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The economic slowdown goes beyond the earthquake

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Key Messages

- **GDP grew 0.5% YoY in the third quarter of 2026**, decelerating sharply from the revised 3.6% in the second quarter and **contracting 0.8% QoQ** in the seasonally adjusted series. Although August recorded a 0.6% YoY decline—deepened by the negative impact of the earthquake—the cooling had been brewing beforehand: the Economic Tracking Indicator (ISE) had already slowed to 0.2% YoY in July (revised down from 1.1%) and showed only a tepid recovery to 1.4% in September in its original series. As a result, year-to-date (YTD) growth stood at 2.1%.

- **Final consumption lost traction due to the rapid pullback in public spending and the weakening of non-durable private demand**.General government consumption suffered a significant quarterly contraction (-2.6% QoQ, with YoY growth of 4.2% compared to 10.1% YTD) as election-related spending expired, the effect of retroactive public sector wage payments faded, and the new administration's freeze on multiple expenditure items and hiring materialized. In household consumption (+1.7% YoY and +0.1% QoQ), only durable goods remained firm (+12.4% YoY), while semi-durables (-1.7%), services (+0.6%), and non-durables (+1.8%) lost momentum under the weight of the high policy rate and the progressive (albeit resilient) cooling of the labor market.

- **Fixed investment lost steam in machinery and equipment, while the external imbalance continues to leak domestic demand abroad**.Gross fixed capital formation grew 2.1% YoY (-1.0% QoQ), sustained by civil works, whereas housing extended its year-on-year declines and investment in machinery and equipment decelerated markedly (+0.7% YoY). Meanwhile, exports remained depressed (-1.8% YoY), in contrast to imports that maintained outstanding momentum (+9.8% YoY and +3.7% QoQ), channeling a large share of domestic demand toward foreign production.

- **The outcome introduces a downward bias to growth in 2026 and possibly 2027.** The reversal of the fiscal impulse was swift and substantial, while private demand lacks the intensity and speed required to offset that pullback, constrained by still-restrictive interest rates and a heterogeneous sectoral supply.

Beyond the August earthquake: a widespread loss of traction

The 0.5% YoY growth in the third quarter confirms a sharper-than-anticipated downturn following the dynamism of the first half of the year (2.1% in the first quarter and 3.6% in the second). In quarter-on-quarter terms, the economy went from expanding 1.2% in the second quarter to contracting 0.8% in the third.

While the August earthquake exacerbated the downturn in activity that month—driving the ISE to a 0.6% YoY drop in its original series and a 2.7% MoM contraction in its seasonally adjusted series—the monthly breakdown shows that the economic slowdown preceded this event. Indeed, DANE's data revisions lowered July's YoY growth from a preliminary 1.1% to barely 0.2%.

Likewise, once the immediate impact of August had passed, September's rebound proved insufficient to regain the pace of the first half of the year, reaching 1.4% YoY growth in the original series. The moderation, therefore, responds to macroeconomic determinants that are more structural than transitory.

Pullback in public consumption and duality in household spending

Final consumption expenditure moderated to 2.1% YoY and fell 0.3% QoQ. Within this aggregate, although public consumption grew 4.2% in year-on-year terms, it suffered a 2.6% contraction on a quarter-on-quarter basis. Three factors explain this reversal in government spending: the expiration of disbursements associated with the electoral periods, accounting normalization following the retroactive payment of public sector wages in the second quarter, and the new administration's decision to freeze multiple spending items and new hiring.

Meanwhile, household consumption grew 1.7% YoY and barely edged up 0.1% compared to the second quarter. Breaking down the figures by durability and purpose reveals a stark divergence driven by the interaction between the exchange rate and interest rates:

- **Resilience in durable goods:** this segment grew 12.4% YoY and 2.1% QoQ, with the automotive sector acting as a major driver, accompanied by furniture and household appliances, as well as recreation and culture. Because these goods are highly import-intensive, currency appreciation has lowered their costs in local currency, effectively offsetting the higher cost of credit.
- **Weakness across the rest of the basket:** semi-durable goods fell 1.7% YoY and 2.4% QoQ—reflected in the contraction of clothing and footwear. Services grew 0.6% YoY and edged down 0.3% QoQ, dragged down by restaurants and hotels, communications, and education—sectors experiencing nominal revenue increases but facing cost pressures that prevent real growth. Non-durable goods posted a modest 1.8% YoY gain (+0.4% QoQ), with food and non-alcoholic beverages stagnating (+0.1% YoY). **Across all these segments of predominantly local production or low import intensity, there is no cost**

relief from currency appreciation, meaning the burden of higher financing costs directly depresses spending decisions.

Investment and foreign trade: positive civil works and leakage into imports

Fixed investment, which advanced 2.1% YoY and fell 1.0% QoQ, displayed clear asymmetries. The "other buildings and structures" category grew 10.3% YoY, consolidating civil works as the sole firm engine of construction investment. In contrast, housing investment remained in contractionary territory with a 2.2% YoY decline, while the machinery and equipment component suffered a notable deceleration, growing barely 0.7% YoY—far from the double-digit dynamism of previous quarters and the 8.5% accumulated YTD. Finally, other fixed assets remained in negative territory, both in cultivated biological resources (-2.5% YoY) and intellectual property products (-2.6% YoY).

On the external front, the trade imbalance continued to subtract significantly from economic growth. Exports remained depressed with a 1.8% YoY drop (subtracting 0.3 percentage points from GDP), explained by a 3.2% decline in goods exports that overshadowed the 13.6% growth in services exports.

Meanwhile, imports exhibited outstanding momentum, expanding 9.8% YoY (subtracting 2.0 percentage points from GDP) and 3.7% QoQ, with gains of 9.7% in goods purchases and 10.1% in services. **This confirms that a substantial portion of domestic demand (+2.6% YoY) continues to leak into foreign production**.

Sectoral balance: contraction in agriculture and manufacturing versus support from mining and energy

In the third quarter, eight of the twelve major economic sectors contracted on the margin, fracturing the productive landscape into three contrasting dynamics: the partial exhaustion of the services that had led the recent expansion, a divergence within goods-producing sectors between branches exposed to foreign competition and extractive enclaves, and a sharp disconnect between commercial links and the rest of their value chain.

The most decisive trend reversal came from the sectors that had underpinned activity during the first half of the year. Public administration, education, and health went from growing 10.1% YoY in the second quarter to barely 1.6% in the third (with a 0.6% QoQ drop), feeling the full brunt of the contraction in non-market education (-2.8% YoY following a 24.6% surge a year earlier) and the 1.1% QoQ pullback in public administration itself. This fiscal drag was compounded by the cooling of other services intensive in local demand and financing: financial and insurance activities fell 0.8% YoY and 1.9% QoQ—dragged down by an 8.3% slump in insurance, which

wiped out the 3.0% gain in financial intermediation—while information and communications deepened its negative streak (-2.9% YoY and -2.0% QoQ) and professional and administrative services retreated 1.0% compared to the previous quarter. Within the tertiary sector, only entertainment (+5.2% YoY, driven by a 7.3% boom in gambling and recreation despite a 6.4% drop in domestic employment) and steady real estate activities (+1.9% YoY) managed to sustain positive contributions, though insufficient to offset the weaker pulse of the public sector.

At the same time, the pressures observed on the expenditure side—currency appreciation, a high monetary policy rate, and strong import penetration—were directly reflected in tradable sectors and construction. Manufacturing (-1.2% YoY and -0.5% QoQ) and agriculture (-6.7% YoY and -2.3% QoQ, single-handedly subtracting 0.8 percentage points from gross value added) were the main drags on supply.

In manufacturing, the branches most sensitive to competition from imported goods and weak semi-durable consumption suffered the heaviest toll, notably the slump in textiles and apparel (-13.4% YoY), wood and paper (-6.2%), and oil refining and chemicals (-1.1%), which outweighed the strong performance of basic metals (+12.3%) and beverage and tobacco production (+7.7%).

In agriculture, the downturn was widespread across crops (-6.9% YoY, with severe contractions in legumes, rice, citrus fruits, and sugarcane), coffee (-11.2%), and fishing (-35.4%), leaving livestock (+1.6%, supported by pork and poultry farming) and specific export crops such as oil palm, flowers, and cocoa as the sole exceptions.

This same duality was replicated in construction (+0.6% YoY and -0.5% QoQ): while the execution of roads, railways, and civil engineering works maintained a solid pace (+9.6% YoY), building construction contracted 4.3% YoY, weighed down by a 7.5% drop in the residential segment amid persistent weakness in housing.

Paradoxically, commerce and mining prevented a year-on-year contraction in GDP. Within the trade, transport, and accommodation group (+0.7% YoY and -0.6% QoQ), wholesale and retail trade grew 3.9% YoY (+0.5% QoQ), buoyed by sales of imported vehicles and durable goods; however, that momentum failed to spill over into related activities: accommodation and food services fell 4.4% YoY and transport contracted 1.7% (hurt by both land and air transport as well as a 39.7% plunge in water transport).

Meanwhile, mining and quarrying (+7.8% YoY and +1.9% QoQ) and electricity, gas, and water supply (+3.9% YoY, led by a 6.0% advance in electric power) spearheaded sectoral growth, yet the mining rebound was concentrated in the surge of metallic minerals (+38.3%, driven by high gold and platinum prices and volumes) and a statistical recovery in coal (+9.2% YoY, despite a 2.1% QoQ drop), whereas crude oil (-2.6%) and natural gas (-12.5%) extraction prolonged their structural decline.

Thus, aggregate supply was left relying on extractive enclaves, specific infrastructure projects, and retail margins on imported goods—a narrow productive base that adds further evidence to the fragility of growth heading into year-end.

Outlook: downward bias for 2026 and 2027

The third quarter's negative surprise makes it clear that the Colombian economy experienced a much deeper and earlier loss of momentum than anticipated, far from being attributable solely to the disruptions caused by the August earthquake. With cumulative growth of 2.1% between January and September and a 0.8% QoQ contraction, the inertia with which economic activity enters the final stretch of the year is weaker than initially envisaged.

This backdrop introduces a downward bias to our GDP growth forecast for 2026 (currently at 2.6%) and, possibly, for 2027 (currently at 2.3%). The pullback in public spending—following the end of the electoral cycle, the fading of extraordinary wage payments, and the government's directive to freeze hiring and expenditures—materialized with unusual speed. At the same time, private demand shows no signs of being able to accelerate with either the intensity or the speed required to offset that fiscal void: the relief from currency appreciation remains encapsulated in imported durable goods, while the bulk of consumption in services, non-durables, housing, and domestically produced machinery posted a subdued performance that could extend for a few more quarters amid high interest rates and substantial leakage into imports.

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