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Economic Watch

Colombia

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Economic Analysis

Colombia

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Colombia: new export markets, but for the same products

Increased diversification of export destinations, but focused on a few commodities

- **Colombia has diversified its export markets**

  Following a dramatic reduction in exports to Venezuela -from 25% of non-mining exports in 2008 to 8% in 2011, as a result of diplomatic restrictions and foreign currency shortages- Colombia has managed to diversify its export markets since 2007. It has increased its trade with neighboring countries such as Peru, Brazil and Chile, which have substantial potential to expand.

- **However, exports are now more focused on a few commodities with low technological contents**

  The value of exports other than coal, ferronickel, oil and coffee (Colombia's traditional exports) was similar in 2008 to 2011. However, in 2011 the composition of exports favored the mining sector (products such as gold and emeralds), with the share of the industrial sector having fallen. This is due to reduced trade with Venezuela, which had been intensive in industrial products, many of which had high added value.

- **Unlike Colombia, Peru and Chile have increased industrial exports at the same time as increasing exports of commodities**

  Furthermore, between 2008 and 2011 the increase in Colombia's exports was based on higher prices for commodities, rather than an increase in volumes traded.

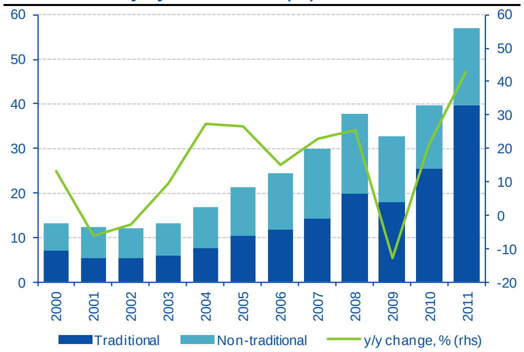
- **The challenge for the country is now to find market niches with new trading partners for products other than commodities.**

  This is particularly important in trade with Europe, Asia and NAFTA countries, where Colombia's sales have increasingly concentrated on fuels, accounting for over 70% of the total. However, other South American countries, except Chile and Argentina, are focusing on selling products not related to mining or energy.

Exports driven by mining and energy sector products

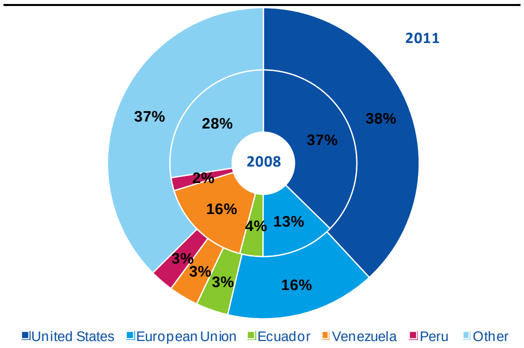
Total exports increased by 43% yoy in 2011, the fastest growth in the last 25 years. These record levels are directly related to the boom in the mining and energy sectors, which accounted for 71% of the total and increased at 62% yoy, due to a combination of higher international prices and an increase -though relatively smaller- in local production (Chart 1). If we also include products such as gold, emeralds and other minerals, 80% of the country's exports are actually commodities.

Chart 1
Total exports
USD bn and yoy variations (%)



Source: DANE and BBVA Research

Chart 2
Export destinations, 2008 and 2011
Percent



Source: DANE, DIAN and BBVA Research

Non-traditional exports (i.e. other than oil, coffee, coal and ferronickel) were at a similar level to the peak of 2008, but they were exported to different destinations (Chart 1). The Venezuelan market has contracted sharply; an increased share of some manufactured products is going to the United States; and Colombia is taking advantage of expanding neighboring markets. There has also been a moderate upturn in food sales to Venezuela, boosted by a policy of internal supply in that country.

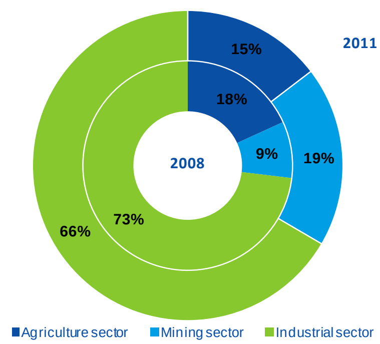
The sector composition of non-traditional exports has also changed since 2008 (Chart 3). Industry continues to lead the country's exports, but its share fell by over 7 percentage points. Four years ago this sector accounted for 73% of the total, and included exports of high technology items such as machinery, vehicles and other commodities, due to demand from Venezuela: in 2011 this had fallen to 66%. Meanwhile, the share of mining sector sales (mainly gold and emeralds) increased from 9% to 19%.

Industrial exports to Venezuela still not substituted

In 2008, non-traditional exports to Venezuela accounted for 25% of the total, with a value of over USD 6 billion, the highest figure in history. The main products exported with livestock (16% of the total), clothing (12%), chemicals (8.5%), leather (8%), textiles (7.8%), paper (5.5%), food (5.3%) and vehicles (5.1%). The majority of exports were therefore medium-high technology. However, Venezuela then broke off diplomatic relations with Colombia, restricting sales of vehicles and livestock; it also imposed very low market shares for other products, due to currency shortages. As a result, Venezuela now accounts for only 8% of Colombia's non-traditional sales.

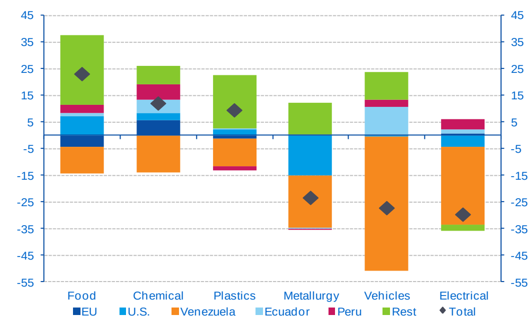
In 2011, only three of the 15 sectors other than fuel and precious metals managed to exceed the export levels of 2008: food, chemicals and plastics (Chart 4). There has been a noteworthy atomization of export destinations in recent years, with strong participation by new trading partners in South America and Europe. There have been reductions in exports of other industrial products, as these have not managed to replace reductions in the Venezuelan market; this resulted in exports from the sector being 11% lower in 2011 than in 2008. However, 2011 was the first year of increased industrial sales, following consecutive falls in 2009 and 2010.

Chart 3
Composition of non-traditional exports 2008 and 2011
As a percentage



Source: DANE, DIAN and BBVA Research

Chart 4
Sector growth 2008-2001
Contribution to change, %



Source: DANE and BBVA Research

Exports concentrated in just a few products

Herfindahl index conclusions

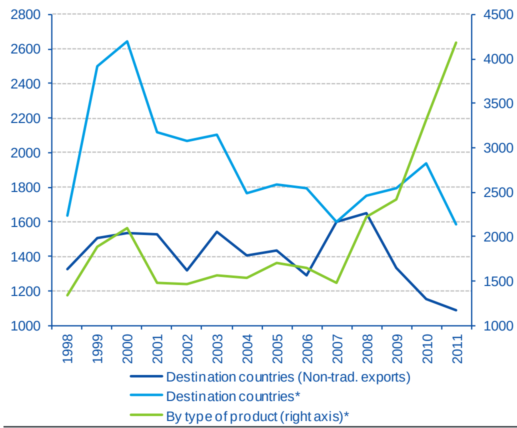
A Herfindahl index constructed to evaluate the level of concentration of exports among destination countries and types of goods concludes there has been greater diversification of the destinations of exports after 2008, but shows how they have concentrated strongly on a few products since that date. A country-by-country analysis reveals that Colombia has accessed new export markets since the international crisis of 2008-2009. These have mainly been for non-traditional exports (including gold and emeralds); this reduced the Herfindahl index by over 30% by 2011, to a level interpreted as a lack of concentration (Chart 5). However, by product type, the index increased by over 180% in this period to a level that signifies a high concentration.

Chart 6 shows these differences in trade by product type. Between 2000 and 2007 basic industry and high technology products led export growth. This created favorable conditions for expansion of the business base with medium-low capital levels (according to a 2009 BASC report), although these were highly concentrated in a few export markets (Venezuela and Ecuador). However, from 2008 to 2011 only sales of primary goods increased, increasing their share of total trade. The high-technology industry was the poorest performer, falling by almost 5% in this period.

Colombia's industrial export growth was slower than that of Chile and Peru

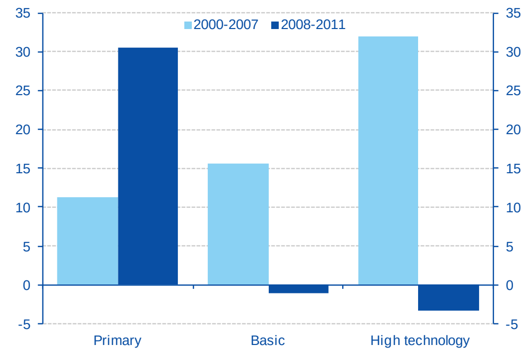
Colombia's performance was noticeably different to that of the countries in the region that are most open to international trade. Over recent years, Peru and Chile have been gradually decreasing their exposure to exports of primary goods through increased foreign sales of industrial products, which is more than offsetting the performance of mining products (Charts 7 and 8). Colombia has only partially diversified its exports, as it is only exporting a few products but to more countries. This reduces the risk of exposure to domestic turmoil in its trading partners, but leaves it more exposed to global shocks to its terms of trade.

Chart 5
Herfindahl index of market concentration
Index from 0 (no concentration) to 10,000 (concentrated)



Source: DANE, DIAN and BBVA Research

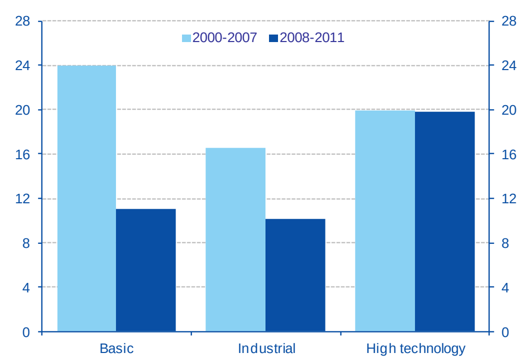
Chart 6
Colombia: export growth by type of goods
Average change in the period indicated, %



Source: DANE, DIAN and BBVA Research

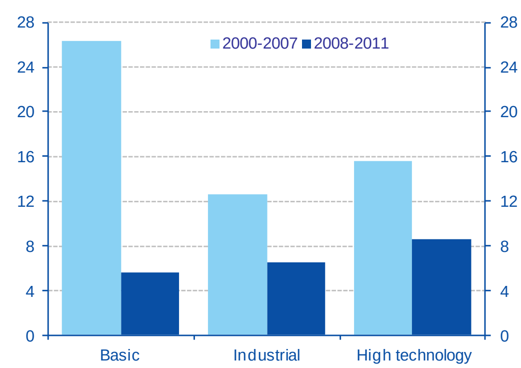
The main difference between the performance of Peru and Chile and that of Colombia is the greater determination of the former to sign free-trade agreements, resulting in greater diversification of markets and products. Chile, for example, has the largest number of free trade agreements in the world. These agreements are with economic areas representing over 62% of global GDP (NAFTA, European Union, EFTA, South Korea, China, etc.). As a result, it has a wider range of destinations for its industrial exports: European Union (17% of the total), USA (12%), Mercosur (12%), CAN (12%), Japan (6%) and China (6%). 50% of Colombia's manufacturing exports meanwhile are to just four countries (the USA, Ecuador, Venezuela and Peru); the European Union accounts for just 7% and Asia less than 2%.

Chart 7
Peru: export growth by type of goods
Average change in the period indicated, %



Source: DANE, DIAN and BBVA Research

Chart 8
Chile: export growth by type of goods
Average change in the period indicated, %

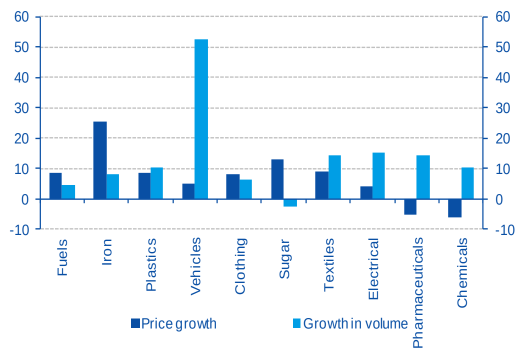


Source: DANE, DIAN and BBVA Research

Exports increase in value, but not in volume

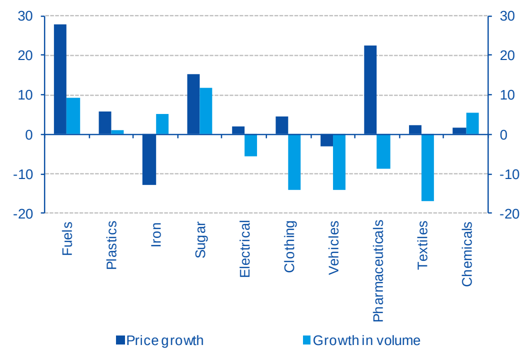
The increase in Colombia's exports over recent years is explained more by positive price changes than by increased volumes (Charts 9 and 10). Comparing changes in some tariff headings over two periods (2000-2007 and 2008-2011), we find that between 2000 and 2007, improved terms of trade performance was accompanied, in most cases, by equal or higher growth in export volumes. However, between 2008 and 2011 only a few sub-sectors saw increased volumes, and even these increases were lower than the price increases. The expansion in exports is therefore based on the terms of trade rather than on internal productivity.

Chart 9
Export growth* 2000-2007
Average change in the period, %



Source: DANE, DIAN and BBVA Research *Ordered by value

Chart 10
Export growth* 2008-2011
Average change in the period, %



Source: DANE, DIAN and BBVA Research *Ordered by value

The challenge for Colombia is to take advantage of the better performance of emerging economies

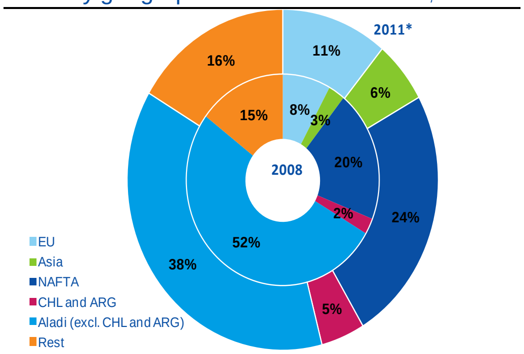
Agricultural industry exports with a high share of the regional market

The balance of global growth is swinging in favor of emerging economies in Asia and Latin America. This is a challenge for Colombia as it needs to direct its efforts to guaranteeing increased access to these expanding markets. Part of its recent trade strategy has focused on this objective. Its free trade and economic complementation agreements with Chile, Mexico (recently revised and expanded), MERCOSUR, Korea and Turkey (being negotiated over the last two years) recognize the growth potential of less developed countries. However, progress in these markets has been very slow and not very diversified (Chart 11), leaving the United States and the European Union as the main substitute for reduced exports to ALADI (as a result of lower sales to Venezuela).

South America is the main destination for Colombia's agricultural industry exports. Over 80% of exports to neighboring countries are products other than fuel, coffee and mining products. However, this indicator for new expanding markets (such as Chile, Argentina and Peru) remains below 30%, showing that there is still room for additional economic complementarity with these countries.

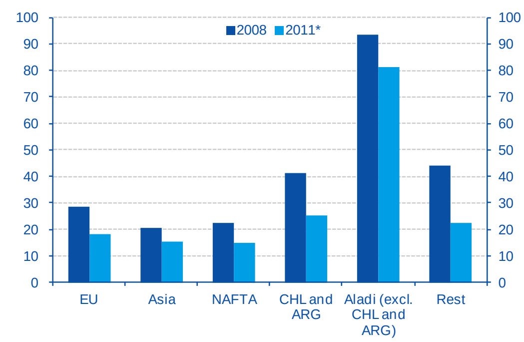
In this regard, Colombia does not seem to be exploiting what should be its natural markets in the region (because of their geographic location, cultural affinity and shared growth). Trade with neighboring countries appears to be underrepresented compared to the predictions of gravitational models. These models conclude in favor of deepening inter-industrial and intra-industrial trade among Latin American countries, although the results are conditional on improvements in multi-mode transport infrastructure. Expansion of the regional market for Colombia is more important as only 12% of its exports to other countries, such as the European Union, Asia and NAFTA, are agricultural (Chart 12).

Chart 11
Industrial and agricultural exports by destination
Share by geographic area 2008 and 2011, %



* Data to November. Source: DANE, DIAN and BBVA Research

Chart 12
The importance of industrial and agricultural exports by destination
Percentage of total exports, %



Source: DANE, DIAN and BBVA Research

Conclusions

Colombian exports have grown rapidly in recent years, boosted by a combination of more external markets and significant increases in the sales of raw materials such as oil and coal, but without significant progress in products with a greater technological input. At the same time, this result was largely dependent on higher international prices, with incipient progress in terms of export volumes. This has increased the country's exposure to the terms of trade shocks that have historically affected economy stability in Colombia and Latin America. Furthermore, concentration of exports in just a few commodities makes the country vulnerable to sharp changes in global demand and supply, which result in rapid price changes.

Even so, the measures taken by Colombia in foreign trade, through free-trade agreements concluded in the past and being negotiated now, are steps in the right direction. They aim to take advantage of those regions with high current demand (such as the United States and Europe), but also to take advantage of countries in a strong expansion phase (such as Chile, Peru, Mexico and Turkey). The challenge for the coming years is to accompany increased diversification of export markets through access of more sectors to these new destinations, thus ensuring the sustainability of long-term export growth and limiting dependency on the terms of trade and the exchange rate.

DISCLAIMER