Índice

01  Global environment
02  Local economic activity
03  Growth projections
04  Inflation and interest rates
05  Macroeconomic balances and the exchange rate
06  Opportunities and challenges
07  Forecast tables
Global activity moderation signals amidst inflation pressures and an aggressive response by central banks.
The persistence of inflation forces central banks to front-load interest rate hikes, contributing to both financial volatility and recession fears

RECENT DEVELOPMENTS IN THE WORLD ECONOMY

GROWTH MODERATION
On inflation, monetary tightening, the UKR war and covid (mostly in China), despite labor markets’ relative strength.

DISRUPTION IN GAS MARKETS
Sharp rise in prices in Europe due to remarkable Russia’s supply cuts.

COMMODITIES (EX-GAS)
Prices are high, but declining on weaker growth prospects.

SUPPLY BOTTLENECKS
Still at high levels, but easing, mainly in the US.

STILL HIGH INFLATION
Inflation continues to surprise upwards, but moderation signs suggest it may soon peak.

FRONT-LOADING OF INTEREST RATES HIKES
Faster and sharper monetary tightening than expected as central banks’ commit to price stability.
Growth is losing momentum as reopening effects fade and inflation, monetary tightening, gas disruptions in Europe and covid in China weigh negatively.

PMI INDICATORS
(MORE THAN 50: EXPANSION; LESS THAN 50: CONTRACTION)

SLOWDOWN AND TECHNICAL RECESSION DESPITE EMPLOYMENT RESILIENCE
DECELERATION, BUT AT A SOFTER THAN EXPECTED PACE
TIMID REBOUND AMID REAL ESTATE TENSIONS AFTER NEW COVID SHOCK

Source: BBVA Research based on data from Haver.
Labor markets exhibit strength despite the ongoing activity deceleration; wages are growing, but at a slower pace than inflation

**LABOR MARKET: VACANCY RATE**
(%, QUARTERLY AVERAGES)

**WAGE GROWTH INDICATORS**
(% YoY, QUARTERLY DATA)

* Vacancies as a proportion of the sum of total employment and the number of vacancies.
Source: BBVA Research based on data from Haver.

Source: BBVA Research based on Atlanta Fed and ECB data
Gas prices have skyrocketed on Russia’s supply cuts, but other commodity prices have eased recently in line with concerns on global moderation.

**COMMODITY PRICES (%)**

- Natural gas prices in Europe jumped 31% in the 3T22 on decreasing supply from Russia.
- Oil, food and metal prices eased from the middle of the year on worse prospects for global demand; supply issues prevented a sharper correction.
- Brent prices declined 23% over the 3T22 despite the announced production cut by the OPEC and the EU embargo on Russia’s oil exports.
- The recent deal to unlock Ukraine grain exports has helped to drive down prices.

Source: BBVA Research based on data from Haver.
Bottlenecks are easing, but remain at very high levels, mainly in Europe

**BBVA RESEARCH BOTTLENECK INDEX**
(INDEX: AVERAGE SINCE 2003 = 0)

**CONTAINER FREIGHT RATES: GLOBAL AND BALTIC**
(INDEX: 2012 = 100)

Source: BBVA Research.

Source: BBVA Research based on data from Haver.
Inflation remains very high and continues to surprise to the upside, but there are increasing signs of moderation.
Price adjustments have become more widespread and also more frequent.

**ITEMS OF THE CPI BASKET WITH ANNUALIZED MONTHLY INFLATION HIGHER THAN 4%**
(share of total 2-digit CPI items)

**ITEMS OF THE CPI BASKET WITH THREE CONSECUTIVE MONTHLY PRICE RISES**
(share of total 2-digit CPI items)

Source: BBVA Research based on local statistics.
The front-loading of interest rate hikes has generated financial volatility; sovereign bond yields moved sharply up and the US dollar strengthened.

- A hawkish Fed has adjusted interest rates, so far, in the year to date by 300bp to 3.25% and has paved the way for extra tightening ahead.
- The ECB has abandoned negative rates; refi rates have reached 1.25% and are set to increase further ahead; a new asset-purchase program (TPI) will help to address fragmentation risks within the region.
- Most currencies have weakened against the dollar, reinforcing inflationary pressures and the risk of financial stress.
- Volatility, sovereign yields and risk premia have increased quickly on prospects of tighter monetary policy, war-related uncertainty and the recent financial stress in the UK.

Source: BBVA Research based on data from Haver.
A further deterioration of macroeconomic prospects: higher inflation, tighter monetary policy and weaker growth than previously expected

BBVA RESEARCH CENTRAL SCENARIO: MAIN ASSUMPTIONS AND IMPACTS

**MONETARY TIGHTENING**
Interest rates remain higher for longer as central banks remain committed to low inflation

**DISRUPTIONS IN GAS MARKETS**
Russia’s supply cuts keep prices close to current levels, but saving measures, flows from alternative sources and inventories prevent large shortages

**COMMODITIES (EX-GAS)**
Prices decline on decelerating global demand, but supply restrictions keep prices relatively high

**SUPPLY BOTTLENECKS**
Bottlenecks continue to ease gradually as the effects of ongoing shocks wane away

**SHARP GROWTH SLOWDOWN**
Global growth is forecast to ease sharply from 6.2% in 2021 to 3.2% (-0.2pp) in 2022 and 2.4% (-0.1pp) in 2023. Mild recessions in the Eurozone, due to gas disruptions, and in the U.S., due to interest rate hikes. Low growth, but no hard-landing in China.

**INFLATION MODERATES SLOWLY**
It remains above targets at least till 2024, but eases from 2023 as current shocks lose steam, monetary tightening reigns on expectations and no significant second-round effects emerge.

**FINANCIAL VOLATILITY**
Strong dollar, high risk premia, capital outflows from EM.
European gas markets: relatively-high reserves, saving measures and flows from alternative sources are likely to prevent significant shortages ahead

**EU GAS: AVERAGE IMPORTS FROM RUSSIA AND FLOWS TO MAKE UP FOR SUPPLY CUTS IN THE NEXT 12 MONTHS (BCM: BILLION CUBIC METERS)**

- Baseline scenario: high gas prices (close to current levels), without gas shortages as flows from other sources, inventories and saving measures are likely to offset supply cuts over 2023-24, at least if imports from Russia remain at current levels and winter temperatures are close to historical averages.
- If Russia further cuts pipeline supply, there would be enough gas for the 2023 winter, but extra rationing would be needed in 2024.
- If Russia cuts liquified natural gas (LNG) provisions, the impact would not be very significant: LNG markets are global and circular, meaning that the EU would end up importing LNG from other producers.

* Assuming imports from Russian remain at the current levels: around 40 BCM (25% of total supply), through pipelines in Türkiye and Ukraine and LNG shipments, but not through Nord Stream and Belarus pipelines. Source: BBVA Research based on data by, Bruegel, EUROSTAT, ENTSOG (European Network of Transmission System Operators for Gas).
Central banks will keep the focus on inflation despite increasing signs of growth weakening: interest rates will remain higher for longer

- The Fed is likely to raise rates to 4.75%, and to keep them at that contractive level till the end of 2023 in order to engineer a slowdown of the economy, and of labor markets in particular, for inflation to converge to 2%.

- The ECB is expected to hike refi rates to 2.75%, well above neutral levels, pressured by high inflation and a more aggressive Fed, and despite the bleak growth prospects.

- Fiscal policy will be more supportive in the EZ than in the US, mostly through NGEU funds and the suspension of fiscal rules until 2023.

- In China, policies are expected to continue exhibiting a moderately expansionary tone.

### MONETARY POLICY INTEREST RATES

<table>
<thead>
<tr>
<th>Year</th>
<th>US</th>
<th>Eurozone</th>
<th>China</th>
</tr>
</thead>
<tbody>
<tr>
<td>2021</td>
<td>-0.25</td>
<td>2.50</td>
<td>3.80</td>
</tr>
<tr>
<td>2022</td>
<td>0.0</td>
<td>2.75</td>
<td>3.60</td>
</tr>
<tr>
<td>2023</td>
<td>4.50</td>
<td>3.60</td>
<td>3.60</td>
</tr>
</tbody>
</table>

* In the case of the Eurozone, interest rates on refinancing operations.

Source: BBVA Research based on Bloomberg data.
Global growth will ease significantly ahead on price pressures, rising interest rates, gas disruptions in Europe and idiosyncratic problems in China

- In the US, growth is revised downwards on (surprising) GDP contractions over 1H22 and higher Fed rates; a recession coupled with a labor market easing is likely by mid-2023.

- In the EZ, positive incoming data supports an upward revision of 2022 growth, but a sharper easing ahead is expected on gas disruptions and higher rates; a recession is likely over the next few quarters.

- Recessions in the US and the EZ are set to be mild given the relative strength in balance sheets of households, firms and banks.

- In China, 2022 growth revised down on the impact of new covid waves and real estate tensions; a recovery is expected in 2023.
Inflation will remain high (more than expected) and well above central bank targets, but is still forecast to trend downwards from 2023 onwards

- Inflation forecasts are revised to the upside, in line with evidence of more widespread and more frequent price adjustments and, in the case of the Eurozone, with prospects of higher gas prices and a weaker Euro.

- Still, recent moderation signs (mainly in the US), reinforce the view that inflation will ease ahead as current shocks lose strength and monetary conditions continue to be tightened.

- While inflation’s convergence to the target will take a relatively long time, expectations are forecast to remain broadly anchored.

- Growth deceleration is expected to reduce the room for relevant wage increases, making significant second-round effects unlikely.

Source: BBVA Research.
Risks: in the current context, a sharper slowdown in global growth and financial turmoil episodes cannot be ruled out

MAIN SHORT-TERM RISKS TO THE WORLD ECONOMY

PERSISTENT INFLATION
Second-round effects, new shocks or policy mismanagement could further spur inflation, requiring higher interest rates

UKRAINE WAR AND GEOPOLITICS
A deterioration of the war and new geopolitical conflicts; significant gas shortages in Europe are among the main risks

HARD-LANDING IN CHINA
“Zero-covid” policy coupled with real estate tensions and other local problems could pave the way for weaker growth in China

SOCIAL TENSIONS AND POPULISM
Macro weakness, political polarization, among other reasons, could trigger social unrest and populist policies

SHARPER GROWTH DECELERATION
Global growth could decelerate faster and more significantly than expected, increasing the odds of a global recession

FINANCIAL TURMOIL
Higher policy rates and risk aversion could trigger financial crises, in particular in debt and EM markets
The factors that have been driving the expansion of the economy are slowing down. During the second half of 2022, the components of domestic demand started to moderate.
The GDP remained strong in the first half of 2022, driven by private consumption and investment in machinery.

Exports have also had an important and swift recovery since the end of 2021. On the contrary, construction investment continues to be lagging and with low growth rates.
With respect to the trend the economy had before the pandemic, the GDP, consumption, investment in machinery and imports are above

GDP TREND(*) AND COMPONENTS
(INDEX, DEC-19 = 100)

(\(^{(\ast)}\): The figure shown in the graphs corresponds to the deviation of Q2 2022 from its pre-COVID trend. The GDP components have been ranked using this figure, displayed from highest to lowest.

Source: BBVA Research based on data by DANE.

Exports are near closing the gap with the previous trend and total investment is lagging due to the construction sector.
The recovery of wage employment has boosted household consumption decisions, but is already showing signs of stabilization.

In addition, the quality of employment improved markedly since the end of 2021, with a partial return in recent data.
Labor formalization led to a significant increase in wages in the economy, as seen in social security contributions.

There were other factors that boosted consumption: regional distribution of resources from high coffee sales (high international price) and growing remittances, as well as high credit growth and a lower household saving rate.
Consumption drivers will slow down in the remainder of 2022 and in 2023. Moderation is already noticeable in household expenditure.

Higher levels of interest rates and rising inflation will lead to a gradual correction in consumption that will help boost household saving rates.
High business confidence boosted spending decisions on machinery and equipment. However, recent data are already showing setbacks.

**BUSINESS CONFIDENCE**
(BALANCE OF RESPONSES, %)

<table>
<thead>
<tr>
<th>Quarter</th>
<th>Industry</th>
<th>Retail and wholesale</th>
</tr>
</thead>
<tbody>
<tr>
<td>1Q21</td>
<td>6.2</td>
<td>-0.8</td>
</tr>
<tr>
<td>2Q21</td>
<td>31.8</td>
<td>17.4</td>
</tr>
<tr>
<td>3Q21</td>
<td>39.9</td>
<td>13.0</td>
</tr>
<tr>
<td>4Q21</td>
<td>41.5</td>
<td>13.9</td>
</tr>
<tr>
<td>1Q22</td>
<td>37.5</td>
<td>12.1</td>
</tr>
<tr>
<td>2Q22</td>
<td>37.2</td>
<td>8.4</td>
</tr>
<tr>
<td>3Q22</td>
<td>28.8</td>
<td>Avg. 15-22 24.4</td>
</tr>
</tbody>
</table>

**INSTALLED CAPACITY UTILIZATION IN INDUSTRY**
(AVERAGE OF RESPONSES, %)

<table>
<thead>
<tr>
<th>Quarter</th>
<th>Industry</th>
<th>Retail and wholesale</th>
</tr>
</thead>
<tbody>
<tr>
<td>1Q21</td>
<td>76</td>
<td>69</td>
</tr>
<tr>
<td>2Q21</td>
<td>76</td>
<td>76</td>
</tr>
<tr>
<td>3Q21</td>
<td>78</td>
<td>78</td>
</tr>
<tr>
<td>4Q21</td>
<td>78</td>
<td>78</td>
</tr>
<tr>
<td>1Q22</td>
<td>78</td>
<td>78</td>
</tr>
<tr>
<td>2Q22</td>
<td>78</td>
<td>78</td>
</tr>
<tr>
<td>3Q22</td>
<td>78</td>
<td>Avg. 15-22(*) 74</td>
</tr>
</tbody>
</table>

(*) Average for third quarters
Source: BBVA Research with Fedesarrollo data.

Despite high installed capacity utilization, which usually leads to upward investment cycles, the industry is already showing lower levels of activity and could reduce machinery spending decisions.
In fact, the industry has been driven not only by domestic demand, but also by external demand. However, that momentum seems to be slowing...

EXEMPLARY GRAPH DATA

EXPORTS IN DOLLARS (*)
(INDEX, DEC-20 = 100)

INDUSTRIAL OUTPUT
(INDEX, DEC-20 = 100; MOBILE ANNUAL CHANGE, %)

(*) Exports of goods are from DANE monthly report. Services exports are from the quarterly balance of payments. (**) Data as of July.
Source: BBVA Research based on data from DANE and Banco de la República.

...in recent results, although at high output levels, industry sales are already starting to grow less, and this is leading to an accumulation of inventories in the sector, which may lead to lower investment.
Investment in residential construction has been less dynamic recently: lower execution of construction works due to high costs and...

NEW HOME SALES
(THOUSANDS OF UNITS PER MONTH AND % OF TOTAL)

NEW HOME PURCHASE CANCELLATIONS
(PER MONTH, 12-MONTH MOVING AVERAGE)

Source: BBVA Research with data from Camacol's Coordenada Urbana.

...lower home sales since the second quarter of 2022. This is coupled with a slight increase in home purchase cancellations.
The probable stronger trade with Venezuela could cushion, at least partially, the expected negative effect of lower global growth on exports

**EX ruler**

**MILLIONS OF DOLLARS AND RATIO 2022 / 2008 IN %**

Some sectors have not yet been reactivated or have done very little in foreign trade with Venezuela: livestock, vegetables, leather, textiles, clothing and vehicles.
Growth projections

The expansionary cycle in Colombia will peak in 2022 and will moderate in 2023 and 2024. Private consumption will slow its dynamics, but from very high levels, and as a result, private investment will also decelerate.
Job creation will decline in the following years, driven by informal employment. Formal employment is expected to fall in 2023.

**URBAN JOB CREATION BY FORMALITY***
(ANNUAL CHANGE FOR THE LAST QUARTER OF THE YEAR, %)

<table>
<thead>
<tr>
<th></th>
<th>2022 (f)</th>
<th>2023 (f)</th>
<th>2024 (f)</th>
</tr>
</thead>
<tbody>
<tr>
<td>Workers</td>
<td>7.6</td>
<td>-2.2</td>
<td></td>
</tr>
<tr>
<td>Formal</td>
<td>9.1</td>
<td>4.0</td>
<td>1.4</td>
</tr>
<tr>
<td>Informal</td>
<td>5.7</td>
<td>1.3</td>
<td>1.6</td>
</tr>
</tbody>
</table>

(*) Formal refers to wage earners and informal to non wage earners.
Source: BBVA Research based on data by DANE.

**URBAN PARTICIPATION AND UNEMPLOYMENT RATES (% AS OF DECEMBER OF EACH YEAR)**

<table>
<thead>
<tr>
<th>Year</th>
<th>Participation rate</th>
<th>Unemployment rate</th>
</tr>
</thead>
<tbody>
<tr>
<td>2021</td>
<td>62.6</td>
<td>11.4</td>
</tr>
<tr>
<td>2022 (f)</td>
<td>65.4</td>
<td>10.8</td>
</tr>
<tr>
<td>2023 (f)</td>
<td>66.0</td>
<td>12.4</td>
</tr>
<tr>
<td>2024 (f)</td>
<td>66.6</td>
<td>12.9</td>
</tr>
</tbody>
</table>

(f): BBVA Research forecasts.

The labor participation rate will gradually recover. With this and lower job creation, we expect an elevated unemployment rate in 2023 and 2024.
Private consumption will slow due to lower labor dynamics and higher interest and inflation rates, but will stabilize at high levels

In addition, the factors that drove consumption in 2022 (credit, coffee and remittances, among others) are expected to be less dynamic going forward. Durable goods consumption will be the factor to experience the greatest decline.
Construction investment will rebound due to civil works in 2023 and non-residential buildings in 2024. Machinery investment will decelerate.

**Fixed Investment and Components**

(Annual % change)

<table>
<thead>
<tr>
<th>Year</th>
<th>Total</th>
<th>Machinery (*)</th>
<th>Construction</th>
</tr>
</thead>
<tbody>
<tr>
<td>2021</td>
<td>2.2</td>
<td>9.2</td>
<td>1.9</td>
</tr>
<tr>
<td>2022</td>
<td>-3.8</td>
<td>17.2</td>
<td>-12.9</td>
</tr>
<tr>
<td>2023</td>
<td>-19.9</td>
<td>5.7</td>
<td>-9.9</td>
</tr>
<tr>
<td>2024</td>
<td>-23.3</td>
<td>3.6</td>
<td>-1.5</td>
</tr>
</tbody>
</table>

(*) Includes intellectual property and biological resources. (f) Forecasts from BBVA Research. Source: BBVA Research based on data by DANE.

**Fixed Investment and Its Composition**

(% of total investment and % of GDP)

<table>
<thead>
<tr>
<th>Year</th>
<th>Machinery (*)</th>
<th>Investment (% of GDP, right)</th>
</tr>
</thead>
<tbody>
<tr>
<td>2019</td>
<td>21.8</td>
<td>41.6</td>
</tr>
<tr>
<td>2020</td>
<td>18.0</td>
<td>47.3</td>
</tr>
<tr>
<td>2021</td>
<td>18.1</td>
<td>49.9</td>
</tr>
<tr>
<td>2022 (f)</td>
<td>18.3</td>
<td>45.3</td>
</tr>
<tr>
<td>2023 (f)</td>
<td>17.5</td>
<td>48.7</td>
</tr>
<tr>
<td>2024 (f)</td>
<td>17.5</td>
<td>49.0</td>
</tr>
</tbody>
</table>

Investment in machinery, although falling in 2023 and growing only slightly in 2024, will remain at high levels as a percentage of GDP. Civil works will be boosted by the high level of construction in the last year by regional and local governments.
Nevertheless, GDP will follow a path of decline from high levels. The subsequent recovery will be gradual.

Lower growth in domestic demand will determine a correction in imports. Exports will also experience slower growth due to the environment in developed countries, but will receive support from Latam neighbors.
Since 2020, growth has been based more on consumption than on investment. Within investment, construction experienced the largest decline...

...in contrast, investment in machinery has performed well. Meanwhile, exports experienced a rapid recovery since the end of 2021 and will remain at high levels thanks to regional trade.
In 2023, the moderation in consumption will lead to low growth in retail and manufacturing...

SECTORS GROWING AT A LOWER RATE THAN GDP IN 2023
- Oil, coal and other mining
- Retail, hotels and restaurants
- Manufacturing industry

SECTORS GROWING AT A SIMILAR RATE AS GDP IN 2023
- Agriculture
- Communications
- Professional services

SECTORS GROWING AT A HIGHER RATE THAN GDP IN 2023
- Construction
- Real estate
- Government, health and education
- Utilities
- Financial services
- Entertainment

Fuente: BBVA Research con datos del DANE.

... meanwhile sectors related to Government expenditure will show higher growth rates due to the push by Government expenditure.
Inflation and interest rates

Inflation has been higher, and more persistent and widespread than expected; however, it will moderate from 2023 onwards. The Central Bank is close to ending its rate hike cycle, and will start a gradual rate reduction at the end of 2023.
Headline inflation reaches over 22-year highs as a result of upward pressures on goods, administered prices and high inflation in food prices

INFLATION OF THE MAIN BASKETS(*)
(ANNUAL CHANGE, %)

MAIN FOOD INFLATION SUB-BASKETS(*)
(ANNUAL CHANGE, %)

This is due to several factors, including global bottlenecks, energy tariff hikes, residual carryover from high international food prices, weather and high demand.

(*) Weight of the basket in parentheses. Source: BBVA Research based on data by DANE.
The price shock has been generalized, reaching 93% of the total basket with annual inflation rates above the target.

Ninety-three percent of food items show monthly increases above the total inflation for the month, with this sub-basket and the goods sub-basket putting upward pressure on the monthly inflation average. On the other hand, services continue to represent a low percentage of their basket, with inflation above the monthly average.
High inflation levels have affected the Colombian population differently, both by region and by income level.

**INFLATION BY MAIN CAPITAL CITIES**
(ANNUAL CHANGE, %)

**INFLATION BY INCOME LEVEL**
(ANNUAL CHANGE, %)

The Caribbean region exhibits the highest levels of inflation, largely associated with the increase in utility rates. Bogotá has the lowest inflation. The most vulnerable population faces the highest inflation due to the high weight of food on their basket.

Source: BBVA Research based on data by DANE.
Fertilizer costs have recently been declining, although this correction has not yet trickled down to food prices.

Food prices react with a delay compared to international prices of agricultural inputs (urea, wheat). Therefore, we expect this inflation to face less pressure as of the last quarter of the year.

Source: BBVA Research based on data by DANE and Haver.
Thus, food inflation will close this year around 23.7% and will slow down significantly in 2023.

Food inflation will ease gradually in 2023 at a slower pace than in previous periods. This is because cost shocks and climate-related effects will dampen the decline in inflation.
Inflation expectations continue to rise and do not seem to have reached their peak; however, two years out, they appear to be less distant from the target.

**Inflation Expectations**

(Annual Change, %)

---

**Expectation Surveys as of September**

(Annual Change, %)

---

Expert surveys, available in September, point to a still wide dispersion of inflation forecasts, however, a significant moderation is expected for 2023.
Inflation will close at 11.8% in 2022, 7.1% in 2023 and 4.5% in 2024. Many uncertainty factors persist in the short and medium term

**INFLATION: TOTAL AND NON-FOOD**
*(ANNUAL CHANGE, %)*

<table>
<thead>
<tr>
<th></th>
<th>2022 (f)</th>
<th>2023 (f)</th>
<th>2024 (f)</th>
</tr>
</thead>
<tbody>
<tr>
<td>Average inflation</td>
<td>9.9</td>
<td>9.1</td>
<td>5.5</td>
</tr>
<tr>
<td>End of period inflation</td>
<td>11.8</td>
<td>7.1</td>
<td>4.5</td>
</tr>
</tbody>
</table>

(f) BBVA Research forecasts. Source: BBVA based on data by DANE.

**FACTORS INCLUDED IN THE FORECAST**

- **Increase in the local price of gasoline:** the aim is to partially close the gap with the international price.
- **Minimum wage increase for 2023:** above inflation for 2022.
- **La Niña weather event until March 2023:** will affect agricultural supply, with an impact on food prices.
- **Global reduction of bottlenecks:** will be gradual in 2023.
- **Peso devaluation:** it will continue to put upward pressure on import prices.
- **More persistent global inflation:** will slow the rate of price reductions.
Banco de la República is nearing the end of its bullish cycle; however, it will have room for some additional increase

**MONETARY POLICY RATE (%)**

Today, the real rate is in positive territory by most metrics (except for total contemporaneous inflation). We expect it to move into contractionary territory (with expected inflation) in this half year and peak in August 2023, just before the start of the bear cycle.

(f): BBVA Research forecasts.
Source: BBVA Research based on data from DANE and Banco de la República.
Macro imbalances and the exchange rate

The economy needs to increase its savings levels to reduce its macroeconomic imbalances. Although smaller than in the past, will continue to be a major challenge in the coming years.
The dynamism of activity in 2022 continues to put upward pressure on the external deficit. Going forward, the slowdown will enable its gradual correction.

Despite the expected reduction in the current account deficit in 2023 and 2024, its level remains high, especially compared to regional peers. Its future reduction to more sustainable levels will remain one of the country's main challenges.

- In the first half of 2022, FDI grew in 8 of the 10 sectors compared to 2021. By the end of the year, the oil, mining and quarrying, and transportation and storage sectors are expected to receive the most FDI. FDI will finance on average 86% of the external deficit between 2022 and 2024.

- From now on, the balance of goods deficit will be the main explanation for the current account deficit. Income from factors will decrease its share in the deficit due to lower profits in sectors with high exposure to foreign companies.

(\textit{f}): BBVA Research forecasts. 
Source: BBVA Research based on data by Banco de la República.
The pandemic left high debt and fiscal deficit, but the positive economic performance in 2021-22 helped to improve the public balance

- The strong economic growth path and high inflation have allowed for improved revenue collection and a reduction in GDP-debt ratio.
- For 2023 and 2024, with a slower economic dynamic, it will be more difficult to attain a significant adjustment in the fiscal balance. However, we consider the lower dynamic could also make the fiscal rule somewhat less strict than that included in the Mid Term Fiscal Plan of 2022.
- The final text of the tax bill has recently been published, with a 1.5% of GDP expected revenue. A significant part of the revenue will come from the corporate sector with a reduction in exemptions and a corporate tax surcharge for several sectors, and from high income households.

CENTRAL NATIONAL GOVERNMENT GROSS BALANCE AND DEBT (% OF GDP)

(f) BBVA Research forecasts.
Source: BBVA Research based on data from the Ministry of Finance.
In 2023 and 2024, expenditure as a percentage of GDP will remain at historically high levels, even when interest expenditure is excluded.

- The 2022 Mid Term Fiscal Plan shows expenditure as a percentage of GDP remaining high by historical standards, with primary expenditure in 2023 higher by 3.2 percentage points of GDP than in 2019 and by 0.6 than in 2022.
- In addition, there is a significant unrealized deficit resulting from the fuel subsidy, which increases the effort required.
- An expenditure review is essential.

**CENTRAL NATIONAL GOVERNMENT TOTAL AND PRIMARY EXPENDITURE (% OF GDP)**

(f) Forecasts of the Ministry of Finance in the Medium-Term Fiscal Framework.
Source: BBVA Research based on data from the Ministry of Finance.
The exchange rate will face various upward pressures: lower global liquidity, domestic deficits and lower GDP growth

- The more aggressive actions and statements from the main central banks increase the pressure to depreciate the exchange rate.
- Uncertainty about the global economy and geopolitics create an appetite for safe havens that pressures the depreciation of the currency.
- An expected closing in the interest rate differential in 2023 and 2024 favors a devaluation trend of the Colombian peso.
- Large fiscal and external deficits pressure on external financing needs and thus put pressure on the exchange rate to depreciate, which adds to other idiosyncratic factors in Colombia.

On average, the exchange rate is expected to devalue by 7.0% in 2023 and 1.8% in 2024.
Challenges and opportunities

Colombia faces considerable challenges in the next years, deepened by a complex international context and significant internal changes: it is important to address not only what is urgent, but what is important as well.
Opportunities and challenges in the Colombian economy

OPORTUNIDADES

Advances in social inclusion enable a more sustainable growth in the medium term.

Energy transition attracts new capitals.

Redistribution of global production chains.

More balanced export basket by product and destination.

RETOS

High macro imbalances, low savings and low productivity, which limit potential growth.

Replace resources from mining and oil activity in the medium term.

Responsiveness to the global slowdown and higher financing costs.

Construction of better public infrastructure and wider provision of public goods.
Forecasts tables
### Main macroeconomic variables

<table>
<thead>
<tr>
<th></th>
<th>2018</th>
<th>2019</th>
<th>2020</th>
<th>2021</th>
<th>2022 (f)</th>
<th>2023 (f)</th>
<th>2024 (f)</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>GDP (% y/y)</strong></td>
<td>2.6</td>
<td>3.2</td>
<td>-7.0</td>
<td>10.7</td>
<td>7.6</td>
<td>0.7</td>
<td>2.0</td>
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<tr>
<td><strong>Private consumption (% y/y)</strong></td>
<td>3.2</td>
<td>4.1</td>
<td>-5.0</td>
<td>14.8</td>
<td>10.7</td>
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<td><strong>Public consumption (% y/y)</strong></td>
<td>7.4</td>
<td>5.3</td>
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<td>5.0</td>
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<td>4.6</td>
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<tr>
<td><strong>Fixed investment (% y/y)</strong></td>
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<td>-23.3</td>
<td>11.2</td>
<td>9.2</td>
<td>-3.8</td>
<td>1.9</td>
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<tr>
<td><strong>Inflation (% y/y. eop)</strong></td>
<td>3.2</td>
<td>3.8</td>
<td>1.6</td>
<td>5.6</td>
<td>11.8</td>
<td>7.1</td>
<td>4.5</td>
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<tr>
<td><strong>Inflation (% y/y. avg)</strong></td>
<td>3.2</td>
<td>3.5</td>
<td>2.5</td>
<td>3.5</td>
<td>9.9</td>
<td>9.1</td>
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<tr>
<td><strong>Exchange rate (eop)</strong></td>
<td>3,212.5</td>
<td>3,277.0</td>
<td>3,469.0</td>
<td>3,968.0</td>
<td>4,395.0</td>
<td>4,520.0</td>
<td>4,550.0</td>
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<tr>
<td><strong>Depreciation (%. eop)</strong></td>
<td>7.4</td>
<td>2.0</td>
<td>5.9</td>
<td>14.4</td>
<td>10.8</td>
<td>2.8</td>
<td>0.7</td>
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<tr>
<td><strong>Exchange rate (avg)</strong></td>
<td>2,956.4</td>
<td>3,272.6</td>
<td>3,693.3</td>
<td>3,744.3</td>
<td>4,151.8</td>
<td>4,440.4</td>
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<tr>
<td><strong>Depreciation (%. avg)</strong></td>
<td>0.2</td>
<td>10.7</td>
<td>12.9</td>
<td>1.4</td>
<td>10.9</td>
<td>7.0</td>
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<td><strong>Policy interest rate (%. eop)</strong></td>
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<td>4.25</td>
<td>1.75</td>
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<td>11.00</td>
<td>9.50</td>
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<tr>
<td><strong>Current Account (% GDP)</strong></td>
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<tr>
<td><strong>Urban Unemployment rate (%. eop)</strong></td>
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<td>11.0</td>
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<td>10.8</td>
<td>12.4</td>
<td>12.9</td>
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</table>

(f): Forecasts by BBVA Research. (*) The unemployment rate series is the new spliced series that DANE made public on September 30, 2022.

Source: BBVA Research with DANE and Banco de la República data.
Main macroeconomic variables

<table>
<thead>
<tr>
<th>Quarter</th>
<th>GDP (% y/y)</th>
<th>Inflation (% y/y, eop)</th>
<th>Exchange rate (vs. USD, eop)</th>
<th>Interest policy rate (%)</th>
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<tr>
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<td>Q4 24</td>
<td>3.5</td>
<td>4.5</td>
<td>4,550</td>
<td>6.00</td>
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</tbody>
</table>

Fuente: BBVA Research con datos de DANE y Banco de la República.
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Colombia economic outlook

October 2022