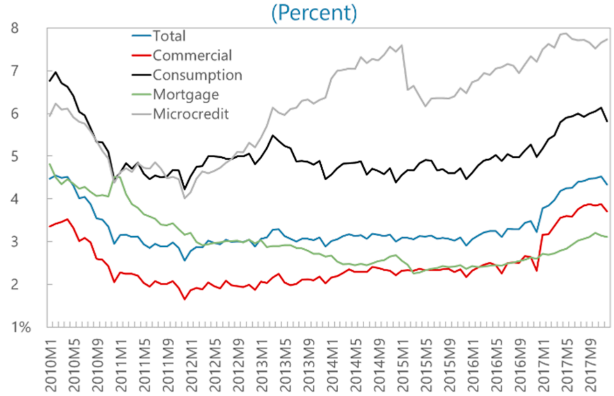
Economic Slowdown affects Credit Portfolio

Credit and Output Gap
(Percent)



Source: IMF staff calculations.
Note: Gaps are calculated through the use of an HP Filter.

NPLs by Sector
(Percent)



Source: Superintendencia Financiera de Colombia.

8. **Implementation of the peace agreement with the FARC is progressing steadily.** The Kroc Institute, an independent observer, reports implementation is on track and slightly faster than other peace agreements. A number of rural development plans are underway, but the substitution of illegal crops is progressing more slowly than expected due to security problems in some areas.

OUTLOOK AND RISKS: A RECOVERY IN THE MAKING

9. **Policy easing and an improving global environment will lift growth to 2.7 percent in 2018.** A slightly expansionary fiscal policy and the lagged effects of monetary policy easing in 2017 will support domestic demand. Investment is projected to increase strongly on the back of 4G infrastructure projects, the 2016 tax reform, and a reviving oil sector. Overall, financial conditions will remain supportive of the recovery, as well-provisioned NPLs peak in 2018H2. Medium-term growth could reach 3.5 percent if strong structural reforms are implemented.

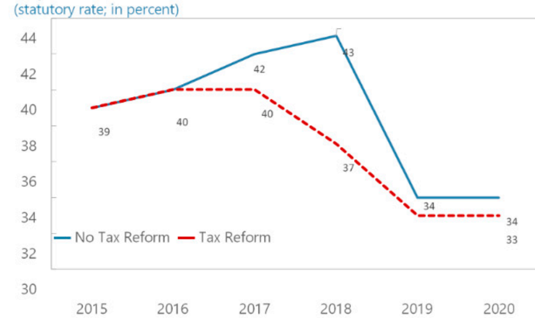
Investment Outlook

Key Drivers of Investment Rebound in 2018
Increase in Investment
(pp of real GDP)

Factor	Impact
4G	0.1
Oil Sector	0.4
Tax Reform	0.6
CPS Public investment	0.1
Subtotal	1.2

Source: National authorities and Fund staff estimates

Corporate Tax Rate and the 2016 Tax Reform
(statutory rate; in percent)



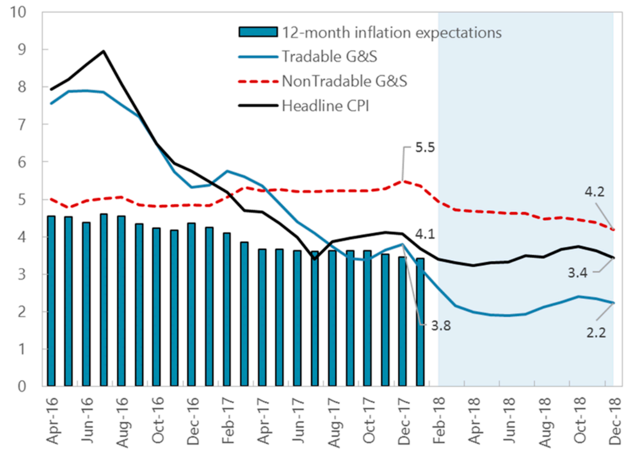
Sources: National authorities

10. **Inflation is projected to end 2018 at 3.4 percent—well within the target band.** Inflation inertia in Colombia is high but three factors will push inflation down: (i) the inflationary effects of the January 2017 VAT increase will disappear from y/y inflation rates in spring 2018; (ii) indexed prices

will reset to December 2017 inflation, lower than in December 2016; (iii) a stable exchange rate and benign weather conditions.

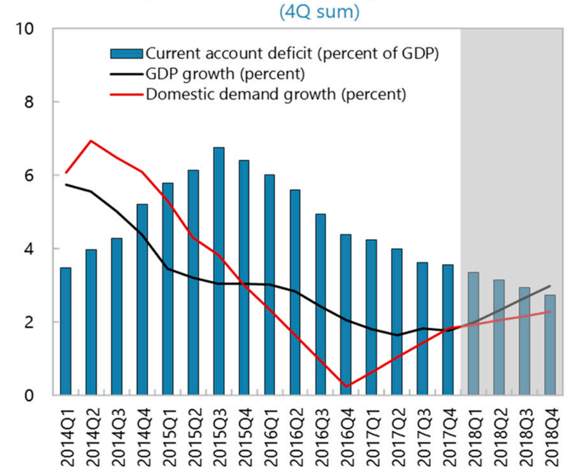
Inflation and the Current Account

Headline, Tradable and NonTradable Inflation



Sources: Banrep; and Haver.

CA djustment to Permanently Lower Oil Prices
(4Q sum)



Sources: Banrep; and IMF staff caluclations.

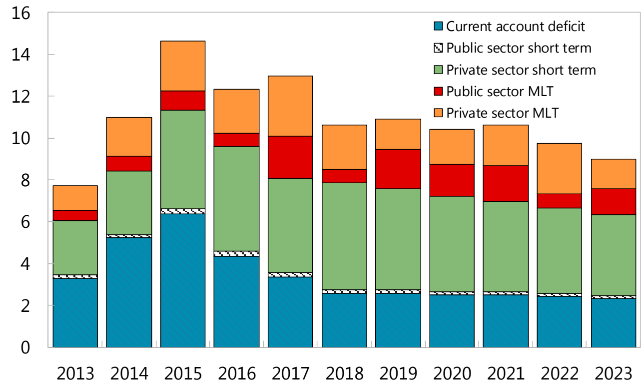
11. The current account is projected to improve to -2.6 percent of GDP this year and narrow further over the medium term. The favorable global growth and oil market outlook will further boost exports, while imports will recover only gradually. Whereas commodity exports will increase in the near term, reflecting higher oil prices, nontraditional exports will be the main driver of the external adjustment over the medium term. Staff analysis of trade elasticities and the response of commodity exporters to large depreciations point to a rebound in nontraditional exports with long lags, suggesting that the impact of the 2015–16 depreciation on nontraditional export growth has yet to fully materialize (SIP 1). FDI will continue to finance a sizable share of the current account deficit.

12. Colombia's external sector position in 2017 was moderately weaker than implied by medium-term fundamentals and desirable policy settings (Annex I). However, this assessment reflects the fact that the large depreciation and strong policy response to the decline in oil exports take time to lead to a stronger external position. As such, staff's assessment is that policies are on their desirable course to contribute to a further narrowing of the current account deficit over the medium term, and there is no need for additional tightening beyond what is already planned.

13. Risks have decreased somewhat but remain tilted to the downside (RAM).

- Global growth and the oil market outlook have improved but the likelihood of a sharp tightening of global financial conditions remains high. The latter could be triggered by an unexpected increase in U.S. inflation and/or an escalation of trade or geopolitical tensions, that have intensified recently and increased the probability of a spike in global risk-aversion. Regionally, risks related to the crisis in Venezuela are growing with gross monthly migration doubling in late 2017 leading to about half a million Venezuelans migrants living in Colombia. If this pace continues, available information, which is rather sketchy, suggests migrants could reach 1.0–1.5 million at end-2018, depending on how many stay in Colombia or continue to other neighboring countries.[2] On the domestic front, electoral risks appear to be contained, while a slower-than-expected recovery could accelerate NPL growth.

Gross External Financing Needs
(In percent of GDP)



Sources: National authorities and Fund staff estimates and projections.

- Colombia's very strong policies, flexible exchange rate, reserve buffers and access to the FCL would cushion the effects of external shocks. Gross external financing needs will decline to about 10 percent of GDP over the forecast horizon. Nonresident participation in the local bond market reached 27 percent in 2017, increasing exposure to foreign investor sentiment.

Authorities' Views

14. The authorities also expect the recovery to gather pace in 2018 and inflation to fall further. Like staff, they project growth to increase to 2.7 percent, supported by investment and exports. The authorities expect inflation to continue to converge to target, reaching 3.5 percent in 2018. They share staff's general view on risks and Colombia's exposures, and noted that risks have evolved during the last few years including those stemming from oil prices, U.S. monetary normalization and lately, Venezuela. On the latter, they perceived the current number of migrant to be manageable with the assistance and control measures recently announced. However, larger scale migration would require international assistance. The authorities agreed that the exchange rate remains the first line of defense against external shocks and that external adjustment needs to continue, but noted the large uncertainty around the current account norm, which they estimate between -3 and -0.5 percent of GDP.

[2] Staff and the authorities agreed that the fiscal costs of Venezuela-related migration are modest so far (0.1-0.2 percent of GDP).

Colombia: Risk Assessment Matrix[1]

Source/Likelihood/Time Horizon of Risks	Impact	Policy Advice
Global		
Tighter global financial conditions. Against the backdrop of continued monetary policy normalization and increasingly stretched valuations across asset classes, an abrupt change in global risk appetite (e.g., due to higher-than-expected inflation in the U.S) could lead to sudden, sharp increases in interest rates and associated tightening of financial conditions. Higher debt service and refinancing risks could stress leveraged firms, households, and vulnerable sovereigns, including through capital account pressures in some cases. **High** ***ST/MT***	**High**	Use the exchange rate as shock absorber and international reserves to tame disorderly market behavior
Lower energy prices, driven by weakening OPEC/Russia cartel cohesion and/or recovery of oil production in the African continent. Low ***ST/MT***	**High**	Use the exchange rate as shock absorber and international reserves to tame disorderly market response
Retreat from cross-border integration. Fraying consensus about the benefits of globalization leads to protectionism and economic isolationism, resulting in reduced global and regional policy and regulatory collaboration with negative consequences for trade, capital and labor flows, sentiment, and growth. **Medium** ***ST/MT***	**Medium**	Speed-up structural reforms and pro-diversification measures
Policy uncertainty. Two-sided risks to U.S. growth with uncertainties about the impact of the tax bill and its international spillovers; uncertainty associated with negotiating post-Brexit arrangements and NAFTA and associated market fragmentation risks; and evolving political processes, including elections in several large economies weigh on global growth. **Medium** ***ST/MT***	**Medium**	Use the exchange rate as shock absorber and international reserves to tame disorderly market behavior
Structurally weak growth in key advanced economies: Low productivity growth (U.S., euro area and Japan), high debt, and failure to fully address crisis legacies by undertaking structural reforms amidst persistently low inflation (euro area and Japan) undermine medium-term growth. **High** ***MT***	**Medium**	Speed up reforms to reduce trade barriers and improve diversification.
Significant China slowdown and its spillovers: While ongoing efforts by the Chinese authorities to "de-risk" the financial system are welcome, too fast an adjustment and improper sequencing of actions may adversely affect near-term growth (low likelihood). Over the medium term, overly ambitious growth targets, including by over reliance on credit stimulus and investment, lead to unsustainable policies, reducing fiscal space, further increasing financial imbalances. A sharp adjustment would weaken domestic demand, with adverse international spillovers, including a pullback in capital flows to EMs (medium likelihood). Low (***ST***) **Medium** (***MT***)	**Medium**	Speed up reforms to reduce trade barriers and improve diversification. Provide monetary policy support only if expectations are anchored
Colombia-specific		
Slower than expected recovery, perhaps due to delays in infrastructure projects, sluggish exports, impact of NPLs on bank balance sheets, or political uncertainty. **Medium** ***ST/MT***	**High**	Speed up reforms to reduce trade barriers and improve diversification. Provide monetary policy support only if expectations are anchored
Spillovers from Venezuela turmoil. **Medium** ***ST***	**Medium**	Provide assistance to border region. Seek donor support in case of large-scale migration

[1] The Risk Assessment Matrix (RAM) shows events that could materially alter the baseline path (the scenario most likely to materialize in the view of IMF staff). The relative likelihood is the staff's subjective assessment of the risks surrounding the baseline ("low" is meant to indicate a probability below 10 percent, "medium" a probability between 10 and 30 percent, and "high" a probability between 30 and 50 percent). Non-mutually exclusive risks may interact and materialize jointly. "Short term (ST)" and "medium term (MT)" are meant to indicate that the risk could materialize within 1 year and 3 years, respectively.

POLICY ISSUES

Strong demand policies have to be fine-tuned to complete the adjustment to lower oil prices. As the recovery takes hold, the focus should shift to structural policies to lift inclusive growth and productivity—including promoting infrastructure and private investment, tackling labor market informality and lowering barriers to trade.

A. Structural Reforms to Support Inclusive Medium-Term Growth

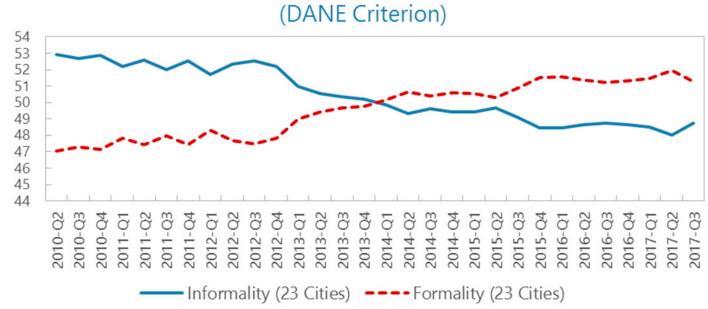
Background

15. As noted in last year's report, structural reforms to improve the functioning of product and labor markets are critical to diversify away from oil and strengthen inclusive medium-term growth. Colombia has made important improvements in governance (see Box 2) and the business environment over the last decade. Nevertheless, productivity growth has been weak in recent years and the WEF and Doing Business surveys show poor scores in infrastructure, logistics, trading across borders, and burden of regulation (Figure 6), as well as in hiring and firing costs and labor taxation. Logistics costs account for 15 percent of corporate sales, mostly due to inefficient transportation.

16. After delays in execution, 4G infrastructure projects began in earnest during 2017. The first wave of projects secured funding but some of the second wave projects are still securing financing. The authorities have moved decisively to address some contractual problems and remove financing constraints in the infrastructure sector (see Box 3). Thus, 4G capex should increase by about 0.2 percent of GDP per year in 2018–19. The government is also pressing ahead with its infrastructure agenda to foster regional development under the peace agreement.

17. Payroll tax cuts and increasing education levels contributed to a substantial fall in labor informality. Informality fell by 3.2−8.2 percentage points between 2007 and 2017, depending on the definition.[3] Labor market and tax reforms in 2010−12, including a reduction in payroll taxes of 13.5 percentage points played an important role, as did an increase in workers with at least secondary education. In Latin American comparison, labor informality in Colombia is in line with that predicted on the basis of its GDP per capita level (see Box 4, SIP 2).

Labor Informality and Formality
(DANE Criterion)



Source: DANE.

[3] The statistical institute (DANE) favors a size-based definition of labor informality, where workers in firms below 5 employees are defined as informal. Alternatively, informality can be defined as workers not contributing to social security.

Box 2. Governance and Transparency

Colombia: Anti-Corruption Legal Framework

Description	Law
Criminalization of bribery of domestic and foreign public officials	Law 599 of 2000
Anti-Corruption Statute	Law 1474 of 2012
Transnational Corruption Act	Law 1778 of 2016

Source: National authorities

Colombia has a comprehensive anti-corruption legal framework. Existing laws provide an ample toolkit to fight transnational offenses and sanctions related to public contracting. In 2013, Colombia joined the Convention on Combating Bribery of Public Officials. Other recent measures include a decree establishing the list of politically exposed persons who would be subject to additional surveillance. In May 2017 Colombia obtained the accession approval from the OECD Public Governance committee which oversees issues related to governance structure, transparency and accountability. A high-level report mechanism forum was established to receive and process any corruption suspicions. Pending priorities include to strengthen protection of whistleblowers and regulation on lobbying activities. Continued efforts to fighting corruption should also focus on the subnational/regional/local level.

Improvements in the legal framework have been accompanied by wider access to information and organizational changes within the public sector. The Transparency and Access to Information Law (2014) defined a set of public sector employees and entities that are obliged to publish information. The citizen participation law (2015) sets organizational principles to guide community selection and planning of public investment projects. Other publicly available data sources include the public contracting information system (SECOP) which has helped identify instances in which public contracts are illegally modified. The creation of the national infrastructure agency (ANI) helped deal with a key source of corruption (public contracting/procurement) and represents an example of the efforts to improve the public sector organization by ring-fencing agencies/activities historically prone to corruption.

Despite such a strong framework, some indicators suggest still weak perception of corruption. Surveys suggest that corruption has remained in the top 2 of the most problematic factors for doing business in Colombia since 2012; and Colombia's trust in politicians has worsened somewhat since then reaching a score of 1.7 (out of 7) in the WEF's 2017-18 report down from 2.3 in 2012–13. Recent analysis suggests Colombia fits well a common transitional process in which perception of corruption may in fact rise even when additional efforts are put in place to investigate and uncovered such activities -the authorities share this view.[1]

In sum, as other countries in the region, Colombia has further strengthened its anti-corruption legal framework combined with improved data transparency and organizational changes. It will nevertheless take time for these mechanisms, proven to uncover and control corruption, to have a strong impact on corruption perceptions.

[1] See https://blogs.imf.org/2017/09/21/corruption-in-latin-america-taking-stock/

Box 3. Recent Progress on the 4G Infrastructure Agenda

After a strong start in 2016, the 4G infrastructure agenda suffered delays in 2017. During 2016, about eight 4G projects reached financial closure and some started the building phase. The unfolding of the Odebrecht scandals led to the annulment of a project that was not part of the 4G agenda, but nevertheless created legal uncertainty about liquidation values in cases of corruption and slowed down financial closures. In response to the scandal, banks tightened credit conditions to infrastructure projects. No new other 4G projects reached financial closure until late 2017; delays are estimated to have reduced GDP growth between 0.2 and 0.5 percent.

Financing of 4G Agenda 1/

	US$ billion	Share
Local	5.8	64.7
Equity Local Sponsor	2.1	23.3
Local Bank Debt	2.6	28.7
FDN Debt	0.7	7.3
Other local debt	0.5	5.3
International	3.2	35.3
Equity International Sponsor	0.7	7.7
Equity International Fund	0.2	2.3
International Bank debt	0.8	9.3
Multilateral banks debt	0.4	4.0
Capital markets debt	1.0	11.3
Pension fund debt	0.1	0.7
Total	9.0	100.0
Memo items:		
Total Debt	6.0	66.7
Total Equity	3.0	33.3

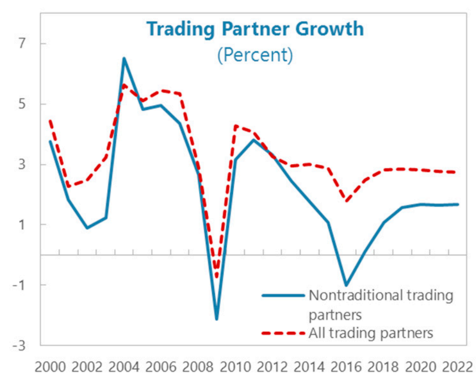
Sources: National authorities; and Fund staff calculations

1/ Based on 13 Financial closures as of end-2017

The authorities reacted promptly and modified the legislation to provide contractual certainty. A new infrastructure law (Law 1882) that clearly specifies procedures to deal with corruption which protect third parties that acted in good-faith was approved in January 2018. The law also improves transparency and procedures for land acquisition and annulment settlement. The new legislation had an immediate effect in restarting the process of financial closures for other projects.

Moreover, the government development bank (FDN) received a capital injection and facilitated the diversification of infrastructure funding away from local banks. FDN received a capital injection from the proceeds of the privatization of an electricity company sold in 2016. Due in part to FDN efforts, the 4G agenda has received funding from other local and foreign sources. About two thirds of the financing so far has been local which includes mostly equity and local bank loans. Debt and equity funds have attracted funding from local and international institutional investors. Furthermore, 4G projects have issued some global bonds as well as received foreign equity and bank loans. Besides direct participation in some projects, FDN has also provided bridge financing and long-term peso loans to foreign lenders to facilitate hedging.

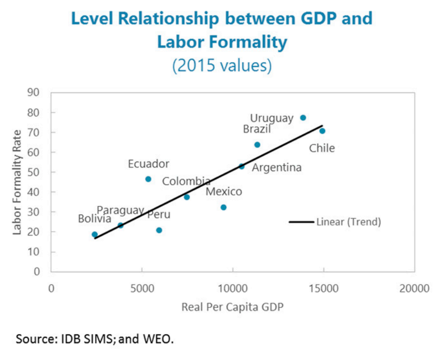
18. While the export outlook is positive, sluggish trading partner growth and barriers to trade have slowed down nontraditional exports. Despite a large real depreciation since 2015, nontraditional exports grew just 7 percent last year, in part due to weak regional growth (Annex I and SIP 1). Moreover, trade barriers, slow customs, infrastructure gaps, and inefficient road transportation add to the cost of exporting.



Source: COMTRADE.

Box 4. Labor Informality

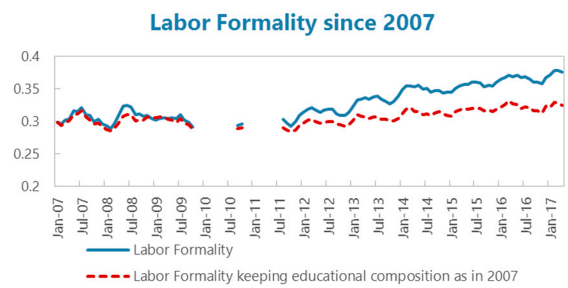
Colombia has achieved an important reduction in labor informality. The share of workers who are not contributing to social security dropped from 70 percent in 2007Q1 to 62.3 percent in 2017Q3. The level remains high but relative to other countries in the region informality is in line with Colombia's GDP per capita.



Source: IDB SIMS; and WEO.

Policy initiatives have contributed to this decline. Among a large number of formalization initiatives, such as the 2006 *Entrepreneurship Law* and the 2010 *Formalization and Job Creation Law*, the 2012 Tax Reform was particularly important in pushing formalization by cutting payroll taxes by 13.5 percentage points. Impact evaluations suggest that the latter led to several hundred-thousand additional formal jobs.

A decomposition of the fall in informality suggests that an improvement in the skill level of the labor force has also been crucial. Informality decreases sharply with education levels. Indeed, 85 percent of workers with postgraduate education are formal but only 9 percent of those without any education are. Since 2007, the formality rate for most education levels has increased modestly (e.g., from 6.7 to 9.3 percent for uneducated workers) but the largest gains are due to an increase in the average level of education. The latter accounts for 5.2 percentage points of the 7.8 percentage points fall in informality between 2007Q1 and 2017Q2.



Source: IMF Staff calculations based on DANE. Data missing for most of 2010-11.

Staff simulations suggest that additional labor market reforms, as well as further cutting firm entry costs, could further lower informality. Staff calibrated STRESS model which is based on one of the key tradeoffs of informality for firms—formal firms have access to larger markets (such as exporting and supplying the government) while informal firms avoid taxes which the formal sector needs to pay. Simulations show that permanently cutting entry costs in the formal sector or labor reforms such as reducing payroll taxes lead to a steady state with lower informality, lower unemployment and higher income, supporting the case for these reforms (see SIP 2 and Anand/Khera (2016) and Munkacsi/Saxegaard (2017)).

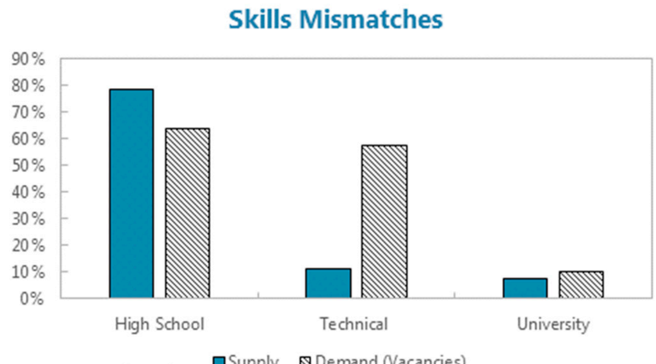
Policy Advice

19. **As the adjustment to lower oil prices is completed and the economy recovers the authorities should give an extra push to productivity-enhancing reforms.** Although public investment will be constrained by the fiscal rule, the 2016 tax reform will spur private investment and complement infrastructure investments—including PPPs and subnational government investment. Further efforts towards training and formalization should also be a priority, together with measures to facilitate export growth.

20. **Avoiding delays in 4G infrastructure projects and implementing planned reforms to road transportation are essential**. The authorities should ensure permits and environmental assessments are ready promptly and remove other obstacles to infrastructure projects. Connection of tertiary roads to the broader transport network, as envisaged for the regions affected by the

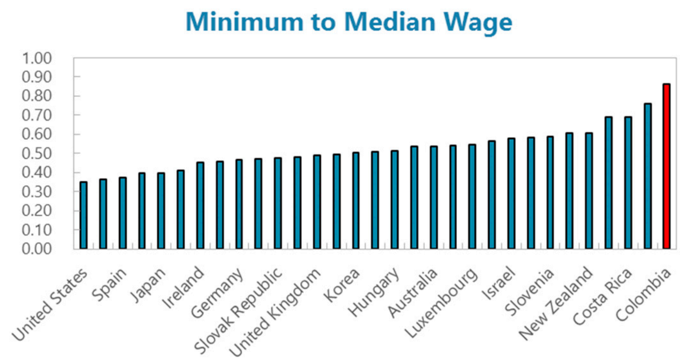
conflict, are essential. Completing the implementation of measures to renew the fleet of trucks and further develop fluvial transportation would also help make Colombian producers more competitive.

21. A continued focus on providing high quality education is key for further gains in productivity and formality of the labor force. Skill mismatches, especially at the technical level, remain large. Further strengthening the coverage and quality of education by building on the expansion of higher education coverage from 37 percent in 2010 to 52 percent of the age cohort in 2017 is crucial. Internalizing fiscal constraints, initiatives could focus on the supply of higher education as well as on programs to support access for low-income students.



Source: Lora (2015)

22. A range of structural reforms would also help reduce informality further. First, non-wage labor costs remain high. Employers pay a four-percent payroll tax to finance so-called *Cajas de Compensación Familiar* which bundle a wide range of services from housing and education to sports and entertainment. Alternative sources of financing for the *Cajas* would be preferable and the services they provide could be reviewed to avoid duplication with other government programs. Second, given large regional differences in human capital, labor productivity varies strongly and the national minimum wage (already high in an international comparison) is much more binding in some regions than others, fomenting informality where it is binding. A regionally differentiated minimum wage could be considered. Third, reducing registration fees for the *registro mercantil* for small firms and cutting red tape through the *Ventanilla Unica Empresarial* would also improve firm formality.

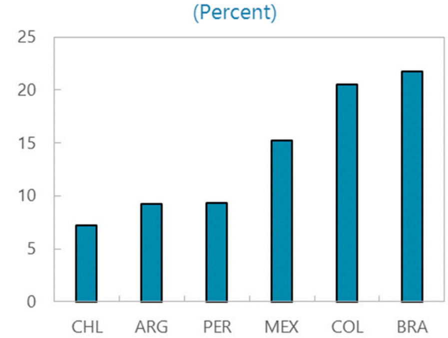


Source: OECD.

23. Tariffs should be realigned to lower the dispersion across products. On average, tariffs are low by regional standards and have fallen significantly in recent years, narrowing the gap with the OECD average to 1.5 percentage points. However, dispersion is high, especially in agricultures. Nominal tariffs average 18 percent but they are as high as 49 and 70 percent for dairy and beef products, respectively. Recent reductions in the VAT for capital goods and in tariffs for intermediate inputs not produced in the country will contribute to a reduction in export costs.

24. A review of nontariff barriers to trade is in order. The average number of nontariff barriers per product category grew from four to 16 in 2001–14. Their tariff equivalent is estimated at 20 percent, which is high by regional standards. A review and rationalization of these new measures with a focus on the largest import categories could reduce the cost of producing tradable goods.

Nontariff Measures--Tariff Equivalent
(Percent)



Source: Fedesarrollo, Universidad EAFIT.

Authorities' Views

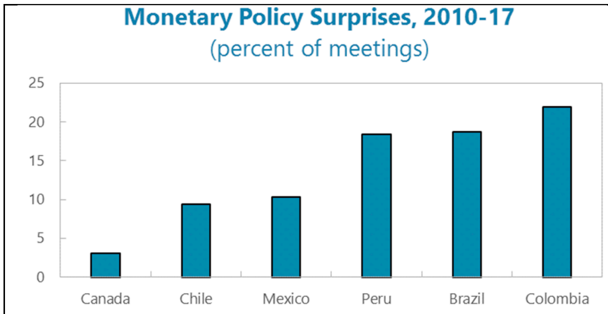
25. The authorities agreed that higher productivity is critical to boost growth. They are confident that the 4G infrastructure agenda will take off this year and agreed that the new infrastructure law has succeed to reignite investors' appetite. The authorities stressed the positive role of the 2012 tax reform in giving the labor market the flexibility necessary to reduce informality and sustain relatively low rates of unemployment after the commodity shock. They also agreed that further structural reforms and improvements in higher education would help, while noting that it is necessary to carefully study what the best instruments are to stimulate broad-based access to high quality education. The authorities are working to facilitate international trade and have made customs procedures faster by reducing duplications in port inspections among other measures.

B. Fine Tuning Monetary Policy Decisions

Background

26. The central bank continued an easing cycle started in December 2016 when inflation was on a firm downward path. The central bank cut the policy rate by 325 bps from a peak of 7¾ percent, somewhat faster than expected. Medium-term inflation expectations continue to fall and stood at 3.25 percent in January 2018. Non-tradable inflation is sticky at over 4.5 percent but is expected to fall due to more favorable indexation dynamics and the continued slack in the economy.

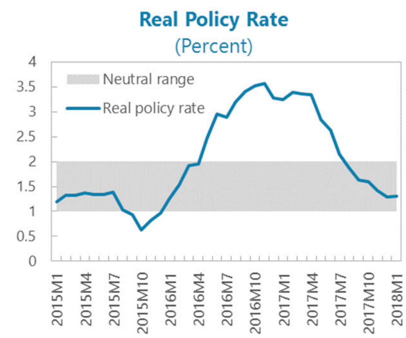
27. The Central Bank frequently surprised markets with its policy decisions. Since 2010, the central bank surprised markets in almost 1/4 of all cases, and in half the policy meetings last year. To strengthen the analysis behind policy decisions and align them with major data releases, the bank reduced the number of policy decision meetings per year to 8 (from 12) last November.



Source: Staff estimates.

Source: Banrep.

Policy Advice



Sources: Banrep; and Haver.

28. **There is scope to further cut the policy rate as inflation converges to target.** The real rate is currently assessed to be marginally expansionary and there is limited space for more cuts. But if lower headline inflation translates into lower expectations, modest additional easing could be warranted in light of the negative output gap, if growth were to surprise on the downside.

29. **It is important to communicate monetary policy decisions more clearly.** The changes in the central bank decision making process that aim to strengthen the analysis behind decisions are welcome. Going forward, the central bank should aim to craft communications that are as consistent as possible over time and more clearly spell out the Board's views on the evolution of policy trade-offs (Box 5).

Authorities' Views

30. **The authorities agreed that policy rate decisions will continue to be data dependent and see limited room for additional cuts.** They consider the easing cycle close to conclusion but continue to monitor the inflation-activity tradeoff closely in making their decisions. While they noted that market surprises are not always a problem, they agreed that despite their conscious effort to better explain rate decisions, press releases and communication more broadly could be expanded and fine-tuned.

C. Continuing Near-Term Fiscal Consolidation

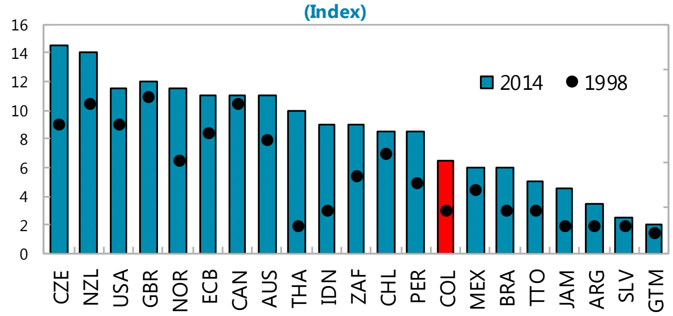
Background

31. **A better than expected oil revenue outlook will help achieve the 2018 deficit target**. Oil revenue will increase to about 0.6 percent of GDP due in part to an improved profitability in Ecopetrol, which will limit the expenditure cuts required to achieve the structural-balance target. The central government fiscal stance will imply a mild contraction (negative fiscal impulse) of about

Box 5. Central Bank Transparency and Communication Frameworks in Colombia[1]

The move toward inflation targeting in Colombia over the past two decades has led to better-anchored inflation expectations. An important aspect of this evolving framework has been the degree of central bank transparency which has clearly improved but still falls below that of comparator countries. Transparency provides the public with a better understanding of the central bank's objectives, and the factors that motivate its monetary policy decisions. This in turn enables public accountability and greater credibility over time. Recent Fund staff work suggests that stronger central bank transparency frameworks are associated with better-anchored inflation expectations.[2]

Central Bank Transparency Index
(Index)

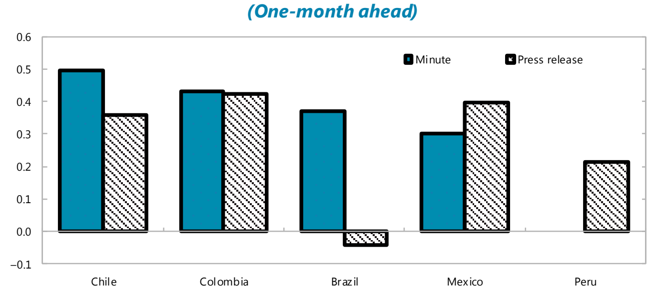


Source: Dincer and Eichengreen (2014).

The central bank's (BanRep) transparency framework includes press releases that explain the policy rate decision and provide an assessment of the balance of risks for inflation. The baseline scenario and balance of risks are delineated in quarterly monetary policy reports. In line with best practices, the central bank releases some of the data used for their monetary policy decisions (inflation, expectations, wages, employment, and GDP), and the minutes of policy meetings. However, names are not assigned to transcribed comments, and votes are not attributed. Shortcomings of the framework relate to the lack of assessments of BanRep's forecasting and operational performance.

Using a text processing algorithm, staff estimated the tone of the language used in BanRep's press releases and minutes. The tone of these documents provides some indication of future policy changes.[3] However, explicit policy guidance on the likely future direction of monetary policy has been used infrequently by BanRep—in less than one of every five statements. In comparator central banks with higher transparency scores, communication is aided by the publication of such guidance.[4] IMF (2018) highlights that the use of this forward-looking language is associated with stronger transmission of monetary policy decisions to inflation expectations.

Correlation Between "Tone" in Communication and Changes in Future Policy Rates
(One-month ahead)



Sources: Central bank websites; and IMF staff calculations.

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[1] Prepared by Yan Carrière-Swallow and Juan Yépez (WHD).

[2] See Brito and others (2018) and Chapter 3 of the forthcoming *Regional Economic Outlook: Western Hemisphere*, IMF, 2018.

[3] See chart, and IMF, 2018, for details.

[4] The Central Bank of Chile, for example, provides qualitative guidance about once every other meeting.

0.2 percent of GDP. At the consolidated public sector level, stronger expenditure execution at the subnational level will support a mild positive fiscal boost of about 0.2 percent of GDP. Public debt will decline slightly.

32. **The medium-term fiscal framework (MTFF) implies a significant fiscal contraction in 2019–20**. In order to reach the authorities' structural-balance targets, primary expenditure will have to decline by about 0.6 percent of GDP between 2018 and 2020, which combined with expected revenue gains from improved tax administration, will imply a cumulative negative fiscal impulse of about 1.4 percent of GDP. Public debt will steadily decline to about 40 percent of GDP in 2023. Efforts at the tax authority (DIAN) have focused on improving human and technological resources. The authorities' agenda to improve the profile of public debt amortizations has included swap and buy-back operations of some bonds due in 2018 and the recent issuance of a 30-year bond.

33. **Public spending does not contribute enough to improving the distribution of income in Colombia.** Among the recommendations of the expert commission on spending, a structural reform of the pension system is key to foster inclusive growth. The current pension system comprises a small non-contributory pillar and competing pay-as-you-go (PAYGO) and capitalization contributory pillars. Several diagnostic studies agree that the system is highly regressive and has very low coverage by international standards. Proposals for reform include parametric changes to the current system as well as deeper architectural reforms (see Box 6).

Fiscal Outlook

(In percent of GDP; unless otherwise indicated)

	2015	2016	2017	2018	2019	2020	2021	2022	2023
Central Government Fiscal Stance									
Headline balance 1/	-3.0	-4.0	-3.6	-3.1	-2.2	-1.6	-1.3	-1.1	-1.1
Expenditure	19.2	19.1	19.2	18.3	17.6	17.7	17.5	17.3	17.2
Fixed capital formation	2.7	2.0	2.3	1.9	1.2	1.3	1.3	1.1	1.2
Structural balance (staff estimate)	-3.7	-3.1	-2.4	-2.3	-2.2	-1.9	-1.8	-1.5	-1.6
Structural balance (staff estimate; excluding one-off)	-3.7	-3.1	-2.9	-2.3	-2.2	-1.9	-1.8	-1.5	-1.6
Structural primary non-oil balance	-1.7	-1.2	-0.7	-0.5	0.0	0.4	0.5	0.6	0.4
CG Fiscal Impulse	-1.2	-0.5	-0.5	-0.2	-0.5	-0.5	-0.1	-0.1	0.2
Consolidated Public Sector									
Headline Balance	-3.4	-2.8	-2.9	-2.5	-1.7	-0.6	-0.5	-0.4	-0.6
of which: Subnationals balance	-0.5	0.3	0.1	0.0	-0.1	0.3	0.1	0.0	-0.1
Fixed capital formation	7.2	5.3	6.0	6.0	5.3	4.9	5.1	5.0	5.0
Structural primary non-oil balance	-2.5	-0.1	-0.2	-0.4	0.1	1.0	0.8	0.8	0.5
CPS Fiscal Impulse	-0.9	-2.4	0.1	0.2	-0.4	-0.9	0.1	0.1	0.3
Public sector gross debt	50.6	50.4	50.2	49.9	48.7	46.5	44.4	42.3	40.4
Public sector net debt 3/	42.2	39.1	39.3	39.9	39.5	38.1	36.6	35.2	33.9

Source: National authorities and Fund staff estimates.
1/ Includes one-off telecom fine in 2017 (0.5 percent of GDP)

Box 6. Colombian Pension System: Diagnosis and Reform Options

The Colombian pension system has multiple components. *Colombia Mayor* is a non-contributory program aimed to provide subsistence support to elderly poor. Formal workers earning at least a minimum wage can choose to make their 16 percent contribution to a defined benefit (DB) program (government-run; ColPensiones) or to a defined contribution (DC) program (individual accounts managed by private pension funds, AFPs) (Pillar 1). All retirees are entitled to a minimum pension (one minimum wage) and most retire under ColPensiones' benefits. Finally, a voluntary savings system complements private pensions and a recently-created one (BEPs) is available for workers who make less than a minimum wage and don't qualify for a pension (and receive a government subsidy of 20 percent).

Low coverage and regresivity are two key weaknesses of the Colombian pension system. Only about one third of the pension-age population receive a contributory pension and about one half of pension-age population is below the poverty line. Low coverage is in part a reflection of the widespread labor informality and the relatively high contribution threshold for eligibility (1350 weeks). For the few eligible, ColPensiones' replacement rate is relatively generous (70−100 percent) and benefit mostly the rich with about half of the implicit subsidy (difference between contributions and pension benefits received) being received by the top income quintile (see chart).

Progressivity (lack of) of Subsidies in Colombia
(incidence per income quintile)

Sources: DNP

There is widespread consensus that parametric changes could improve progressivity and generate savings to expand non-contributory programs.[1] The retirement age (currently 57 for women and 62 for men) could be unified and increased. The replacement rate in ColPensiones could be lowered, for instance, by increasing the number of years used to compute pension benefits. Removing the tax-free status of pension benefits could also be considered to improve progressivity. Contribution rates could be increased, including by exploring the possibility to re-assign some of the existing payroll-related taxes

Deeper structural reforms should aim to expand pension coverage while ensuring progressivity and fiscal sustainability:

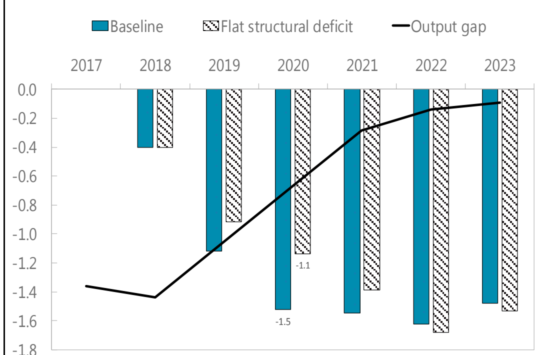
- A much strengthened Colombia Mayor and together with wider eligibility targeted subsidies for BEPS could increase coverage and progressivity. Coverage could be increased by lowering the relatively high eligibility threshold (number of weeks) and improving labor market formality.
- Reform options recognize the need to provide a minimum pension. One proposal is to downsize the DB system (e.g. Colpensiones) to receive contributions on the first minimum wage of all contributors, and in the future, pay only the minimum pension. The existing DC system would become a strong complement, rather than a competitor, of the basic Pillar 1, providing pensions beyond the minimum. Another proposal, is to close entry of new members to Colpensiones and extend the currently privately-managed minimum pension insurance to cover all contributors. In either case, it will be important to ensure a properly timed and fiscally sustainable transition of existing contributors. It will also be important to increase competition among AFPs would help achieve higher pension benefits and contribute to Colombia's capital market development.

[1] Recent studies include FMI (2012, 2017), IADB (2015), OECD (2015), Expert Commission (2017), ANIF (2017), Fedesarrollo (2018).

Policy Advice

34. Keeping public debt on a downward path remains an appropriate strategy which could also leave some space to react to negative shocks. The recent underperformance of tax revenue, while due mostly to lower-than-expected growth, calls for continued efforts to improve tax administration and formalization as envisaged in the 2016 tax reform. The fiscal rule legal mandate offers some flexibility in the pace of consolidation beyond 2018[4]; in the event negative shocks materialize, the rule allows to shift the adjustment planned for 2019/2020 to 2021/22 -an illustrative scenario in which the central government structural deficit is left unchanged during 2019 and 2020 is presented below. In case additional positive oil revenue surprises occur, the rule will allow to spend the structural component including in public investment and save the rest.

Fiscal Impulse During Different Scenarios
(cumulative since 2017; in percent of GDP except for output gap)



Sources: National authorities and Fund staff estimates

Illustrative Fiscal Rule Scenarios
(in percent of GDP)

	2017	2018	2019	2020	2021	2022	2023
Structural deficit (official parameters)							
Baseline	-1.9	-1.9	-1.7	-1.4	-1.3	-1.0	-1.0
Flat structural deficit	*-1.9*	*-1.9*	*-1.9*	*-1.9*	*-1.5*	*-1.0*	*-1.0*
Primary expenditure							
Baseline	16.3	15.4	14.7	14.8	14.8	14.6	14.7
Flat structural deficit	*16.4*	*15.5*	*15.0*	*15.4*	*15.0*	*14.6*	*14.7*
Gross Debt							
Baseline	50.2	49.9	48.7	46.5	44.4	42.3	40.4
Flat structural deficit	*49.4*	*49.3*	*48.4*	*46.7*	*44.7*	*42.6*	*41.0*
Fiscal impulse CG (change in the non-oil primary structural deficit)							
Baseline	-0.5	-0.2	-0.5	-0.5	-0.1	-0.1	0.2
Flat structural deficit	*-0.5*	*-0.1*	*-0.3*	*-0.2*	*-0.4*	*-0.3*	*0.2*

Sources: National authorities and Fund staff estimates

35. Strengthened capacity in subnational governments would improve public expenditure. As the report from an expert commission notes, increasing the participation of subnational governments in health and education spending stands to boost the efficiency and progressivity of social programs. Subnationals can do this and fund the additional spending from previously unexecuted budgets (gross assets of about 4 percent of GDP at end-2017). The implementation of the peace agreements will strengthen capacity in subnational governments and could help relieve those constraints.

Authorities' Views

36. The authorities broadly agreed with staff advice including on the importance of keeping public debt on a downward path. While the MTFF deficit target should be attainable through a combination of tax administration gains and expenditure cuts, the authorities also noted that exploiting any room to smooth the fiscal adjustment within the existing legal framework will

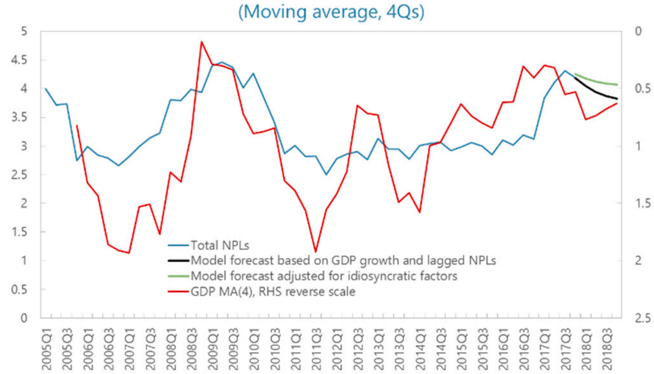
[4] The rule includes precise structural deficit targets for 2018 (1.9 percent of GDP) and 2022 (1 percent of GDP); but the pace of consolidation between those two years is somewhat flexible -the only requirement is for the structural deficit not to worsen across years.

help preserve the credibility of the fiscal rule. Also, there could be an upside risk to oil-revenues which could create space for additional public investment. They also agreed that a pension reform should be a priority of the next government.

D. Preserving Financial Stability

Background

NPLs and GDP growth
(Moving average, 4Qs)



Sources: Superintendencia Financiero; and IMF staff calculations.

37. NPLs are still rising but staff expect them to stabilize with the rebound in activity during 2018H2 and banks have strong buffers. The increase in NPLs to 4.3 percent in December 2017, from 3.2 percent a year earlier, was partly due to the economic slowdown and partly to large idiosyncratic increases in the electricity and transportation sectors. With macroeconomic conditions improving, we expect NPLs to start decreasing in 2018H2 (see Box 7). Provisions fell to 126 percent of NPLs but continue to be ample. Tier-1 and regulatory capital increased to 12.4 percent and 18.6 percent of RWAs respectively by December 2017, almost a one percent increase from the beginning of the year.

38. The financial supervisor (SFC) introduced new regulation to foster early detection of credit risk and intensified bank-by-bank monitoring.[5] In October 2017, the SFC issued regulation to standardize loan restructuring practices and foster early credit risk monitoring through modified loans and improved bank-by-bank monitoring.[6] Banks are encouraged to approach borrowers that show early signs of distress with the option to modify loans (interest, maturity, but not the principal). A modified loan does not entail additional provisions or a negative credit mark for the borrower, but leads to more intensive surveillance thereafter. This is an improvement from previous restructuring practices. Moreover, SFC closely monitors and will soon make public information about modified loans.

[5] AML/CFT assessment led by the Fund is expected to be finalized and approved in July 2018.

[6] The new regulations bring restructuring practices closer to Basel principles.

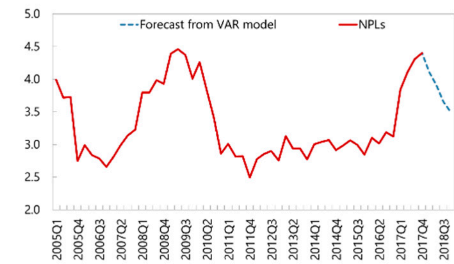
Box 7. Non-Performing Loans Forecast to Decline with Recovery

The economic recovery suggests that NPLs should start falling. Using a VAR to model the relationship between NPLs and macroeconomic variables shows that the credit gap, the nominal exchange rate and real GDP growth are the main drivers of NPLs. Forecasting NPLs with this model suggests that they should start falling in tandem with the economic recovery in 2018.

Given the high level and continued rise of risky loans in 2017, it is unlikely that NPLs will start to fall in the first half of 2018. The proportion of risky loans has strongly correlated with NPLs. In the corporate sector, which accounts for more than half of the credit portfolio, NPLs have lagged risky loans by approximately one year. Given the high level and continued rise of risky loans in 2017, it is hence unlikely that NPLs start to fall during the first half of 2018.[1]

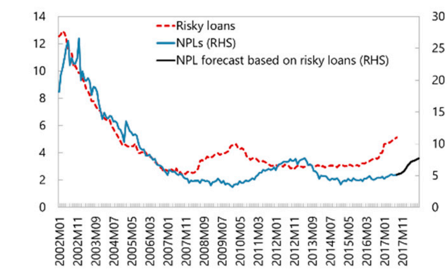
NPLs would start declining by mid-year 2018. Taking into account both the economic recovery and the high level of risky loans, we forecast NPLs to stabilize by mid-2018 and to gradually start falling in 2018H2. Efforts by the SFC to intensify monitoring and recoveries swill reinforce this trend.

NPLs and Forecast from VAR Model



Sources: Superintendencia Financiera de Colombia; and IMF staff calculations.

Corporate Sector: NPLs and Risky Loans



Sources: Banco de la Republica de Colombia; and IMF staff calculations.

[1] In the absence of updated corporate balance sheet data, risky loans are a good leading indicator of NPLs.

39. **The Conglomerates Law that follows FSAP recommendations (IMF Country Report No. 16/129), passed in September 2017 and will come into effect in 2018.** Draft regulation specifying capital adequacy and related-party exposures for conglomerates has been circulated for comments, and a final version is expected to come into effect by September 2018. Capital requirements for all banks are to be gradually strengthened over a six-year period (see the text table).

Agenda to Strengthen Capital and Liquidity

Measure	Status/Planned Timeline
I. Capital	
Modification of the definition of capital and risk-weighted assets to bring them closer to international standards.	During 2018
Introduce conservation and D-SIB buffers at 2.5 and 1 percent respectively.	By 2023
Introduce Tier-1 capital minimum of 6 percent.	By 2023
II. Liquidity	
Modification of the liquidity-coverage-ratio to differentiate by type of depositor in accordance with Basel III.	In progress; to be sent for comments during 2018H1
Introduction of a liquidity indicator similar to the net-stable-funding ratio, but taking into account currency mismatches and roll-over risks of derivatives.	In progress; to be sent for comments during 2018H1

Source: National authorities

Policy Advice

40. **Staff supports the improved incentives to anticipate the deterioration in loan portfolios and facilitate detection and recoveries.** Under the new regulation, modified loans cannot be reclassified to a lower risk category. Furthermore, if borrowers with modified loans fail to meet payments, their loans will be downgraded faster and hence require more provisioning. The modification of loans should not lead to the delayed recognition of asset

deterioration. Carefully monitoring modified loans of individual banks is essential to avoid evergreening of loans.

41. **Finalizing the Conglomerates Law and moving closer to Basel III standards will strengthen financial stability.** The former is an important step to contain spillovers of financial shocks as it will give the SFC a mandate to regulate and supervise entities at the conglomerate level. The latter will enhance stability, create a more leveled playing field and facilitate rating assessments.

Authorities' Views

42. **The authorities continue to refine their supervision and regulation framework and are confident about the system's resilience.** They agreed with staff's assessment of the enhanced credit risk monitoring system and noted that further impetus of reforms towards Basel III will follow the implementation of the Conglomerates Law. Official stress tests suggest banks are resilient to macroeconomic shocks. The authorities performed a top-down stress testing exercise in which the economy experiences a slowdown over six quarters. The scenario would lead to a significant deterioration of the lending portfolio, with NPLs nearly doubling, but the aggregate solvency ratio would remain above the 9 percent regulatory minimum. Furthermore, the authorities and market participants agreed with staff's baseline forecast that NPLs will stabilize in 2018H2.

STAFF APPRAISAL

43. **A very strong policy framework and well-executed policies narrowed external imbalances after the oil price shock of 2015-16 and laid the foundations for an economic recovery.** The monetary easing cycle has brought the ex-ante real policy rate to slightly expansionary levels and staff believes that limited further cuts may be feasible in a scenario with below baseline growth and continued convergence of inflation expectations to target. Better communication of policy tradeoffs would complement recent improvements to the policy rate decision process. The fiscal policy stance is appropriate and consolidation should continue. While complying with the fiscal rule requires some cuts in central government public investment, these will be more than offset by increases in PPP-infrastructure, private sector and subnational government's investment. Further strengthening tax administration, including through stronger sanctions, is imperative. The external sector position last year was moderately weaker than implied by fundamentals and desirable policy settings, reflecting the ongoing adjustment. However, policies are on their desirable course and there is no need for additional tightening beyond what is already planned.

44. **As demand policies are fine-tuned to complete the adjustment the focus should shift to structural reforms to lift productivity and inclusive growth.** Top structural priorities include lowering barriers to international trade, tackling labor-market informality, and promoting infrastructure investment. Lowering remaining non-wage labor costs and barriers to entry will further decrease informality, while lowering transport and other exporting costs will further increase productivity and competitiveness of Colombian businesses, supporting the external adjustment. A comprehensive pension reform is needed to increase coverage and progressivity. Focus on these

structural reforms and strong policy framework is widely-expected to continue in the next administration as they are broadly endorsed by the leading candidates.

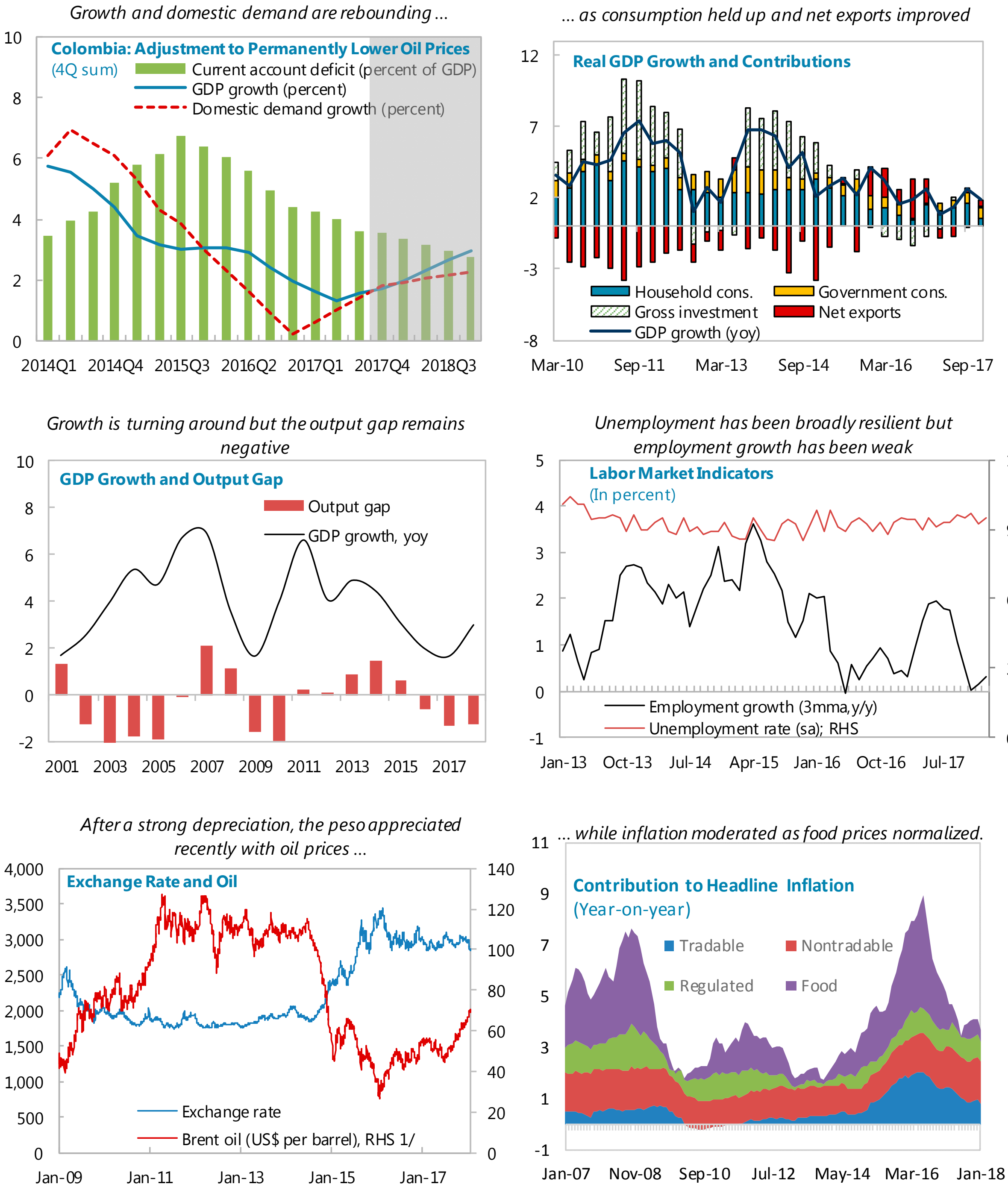
45. Banks have adjusted well to the economic downturn and the regulatory and supervisory policy agenda is focused on the right issues. Staff supports the improved incentives to facilitate detection and recoveries in loan portfolios, subject to increased monitoring and avoiding delayed recognition of asset deterioration. The Conglomerates Law to be implemented this year is an important step towards preserving financial stability, and will allow focus on further convergence to Basel III standards.

46. Risks have decreased somewhat but remain tilted to the downside. Global growth and the oil market outlook have improved but global financial markets are vulnerable to a sudden, sharp tightening of financial conditions. The latter could be triggered by an unexpected increase in U.S. inflation and/or an escalation of trade or geopolitical tensions, that have intensified recently and increased the probability of a spike in global risk-aversion. Regionally, risks related to the crisis in Venezuela are growing, but they appear manageable so far. Should immigration continue to increase at the current pace, international support would be needed. On the domestic front, a weaker than expected response in infrastructure investment or exports could lead to a slower recovery. Colombia's very strong policies, flexible exchange rate, and reserve buffers would cushion the effects of shocks.

47. Staff does not recommend approval of the retention of the exchange restriction arising from the special regime for the hydrocarbon sector, since the authorities have no plans for its removal. Colombia has a floating exchange rate regime (*de jure*: free floating; *de facto*: floating) and maintains an exchange restriction subject to Fund approval under Article VIII arising from the special regime for the hydrocarbon sector (see IMF Country Report No. 13/35 for details).

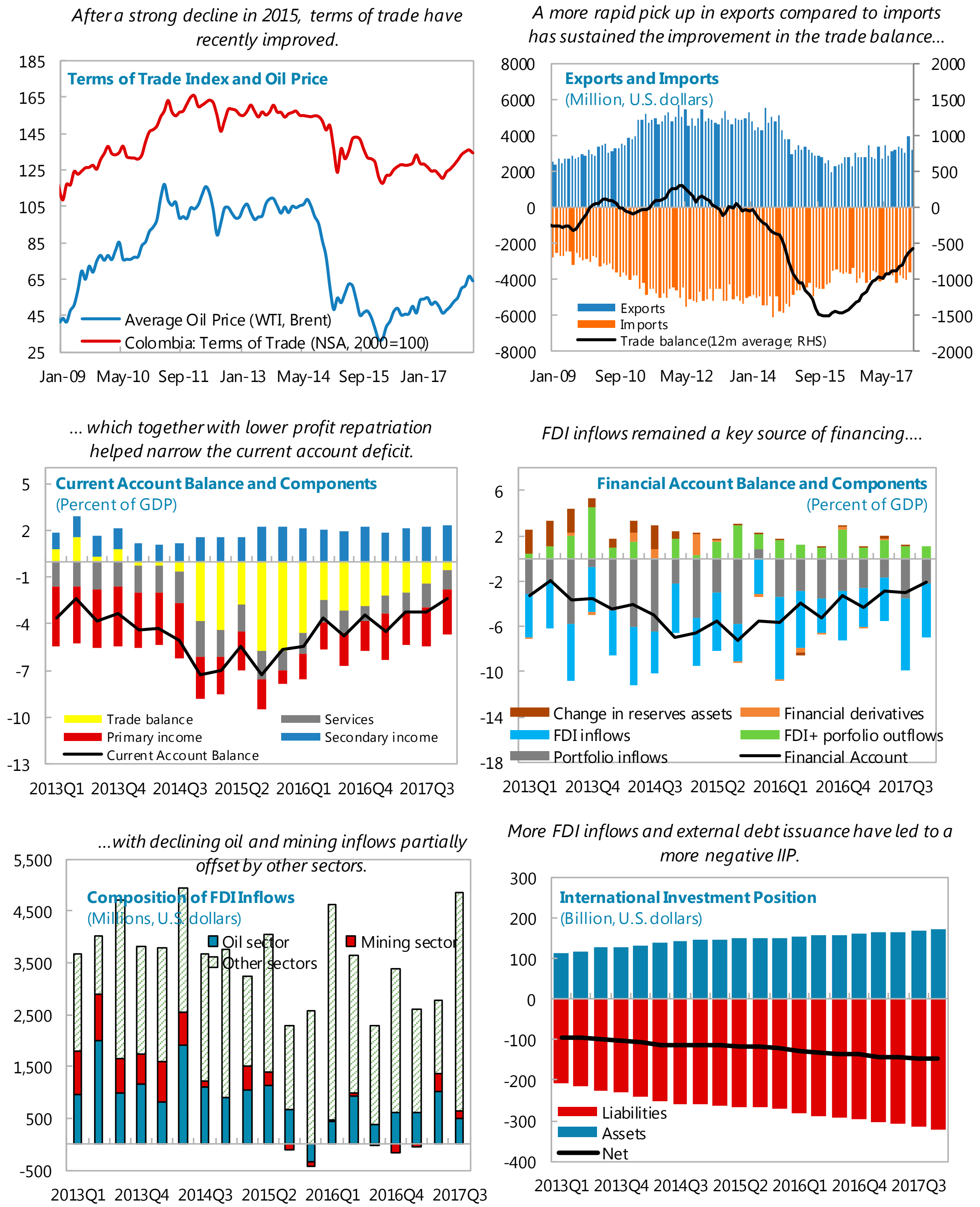
48. Staff recommends that the next Article IV takes place on the standard 12-month cycle.

Figure 1. Colombia: Recent Economic Developments



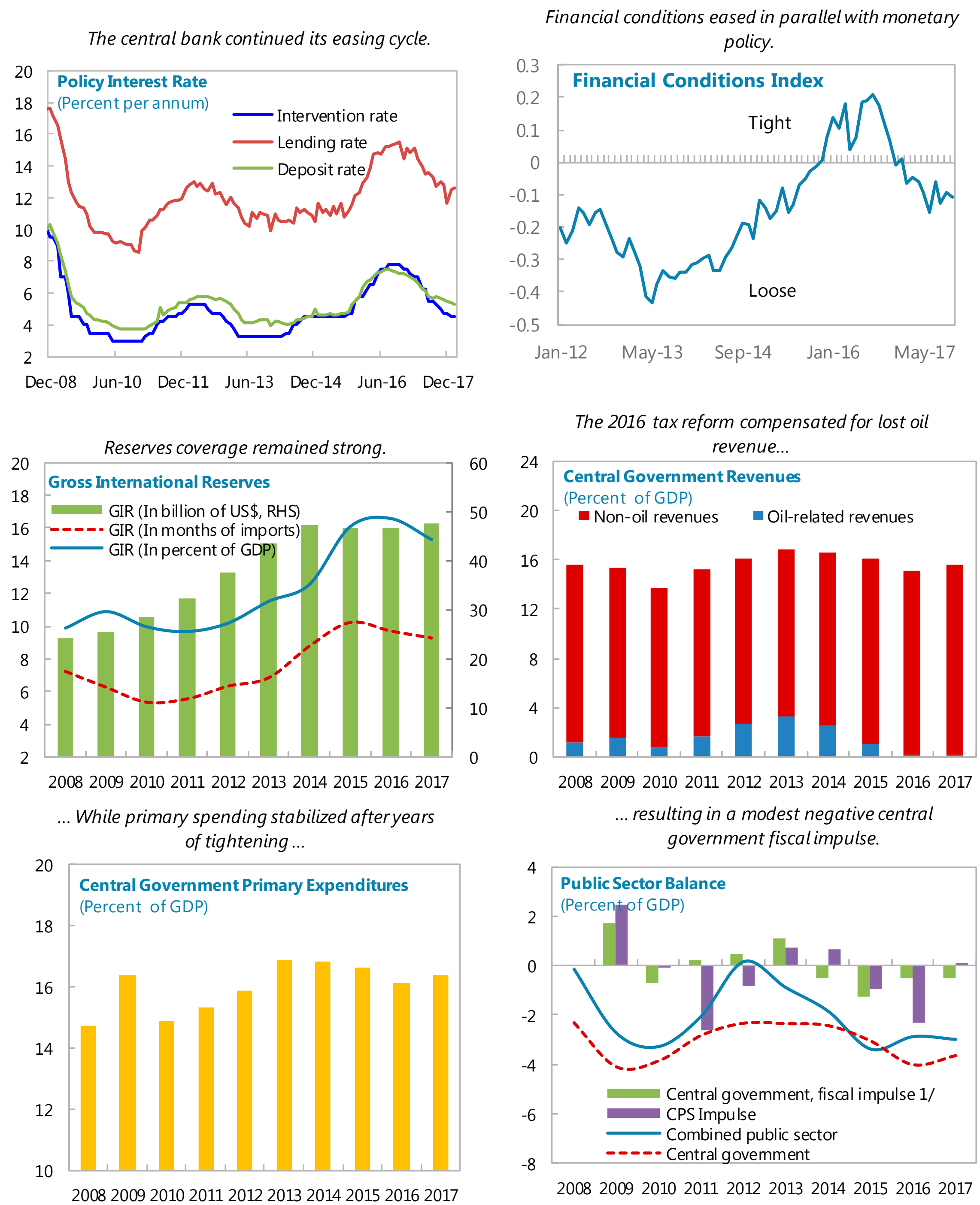
Sources: Banco de la República; DANE; Bloomberg; and Fund staff estimates.
1/ Colombia mix follows closely Brent oil prices.

Figure 2. Colombia: External Sector Developments



Sources: Banco de la República; Haver Analytics; and Fund staff estimates.

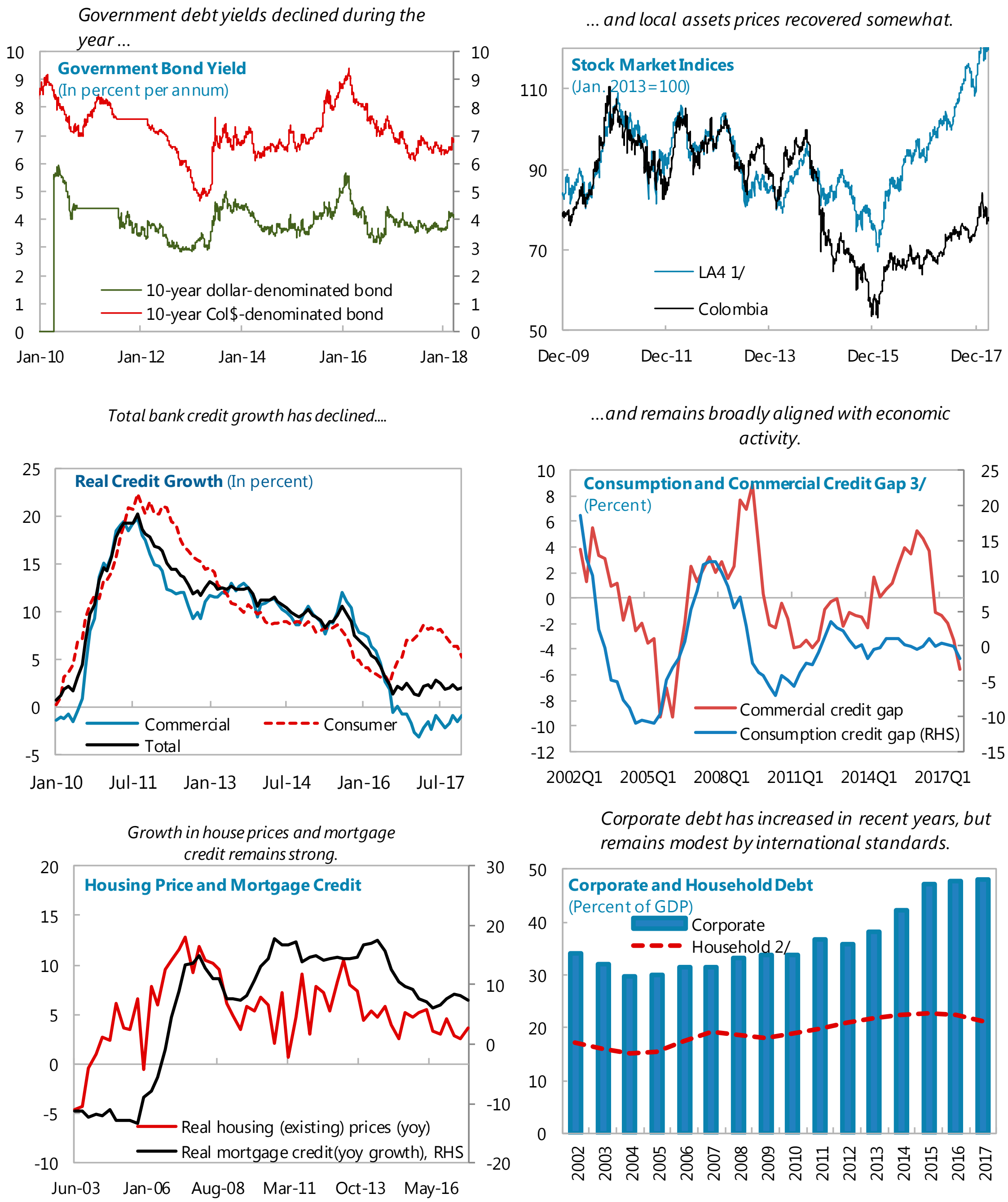
Figure 3. Colombia: Macroeconomic Policies



Sources: Banco de la República; and Fund staff estimates.

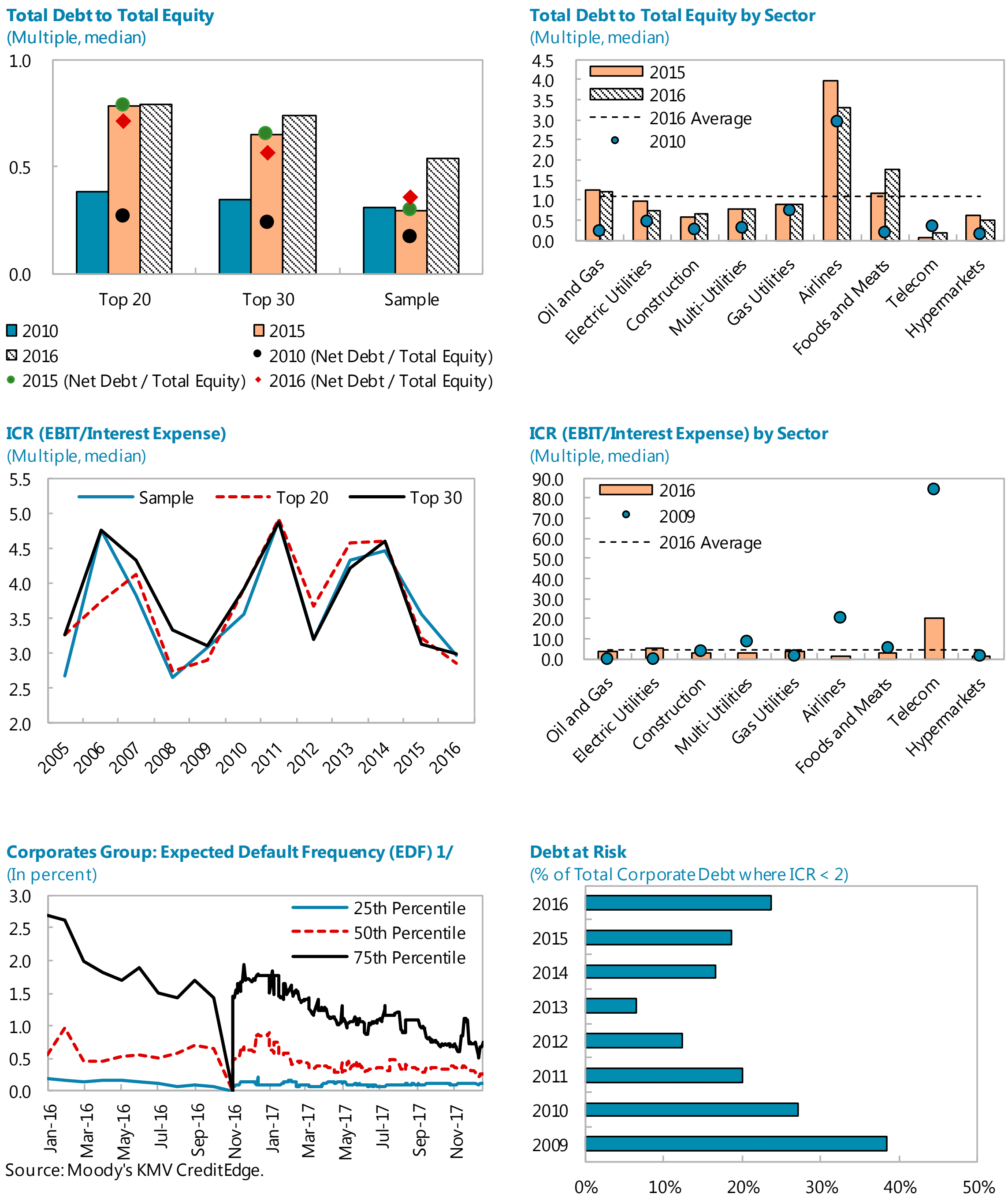
1/ Corresponds to the change in the non-oil structural primary deficit.

Figure 4. Colombia: Recent Macro-Financial Developments



Sources: Banco de la República; DANE; Bloomberg; and Fund staff estimates.
1/ LA4 corresponds to the average of Brazil, Colombia, Peru and Mexico.
2/ Data for 2017 refers to June 2017.
3/ Consumer and commercial credit gaps are computed as percentage-point deviations from an HP-filtered consumer-credit-to-private-consumption ratio and commercial-to-private-investment ratio, respectively.

Figure 5. Corporate Developments

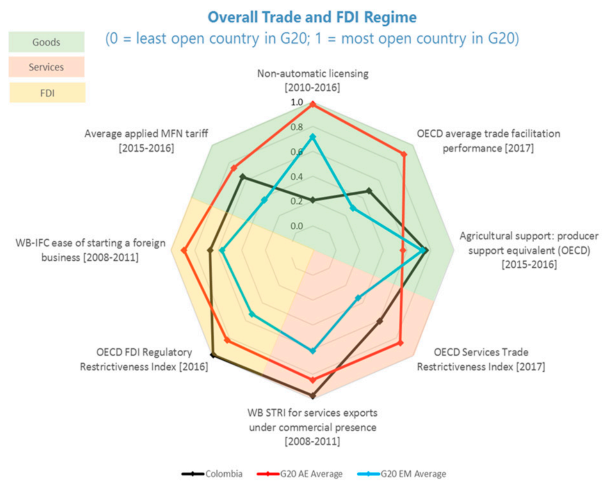


Sources: S&P Capital IQ; Moody's KMV CreditEdge; and IMF staff calculations.

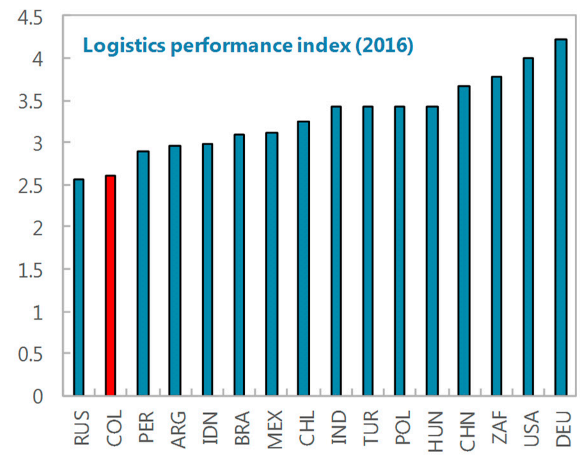
1/ The Expected Default Frequency (EDF) is the probability that a company will default within a given time horizon, typically one year, where default means the failure to make a scheduled debt payment.

Figure 6. Colombia: Structural Bottlenecks

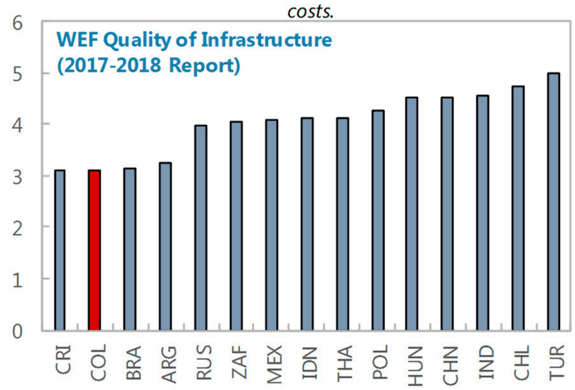
Trade is relatively open. But trade procedures are complicated....



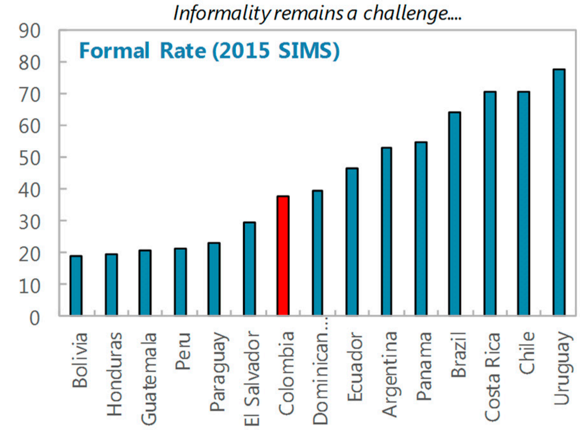
... and weak logistics...



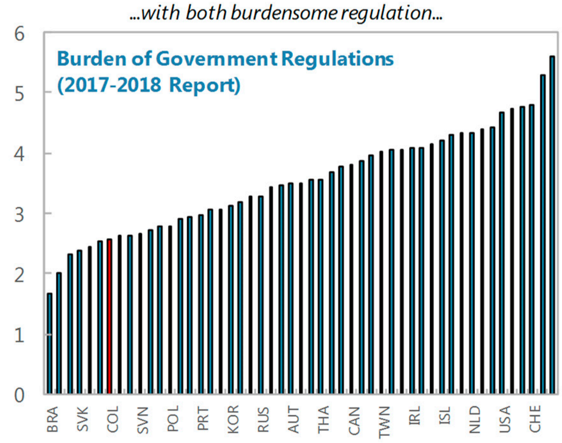
... as well as infrastructure gaps impose important costs.



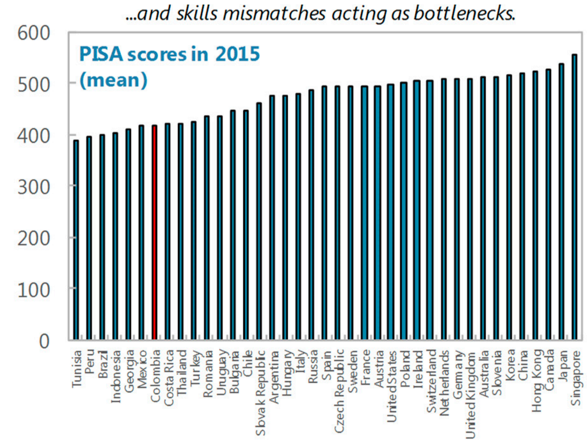
Informality remains a challenge....



...with both burdensome regulation...

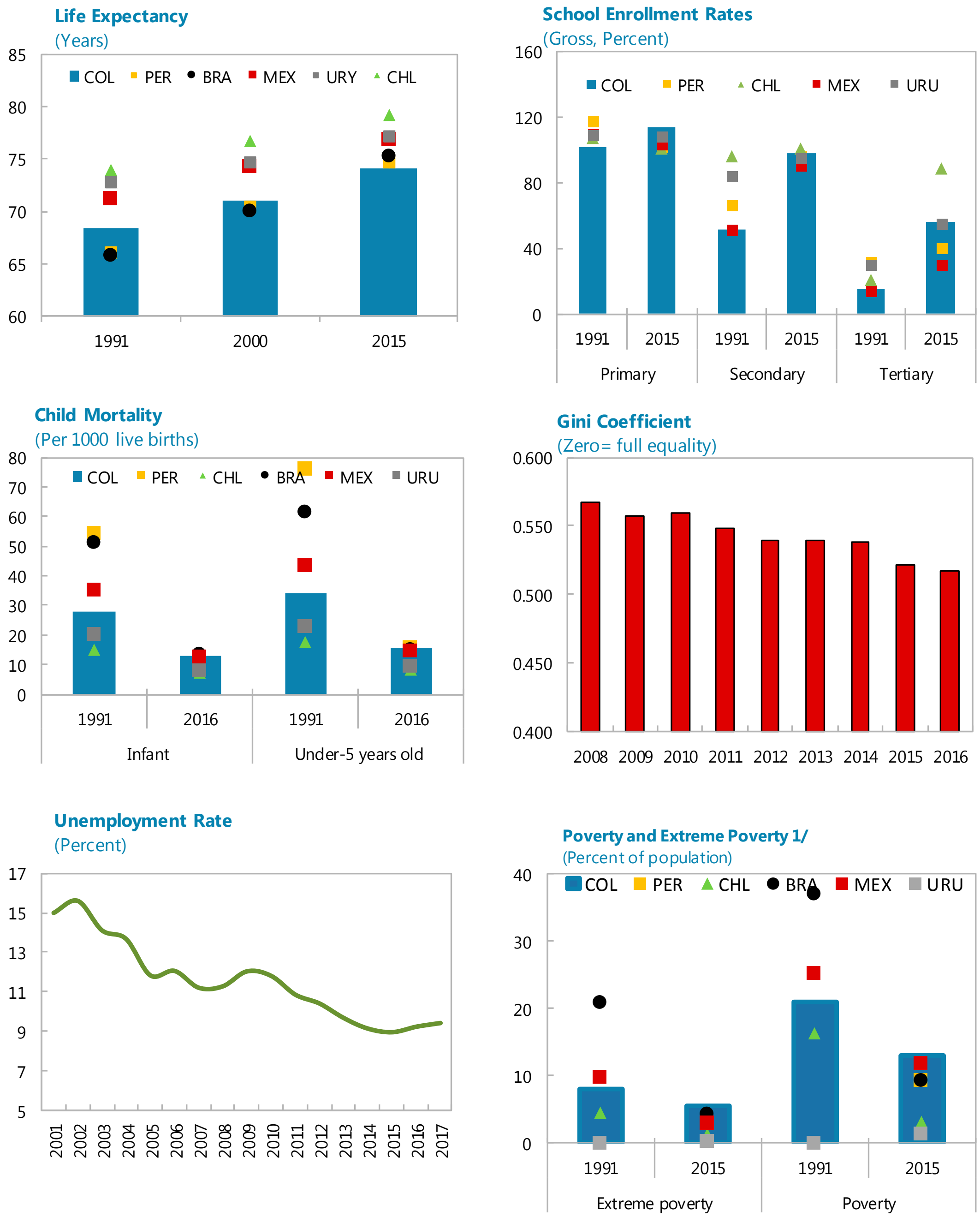


...and skills mismatches acting as bottlenecks.



Sources: WEF; World Bank; staff calculations.

Figure 7. Colombia: Social Indicators



Sources: World Development Indicators; and DANE.

1/ Poverty corresponds to the poverty headcount ratio at $3.20 a day (2011 PPP) and extreme poverty to the headcount ratio at $1.90 a day (2011 PPP).

Table 1. Colombia: Selected Economic and Financial Indicators

I. Social and Demographic Indicators

Population (million), 2015	48.2	Unemployment rate, 2015 (percent)	8.9
Urban population (percent of total), 2014	76.2	Physicians (per 1,000 people), 2010	1.5
GDP, 2016		Adult illliteracy rate (ages 15 and older), 2011	6.4
Per capita (US$)	5,808	Net secondary school enrollment rate, 2013	73.8
In billion of Col$	855,432	Access to water (percent of population), 2015	91.4
In billion of US$	280	Gini coefficient, 2017	50.8
Life expectancy at birth (years), 2013	73.8	Poverty rate (US$3.2 a day, PPP), 2015	13.1
Mortality rate, (under 5, per 1,000 live births), 2015	15.9	Extreme poverty rate (US$1.9 a day, PPP), 2015	5.5

II. Economic Indicators

						Projections					
	2013	2014	2015	2016	2017	2018	2019	2020	2021	2022	2023
	(In percentage change, unless otherwise indicated)										
National income and prices											
Real GDP	4.9	4.4	3.1	2.0	1.8	2.7	3.3	3.6	3.6	3.6	3.5
Potential GDP	4.2	3.9	3.3	3.0	3.0	3.1	3.2	3.3	3.3	3.4	3.5
Output Gap	0.6	1.1	0.9	-0.1	-1.4	-1.5	-1.1	-0.7	-0.4	-0.1	0.0
GDP deflator	2.0	2.1	2.5	4.9	4.8	3.3	3.0	3.0	3.0	3.0	3.0
Consumer prices (end of period)	2.0	3.7	6.9	5.8	4.1	3.4	3.0	3.0	3.0	3.0	3.0
External sector											
Exports (f.o.b.)	-2.1	-5.6	-32.2	-11.6	15.8	14.3	2.9	6.5	5.8	5.8	6.0
Imports (f.o.b.)	0.8	7.8	-15.4	-16.9	2.3	6.8	5.6	6.3	5.7	5.4	5.6
Export volume	5.2	-1.5	-2.0	-2.5	0.0	4.6	5.7	7.2	6.0	5.8	5.8
Import volume	6.0	7.9	-6.8	-11.5	-2.0	-0.3	4.6	5.6	4.7	5.2	5.5
Terms of trade (deterioration -)	-2.1	-3.2	-19.3	-3.0	7.9	1.7	-2.3	-1.2	-1.0	-0.1	0.4
Real effective exchange rate (depreciation -)	-2.9	-6.9	-20.6	-4.7	2.8	0.6	0.1	0.0	-0.1	0.5	0.3
Money and credit											
Broad money	13.4	10.0	11.7	11.5	4.2	9.8	9.7	10.0	9.9	9.7	9.6
Credit to the private sector	12.1	14.7	16.8	7.7	11.0	7.5	8.9	9.6	10.8	11.6	11.6
Policy rate (end of period)	3.25	4.5	5.75	7.5	4.8	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.
	(In percent of GDP)										
Central government balance	-2.3	-2.4	-3.0	-4.0	-3.6	-3.1	-2.2	-1.6	-1.3	-1.1	-1.1
Central government structural balance	-3.5	-3.4	-3.8	-3.1	-2.4	-2.3	-2.1	-1.9	-1.8	-1.5	-1.6
Combined public sector (CPS) balance 1/	-0.9	-1.8	-3.4	-2.8	-2.9	-2.5	-1.7	-0.6	-0.5	-0.4	-0.6
CPS non-oil structural primary balance	-2.8	-3.4	-2.5	-0.1	-0.2	-0.4	0.0	0.9	0.8	0.7	0.4
CPS fiscal impulse	0.7	0.6	-0.9	-2.4	0.1	0.2	-0.4	-0.9	0.1	0.1	0.3
Public debt	37.8	43.7	50.6	50.4	50.2	49.9	48.7	46.5	44.4	42.3	40.4
Public debt, excluding Ecopetrol	36.1	40.8	45.8	45.9	46.9	46.7	46.0	43.9	42.0	39.9	38.1
Gross domestic investment	24.3	26.3	26.7	24.7	23.4	23.6	23.7	23.7	23.6	23.5	23.4
Gross national savings	21.0	21.1	20.3	20.4	20.0	21.0	21.1	21.2	21.1	21.1	21.0
Current account (deficit -)	-3.3	-5.2	-6.4	-4.3	-3.4	-2.6	-2.6	-2.5	-2.5	-2.4	-2.3
External debt 2/	25.7	30.1	42.5	49.6	47.5	46.6	45.4	44.3	43.3	42.7	42.1
Of which: public sector 2/	15.3	19.1	27.3	32.1	30.5	30.0	29.4	28.8	27.9	27.3	26.6
	(In percent of exports of goods and services)										
External debt service	30.3	40.2	62.1	64.9	73.1	61.6	64.8	61.9	62.8	57.6	53.3
Of which: public sector	7.3	9.0	14.0	13.4	15.7	11.1	18.5	15.5	16.5	9.0	n.a.
Interest payments	5.4	6.3	9.9	11.4	11.0	13.0	13.7	13.8	13.5	13.3	13.2
Of which: public sector	3.5	4.1	6.7	7.4	7.0	6.0	5.7	5.2	5.0	4.0	3.7
	(In billion of U.S. dollars; unless otherwise indicated)										
Exports (f.o.b.)	60.3	56.9	38.6	34.1	39.5	45.1	46.4	49.5	52.3	55.4	58.7
Of which: Petroleum products	32.0	28.9	14.5	10.8	13.0	15.4	14.1	13.3	12.7	12.4	12.2
Gross official reserves 3/	43.2	46.8	46.3	46.2	47.1	47.9	48.9	50.2	51.5	52.9	54.2
Share of ST debt at remaining maturity + CA deficit	104	110	134	115	135	126	128	122	129	135	n.a.

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

1/ Includes the quasi-fiscal balance of Banco de la República, sales of assets, phone licenses, and statistical discrepancy.

2/ Includes foreign holdings of locally issued public debt (TES); does not include Banco de la República's outstanding external debt.

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

Table 2a. Colombia: Summary Balance of Payments
(In millions of US$, unless otherwise indicated)

					Projections						
	2013	2014	2015	2016	2017	2018	2019	2020	2021	2022	2023
Current account balance	**-12,504**	**-19,768**	**-18,586**	**-12,129**	**-10,359**	**-8,451**	**-8,967**	**-9,149**	**-9,720**	**-10,021**	**-10,176**
Goods balance	3,179	-4,641	-13,479	-9,160	-4,766	-2,114	-3,412	-3,532	-3,675	-3,661	-3,606
Exports, f.o.b.	60,282	56,899	38,572	34,079	39,474	45,114	46,445	49,455	52,334	55,383	58,725
Commodities	43,361	41,081	24,132	20,396	25,629	29,279	27,906	27,304	27,033	27,139	27,380
Fuel	32,011	28,947	14,518	10,784	13,047	15,377	14,130	13,252	12,685	12,353	12,155
Non-fuel	11,350	12,134	9,614	9,612	12,582	13,902	13,775	14,052	14,348	14,787	15,225
Non-traditional exports	12,488	11,879	10,493	9,614	10,256	11,795	13,972	16,892	19,426	21,777	24,251
Other	4,433	3,939	3,947	4,070	3,589	4,040	4,568	5,258	5,875	6,467	7,093
Imports, f.o.b.	57,103	61,539	52,051	43,239	44,241	47,228	49,857	52,986	56,009	59,044	62,331
Consumer goods	12,073	13,120	11,103	10,114	10,161	10,567	11,064	11,783	12,572	13,327	14,126
Intermediate goods	24,145	26,278	21,814	18,809	18,889	20,306	21,362	22,649	24,008	25,448	26,975
Capital goods	18,795	20,160	17,407	12,527	13,210	14,293	15,222	16,151	16,838	17,478	18,218
Other	2,090	1,980	1,726	1,789	1,981	2,061	2,209	2,404	2,591	2,791	3,011
Services balance	-6,340	-7,222	-4,776	-3,608	-4,111	-3,876	-3,650	-3,811	-3,995	-4,080	-4,094
Exports of services	7,022	7,156	7,426	7,677	8,326	9,211	10,203	10,927	11,590	12,370	13,281
Imports of services	13,362	14,378	12,203	11,284	12,438	13,087	13,853	14,739	15,585	16,450	17,376
Primary income balance	-14,230	-12,527	-5,761	-5,249	-8,167	-9,405	-9,131	-9,307	-9,836	-10,359	-10,865
Receipts	3,624	3,997	4,483	4,996	5,475	5,207	5,702	6,308	6,559	6,897	7,338
Expenditures	17,855	16,525	10,244	10,245	13,641	14,612	14,834	15,615	16,395	17,256	18,204
Secondary income balance	4,887	4,622	5,430	5,887	6,685	6,944	7,226	7,500	7,786	8,079	8,389
Financial account balance	**-11,739**	**-19,292**	**-18,263**	**-12,682**	**-9,694**	**-8,451**	**-8,967**	**-9,149**	**-9,720**	**-10,021**	**-10,176**
Direct Investment	-8,557	-12,268	-7,518	-9,332	-10,828	-7,709	-8,195	-8,798	-9,313	-9,845	-10,403
Assets	7,652	3,899	4,218	4,517	3,690	3,779	3,864	3,936	4,007	4,074	4,144
Liabilities	16,209	16,167	11,736	13,849	14,518	11,488	12,059	12,734	13,319	13,919	14,547
Oil sector	5,112	4,732	2,514	2,385	3,458	4,188	3,930	3,647	3,448	3,307	3,203
Non-oil sectors	11,098	11,435	9,222	11,463	11,060	7,300	8,129	9,087	9,872	10,612	11,344
Portfolio Investment	-7,438	-11,565	-10,283	-3,718	-1,577	-2,102	-1,805	-1,319	-1,744	-1,392	-1,004
Assets	3,635	7,096	-475	5,190	6,217	2,764	2,803	2,927	3,197	3,363	3,454
Liabilities	11,073	18,661	9,808	8,908	7,793	4,866	4,608	4,246	4,941	4,755	4,459
Equity	1,921	1,823	1,757	-1,484	245	260	275	291	308	326	345
Debt instruments	9,152	16,838	8,051	10,392	7,548	4,606	4,333	3,956	4,633	4,429	4,114
General government	4,913	12,835	5,651	8,792	6,011	3,369	3,024	2,572	3,167	2,878	2,474
Banks	1,300	-17	400	1,100	300	-76	-80	-85	-90	-95	-100
Corporates and households	2,939	4,020	2,000	500	1,237	1,312	1,389	1,468	1,555	1,647	1,741
Derivatives	118	608	1,956	-621	203	0	0	0	0	0	0
Other Investments	-2,808	-504	-2,833	823	1,963	582	4	-304	31	-123	-143
Change in reserve assets	6,946	4,437	415	165	545	778	1,029	1,272	1,305	1,339	1,374
Net errors and omissions	**765**	**476**	**323**	**-553**	**665**	**0**	**0**	**0**	**0**	**0**	**0**
Memorandum items:											
GDP (billion USD)	380	378	292	280	309	328	347	367	389	411	435
GIR (IMF Definition)	43.2	46.8	46.3	46.2	47.1	47.9	48.9	50.2	51.5	52.9	54.2
GIR/(st debt at remaining maturity + ca deficit)	103.9	110.0	134.2	115.3	135.3	126.4	128.1	121.7	128.7	135.3	n.a.
GIR/GDP	11.4	12.4	15.9	16.5	15.2	14.6	14.1	13.7	13.3	12.8	12.5
GIR (months of imports of G&S)	6.8	8.7	10.2	9.8	9.4	9.0	8.7	8.4	8.2	8.0	7.7
GIR/ARA	141.0	147.2	154.5	138.5	145.9	141.2	138.7	136.8	134.2	131.1	127.9

Sources: Banco de la República and Fund staff estimates and projections.

Table 2b. Colombia: Summary Balance of Payments

(In Percent of GDP)

	2013	2014	2015	2016	2017	2018	2019	2020	2021	2022	2023
					Projections						
Current account balance	**-3.3**	**-5.2**	**-6.4**	**-4.3**	**-3.4**	**-2.6**	**-2.6**	**-2.5**	**-2.5**	**-2.4**	**-2.3**
Goods balance	0.8	-1.2	-4.6	-3.3	-1.5	-0.6	-1.0	-1.0	-0.9	-0.9	-0.8
Exports, f.o.b.	15.9	15.0	13.2	12.2	12.8	13.8	13.4	13.5	13.5	13.5	13.5
Commodities	11.4	10.9	8.3	7.3	8.3	8.9	8.0	7.4	7.0	6.6	6.3
Fuel	8.4	7.7	5.0	3.9	4.2	4.7	4.1	3.6	3.3	3.0	2.8
Non-fuel	3.0	3.2	3.3	3.4	4.1	4.2	4.0	3.8	3.7	3.6	3.5
Non-traditional exports	3.3	3.1	3.6	3.4	3.3	3.6	4.0	4.6	5.0	5.3	5.6
Other	1.2	1.0	1.4	1.5	1.2	1.2	1.3	1.4	1.5	1.6	1.6
Imports, f.o.b.	15.0	16.3	17.9	15.4	14.3	14.4	14.4	14.4	14.4	14.3	14.3
Consumer goods	3.2	3.5	3.8	3.6	3.3	3.2	3.2	3.2	3.2	3.2	3.2
Intermediate goods	6.4	6.9	7.5	6.7	6.1	6.2	6.2	6.2	6.2	6.2	6.2
Capital goods	4.9	5.3	6.0	4.5	4.3	4.4	4.4	4.4	4.3	4.2	4.2
Other	0.5	0.5	0.6	0.6	0.6	0.6	0.6	0.7	0.7	0.7	0.7
Services balance	-1.7	-1.9	-1.6	-1.3	-1.3	-1.2	-1.1	-1.0	-1.0	-1.0	-0.9
Exports of services	1.8	1.9	2.5	2.7	2.7	2.8	2.9	3.0	3.0	3.0	3.1
Imports of services	3.5	3.8	4.2	4.0	4.0	4.0	4.0	4.0	4.0	4.0	4.0
Primary income balance	-3.7	-3.3	-2.0	-1.9	-2.6	-2.9	-2.6	-2.5	-2.5	-2.5	-2.5
Receipts	1.0	1.1	1.5	1.8	1.8	1.6	1.6	1.7	1.7	1.7	1.7
Expenditures	4.7	4.4	3.5	3.7	4.4	4.5	4.3	4.3	4.2	4.2	4.2
Secondary income balance	1.3	1.2	1.9	2.1	2.2	2.1	2.1	2.0	2.0	2.0	1.9
Financial account balance	**-3.1**	**-5.1**	**-6.3**	**-4.5**	**-3.1**	**-2.6**	**-2.6**	**-2.5**	**-2.5**	**-2.4**	**-2.3**
Direct Investment	-2.3	-3.2	-2.6	-3.3	-3.5	-2.4	-2.4	-2.4	-2.4	-2.4	-2.4
Assets	2.0	1.0	1.4	1.6	1.2	1.2	1.1	1.1	1.0	1.0	1.0
Liabilities	4.3	4.3	4.0	4.9	4.7	3.5	3.5	3.5	3.4	3.4	3.3
Oil sector	1.3	1.3	0.9	0.9	1.1	1.3	1.1	1.0	0.9	0.8	0.7
Non-oil sectors	2.9	3.0	3.2	4.1	3.6	2.2	2.3	2.5	2.5	2.6	2.6
Portfolio Investment	-2.0	-3.1	-3.5	-1.3	-0.5	-0.6	-0.5	-0.4	-0.4	-0.3	-0.2
Assets	1.0	1.9	-0.2	1.9	2.0	0.8	0.8	0.8	0.8	0.8	0.8
Liabilities	2.9	4.9	3.4	3.2	2.5	1.5	1.3	1.2	1.3	1.2	1.0
Equity	0.5	0.5	0.6	-0.5	0.1	0.1	0.1	0.1	0.1	0.1	0.1
Debt instruments	2.4	4.5	2.8	3.7	2.4	1.4	1.2	1.1	1.2	1.1	0.9
General government	1.3	3.4	1.9	3.1	1.9	1.0	0.9	0.7	0.8	0.7	0.6
Banks	0.3	0.0	0.1	0.4	0.1	0.0	0.0	0.0	0.0	0.0	0.0
Corporates and households	0.8	1.1	0.7	0.2	0.4	0.4	0.4	0.4	0.4	0.4	0.4
Derivatives	0.0	0.2	0.7	-0.2	0.1	0.0	0.0	0.0	0.0	0.0	0.0
Other Investments	-0.7	-0.1	-1.0	0.3	0.6	0.2	0.0	-0.1	0.0	0.0	0.0
Change in Reserve Assets	1.8	1.2	0.1	0.1	0.2	0.2	0.3	0.3	0.3	0.3	0.3
Net errors and omissions	**0.2**	**0.1**	**0.1**	**-0.2**	**0.2**	**0.0**	**0.0**	**0.0**	**0.0**	**0.0**	**0.0**

Sources: Banco de la República and Fund staff estimates and projections.

Table 3. Colombia: Operations of the Central Government 1/

(In percent of GDP, unless otherwise indicated)

					Projections						
	2013	2014	2015	2016	2017	2018	2019	2020	2021	2022	2023
Total revenue	**16.9**	**16.6**	**16.2**	**15.1**	**15.7**	**15.3**	**15.5**	**16.1**	**16.3**	**16.2**	**16.2**
Current revenue	**14.3**	**14.4**	**14.6**	**13.9**	**13.9**	**14.1**	**14.1**	**14.7**	**14.8**	**14.9**	**14.9**
Tax revenue	**14.2**	**14.3**	**14.5**	**13.8**	**13.8**	**14.0**	**14.0**	**14.6**	**14.7**	**14.8**	**14.8**
Net income tax and profits 2/	6.3	5.0	4.5	4.1	4.0	4.2	4.4	4.5	4.5	4.6	4.6
Goods and services	4.9	5.1	5.2	5.1	5.5	5.5	5.5	5.5	5.5	5.5	5.5
Value-added tax	4.9	5.1	5.2	5.1	5.4	5.4	5.4	5.5	5.5	5.5	5.5
International trade	0.5	0.5	0.5	0.4	0.4	0.4	0.4	0.4	0.4	0.4	0.4
Financial transaction tax	0.8	0.9	0.9	0.8	0.8	0.8	0.8	0.8	0.8	0.8	0.8
Stamp and other taxes	1.6	2.8	3.3	3.2	3.2	3.0	2.9	3.4	3.4	3.5	3.5
Nontax revenue	**2.7**	**2.3**	**1.7**	**1.3**	**1.8**	**1.3**	**1.5**	**1.5**	**1.5**	**1.4**	**1.4**
Property income	0.1	0.2	0.4	0.4	0.4	0.4	0.4	0.5	0.5	0.4	0.4
Other	2.6	2.2	1.3	0.9	1.4	0.8	1.0	1.0	1.1	1.0	1.0
Total expenditure and net lending	**19.2**	**19.1**	**19.2**	**19.1**	**19.3**	**18.4**	**17.7**	**17.7**	**17.6**	**17.3**	**17.3**
Current expenditure	**14.6**	**14.8**	**15.2**	**15.8**	**15.6**	**15.1**	**15.2**	**15.1**	**15.0**	**14.9**	**14.8**
Wages and salaries	2.1	2.3	2.4	2.4	2.5	2.5	2.5	2.5	2.4	2.4	2.4
Goods and services	0.9	0.8	0.8	0.8	0.9	0.9	0.9	0.9	0.9	0.9	0.9
Interest	2.3	2.2	2.6	3.0	2.9	2.9	2.9	2.8	2.8	2.7	2.5
External	0.5	0.5	0.6	0.7	0.7	0.7	0.7	0.7	0.7	0.7	0.7
Domestic	1.8	1.7	2.1	2.3	2.2	2.2	2.2	2.2	2.1	2.0	1.9
Current transfers	9.3	9.4	9.4	9.6	9.3	8.8	8.9	8.9	8.9	8.9	8.9
Capital expenditure	**4.5**	**4.3**	**4.0**	**3.3**	**3.7**	**3.2**	**2.5**	**2.6**	**2.5**	**2.4**	**2.5**
Fixed capital formation	3.2	2.9	2.7	2.0	2.4	2.0	1.2	1.4	1.3	1.2	1.3
Capital transfers	1.3	1.3	1.3	1.3	1.3	1.2	1.2	1.2	1.2	1.2	1.2
Net lending	**0.0**	**0.0**	**0.0**	**0.0**	**0.0**	**0.0**	**0.0**	**0.0**	**0.0**	**0.0**	**0.0**
Overall balance	**-2.3**	**-2.4**	**-3.0**	**-4.0**	**-3.6**	**-3.1**	**-2.2**	**-1.6**	**-1.3**	**-1.1**	**-1.1**
Memorandum items:											
Oil-related revenues 3/	3.3	2.6	1.1	0.2	0.2	0.6	0.9	0.9	1.0	1.0	1.0
Structural balance 4/	-3.5	-3.4	-3.8	-3.1	-2.4	-2.3	-2.1	-1.9	-1.8	-1.5	-1.6
Structural primary non-oil balance	-3.5	-3.0	-1.7	-1.2	-0.7	-0.6	-0.1	0.4	0.5	0.5	0.4
Fiscal Impulse	1.1	-0.5	-1.2	-0.5	-0.5	-0.1	-0.5	-0.5	-0.1	-0.1	0.2
Non-oil balance	-5.7	-5.0	-4.1	-4.2	-3.8	-3.7	-3.1	-2.5	-2.3	-2.1	-2.1
Primary balance	0.0	-0.2	-0.5	-1.0	-0.7	-0.2	0.7	1.2	1.4	1.5	1.4
Nominal GDP (in Col$ trillion)	710.5	757.1	799.3	855.4	912.5	968.5	1,029.5	1,099.1	1,173.4	1,251.5	1,334.8

Sources: Ministry of Finance; Banco de la República; and Fund staff estimates and projections.
1/ Includes central administration only.
2/ The increase in tax revenue in 2012 reflects the elimination of the fixed asset tax credit, which was part of the end-2010 tax reform.
3/ Includes income tax payments and dividends from Ecopetrol corresponding to earnings from the previous year.
4/ In percent of potential GDP. Adjusts non-commodity revenues for the output gap and commodity revenues for differentials between estimated equilibrium oil price and production levels. Adjustments are made to account for fuel subsidy expenditures and the accrual of Ecopetrol dividends.

Table 4. Colombia: Operations of the Combined Public Sector 1/

(In percent of GDP, unless otherwise indicated)

					Projections						
	2013	2014	2015	2016	2017	2018	2019	2020	2021	2022	2023
Total revenue	**28.1**	**27.7**	**26.4**	**25.1**	**25.6**	**25.7**	**25.9**	**26.5**	**26.6**	**26.4**	**26.2**
Tax revenue	19.8	19.9	20.1	19.4	19.5	19.6	19.6	20.3	20.4	20.5	20.4
Nontax revenue	8.3	7.7	6.3	5.7	6.1	6.1	6.3	6.2	6.2	6.0	5.8
Financial income	0.5	0.5	0.5	0.5	0.5	0.5	0.5	0.5	0.5	0.5	0.5
Operating surplus of public enterprises 2/	-0.1	-0.3	-0.3	-0.2	-0.3	-0.2	-0.2	-0.2	-0.2	-0.2	-0.2
Other 3/	7.8	7.5	6.1	5.4	5.9	5.8	6.0	5.9	5.9	5.6	5.4
Total expenditure and net lending 4/	**29.1**	**29.4**	**29.8**	**28.1**	**28.7**	**28.4**	**27.9**	**27.4**	**27.4**	**27.1**	**27.0**
Current expenditure	21.5	21.9	22.0	22.6	22.5	22.1	22.4	22.3	22.1	21.9	21.7
Wages and salaries	5.2	5.3	5.2	5.3	5.4	5.4	5.3	5.3	5.3	5.3	5.3
Goods and services	3.1	3.1	3.1	3.1	3.1	3.0	3.0	3.0	3.0	3.0	3.0
Interest	2.6	2.6	3.2	3.6	3.4	3.3	3.3	3.2	3.0	2.9	2.7
External	0.6	0.6	0.8	1.1	1.0	1.0	1.0	1.0	1.0	1.0	1.0
Domestic	2.0	2.0	2.3	2.6	2.4	2.3	2.3	2.2	2.1	1.9	1.8
Transfers to private sector	7.8	8.0	7.7	7.7	7.8	7.6	7.9	7.9	7.9	7.9	7.9
Other 5/	2.7	2.9	2.9	2.9	2.9	2.9	2.9	2.9	2.9	2.9	2.9
Capital expenditure	7.6	7.6	7.8	5.5	6.2	6.3	5.5	5.1	5.3	5.2	5.2
Statistical discrepancy	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0
Nonfinancial public sector balance	**-0.9**	**-1.8**	**-3.4**	**-3.0**	**-3.1**	**-2.7**	**-1.9**	**-0.9**	**-0.7**	**-0.7**	**-0.8**
Quasi-fiscal balance (BR cash profits)	-0.1	-0.1	-0.1	0.1	0.1	0.1	0.1	0.1	0.1	0.1	0.1
Fogafin balance	0.1	0.1	0.1	0.1	0.1	0.1	0.1	0.1	0.1	0.1	0.1
Net cost of financial restructuring 6/	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Combined public sector balance	**-0.9**	**-1.8**	**-3.4**	**-2.8**	**-2.9**	**-2.5**	**-1.7**	**-0.6**	**-0.5**	**-0.4**	**-0.6**
Overall financing	**0.9**	**1.8**	**3.4**	**2.8**	**2.9**	**2.5**	**1.7**	**0.6**	**0.5**	**0.4**	**0.6**
Foreign, net	1.2	2.8	2.6	1.6	1.1	1.2	1.5	1.0	1.0	0.0	0
Domestic, net	-0.3	-1.0	0.8	1.1	1.8	1.3	0.2	-0.4	-0.5	0.4	0.6
Memorandum items:											
Overall structural balance 7/	-2.5	-3.0	-3.5	-1.7	-1.4	-1.7	-1.8	-1.0	-1.1	-1.0	-1.2
Primary balance 8/	1.8	0.7	-0.2	0.9	0.5	0.8	1.6	2.5	2.5	2.4	2.1
Oil-related revenues 9/	4.9	4.0	2.0	1.1	1.2	1.7	1.9	1.8	1.7	1.7	1.6
Total public debt 10/	37.8	43.7	50.6	50.4	50.2	49.9	48.7	46.5	44.4	42.3	40.4
Nominal GDP (In Col$ trillion)	710.5	757.1	799.3	855.4	912.5	968.5	1,029.5	1,099.1	1,173.4	1251.5	1334.8

Sources: Ministry of Finance; Banco de la República; and Fund staff estimates and projections.

1/ The combined public sector includes the central, regional and local governments, social security, and public sector enterprises. Excludes Ecopetrol.

2/ For 2016, excludes proceeds from the sale of

3/ Includes royalties, dividends and social security contributions.

4/ Expenditure reported on commitments basis.

5/ Includes adjustments to compute spending on commitment basis and the change in unpaid bills of nonfinancial public enterprises.

6/ Interest payments on public banks restructuring bonds and mortgage debt relief related costs.

7/ Adjusts non-commodity revenues for the output gap and commodity revenues for differentials between estimated equilibrium oil price and production levels. Adjustments are made to account for fuel subsidy expenditures and the accrual of Ecopetrol dividends. Excludes private pension transfers from revenues.

8/ Includes statistical discrepancy. Overall balance plus interest expenditures

9/ Includes income tax payments and dividends from Ecopetrol that correspond to earnings from the previous year, and royalties to local governments.

10/ Includes Ecopetrol and Banco de la República's outstanding external debt.

Table 5. Colombia: Monetary Indicators

	2013	2014	2015	2016	2017	2018	2019	2020	2021	2022	2023
					Projections						
	(In billion of Col$, unless otherwise indicated)										
Central Bank											
Net Foreign Assets	83,091.8	112,111.1	145,917.4	138,945.7	140,672.1	146,961.8	150,573.4	155,728.4	161,316.7	166,495.9	172,140.9
Gross official reserve assets	88,927.7	112,101.2	145,726.0	138,631.7	140,724.9	143,819.6	147,587.6	152,899.0	158,623.8	163,938.5	169,712.5
In billion of US$	43.2	46.8	46.3	46.2	47.1	47.9	49.0	50.2	51.5	52.9	54.2
Short-term foreign liabilities	5,769.9	25.0	43.1	20.2	64.8	42.7	42.6	50.0	45.1	45.9	47.0
Other net foreign assets	2,298.1	2,812.1	3,657.2	3,522.8	3,349.6	3,185.0	3,028.4	2,879.5	2,737.9	2,603.3	2,475.4
Net domestic assets	-17,993.0	-42,428.7	-63,395.4	-54,345.8	-51,859.4	-52,699.3	-50,373.1	-48,756.1	-47,113.7	-44,691.0	-42,228.0
Net credit to the public sector	-14,526.1	-21,025.7	-9,269.8	-5,989.4	-2,492.2	-2,532.6	-2,420.8	-2,343.1	-2,264.2	-2,147.7	-2,029.4
Net credit to the financial system	3,732.0	6,768.0	6,525.0	5,678.6	3,808.4	3,870.1	3,699.3	3,580.6	3,459.9	3,282.0	3,101.1
Other	-7,198.9	-28,171.0	-60,650.6	-54,035.0	-53,175.6	-54,036.8	-51,651.6	-49,993.6	-48,309.5	-45,825.3	-43,299.8
Monetary base	65,098.8	69,682.4	82,522.0	84,599.9	88,812.7	94,262.5	100,200.3	106,972.3	114,203.0	121,804.9	129,912.9
Currency in circulation	39,751.0	45,428.6	53,864.8	49,457.8	52,172.4	55,373.9	58,862.0	62,840.2	67,087.8	71,553.5	76,316.5
Deposit money banks reserves	25,253.7	24,170.4	28,586.2	28,233.9	28,943.4	30,263.0	32,143.8	34,239.9	36,554.2	39,195.3	42,007.5
Other deposits	94.1	83.4	70.9	6,908.2	7,696.9	7,696.9	7,696.9	7,696.9	7,696.9	7,696.9	7,696.9
Financial system											
Net foreign assets	67,826.3	92,814.8	131,857.1	130,910.9	128,900.4	133,877.2	136,664.5	140,879.6	145,464.1	149,588.1	154,107.6
In billion of US$	35.2	38.8	41.9	43.6	43.2	44.6	45.3	46.3	47.3	48.3	49.3
Net domestic assets	261,480.4	269,523.0	272,760.4	320,394.6	341,456.8	382,360.8	429,771.5	482,237.4	539,414.1	601,828.7	669,671.5
Net credit to public sector	33,150.7	30,800.1	32,253.4	34,552.8	33,050.3	40,591.4	52,673.1	56,516.0	61,730.2	62,703.9	64,536.3
Credit to private sector	281,747.0	323,152.2	377,281.0	406,280.2	451,032.3	485,023.5	528,186.7	578,673.3	640,935.0	715,004.7	797,634.2
Other net	-53,417.3	-84,429.2	-136,774.0	-120,438.4	-142,625.8	-143,254.1	-151,088.3	-152,951.9	-163,251.1	-175,879.9	-192,499.0
Broad money	329,306.7	362,337.8	404,617.5	451,305.4	470,357.1	516,238.0	566,436.0	623,117.0	684,878.2	751,416.8	823,779.1
	(Annual percentage change)										
Credit to private sector	12.1	14.7	16.8	7.7	11.0	7.5	8.9	9.6	10.8	11.6	11.6
Currency	13.4	14.3	18.6	-8.2	5.5	6.1	6.3	6.8	6.8	6.7	6.7
Monetary base	15.3	7.0	18.4	2.5	5.0	6.1	6.3	6.8	6.8	6.7	6.7
Broad money	13.4	10.0	11.7	11.5	4.2	9.8	9.7	10.0	9.9	9.7	9.6
	(In percent of GDP)										
Credit to private sector	39.7	42.7	47.2	47.5	49.4	50.1	51.3	52.6	54.6	57.1	59.8
Currency	5.6	6.0	6.7	5.8	5.7	5.7	5.7	5.7	5.7	5.7	5.7
Monetary base	9.2	9.2	10.3	9.9	9.7	9.7	9.7	9.7	9.7	9.7	9.7
Broad money	46.3	47.9	50.6	52.8	51.5	53.3	55.0	56.7	58.4	60.0	61.7
Memorandum items:											
Central bank inflation target	2.0-4.0	2.0-4.0	2.0-4.0	2.0-4.0	2.0-4.0	2.0-4.0	2.0-4.0	2.0-4.0	2.0-4.0	2.0-4.0	2.0-4.0
CPI inflation, eop	2.0	3.7	6.9	5.8	4.1	3.4	3.0	3.0	3.0	3.0	3.0
Nominal GDP (In Col$ billion)	710,497	757,065	799,312	855,432	912,525	968,520	1,029,529	1,099,110	1,173,403	1,251,511	1,334,817

Sources: Banco de la Republica; and Fund staff estimates and projections.

Table 6. Colombia: Medium-Term Outlook

	2013	2014	2015	2016	2017	2018	2019	2020	2021	2022	2023
					Projections						
					(In percent of GDP, unless otherwise indicated)						
Real GDP (in percent change)	4.9	4.4	3.1	2.0	1.8	2.7	3.3	3.6	3.6	3.6	3.5
Consumer prices (in percent change; end of period)	2.0	3.7	6.9	5.8	4.1	3.4	3.0	3.0	3.0	3.0	3.0
Gross national savings	21.0	21.1	20.3	20.4	20.0	21.0	21.1	21.2	21.1	21.1	21.0
Private sector	14.6	15.5	16.5	17.7	17.3	17.5	16.8	16.0	15.8	15.8	16.0
Public sector	6.5	5.6	3.8	2.7	2.7	3.5	4.3	5.3	5.3	5.2	5.0
Gross domestic investment	24.3	26.3	26.7	24.7	23.4	23.6	23.7	23.7	23.6	23.5	23.4
Private sector	16.9	18.4	19.2	19.1	17.3	17.4	17.7	17.9	17.8	17.8	17.7
Public sector	7.3	7.4	7.2	5.5	5.6	6.0	6.0	5.9	5.8	5.7	5.6
					(In percent of GDP, unless otherwise indicated)						
Nonfinancial public sector 1/											
Revenue	28.1	27.7	26.4	25.1	25.6	25.7	25.9	26.5	26.6	26.4	26.2
Expenditure	29.1	29.4	29.8	28.1	28.7	28.4	27.9	27.4	27.4	27.1	27.0
Current expenditure	21.5	21.9	22.0	22.6	22.5	22.1	22.4	22.3	22.1	21.9	21.7
Capital expenditure	7.6	7.6	7.8	5.5	6.2	6.3	5.5	5.1	5.3	5.2	5.2
Primary balance 2/	0.0	-0.2	-0.5	-1.0	-0.7	-0.2	0.7	1.2	1.4	1.5	1.4
Overall balance 2/	-0.9	-1.8	-3.4	-3.0	-3.1	-2.7	-1.9	-0.9	-0.7	-0.7	-0.8
Combined public sector balance	-0.9	-1.8	-3.4	-2.8	-2.9	-2.5	-1.7	-0.6	-0.5	-0.4	-0.6
External financing	1.2	2.8	2.6	1.6	1.1	1.2	1.5	1.0	1.0	0.0	0.0
Domestic financing	-0.3	-1.0	0.8	1.1	1.8	1.3	0.2	-0.4	-0.5	0.4	0.6
External current account balance	-3.3	-5.2	-6.4	-4.3	-3.4	-2.6	-2.6	-2.5	-2.5	-2.4	-2.3
Trade balance	0.8	-1.2	-4.6	-3.3	-1.5	-0.6	-1.0	-1.0	-0.9	-0.9	-0.8
Exports	15.9	15.0	13.2	12.2	12.8	13.8	13.4	13.5	13.5	13.5	13.5
Imports	15.0	16.3	17.9	15.4	14.3	14.4	14.4	14.4	14.4	14.3	14.3
Financial account balance	-3.1	-5.1	-6.3	-4.5	-3.1	-2.6	-2.6	-2.5	-2.5	-2.4	-2.3
Direct Investment	-2.3	-3.2	-2.6	-3.3	-3.5	-2.4	-2.4	-2.4	-2.4	-2.4	-2.4
Portfolio Investment	-2.0	-3.1	-3.5	-1.3	-0.5	-0.6	-0.5	-0.4	-0.4	-0.3	-0.2
Other Investments and Derivatives	0.0	0.2	0.7	-0.2	0.1	0.0	0.0	0.0	0.0	0.0	0.0
Change in Reserve Assets	1.8	1.2	0.1	0.1	0.2	0.2	0.3	0.3	0.3	0.3	0.3
Gross public sector debt 3/	37.8	43.7	50.6	50.4	50.2	49.9	48.7	46.5	44.4	42.3	40.4
Gross public sector debt, excluding Ecopetrol	36.1	40.8	45.8	45.9	46.9	46.7	46.0	43.9	42.0	39.9	38.1
Total public net debt 4/	27.0	33.2	42.2	39.1	39.3	39.9	39.5	38.1	36.6	35.2	33.9
Memorandum items:											
Nominal GDP (in Col$ billion)	710,497	757,065	799,312	855,432	912,525	968,520	1,029,529	1,099,110	1,173,403	1,251,511	1,334,817
Crude oil, spot price	104.1	96.2	50.8	42.8	52.8	62.3	58.2	55.6	54.1	53.6	53.6

Sources: Colombian authorities and Fund staff estimates and projections.
1/ Excludes Ecopetrol.
2/ Includes statistical discrepancy.
3/ Includes debt of the non-financial public sector, plus Ecopetrol, FOGAFIN and FINAGRO.
4/ Gross debt minus financial assets (public sector deposits in domestic and foreign financial institutions).

Table 7. Colombia: Financial Soundness Indicators 1/

(In percent, unless otherwise indicated; end-of-period values)

	2009	2010	2011	2012	2013	2014	2015	2016	2017
Capital Adequacy									
Regulatory capital to risk-weighted assets	17.2	17.3	16.9	18.1	17.0	17.0	16.9	17.5	18.6
Regulatory Tier 1 capital to risk-weighted assets	13.4	13.0	13.4	13.7	12.0	11.7	11.4	11.4	12.4
Capital (net worth) to assets 2/	14.2	14.2	14.3	14.7	14.8	14.9	14.1	16.2	16.1
Asset Quality and Distribution									
Nonperforming loans to gross loans	4.0	2.9	2.5	2.8	2.8	2.9	2.8	3.1	4.2
Provisions to nonperforming loans	140.1	175.0	182.0	163.9	160.7	151.3	155.5	153.5	126.5
Gross loans to assets	64.3	67.9	70.4	69.6	68.2	69.3	70.2	69.3	69.7
Earnings and Profitability									
ROAA	3.5	3.4	3.3	3.1	2.8	2.9	2.7	3.0	2.2
ROAE	26.2	23.7	23.0	21.2	19.5	19.8	18.9	18.3	13.8
Interest margin to gross income	54.0	55.6	58.4	58.7	61.3	60.6	58.7	53.7	59.2
Noninterest expenses to gross income	43.2	47.0	49.3	47.2	47.0	44.6	43.4	41.2	43.9
Liquidity									
Liquid assets to total assets 3/	24.6	22.1	21.5	21.6	21.4	19.8	18.9	18.0	18.6
Liquid assets to short-term liabilities 3/	47.8	42.7	43.7	43.6	41.9	40.3	39.9	39.9	42.6
Deposit to loan ratio	98.8	93.5	91.4	94.7	96.3	91.6	88.3	88.4	88.4
Other									
Foreign-currency-denominated loans to total loans	4.2	6.9	7.7	7.5	7.3	8.4	8.3	6.9	6.1
Foreign-currency-denominated liabilities to total liabilities	7.1	9.8	11.5	10.5	11.9	13.5	13.9	11.8	11.0
Net open position in foreign exchange to capital 4/	0.5	0.6	1.0	0.6	0.5	0.7	1.3	5.5	6.4

Source: Superintendencia Financiera.

1/ Total Banking System. All deposit taking institutions.

2/ Large increase in 2016 due to a change to IFRS in January 2016 where deposit insurance that used to be recorded as a liability is now recorded as capital.

3/ Data after 2011 refers to broader definition of liquid assets in line with international standards.

4/ Since January 2016, goodwill and retained earnings started to be recorded in foreign currency. Before January of 2016, they were recorded in Colombian pesos and weren't included in the foreign exchange position.

Table 8. Colombia: Indicators of External Vulnerability 1/

(In billions of US$, unless otherwise indicated)

						Projections					
	2013	2014	2015	2016	2017	2018	2019	2020	2021	2022	2023
External indicators											
Exports of GNFS 1/	67.3	64.1	46.0	41.8	47.8	54.3	56.6	60.4	63.9	67.8	72.0
Imports of GNFS 1/	70.5	75.9	64.3	54.5	56.7	60.3	63.7	67.7	71.6	75.5	79.7
Terms of trade (12-month percent change)	146.5	141.8	114.4	111.0	119.9	121.9	119.2	117.8	116.5	116.4	116.9
Current account balance	-12.5	-19.8	-18.6	-12.1	-10.4	-8.5	-9.0	-9.1	-9.7	-10.0	-10.2
In percent of GDP	-3.3	-5.2	-6.4	-4.3	-3.4	-2.6	-2.6	-2.5	-2.5	-2.4	-2.3
Financial account balance	-11.7	-19.3	-18.3	-12.7	-9.7	-8.5	-9.0	-9.1	-9.7	-10.0	-10.2
Of which: Foreign direct investment (net)	-8.6	-12.3	-7.5	-9.3	-10.8	-7.7	-8.2	-8.8	-9.3	-9.8	-10.4
Of which: Portfolio investment (net)	-7.4	-11.6	-10.3	-3.7	-1.6	-2.1	-1.8	-1.3	-1.7	-1.4	-1.0
Total external debt 2/	97.9	113.9	123.8	138.9	146.8	152.7	157.6	162.5	168.5	175.6	183.1
Of which: Public sector 2/	58.0	72.3	79.5	89.9	94.3	98.3	102.1	105.5	108.5	112.3	115.8
In percent of gross international reserves	226.8	243.1	267.7	300.7	311.5	318.6	322.1	323.6	327.0	332.2	337.6
Short-term external debt 3/	12.2	14.4	14.8	14.6	17.3	17.3	17.3	17.3	17.4	17.4	17.4
Of which: Public sector	0.5	0.7	0.7	0.7	0.6	0.6	0.6	0.6	0.6	0.6	0.6
Of which: Private sector	11.6	13.7	14.1	13.9	16.7	16.7	16.7	16.8	16.8	16.8	16.8
Amortization of MLT external debt (in percent of GNFS exports)	9.3	15.0	20.8	18.1	31.6	16.7	20.6	19.5	22.2	18.7	16.0
External interest payments (in percent of GNFS exports)	5.4	6.3	9.9	11.4	11.0	13.0	13.7	13.8	13.5	13.3	13.2
Gross international reserves 4/ 5/	43.2	46.8	46.3	46.2	47.1	47.9	48.9	50.2	51.5	52.9	54.2
In months of prospective GNFS imports	6.8	8.7	10.2	9.8	9.4	9.0	8.7	8.4	8.2	8.0	7.7
In percent of broad money	24.5	25.9	31.3	31.3	29.6	27.4	25.6	24.1	22.7	21.4	20.2
In percent of short-term external debt on residual maturity plus current account deficit	103.9	110.0	134.2	115.3	135.3	126.4	128.1	121.7	128.7	135.3	…
Nominal exchange rate (Col$/US$, period average)	1,869	2,001	2,742	3,055	2,951	2,953	…	…	…	…	…
Real effective exchange rate (percentage change, + = appreciation)	-2.9	-6.9	-20.6	-4.7	2.8	0.6	…	…	…	…	…

Sources: Banco de la República; and Fund staff estimates and projections.
1/ GNFS stands for goods and nonfactor services; MLT stands for medium and long-term.
2/ Includes foreign holdings of locally issued public debt (TES).
3/ Original maturity of less than 1 year. Stock at the end of the previous period.
4/ Estimate for 2009 includes the SDR allocation (US$972 million).
5/ IMF definition that excludes Colombia's contribution to Fondo Latinoamericano de Reservas (FLAR) and includes valuation changes of reserves denominated in other currencies than U.S. dollars.

Table 9. Colombia: Public Sector Debt Sustainability Analysis (DSA) – Baseline Scenario

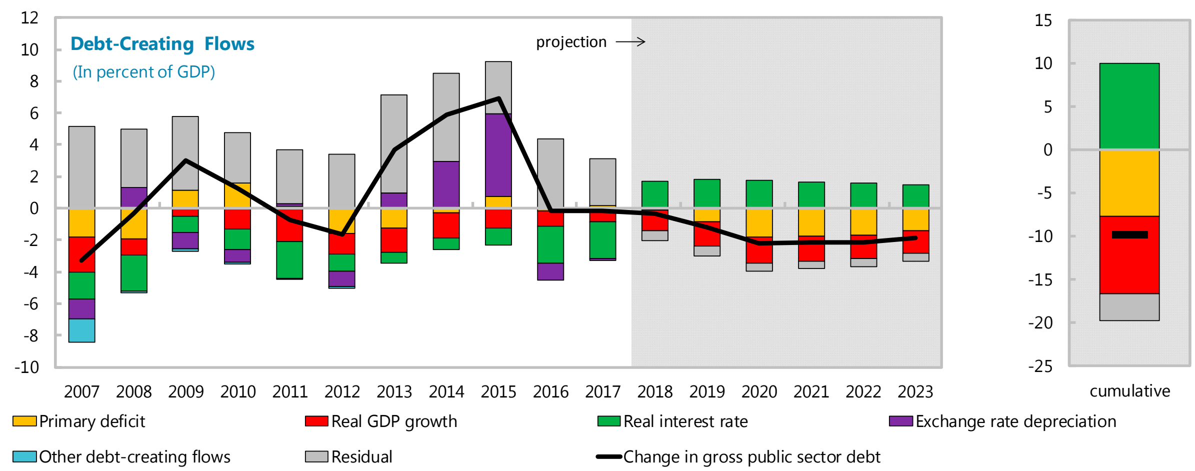
(In percent of GDP, unless otherwise indicated)

Debt, Economic and Market Indicators [1/]

	Actual			Projections						As of January 19, 2018		
	2007-2015 [2/]	2016	2017	2018	2019	2020	2021	2022	2023	Sovereign Spreads		
Nominal gross public debt	37.6	50.4	50.2	49.9	48.7	46.5	44.4	42.3	40.4	EMBIG (bp) 3/		157
Public gross financing needs	6.2	5.0	6.0	4.5	5.1	3.4	3.2	2.3	2.6	5Y CDS (bp)		91
Real GDP growth (in percent)	4.3	2.0	1.8	2.7	3.3	3.6	3.6	3.6	3.5	Ratings	Foreign	Local
Inflation (GDP deflator, in percent)	4.0	4.9	4.8	3.3	3.0	3.0	3.0	3.0	3.0	Moody's	Baa2	Baa2
Nominal GDP growth (in percent)	8.5	7.0	6.7	6.1	6.3	6.8	6.8	6.7	6.7	S&Ps	BBB-	BBB
Effective interest rate (in percent) [4/]	9.4	7.7	7.2	7.0	6.9	6.9	6.9	6.9	6.8	Fitch	BBB	BBB

Contribution to Changes in Public Debt

	Actual			Projections							
	2007-2015	2016	2017	2018	2019	2020	2021	2022	2023	cumulative	debt-stabilizing
Change in gross public sector debt	1.6	-0.2	-0.1	-0.3	-1.2	-2.2	-2.1	-2.1	-1.8	-9.8	primary
Identified debt-creating flows	-2.6	-4.5	-3.1	0.3	-0.6	-1.7	-1.7	-1.6	-1.3	-6.7	balance [9/]
Primary deficit	-0.4	-0.2	0.2	-0.1	-0.9	-1.8	-1.8	-1.7	-1.4	-7.7	0.07
Primary (noninterest) revenue and grants	26.0	24.6	25.1	25.2	25.4	26.0	26.1	25.9	25.7	154.4	
Primary (noninterest) expenditure	25.7	24.4	25.3	25.1	24.6	24.2	24.3	24.2	24.3	146.7	
Automatic debt dynamics [5/]	-2.1	-4.4	-3.3	0.4	0.3	0.1	0.1	0.1	0.1	1.0	
Interest rate/growth differential [6/]	-2.8	-3.3	-3.1	0.4	0.3	0.1	0.1	0.1	0.1	1.0	
Of which: real interest rate	-1.3	-2.3	-2.3	1.7	1.8	1.7	1.7	1.6	1.5	10.0	
Of which: real GDP growth	-1.4	-1.0	-0.8	-1.3	-1.5	-1.7	-1.6	-1.5	-1.4	-9.0	
Exchange rate depreciation [7/]	0.7	-1.1	-0.1	…	…	…	…	…	…	…	
Other identified debt-creating flows	-0.2	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	
Privatization (incl. concessions) (negative)	-0.2	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	
Contingent liabilities	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	
Please specify (2) (e.g., ESM and Euroarea loans)	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	
Residual, including asset changes [8/]	4.3	4.4	2.9	-0.6	-0.6	-0.5	-0.4	-0.5	-0.5	-3.2	



Source: Fund staff estimates.

1/ Public sector is defined as non-financial public sector.

2/ Based on available data.

3/ EMBIG.

4/ Defined as interest payments divided by debt stock (excluding guarantees) at the end of previous year.

5/ Derived as [(r - π(1+g) - g + ae(1+r)]/(1+g+π+gπ)) times previous period debt ratio, with r = interest rate; π = growth rate of GDP deflator; g = real GDP growth rate; a = share of foreign-currency denominated debt; and e = nominal exchange rate depreciation (measured by increase in local currency value of U.S. dollar).

6/ The real interest rate contribution is derived from the numerator in footnote 5 as r - π (1+g) and the real growth contribution as -g.

7/ The exchange rate contribution is derived from the numerator in footnote 5 as ae(1+r).

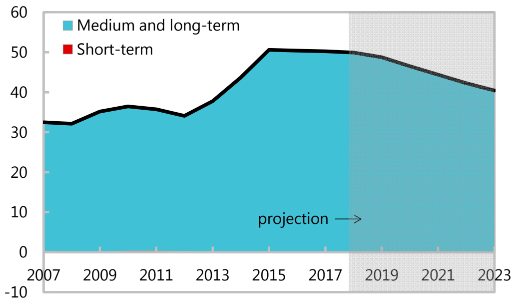
8/ Includes asset changes and interest revenues (if any). For projections, includes exchange rate changes during the projection period.

9/ Assumes that key variables (real GDP growth, real interest rate, and other identified debt-creating flows) remain at the level of the last projection year.

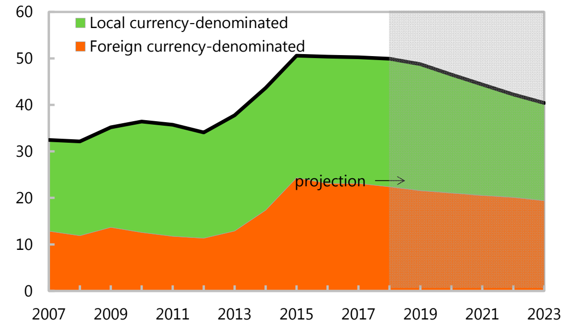
Table 10. Colombia: Public DSA – Composition of Public Debt and Alternative Scenarios

Composition of Public Debt

By Maturity
(In percent of GDP)



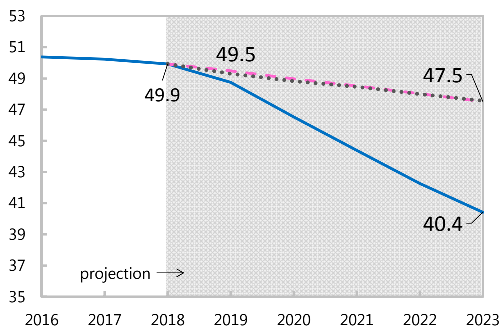
By Currency
(In percent of GDP)



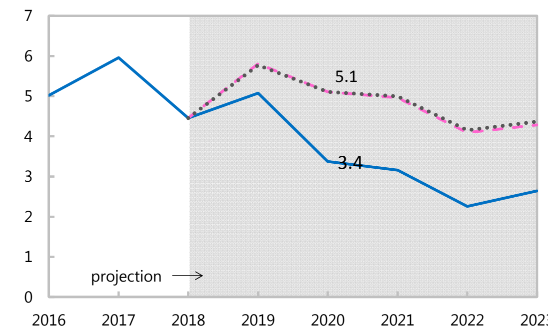
Alternative Scenarios

Baseline Historical Constant Primary Balance

Gross Nominal Public Debt
(In percent of GDP)



Public Gross Financing Needs
(In percent of GDP)



Underlying Assumptions
(In percent)

Baseline Scenario	2018	2019	2020	2021	2022	2023
Real GDP growth	2.7	3.3	3.6	3.6	3.6	3.5
Inflation	3.3	3.0	3.0	3.0	3.0	3.0
Primary Balance	0.1	0.9	1.8	1.8	1.7	1.4
Effective interest rate	7.0	6.9	6.9	6.9	6.9	6.8
Constant Primary Balance Scenario						
Real GDP growth	2.7	3.3	3.6	3.6	3.6	3.5
Inflation	3.3	3.0	3.0	3.0	3.0	3.0
Primary balance	0.1	0.1	0.1	0.1	0.1	0.1
Effective interest rate	7.0	6.9	6.9	6.9	6.9	6.8

Historical Scenario	2018	2019	2020	2021	2022	2023
Real GDP growth	2.7	3.6	3.6	3.6	3.6	3.6
Inflation	3.3	3.0	3.0	3.0	3.0	3.0
Primary balance	0.1	0.1	0.1	0.1	0.1	0.1
Effective interest rate	7.0	6.9	7.0	7.0	7.0	7.0

Source: Fund staff estimates.

Table 11. Colombia: External Debt Sustainability Framework, 2013–24

(In percent of GDP, unless otherwise indicated)

	Actual							Projections							
	2013	2014	2015	2016	2017			2018	2019	2020	2021	2022	2023	2024	Debt-stabilizing non-interest current account 6/
Baseline: External debt	25.7	30.1	42.5	49.6	47.5			**46.6**	**45.4**	**44.3**	**43.3**	**42.7**	**42.1**	**41.5**	**-2.2**
Change in external debt	3.6	4.4	12.4	7.1	-2.1			-0.9	-1.1	-1.1	-0.9	-0.7	-0.6	-0.6	
Identified external debt-creating flows (4+8+9)	0.4	1.9	12.0	4.6	-4.1			-0.5	-0.7	-1.0	-1.0	-1.0	-1.1	-1.2	
Current account deficit, excluding interest payments	2.3	4.2	4.8	2.6	1.7			0.4	0.3	0.2	0.3	0.2	0.2	0.1	
Deficit in balance of goods and services	0.8	3.1	6.3	4.6	2.9			1.8	2.0	2.0	2.0	1.9	1.8	1.7	
Exports	17.7	16.9	15.8	14.9	15.5			16.6	16.3	16.5	16.4	16.5	16.6	16.6	
Imports	18.5	20.1	22.0	19.5	18.3			18.4	18.4	18.5	18.4	18.3	18.3	18.3	
Net non-debt creating capital inflows (negative)	-2.2	-3.3	-2.1	-1.0	-3.0			-1.8	-1.9	-1.9	-2.0	-2.0	-2.0	-2.0	
Automatic debt dynamics 1/	0.3	1.1	9.3	2.9	-2.8			0.9	0.8	0.7	0.7	0.7	0.7	0.7	
Contribution from nominal interest rate	1.0	1.1	1.6	1.7	1.7			2.2	2.2	2.3	2.2	2.2	2.2	2.2	
Contribution from real GDP growth	-1.0	-1.1	-1.2	-0.9	-0.8			-1.2	-1.4	-1.6	-1.5	-1.5	-1.4	-1.4	
Contribution from price and exchange rate changes 2/	0.4	1.2	9.0	2.1	-3.7			...	...	...	...	...	...	...	
Residual, incl. change in gross foreign assets (2-3) 3/	3.1	2.4	0.4	2.5	1.9			-0.4	-0.4	-0.1	0.1	0.3	0.5	0.7	
External debt-to-exports ratio (in percent)	145.4	177.8	269.2	332.6	307.1			281.1	278.3	269.1	263.5	259.2	254.3	249.6	
Gross external financing need (in billions of US dollars) 4/	29.3	41.5	42.6	34.5	40.1			34.8	37.9	38.2	41.3	40.0	39.1	38.2	
in percent of GDP	7.7	11.0	14.6	12.3	13.0	10-Year	10-Year	10.6	10.9	10.4	10.6	9.7	9.0	8.3	
Scenario with key variables at their historical averages 5/								**46.6**	**47.2**	**47.9**	**48.8**	**50.0**	**51.4**	**52.9**	**-2.6**
Key Macroeconomic Assumptions Underlying Baseline						Historical Average	Standard Deviation								For debt stabilization
Real GDP growth (in percent)	4.9	4.4	3.1	2.0	1.8	3.6	1.5	2.7	3.3	3.6	3.6	3.6	3.5	3.5	
GDP deflator in US dollars (change in percent)	-1.9	-4.7	-25.2	-5.9	8.5	1.2	12.6	3.2	2.5	2.0	2.2	2.3	2.1	2.1	
Nominal external interest rate (in percent)	4.4	4.1	4.0	3.8	3.8	4.8	1.0	4.8	5.1	5.3	5.3	5.4	5.4	5.4	
Growth of exports (US dollar terms, in percent)	-1.1	-4.8	-28.2	-9.2	14.5	5.0	19.8	13.6	4.3	6.6	5.9	6.0	6.3	6.3	
Growth of imports (US dollar terms, in percent)	1.8	7.7	-15.4	-15.1	4.0	5.2	16.3	6.4	5.6	6.3	5.7	5.4	5.6	5.6	
Current account balance, excluding interest payments	-2.3	-4.2	-4.8	-2.6	-1.7	-2.4	1.2	-0.4	-0.3	-0.2	-0.3	-0.2	-0.2	-0.1	
Net non-debt creating capital inflows	2.2	3.3	2.1	1.0	3.0	2.4	1.2	1.8	1.9	1.9	2.0	2.0	2.0	2.0	

1/ Derived as [r - g - r(1+g) + ea(1+r)]/(1+g+r+gr) times previous period debt stock, with r = nominal effective interest rate on external debt; r = change in domestic GDP deflator in US dollar terms, g = real GDP growth rate, e = nominal appreciation (increase in dollar value of domestic currency), and a = share of domestic-currency denominated debt in total external debt.

2/ The contribution from price and exchange rate changes is defined as [-r(1+g) + ea(1+r)]/(1+g+r+gr) times previous period debt stock. r increases with an appreciating domestic currency (e > 0) and rising inflation (based on GDP deflator).

3/ For projection, line includes the impact of price and exchange rate changes.

4/ Defined as current account deficit, plus amortization on medium- and long-term debt, plus short-term debt at end of previous period.

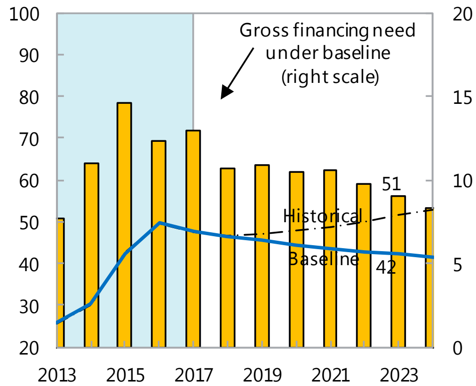
5/ The key variables include real GDP growth; nominal interest rate; dollar deflator growth; and both non-interest current account and non-debt inflows in percent of GDP.

6/ Long-run, constant balance that stabilizes the debt ratio assuming that key variables (real GDP growth, nominal interest rate, dollar deflator growth, and non-debt inflows in percent of GDP) remain at their levels of the last projection year.

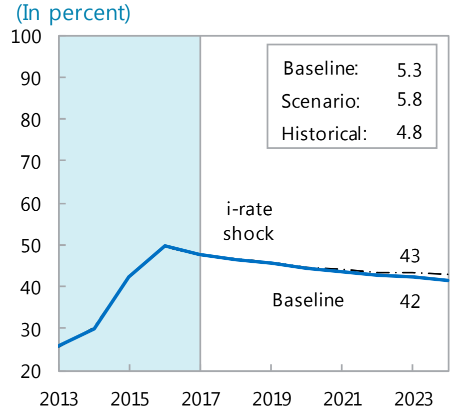
Table 12. Colombia: External Debt Sustainability: Bound Tests 1/ 2/

(External debt in percent of GDP)

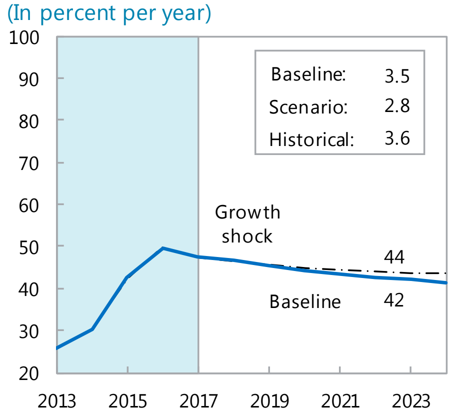
Baseline and Historical Scenarios



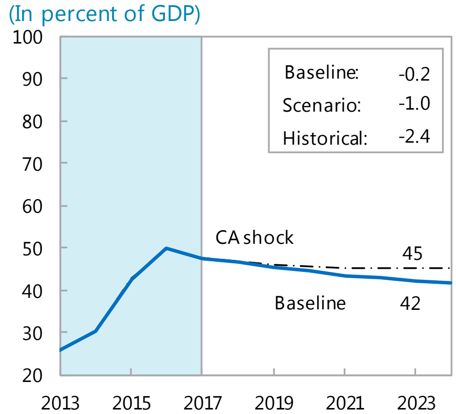
Interest Rate Shock
(In percent)



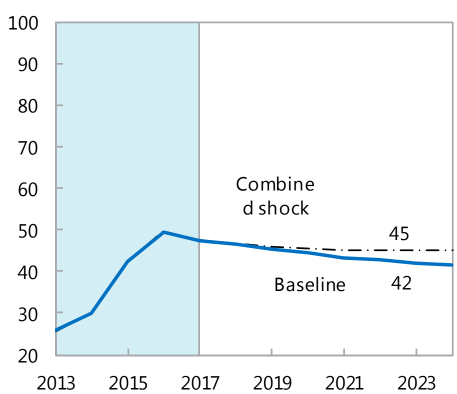
Growth Shock
(In percent per year)



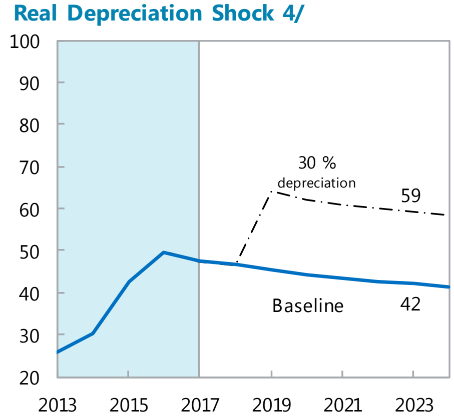
Non-Interest Current Account Shock
(In percent of GDP)



Combined Shock 3/



Real Depreciation Shock 4/



Sources: International Monetary Fund, Country desk data, and staff estimates.
1/ Shaded areas represent actual data. Individual shocks are permanent one-half standard deviation shocks. Figures in the boxes represent average projections for the respective variables in the baseline and scenario being presented. Ten-year historical average for the variable is also shown.
2/ For historical scenarios, the historical averages are calculated over the ten-year period, and the information is used to project debt dynamics five years ahead.
3/ Permanent 1/4 standard deviation shocks applied to real interest rate, growth rate, and current account balance.
4/ One-time real depreciation of 30 percent occurs in 2017.

Annex I. External Sector Assessment

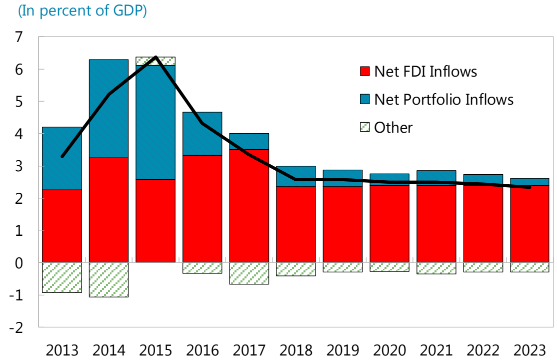
The external sector position of Colombia in 2017 was moderately weaker than implied by fundamentals and desirable policy settings. The adjustment to the large commodity shock continued last year, with the current account deficit reaching 3.4 percent of GDP, down from a peak of 6.4 percent of GDP in 2015. This deficit is expected to further narrow over the medium term, reflecting the lagged effects of the large real exchange rate depreciation and a further tightening of fiscal policy.

1. **The current account deficit narrowed to 3.4 percent of GDP in 2017, down from 4.3 percent of GDP the year before.** The adjustment reflected mainly a trade balance improvement, as exports continued to recover faster than imports, and the trade deficit declined to 1.5 percent from 3.3 percent the year before. The adjustment of the trade balance more than offset a worsening of the primary income deficit, to 2.6 percent from 1.9 percent the year before, mostly due to higher FDI-related payments (dividends and repatriated earnings).

2. **Despite a large real exchange rate depreciation of 36 percent since 2014, the increase in exports has so far been moderate.** Staff estimated a distributed lag model for total export volume growth, and found that weak trading partner growth have largely offset the positive effects of the real depreciation so far (see SIP 1).

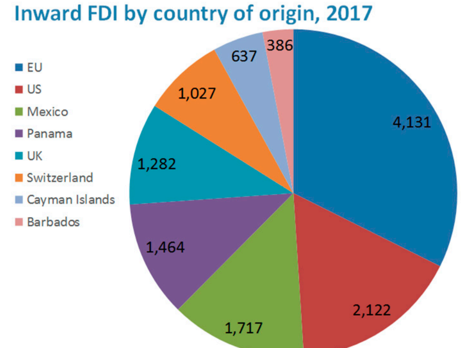
3. **The current account deficit continues to be financed mainly by FDI and government bonds.** Despite the decline in oil-related FDI, FDI remains a key source of financing, although well below the pre-2015 levels—gross inflows have been hovering at about 3.8−4 percent of GDP since 2015,[7] and are projected at around 3.5 percent in the medium term. The bulk of these inflows continue to originate in the EU, U.S., Mexico, and Panama. While portfolio inflows have declined in 2017, reflecting lower government debt financing, the participation of foreign investors in local current government bonds has reached an all-time high 27 percent.

Financial account
(In percent of GDP)



Sources: National authorities; and Fund staff estimates.

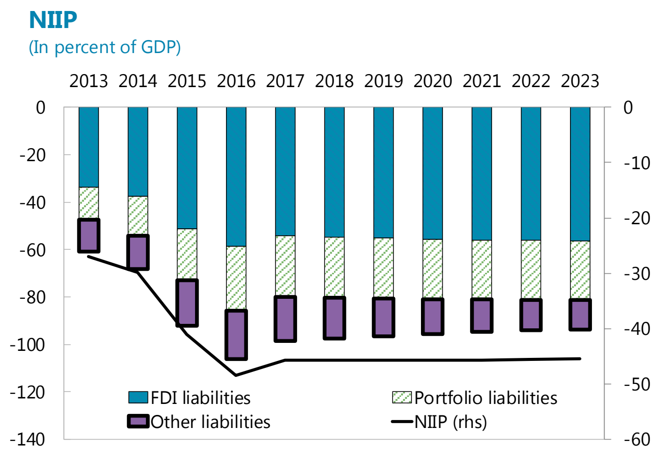
Inward FDI by country of origin, 2017



Sources: National authorities; and Fund staff estimates.

[7] These figures exclude the one-off receipts from the sale of ISAGEN in 2016 and fines charged to two foreign telecom companies in 2017.

4. The NIIP is at moderate levels and mainly in the form of FDI, but vulnerabilities remain. Colombia's NIIP reached -46 percent of GDP at end-2017 from -41 percent of GDP at end-2015. Most of the recent increase stems from an increase in liabilities to 99 percent of GDP, of which slightly more than half represents FDI. While the NIIP is sustainable, and projected to stabilize at about 45 percent of GDP, increases over the past few years in portfolio liabilities, now amounting to 26 percent of GDP, could lead to heightened vulnerability to global financial volatility.



Sources: National authorities; and Fund staff estimates.

5. Reserve buffers remain adequate. Colombia is committed to a floating exchange rate, as demonstrated by the significant depreciation of the peso in response to the large commodity shocks. These developments have also led to a halt in reserve accumulation, but strong buffers have been build up in past years with foreign exchange reserves amounting to about 146 percent of the ARA metric in 2017. The FCL represents an additional buffer. Reserve buffers measured relative to the ARA metric are projected to decline somewhat over the medium term, partly reflecting higher exports, but would remain comfortably within the 100-150 percent range. In addition, reserves relative to short-term debt and current account deficit will increase to about 135 percent over the medium term.

6. According to the adjusted EBA CA analysis, the external sector position in 2017 was moderately weaker than implied by fundamentals and desirable policy settings. The CA norm based on the CA method is +0.1 percent of GDP, implying a CA gap of -3.9 percent of GDP. This estimate, however, reflects a very large unexplained residual (-4.6 percent), and there is significant uncertainty around the estimated norm—the standard deviation of 1.3 percent is higher than for most other EBA countries. Staff believes that the poor fit of the CA method in the case of Colombia is due mainly to its failure to capture Colombia's ongoing export diversification and large oil-related outflows from earning repatriation, and its large infrastructure gap and other investment needs. Taking recent improvements in the terms of trade into account (estimated to have improved the cyclically adjusted CA by about 0.4 percentage points), and using the *medium-term* ratio of net oil

EBA analysis of the CA and the REER 1/ 2/

	Cyclically adjusted 2017 CA	CA norm	Contribution of policy gaps	CA gap	REER gap
CA	-3.8	0.1	0.7	-3.9	29.0
ES		-2.4		-0.5	3.6
REER level 1/			-2.4	3.8	-27.4

Source: IMF staff estimates.
1/ Reflecting estimates as of October 25, 2017.
2/ Using an elasticity of the CA/GDP to the REER of 0.14, derived based on the common assumptions of 0.71 for the export elasticity and 0.92 for the import elasticity.

exports to GDP, and excluding the oil-related repatriated earnings (estimated to reduce the CA norm by about 1.6 percentage points) reduces the CA gap to 1.9 percent.[8]

7. **Staff's assessment is that policies are on their desirable course, and there is no need for additional tightening.** The identified gap reflects the fact that the large depreciation and strong policy response take time to lead to a stronger external position. In staff's view, policies are on their desirable course to contribute to a further narrowing of the current account deficit over the medium term, and there is no need for additional tightening beyond what is already planned.

8. **Going forward, the accumulated real depreciation and an improved international environment will be supportive of exports.** The distributed lag total export volume growth model (see SIP 1) projects average quarterly real total export growth around 3 percent in Colombia for 2018Q1–Q4, relative to the average of -1.6 percent growth rate observed in 2016Q1−17Q2. This will contribute to bringing the CA to the norm in the medium term.

9. **Evidence from past large depreciations in commodity exports also suggest that increases in nontraditional exports can be significant, but could take several years to fully materialize.** Staff analyzed the behavior of nontraditional export market shares in a sample of 61 large depreciations (17 in LA) in 53 commodity exporters in 1985–2015 to gauge the outlook for non-traditional exports more specifically. If Colombia tracks the median commodity exporter experiencing a large depreciation, cumulative nontraditional export growth in 2015–20 would reach 30 percent—growth would be much higher still if Colombia performs in line with the top quarter of episodes. Importantly, staff found that the effects of large depreciations on non-traditional exports take several years to materialize in full.

10. **Reducing nontariff costs, which are a major constraint to trade in Colombia, could improve competitiveness.** Nontariff costs account for three quarters of the cost of imports, acting as a barrier to exports since exporters often use imported inputs. Direct non-tariff barriers per product category grew from four in 2001 to 16 in 2014. Infrastructure and transportation as well as customs procedures also stand out as nontariff costs. The infrastructure gap in Colombia is significant, adding to the cost of transporting goods from/to the border. Inefficient service providers also add to road transportation costs. Last, World Bank data show that Colombian customs are relatively slow, especially when it comes to exporting.

[8] The REER and ES methodologies produce different results. The REER approach suggests a CA gap of +3.8 percent of GDP. However, the estimated 27.4 percent REER undervaluation is due mainly to the unexplained residual (25 percent), as the model does not capture the delayed response of the trade balance to the real depreciation and the large structural changes experienced by Colombia in recent years. The ES method estimates the CA balance needed to stabilize the net external position at the 2016 level (-44.9 percent of GDP) at -2.4 percent, implying a CA gap of 0.5 percent of GDP.

INTERNATIONAL MONETARY FUND

COLOMBIA

STAFF REPORT FOR THE 2018 ARTICLE IV CONSULTATION—INFORMATIONAL ANNEX

April 16, 2018

Prepared By: The Western Hemisphere Department (In collaboration with other Departments)

CONTENTS

FUND RELATIONS

(As of February 28, 2018)

Membership status: Joined: December 27, 1945; Article VIII.

General Resources Account:

	SDR Million	%Quota
Quota	2,044.50	100
IMF's Holdings of Currency (Holdings Rate)	1,838.39	89.92
Reserve Tranche Position	206.11	10.08

SDR Department:

	SDR Million	%Allocation
Net cumulative allocation	738.32	100
Holdings	672.77	91.12

Outstanding Purchases and Loans: None.

Latest Financial Arrangements:

			In million of SDR	
Type	Date of Arrangement	Expiration Date	Amount Approved	Amount Drawn
FCL	Jun 13, 2016	Jun 12, 2018	8,180.00	0.00
FCL	Jun 17, 2015	Jun 12, 2016	3,870.00	0.00
FCL	Jun 24, 2013	Jun 16, 2015	3,870.00	0.00

Projected Payments to the Fund (in SDR million):

	forthcoming				
	2018	2019	2020	2021	2022
Principal					
Charges/interest	0.42	0.56	0.56	0.56	0.56
Total	**0.42**	**0.56**	**0.56**	**0.56**	**0.56**

Implementation of HIPC Initiative: Not applicable.

Implementation of Multilateral Debt Relief Initiative (MDRI): Not applicable.

Exchange Rate: Arrangement: Colombia has a floating exchange rate regime (de jure: free floating; de facto: floating) and maintains an exchange restriction subject to Fund approval under Article VIII arising from the special regime for the hydrocarbon sector (see IMF Country Report No. 13/35 for details).

Article IV Consultation: The last Article IV Consultation was concluded on May 4, 2017 (IMF Country Report No. 17/138).

FSAP participation and ROSCs: The FSAP took place in 2000 and was updated in 2008 and 2013. A data ROSC took place in 2006 and a fiscal ROSC in 2003.

Technical Assistance:

Department	Time of Delivery	Purpose
STA	Jan. 14	National Accounts Statistics
STA	Jan. 14	Consumer Prices/Producer Price
MCM	Jul. 14	Bank Supervision & Regulations
FAD	Jul. 14	RA Gap
FAD	Jun. 14	Customs Administration
FAD	Feb. 15	Tax Policy
FAD	Nov. 14	Public Financial Management
FAD	Sep. 14	Tax and Customs Administration
FAD	Oct. 14	Tax Administration
FAD	Nov. 14	2012 Tax reform and New Challenges for Tax Policy
MCM	Jan. 15	Enhancing the Macroprudential Stress Testing Framework of Banco de la Republica.
FAD	Aug. 16	Discussion of the 2017 structural tax reform
FAD	Feb. 17	Revenue Administration
FAD	Mar. 17	Fiscal Transparency Assessment

WORLD BANK RELATIONS[1]

The World Bank Group Country Partnership Framework (CPF) for FY 16–21 aims to support the government's development goals. The CPF is aligned with both the Government's National Development Plan and the Bank Group's twin goals. Informed by a Systematic Country Diagnostic, the demand expressed by Colombian authorities and the WBG's comparative advantage in Colombia, the CPF selectively focuses on three strategic areas of engagement: (i) fostering balanced territorial development; (ii) enhancing social inclusion and mobility through improved service delivery; and (iii) supporting fiscal sustainability and productivity. Support for the peace building process cuts across all areas of Bank Group engagement, from land property rights in rural areas, for instance, to improving justice service delivery and access to justice.

The CPF adopts a flexible approach that enables adjustments to respond to changing client needs and macroeconomic developments. In implementing the CPF the World Bank Group will continue to provide integrated packages of services spanning World Bank, IFC and MIGA contributions, guaranteeing the quality of the World Bank Group's (WBG) financial, knowledge and convening services to respond to the specific development needs of Colombia. In addition to providing programmatic knowledge services, many South-South Knowledge Exchanges have been organized by the Bank under the different engagement areas.

Colombia is IBRD's 7th largest borrower per outstanding debt with US$9.9 billion as of end-March 2018. The current active portfolio is composed of 14 projects (including 2 stand-alone GEF and 1 Bio-Carbon fund project), totaling $2.0 billion in net commitments. Colombia's current Trust Fund portfolio amounts to US$85 million representing a variety of sectors. Lending in FY 17 amounted to US$1.7 billion comprised of two Development Policy Financing (DPF) operations for Territorial Development (US$800 million) and Fiscal Sustainability and Competitiveness (US$600 million), respectively, along with two Investment Project Financing (IPF) operations in the water and tertiary education sectors. Three IBRD operations have been approved by the Board in FY 18 to date totaling US$742 million: Second Sustainable Development and Green Growth DPF (US$500 million), Enhancing Waterway Connectivity and Water Service Provision in Colombia's Plan Pazcifico Project (US$42 million) and Additional Financing for Access to Higher Quality Education-PACES (US$160 million). One Guarantee on Clean Energy Development (US$41 million IBRD plus US$40 million Clean Technology Fund) is scheduled for approval at the end of the fiscal year. Two trust-funded (TF) operations were approved in FY 18 to date: a Global Environment Facility (GEF)-funded operation to consolidate forest and biodiversity conservation efforts in the Amazon and a BioCarbon TF to support sustainable low-carbon development in the Orinoquia region.

IFC's current committed own account and syndications portfolio in Colombia stands at $1.4 billion in 60 projects. It is the 12th largest portfolio worldwide and 4th largest regionally. The

[1] Prepared by the World Bank.

top sectors are: finance and insurance (59 percent), infrastructure (14 percent), collective investment vehicles (9 percent), and chemicals (6 percent). IFC Advisory in Colombia is active in PPPs (schools, hospitals, physical infrastructure), corporate governance, collateral registries, microfinance and sustainable energy finance, royalties' management, sustainable community investment, investment policy promotion, cities, taxes, and green building codes. In FY 18 to date, IFC has committed 9 projects for US$236 million, including: US$105 million loan (IFC+Mob) to Itau to increase financial access for two markets in need: climate/green projects and SMEs; US$90 million equity investment in Procaps to finance its investment program to increase access to quality affordable pharma products; and about US$8 million equity rights issue in FDN to help finance the Company's capital increase.

MIGA's current portfolio stands at US$91 million. MIGA coverage is entirely in the financial services sector across two projects: (i) Findeter, the first Non-Honoring of a Financial Obligation of a State-Owned Enterprise (US$89 million); and (ii) ProCredit Holding, the insurance of mandatory reserve at the Central Bank of Colombia (US$2 million). The Findeter project was issued in December 2015 and supports the expansion of lending operations by Findeter to intermediary financial institutions for urban infrastructure development projects in several cities across Colombia, with a tenor of 10 years. The ProCredit Holding project was issued in December 2010, with a focus on banks' capital optimization, such as reduction of risk weighting for mandatory reserves on a group's consolidated balance sheet thereby reducing capital provisioning. Its tenor is 10 years. MIGA remains open to support foreign direct investments in the country via its traditional political risk insurance products and non-honoring, credit guarantee products for sovereign, sub-sovereign and state-owned enterprises.

INTER-AMERICAN DEVELOPMENT BANK RELATIONS[1]

Colombia's current Country Strategy covers the period 2015–18 and identifies three policy areas of dialogue with the government: productivity, effectiveness of public management and social mobility. These areas are part of a comprehensive vision for the development process of the country, aimed at a vision where the country can achieve a path of sustainable growth and become a developed country in the long run. There are cross-cutting requirements associated with this objective and to growth and overcome conditions of poverty and inequity, which are: (i) increase tax-fiscal revenues in order to ensure a sizable flow of public goods, and (ii) recognizing both infrastructure development, and human and social capital development as necessary factors for greater productivity and strengthen the middle class.

The sovereign guarantee lending envelope (approvals) under the current Strategy is estimated at US$890 million in 2015 and US$800 million per year during 2016–18 term, which total US$3.3 billion for the years 2015 to 2018. In 2017, the Bank approved 6 operations for US$1,010.7 million in sovereign guarantee operations, of which US$750 million in Policy Based Loans.

As of February 2018, the Bank portfolio is currently composed of 27 sovereign guarantee operations, totaling US$2.0 billion, with a disbursed percentage of 19.5 percent. Operations are concentrated in infrastructure (55.6 percent), governance (12.6 percent), Climate Change and Sustainable Development (28.9 percent) and social development and integration (2.9 percent). The IDB is the second multilateral creditor with a total debt owed of US$7.7 billion (41.9 percent of Colombia's total multilateral debt). The non-reimbursable technical cooperation portfolio includes 56 operations, with an approved value of US$54.7 million.

The current portfolio of private sector initiatives (non-sovereign guarantee) in Colombia totals US$637.6 million. The Inter-American Investment Corporation (BID Invest) has a portfolio of US$574.8 million and the Multilateral Investment Fund (MIF) has a portfolio of US$62.8 million distributed in technical cooperation, equity and loans.

Colombia: Sovereign Loan Portfolio

	Number of Operations	Current Approved US$ million	Disbursement (Percent)
Infrastructure	11	1096.5	53.9
Integration and Trade	1	12.0	29.0
Climate change and sustainable development	5	570.0	13.6
Institutions for development	9	248.0	21.4
Social	1	46	88.0
TOTAL	**27**	**1,972.5**	**39.5**

[1] Prepared by Inter-American Development Bank. A new country strategy will be ready by end 2018/early 2019.

STATISTICAL ISSUES

(As of March 31, 2018)

I. Assessment of Data Adequacy for Surveillance
General: Data provision is adequate for surveillance.
National Accounts: The National Department of Statistics (DANE) is responsible for the compilation of the national accounts, although the Banco de la República (BdR) compiles the financial accounts. Annual and quarterly estimates of GDP by the production and the expenditure approaches use 2005 as the reference year for the annually chained volume measures. GDP compilation conforms to the methodological recommendations of the System of National Accounts 1993 (1993 SNA) and some recommendations of the 2008 SNA. Work is underway to update the benchmark year for the national accounts to 2014, which will be disseminated, along with the rebased series, by mid-2018. Ongoing STA continues to assist DANE and BdR on improving sectoral accounts and developing quarterly accounts by institutional sectors.
Price Statistics: DANE is also responsible for price statistics, and currently compiles and disseminates the consumer price index (CPI) and the producer price index (PPI). The basket and weights of the CPI have not been updated since 2008 and are based on the Income-Expenditure Survey (2006–07). These CPI weights are out of date and may not reflect current expenditure patterns. Although DANE disseminated an updated PPI in 2015 the weights are based on the structure of economic activity in 2012 and there is a need to expand coverage to include additional economic activities. STA is assisting DANE and BdR to improve residential property price statistics.
Government Finance Statistics: The Ministry of Finance and Public Credit (MFPC) is responsible for the compilation of public revenue, expenditure, and financing data. The Colombian authorities have reaffirmed their commitment to adopt the GFSM 2001 framework, enhance inter-institutional coordination, and increase the resources allocated to compiling government finance statistics. The latest reported data has been published in the Government Finance Statistics Yearbook (GFSY). Next steps include: improving classification of revenue and expense, consolidation, adopting a common list of public sector entities, and disseminating high-frequency data on a national and international level. The General Accounting Office (GAO) developed a single accounting framework for the public sector based on International Public Sector Accounting Standards and maintains a financial management information system containing accounting information of all public sector units. The MFPC's Macroeconomic Policy Unit and the GAO developed a bridge table that converts national accounting classification to the GFSM 2001 framework to compile GFS on accrual and cash bases.

I. Assessment of Data Adequacy for Surveillance (Concluded)	
Monetary and Financial Statistics: The *Banco de la República* (BdR) reports the Standardized Report Forms (SRFs) 1SR for the central bank, 2SR for the other depository corporations (ODCs), and 5SR for monetary aggregates for publication in the IMF's *International Financial Statistics (IFS)* on a monthly basis with a lag of two months. The *Superintendencia Financiera de Colombia* (SFC) compiles data for other financial corporations (OFC) using SRF 4SR. However, the last reported OFC data are for December 2014. This delay in reporting is due to an ongoing review of the SFC and efforts to map the former to the International Financial Reporting Standards (IFRS). The classification of financial instruments and economic sectors follows the *MFSM*.	
Financial Sector Surveillance: Colombia is currently reporting some of the core Financial Soundness Indicators (FSI). Colombia reports all (except one) core and all (except one) encouraged Financial Soundness Indicators (FSI) for deposit takers on a regular monthly basis, for publication on the IMF's website	
External Sector Statistics: The BdR is in charge of compiling and disseminating quarterly balance of payments and international investment position (IIP) statistics, which are produced on a sixth edition of the Balance of Payments and International Investment Position Manual (BPM6) basis. Improved surveys, particularly in the services sector, have enhanced the coverage of balance of payments statistics. Recording of transactions in securities between residents and nonresidents in secondary markets could be improved. The BdR also monthly compiles and disseminates the Data Template on International Reserves and Foreign Currency Liquidity, reports semi-annual data to the Coordinated Portfolio Investment Survey (CPIS), and submits quarterly external debt statistics to the Quarterly External Debt Statistics (QEDS) database. However, Colombia has not reported data to the Coordinated Direct Investment Survey (CDIS) yet.	
II. Data Standards and Quality	
Colombia subscribes to the Special Data Dissemination Standard (SDDS) and metadata are posted on the Fund's Dissemination Standards Bulletin Board (DSBB).	A data ROSC was published in October 2006.

Colombia: Table of Common Indicators Required for Surveillance
(As of March 30, 2018)

	Date of Latest Observation	Date Received	Frequency of Data[1]	Frequency of Reporting[1]	Frequency of Publication[1]	Memo Items: Data Quality – Methodological Soundness[8]	Memo Items: Data Quality – Accuracy and Reliability[9]
Exchange Rates	Mar. 30, 2018	Mar. 30, 2018	D	D	D		
International Reserve Assets and Reserve Liabilities of the Monetary Authorities[2]	Feb. 2018	Mar. 2018	M	M	M		
Reserve/Base Money	Mar. 2017	Mar. 2017	W	W	W	LO, O, LO, LO	O, O, O, O, O
Broad Money	Mar. 2017	Mar. 2017	W	W	W		
Central Bank Balance Sheet	Dec. 2017	Mar. 2018	W	W	W		
Consolidated Balance Sheet of the Banking System	Dec. 2017	Mar. 2018	M	M	M		
Interest Rates[3]	Mar. 30, 2018	Mar. 30, 2018	D	D	D		
Consumer Price Index	Feb. 2018	Mar. 2018	M	M	M		
Revenue, Expenditure, Balance and Financing Composition[4] – General Government (GG)[5]	Q4 2017	Mar. 2018	Q	Q	Q	O, O, LO, O	LO, O, O, O, NO
Revenue, Expenditure, Balance and Financing Composition[4] – Central Government	Dec. 2017	Mar. 2018	M	M	M		
Stocks of Central Government and Central Government-Guaranteed Debt[6]	Dec. 2017	Mar. 2018	M	M	M		
External Current Account	Q4 2017	Mar. 2018	Q	Q	Q	O, LO, LO, LO	O, O, O, O, LO
Exports and Imports of Goods and Services	Q4 2017	Mar. 2018	Q	Q	Q		
GDP/GNP	Q4 2017	Mar. 2018	Q	Q	Q	O, LO, O, O	LO, O, LO, LO,
Gross External Debt	Dec. 2017	Mar. 2018	M	M	M		
International Investment	Q4 2017	Mar. 2018	Q	Q	Q		

[1] Daily (D); Weekly (W); Monthly (M); Bi-monthly (B); Quarterly (Q); Annually (A); Irregular (I); Not Available (NA).
[2] Any reserve assets that are pledged or otherwise encumbered should be specified separately. Also, data should comprise short-term liabilities linked to a foreign currency but settled by other means as well as the notional values of financial derivatives to pay and to receive foreign currency, including those linked to a foreign currency but settled by other means.
[3] Both market-based and officially-determined, including discount rates, money market rates, rates on treasury bills, notes and bonds.
[4] Foreign, domestic bank, and domestic nonbank financing.
[5] The GG consists of the central government (budgetary funds, extra budgetary funds, and social security funds) and state and local governments.
[6] Including currency and maturity composition.
[7] Includes external gross financial asset and liability positions vis-à-vis nonresidents.
[8] Reflects the assessment provided in the data ROSC published in October 2006 for the dataset corresponding to the variable in each row. The assessment indicates whether international standards concerning concepts and definitions, scope, classification/sectorization, and basis for recording are fully observed (O); largely observed (LO); largely not observed (LNO); not observed (NO); and not available (NA).
[9] Same as Footnote 8, except referring to international standards concerning (respectively) source data, assessment of source data, statistical techniques, assessment and validation of intermediate data and statistical outputs, and revision studies.

Statement by Carlos Hurtado, Executive Director for Colombia
and Tomas Gonzalez, Senior Advisor to Executive Director
April 27, 2018

We would like to thank staff for its comprehensive and insightful reports that reflect the extensive and constructive discussions with authorities during the recent mission in Bogota. We broadly agree with the analysis and recommendations presented, but would like to expand on some of the key issues discussed.

Shocks

Colombia is in the final stages of the adjustment process after a series of strong shocks that hit the economy between 2014 and 2016. The first was the rapid decline in oil prices that took place in the second half of 2014—one of the largest adverse external shocks the country has ever had to deal with. The impact on the terms of trade was larger than for most of our peers, leading in less than two years to a fall in exports, foreign direct investment and growth to half of their pre-crisis levels. So was the case with government oil revenue that declined almost to zero.

The shock prompted a significant change in policy. Up to that point the government was focused on a reform agenda to reduce poverty, lower structural unemployment, remove the main barriers to growth and put an end to a five-decade-long civil conflict. The authorities' response was to protect the reform agenda while adjusting to a new reality that entailed significant changes in public spending—including accommodating a loss in revenue of 3pp of GDP—substantial pressure on the financial system to maintain funding for the main infrastructure projects, and dealing with a current account deficit that widened to 6.5 percent of GDP.

Building on the strength of the existing macroeconomic framework and recognizing the permanent component of the shock were the guiding principles behind the response which materialized on three specific pillars: allowing the exchange rate to act as the primary shock absorber; cautious monetary and financial policy to keep inflation under control, maintain sustainable credit growth and limit currency mismatches; and commitment to a medium-term fiscal rule to keep spending and debt at sustainable levels.

These pillars were also critical in facing the two additional supply shocks which hit the economy in 2016. First, a severe drought caused by el Niño weather phenomenon, that led to food shortages and a sharp increase in energy prices given the weight of hydroelectricity in the country's electricity matrix. Second, a strike by truck drivers that disrupted the supply of goods to major urban areas around the country. The combined effects of the two, together with the peso's sharp nominal depreciation (over 80 percent in terms of the price of the US dollar in pesos) prompted by the first shock, sent headline inflation in mid-2016 to three times the target.

Policy response

The response by the Central Bank was a sustained tightening cycle that broke inflation's trend in the second half of 2016 and helped firmly anchor expectations at close to the 3 percent target rate. Data shows this downward trend was sustained as the effects of the currency depreciation and supply shocks subsided, leading to a headline inflation of only 14 basis points above the target in March. Domestic demand also appears to have adjusted and policy reactions—both fiscal and monetary—seem to have been successful in reducing capacity utilization and pressuring prices downwards.

Under a scenario of falling inflation jointly with anchored inflation expectations and a negative output gap, the Bank followed with a cautious cycle of monetary policy easing. Over the past year. the policy rate was cut by 325 basis points to 4.5 percent indicating it will continue making data dependent decisions and closely monitoring expectations, the uncertainty about potential growth and natural interest rates, and the consolidation of the external adjustment.

To that end, authorities intend to continue strengthening their decision-making process and communications to ensure that monetary policy is transparent, well understood and adapted to best practices. In that respect, we would like to thank staff and colleagues for the very productive meetings they helped set between the authorities and the governors of the banks that top the ranking of the Central Bank Transparency Index—including the Czech National Bank, the Bank of England and the Swedish National Bank, the Federal Reserve and the New Zealand's Central Bank—as well as with key staff doing research in these areas.

The Bank has also paid close attention to the effects of monetary policy on financial imbalances and risk-taking, as well as the effects that low real interest rates and the availability of excessive external funding can have in risk taking decisions—affecting the orderly completion of the adjustment process.

The coordination between different institutions involved in financial stability surveillance and regulation should facilitate monitoring and early detection of asset deterioration. The approval of the Conglomerates Law that was presented to Congress at the end of 2017 will strengthen supervisory powers and will facilitate further convergence to Basel III standards. Overall, authorities feel confident about the financial system's resilience and will continue to refine the relevant regulation and supervision.

On the fiscal side, efforts have been centered on consolidation in line with the medium-term fiscal rule. This included passing a comprehensive tax reform that increased the general VAT rate by 3 percentage points and limited exemptions in personal income tax, reduced corporate tax rates and simplified tax procedures for small businesses, introducing also procedures to strengthen the tax administration and penalties to tackle evasion. The reform had negative short-run effects on growth via consumption and slowed the convergence of inflation to target, but they should be outweighed by the positive effects on investment of lower corporate tax rates that are supporting recovery and will positively impact medium-term growth.

Along the same lines, recent developments in the oil markets are having a better-than-expected impact on government revenue. The combined effect of higher prices and strict cost and investment discipline has improved the profitability in Ecopetrol—Colombia's NOC—rising oil revenue and giving the government additional room to meet fiscal-rule targets, which adds to the ongoing efforts to improve the efficiency of tax collection, the profile of public debt amortizations and the quality of public spending.

We recognize the scope for improving the progressivity of Colombia's pension system highlighted in the report, but do think overall public spending makes significant contributions to the social goals of protecting the most vulnerable Colombians and improving income distribution. In fact, free access to basic education, near-universal health insurance coverage, subsidizing public utilities for the poorest, conditional cash-transfer programs and university scholarships for low-income students are all programs that have played a key role in almost halving multidimensional poverty and reducing inequality.

In moving forward, authorities are committed to the structural deficit path in accordance with the fiscal rule. The combination of tax administration gains, expenditure cuts and expected recovery discussed in the previous paragraphs should allow the government to reach these targets. Work with subnational governments will provide significant help by strengthening PFM and improving the overall efficiency and quality of social spending.

Outlook and risks

These policy actions have facilitated a relatively smooth adjustment that now appears to be giving way to recovery. Growth reached 1.8 percent last year and is expected to reach 2.7 percent this year—with leading indicators in line with forecasts—and to continue increasing to 3.5 percent by the end of the decade; inflation is very close to target with expectations firmly anchored below 4 percent; the current account is estimated to fall to the 2-3 percent of GDP deemed sustainable by authorities; the labor market has been resilient and capable of maintaining unemployment at 9 percent levels despite the slowdown; formality rates are now larger than informality rates and the upward trend brought about by education gains and tax reform is being maintained; and investment rates are at pre-crisis levels and FDI has substantially increased thanks to the recovery in oil and mining, but also by historic highs in the other sectors.

The focus now must be on consolidating structural reforms that will raise productivity and potential growth. They will involve, mainly, completing the 4G road-building program and implementing the negotiated peace agreement. The road program is the biggest in the country's history and is a key source for reducing the time and cost of travel among the country's main centers of production, consumption and trade. It has reached preliminary financial closures in a third of the projects and expenditure is set to increase by 40 percent this year.

The peace agreement is probably the most important opportunity to foster inclusive growth and close the regional disparities Colombia has had for decades. Agreed investments will cover more than half of the nation's territory and a third of its towns with much needed infrastructure and social spending. Implementation of the peace agreement is expected to gain momentum throughout 2018 as the programs' institutional capacities are strengthened.

Beyond structural reform, authorities are aware of the need to build policy space as recovery gains pace. Despite a relatively smooth adjustment the economy is still vulnerable. It has received substantial capital inflows, helping adjust to external shocks; however, the large increase in participation of foreign investors in local debt markets poses challenges to stability, especially in the face of ample evidence showing that the depth and composition of international investors can expand the impact of external shocks, and that large institutional investors can react more strongly and persistently to economic shocks.

We cannot afford a disorderly adjustment in any of the major identified global risks—the possibility of a sharp correction in financial markets, the buildup of vulnerabilities if financial conditions remain loose, a choke on growth via an escalation in trade restrictions, or the fact that debt is reaching concerning levels in many advanced economies.

Our main line of defense against a more volatile and uncertain external environment will be maintaining strong fundamentals and a strong institutional policy framework. The authorities remain committed to an inflation targeting framework and flexible exchange rate regime, to public finances firmly anchored in a fiscal rule based on sustainability, and to strong financial regulation and supervision. This macro framework has served the country well. Together with an adequate reserves position and access to the Flexible Credit Line have allowed us to maintain confidence in the economy and to balance adjustment and reform in the face of very large negative shocks.

We will continue to pursue stability and growth, and we believe the respectful and productive relationship we have with the IMF should continue to help us build better polices towards that end.