

# **From Old to New Economic Crisis. What Have We Learned? The Case of Colombia**

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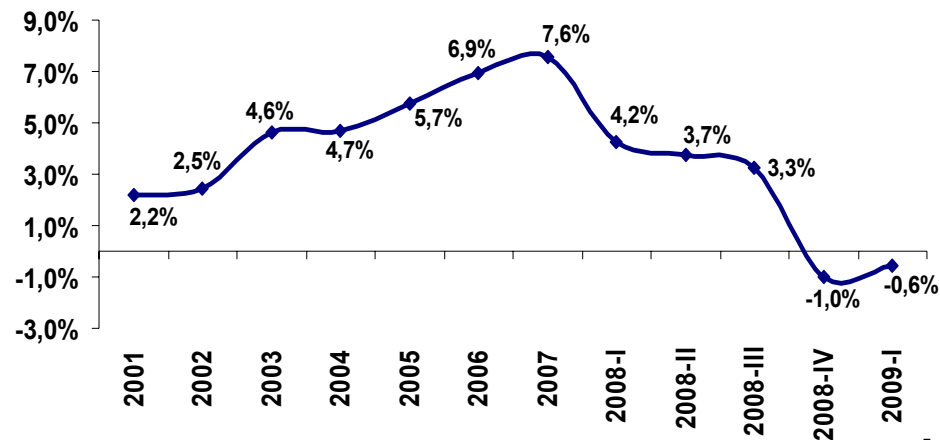
Head of the Economics Studies Department  
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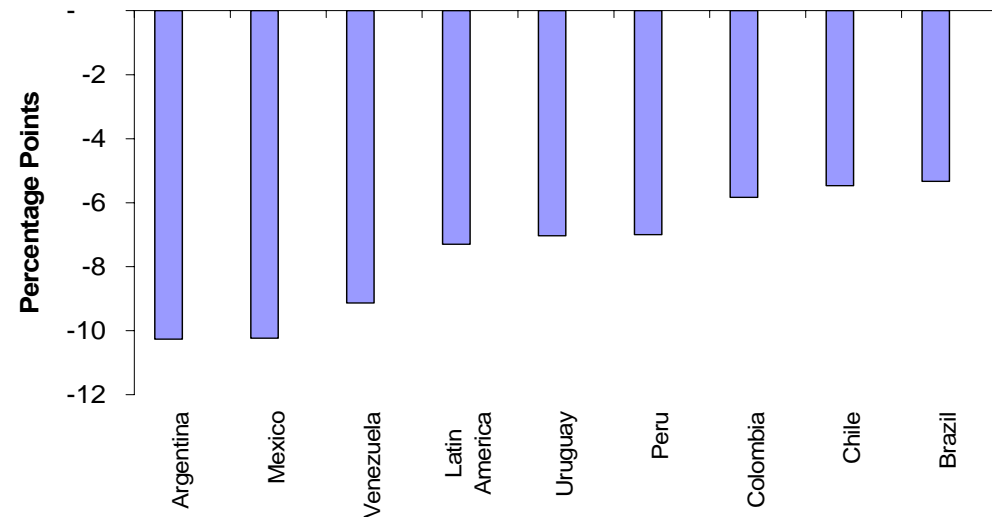
- **The financial world wide turmoil spared the Colombian financial system:**
  - **Financial stability indicators are sound**
  - **No signs of credit crunch**
  - **No signs of liquidity restrictions**
  - **Confidence on the institutions remains solid**

# Besides, economic slowdown has been mild, at least compared with other economies in the region

Colombia - Real GDP  
Annual Growth (%)



Difference Between 2009 GDP Forecast and the  
Average GDP Growth in 2006-08



Source: Banco de la República de Colombia

2009 GDP Forecasts: FocusEconomics

# What are the reasons behind the resilience of the Colombian economy, compared to events elsewhere?

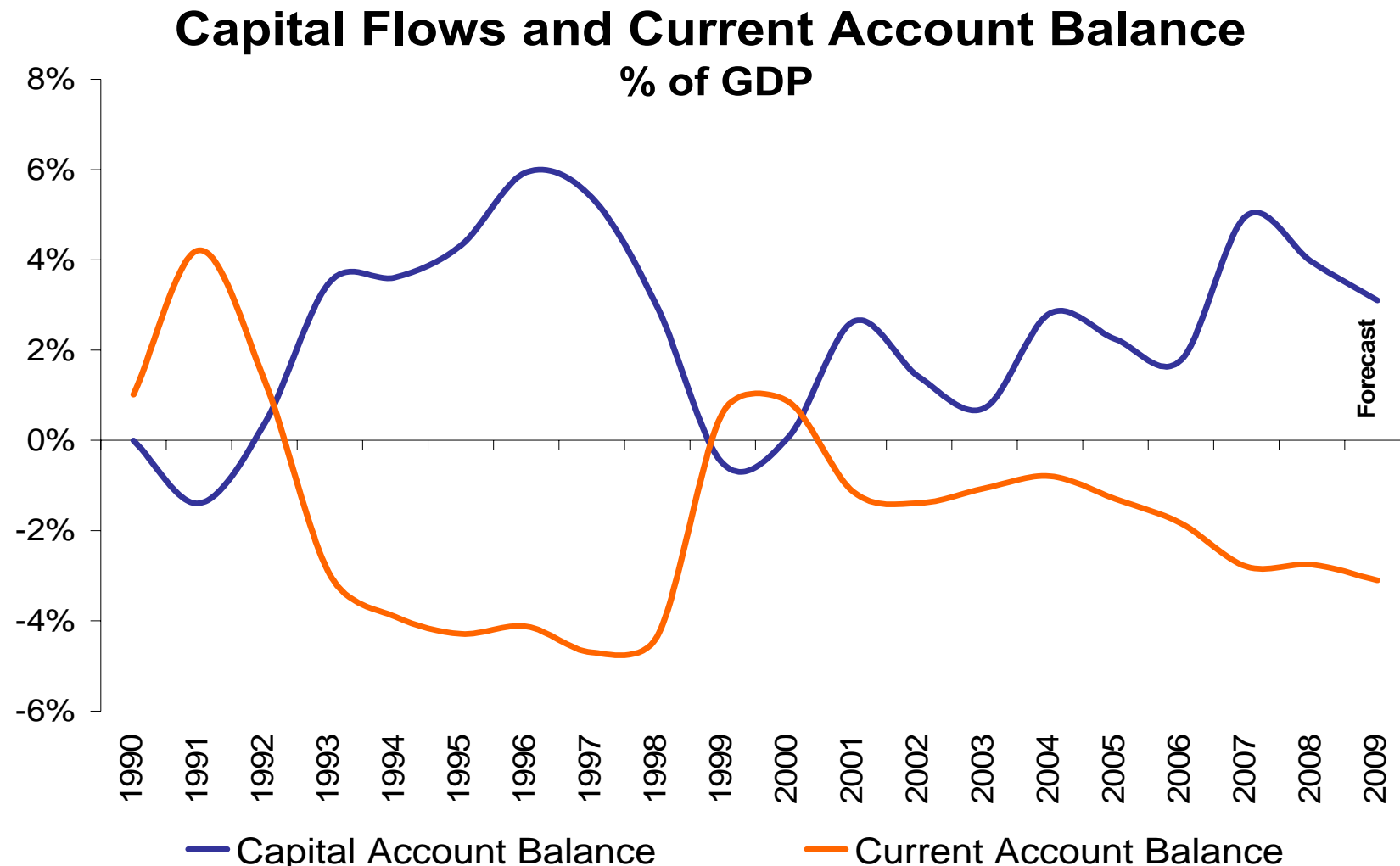
- ***Exogenous factors:*** stronger macroeconomic fundamentals in the Latin American region
- ***Endogenous factors:***
  - The lessons of the financial crisis of the 90s
  - The macro-prudential policies that followed

## **The Financial Crisis of the 90s**

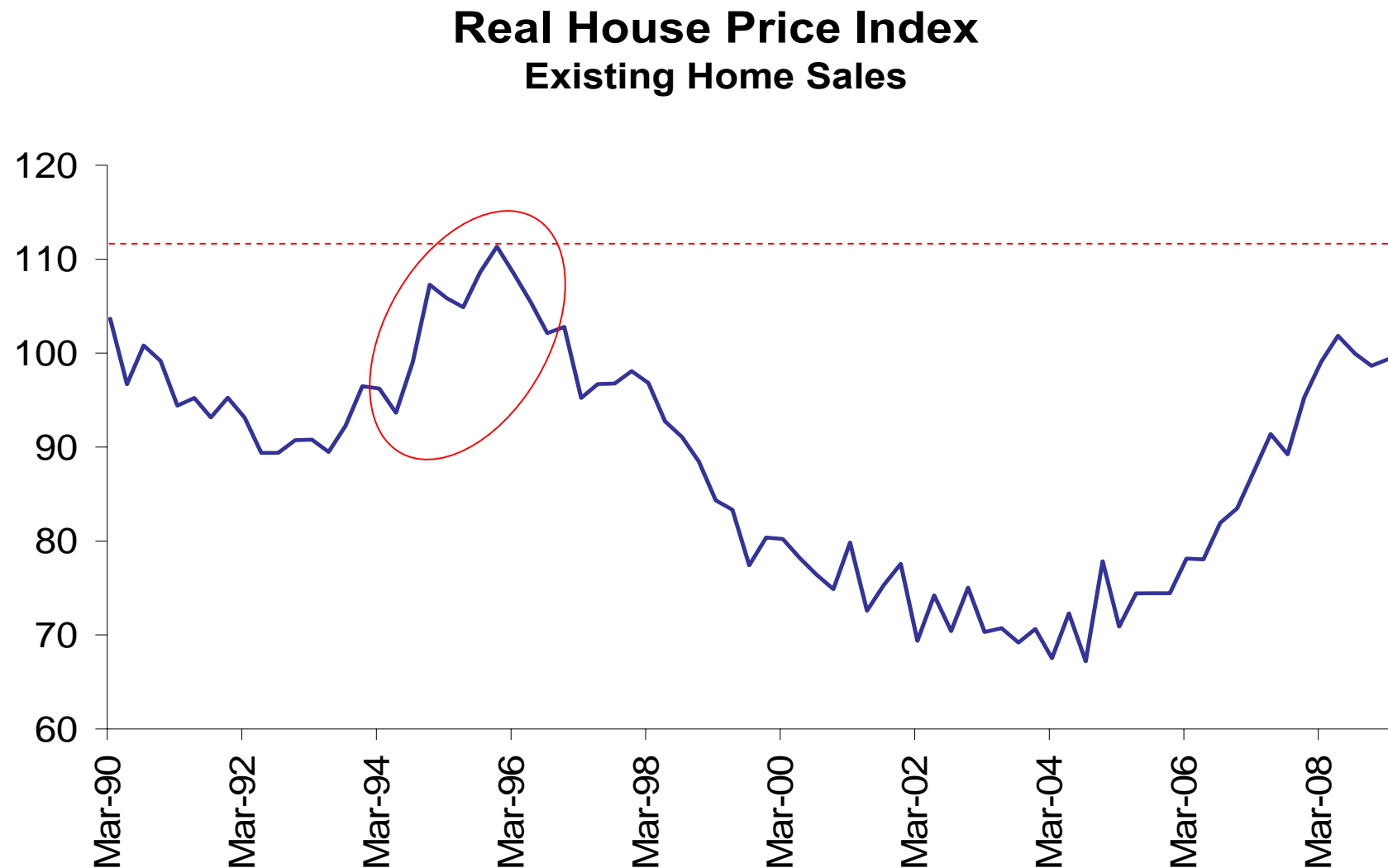
- **What happened in the 90s?**
  - **Large capital inflows to emerging markets**
  - **Persistent current account deficit under a fixed exchange rate regime (target zone)**
  - **Bubble in housing prices and a credit boom**
  - **Large fiscal deficit**
  - **Large external debt (public and private)**

**Sudden stop**  **A costly financial crisis**

**A sudden stop of capital inflows in 1999 imposed a harsh adjustment on domestic private expenditure, that abruptly closed the external deficit**

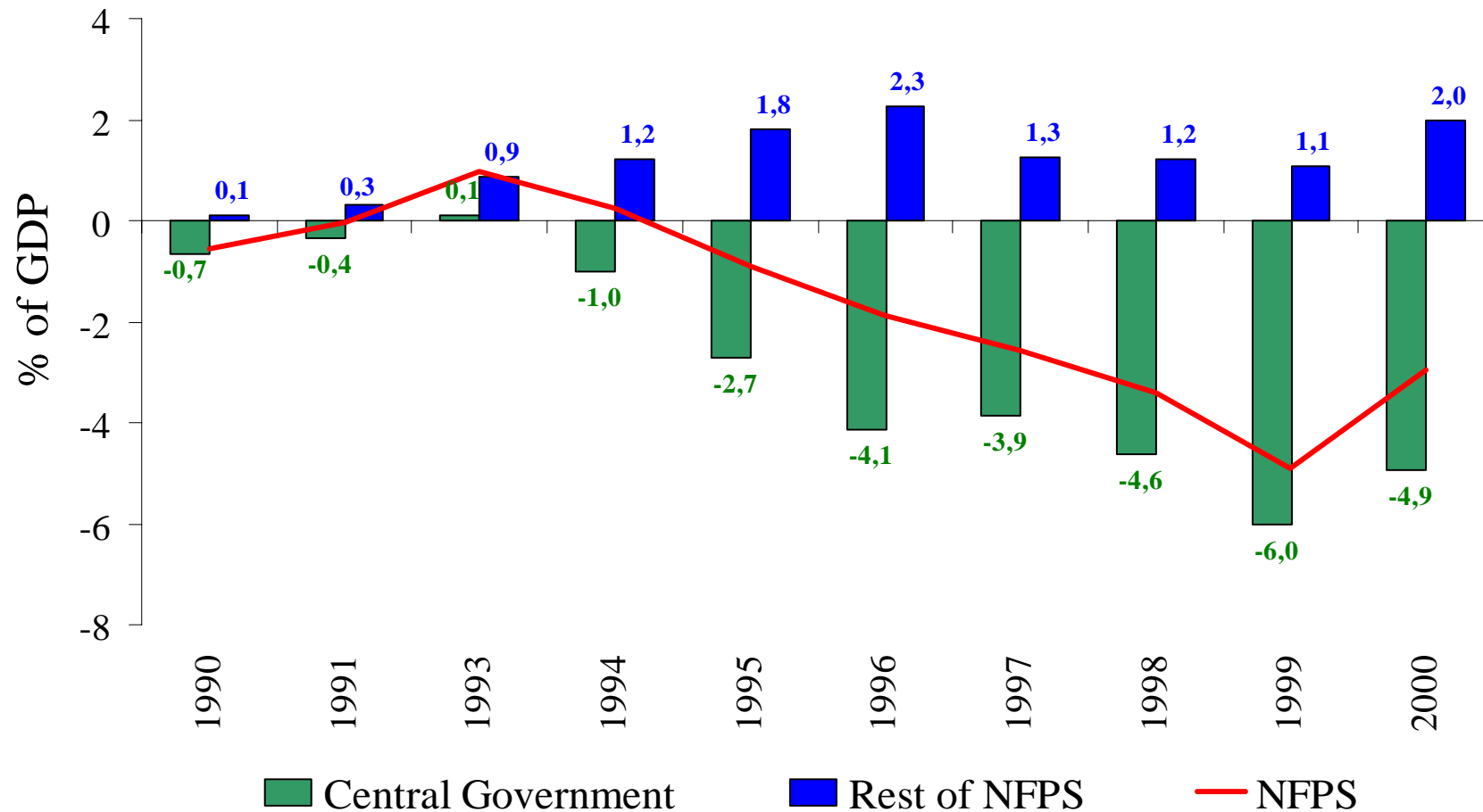


**After attaining a peak, real state prices plummeted during the crisis.**



# Central Government deficit achieved in 1999 an historical record

## Public Sector Fiscal Balance 1990-2000



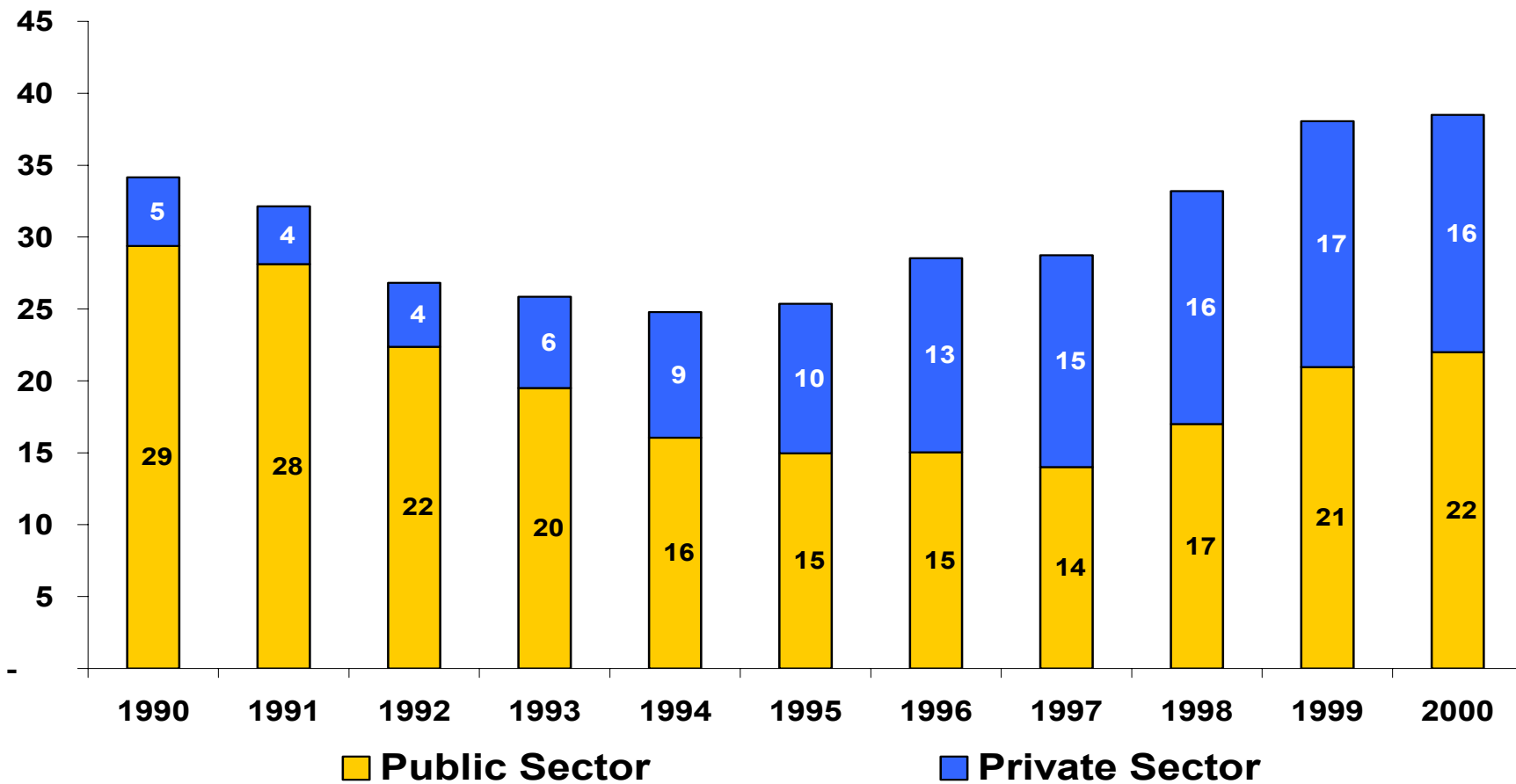
NFPS: Nonfinancial Public Sector; Rest of NFPS: Decentralized Sector

Source: Banco de la República de Colombia



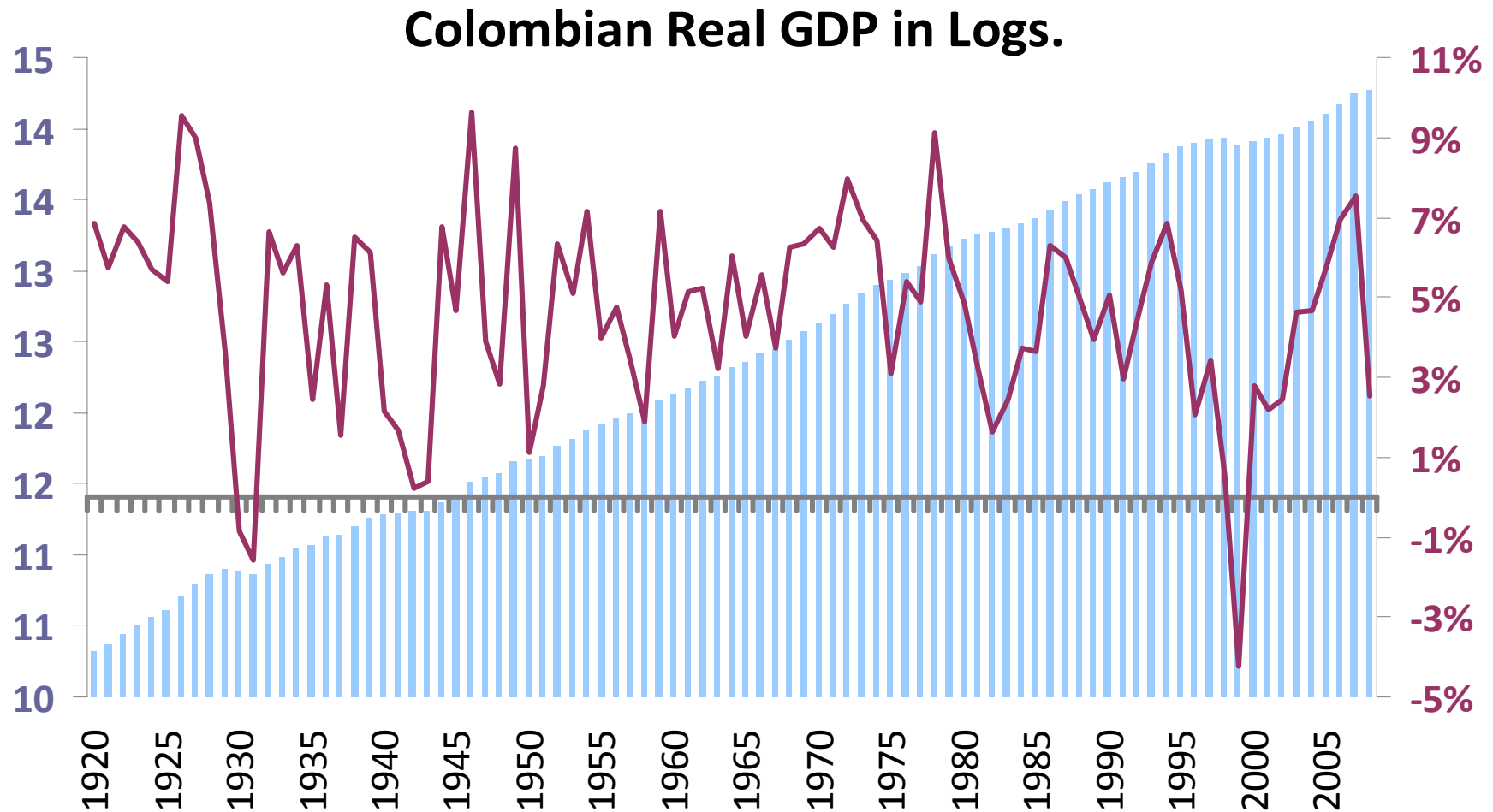
As well as external debt...

## External Debt (% GDP)



Source: Banco de la República de Colombia

**In these conditions, Colombia faced in 1999 the worst economic crisis in half a century. GDP shrank - 4.2% and unemployment got to 20%**



Source: Banco de la República de Colombia; DANE

LogGDP Annual growth

# The Lessons of the Financial Crisis of the 90s

- Households, firms, banks and policymakers learned from the crisis:
  - **Households:** consumers became more cautious about high levels of debt
  - **Firms and banks:**
    - avoiding currency mismatches
    - improving credit standards
    - slowing the adoption of financial innovation

# **The lessons of the financial crisis of the 90s**

## **Policy Makers:**

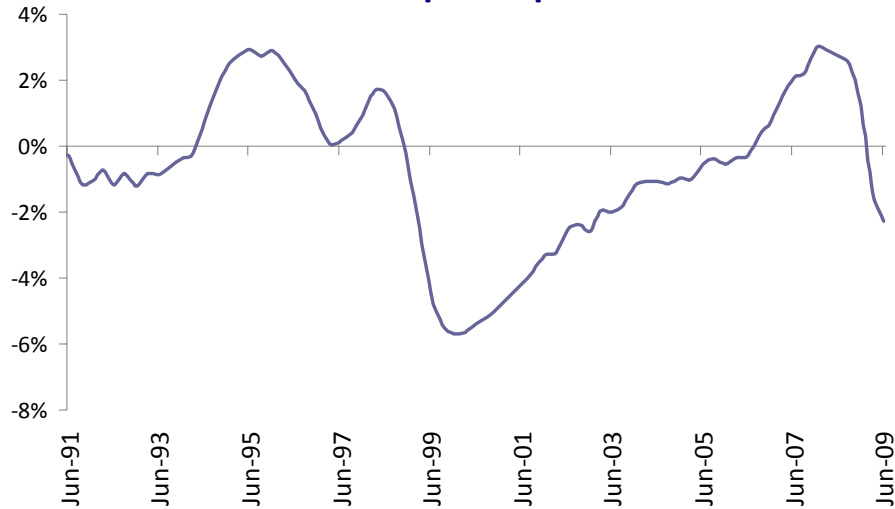
- Staying alert of possible asset price bubbles and credit booms**
- Paying attention to currency and term mismatches between assets and liabilities in the financial system**
- Rising loan-loss provisions and capital requirements**
- The importance of floating**
- The need for a fiscal adjustment and reduction of external debt**

## Macro-prudential policies

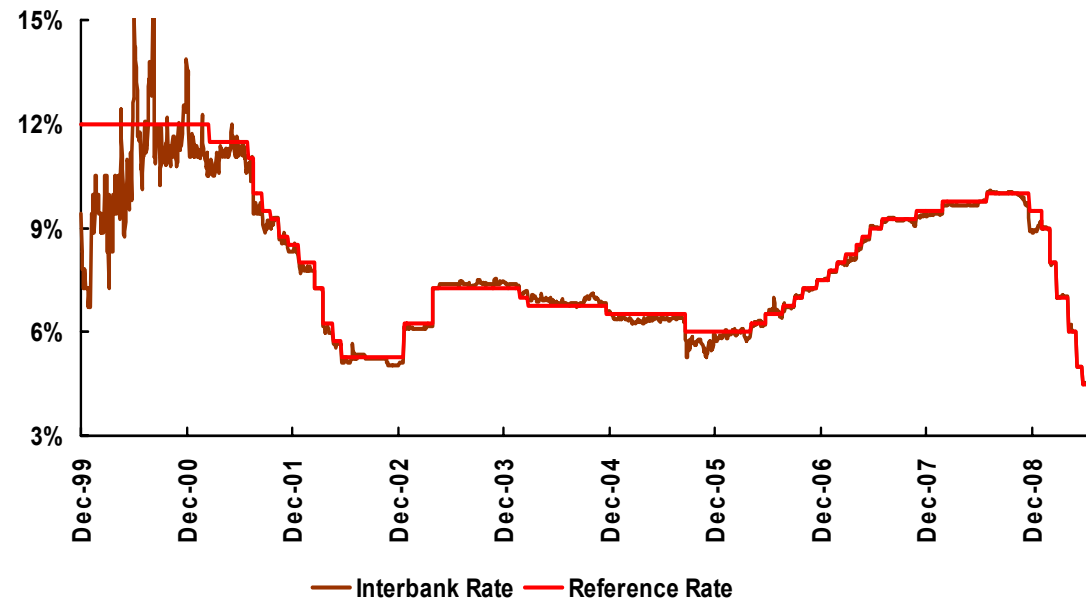
- The lessons of the 90s were materialized in a sequence of policy decisions that contributed to financial stability in the context of an inflation targeting scheme.
- The policies:
  - 1. Countercyclical Monetary Policy: Low levels of the central bank intervention rate for encouraging recovery after 2000, and consecutive increases during the recent expansion period (from 6% in April 2006 to 10% in July 2008).

# 1. Countercyclical Monetary Policy

Output Gap

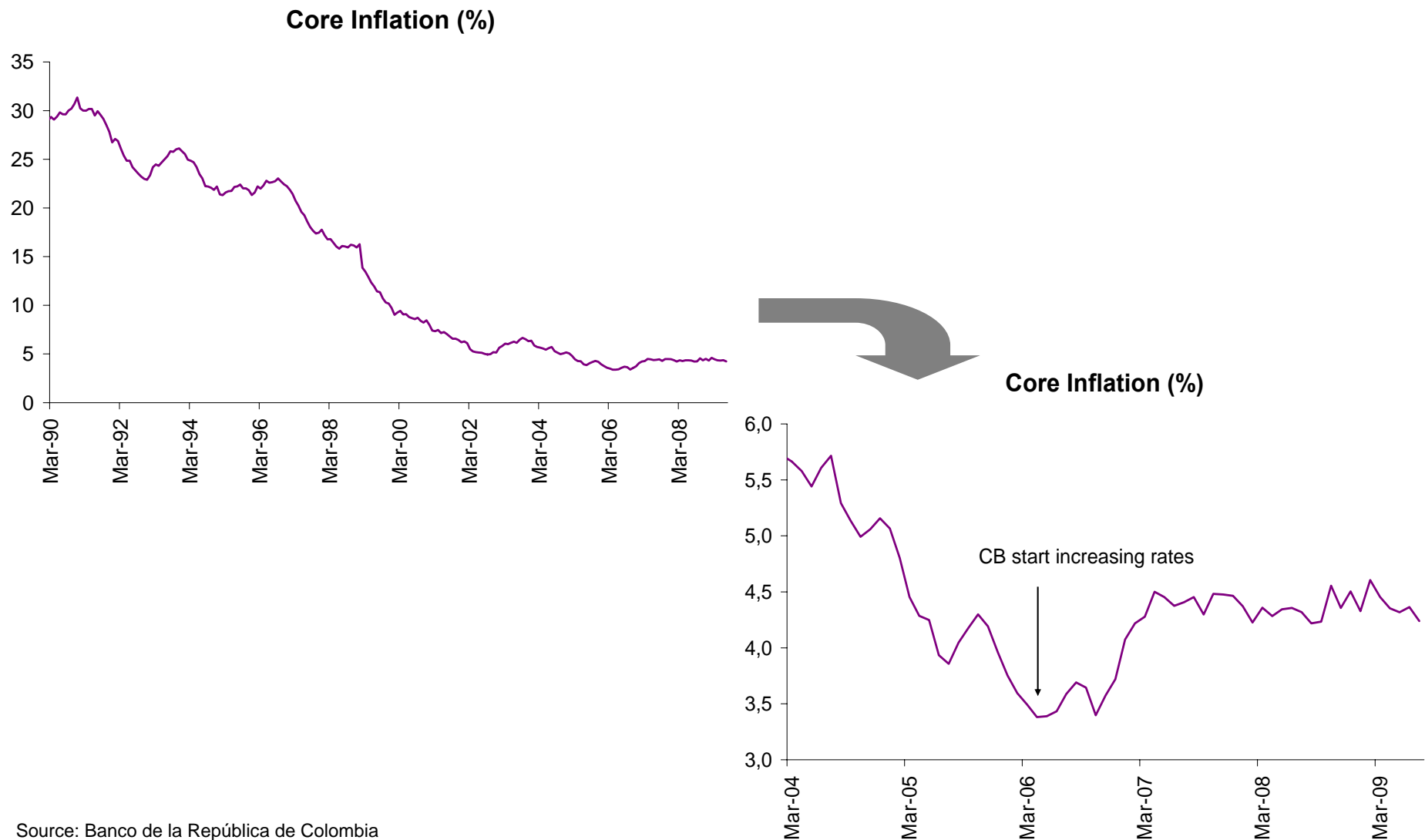


Short Term Interest Rates



Source: Banco de la República de Colombia

# Monetary stimulus did not sacrifice progress towards a lower inflation rate



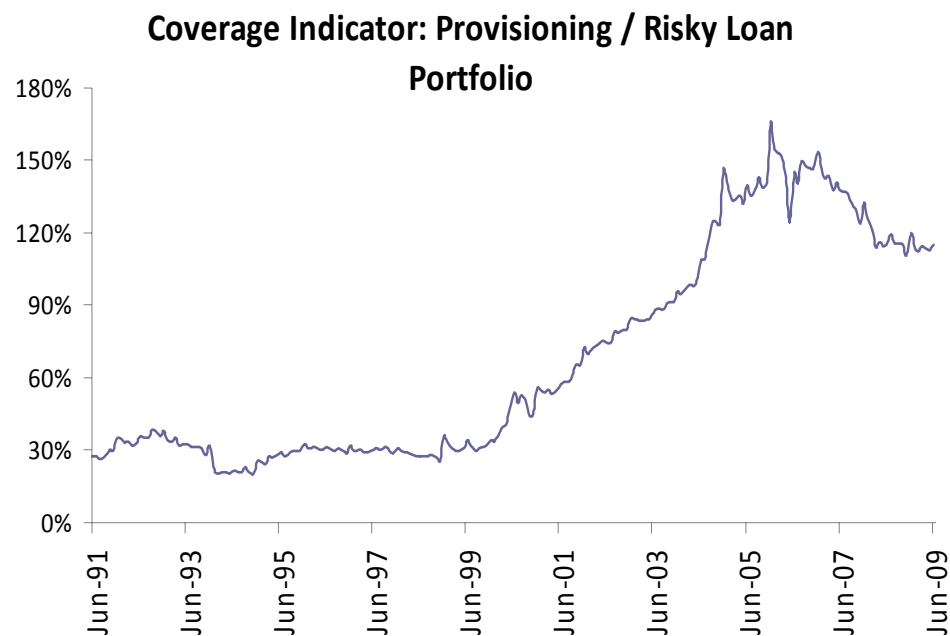
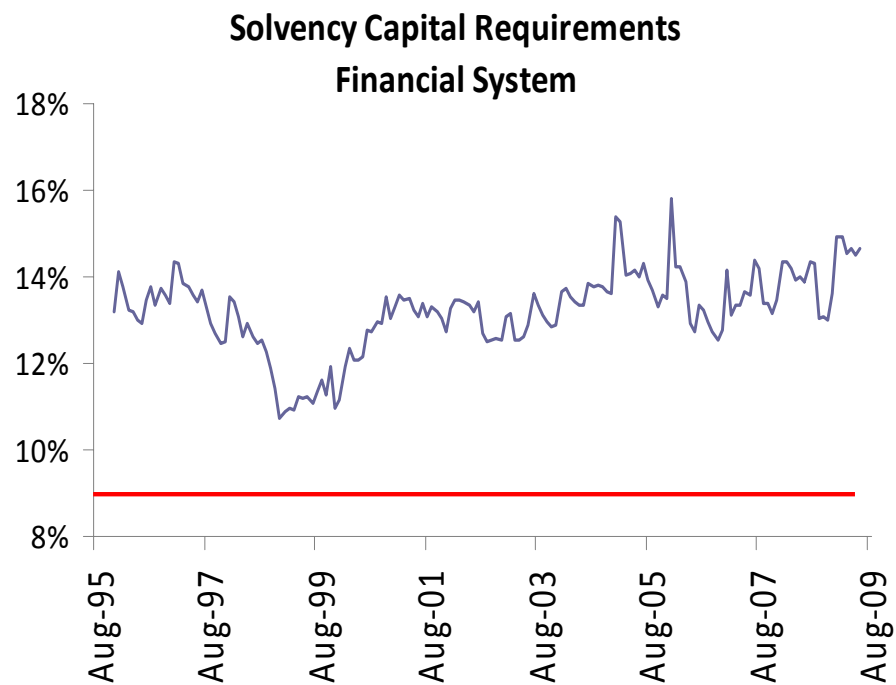
## **2. Financial Macro-prudential Policies**

**Preventing credit booms and strengthening financial sector indicators:**

- **Transitory Increase of compulsory reserve ratios to tame credit growth (May 2007 to Sept 2008)**
- **Capital Controls: Deposit requirements on external debt and portfolio investment (May 2007 to Sept 2008)**
- **Increases in loan-loss provisioning requirements**
- **Strong regulation on currency and term mismatches in the financial system**



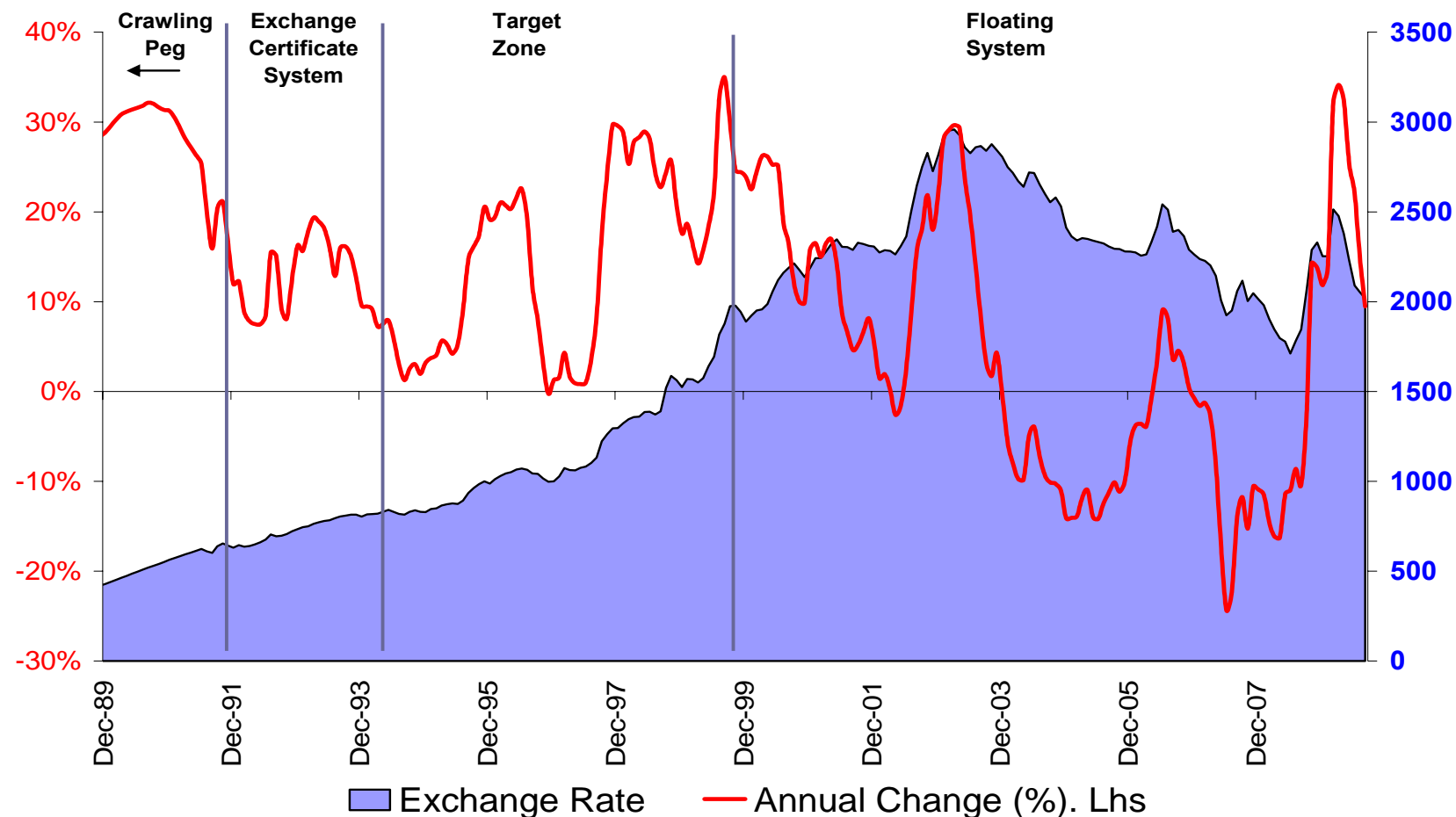
# Solvency and provisions were raised to safer levels



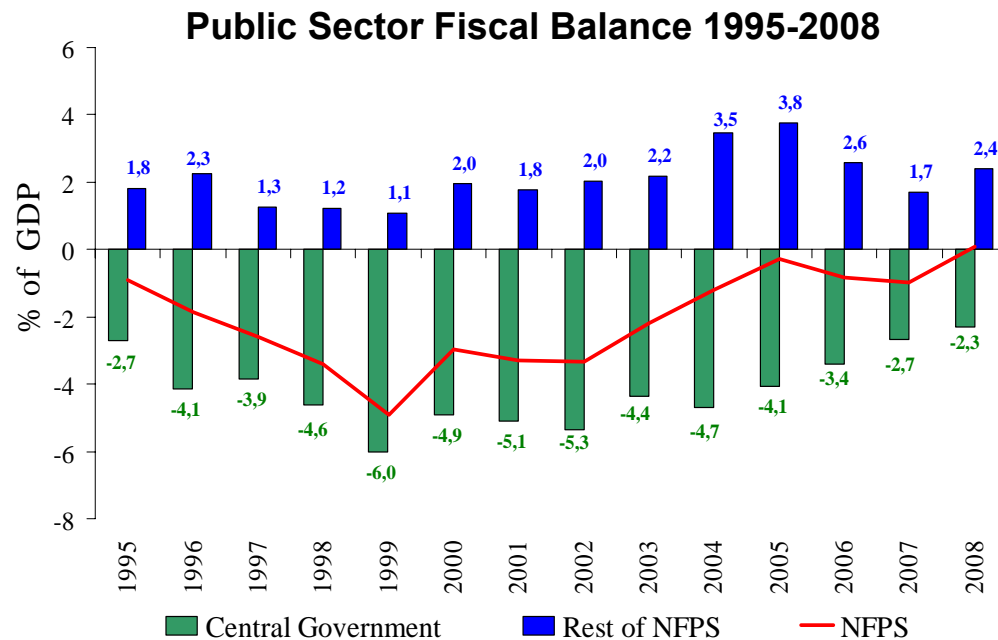
### 3. Floating: Since 1999 the exchange rate was let to float, despite periods of sharp appreciation

#### Colombia - Exchange Rate

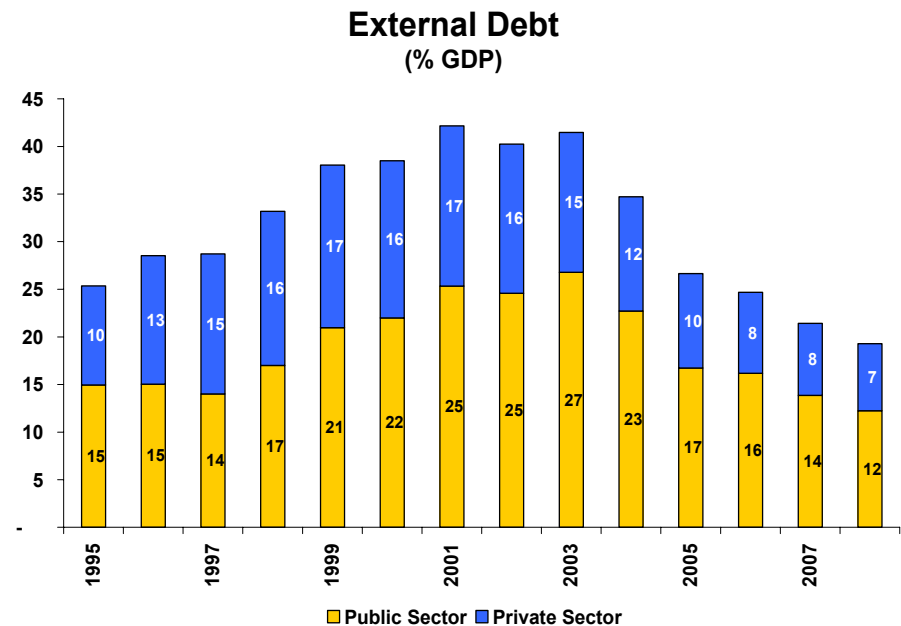
Colombian Peso (COP) vs. US\$



## 4. Fiscal consolidation: reduction of both fiscal deficit and external debt



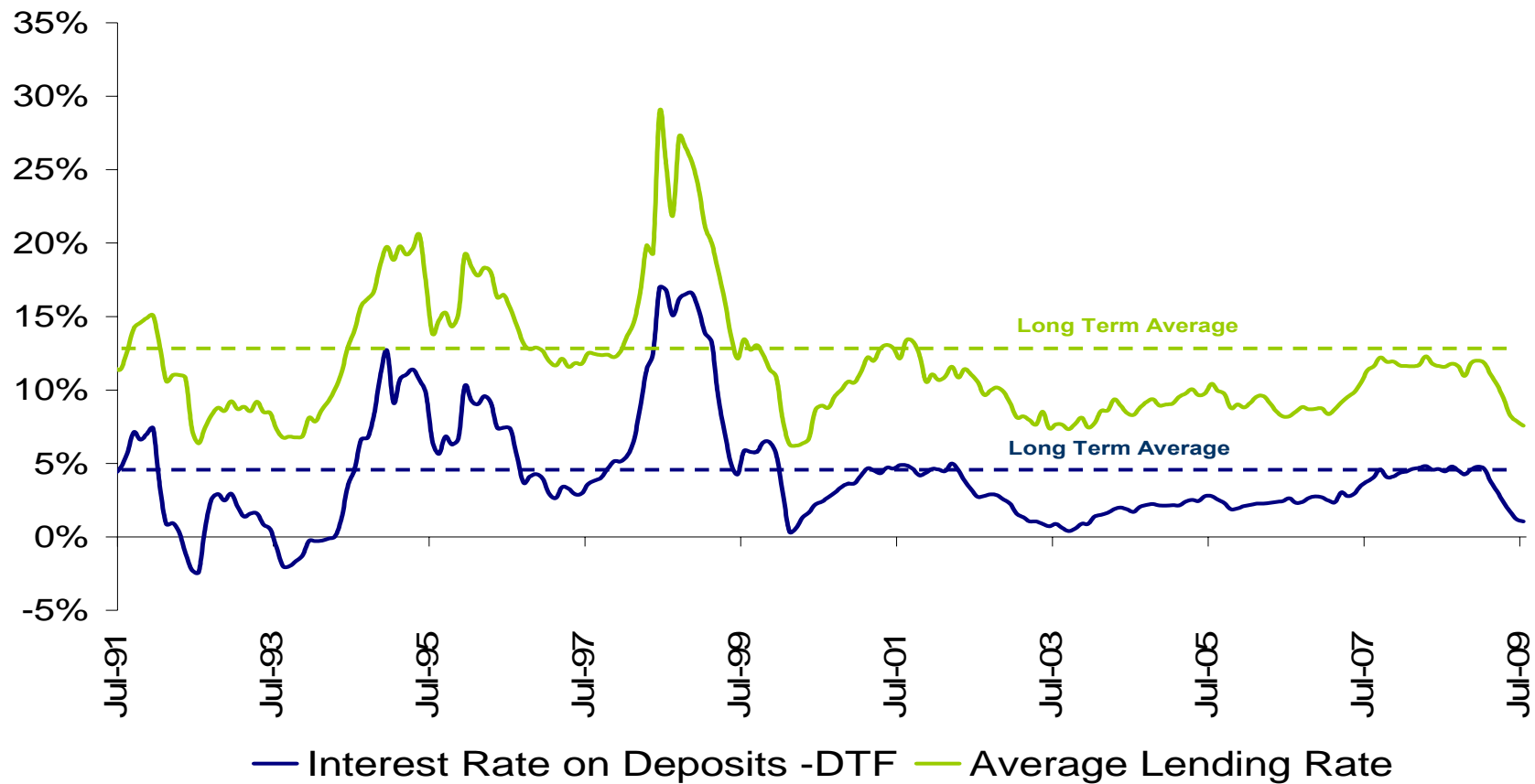
NFPS: Nonfinancial Public Sector; Rest of NFPS: Decentralized Sector



# What is the Current Situation ?

- No signs of liquidity constraints

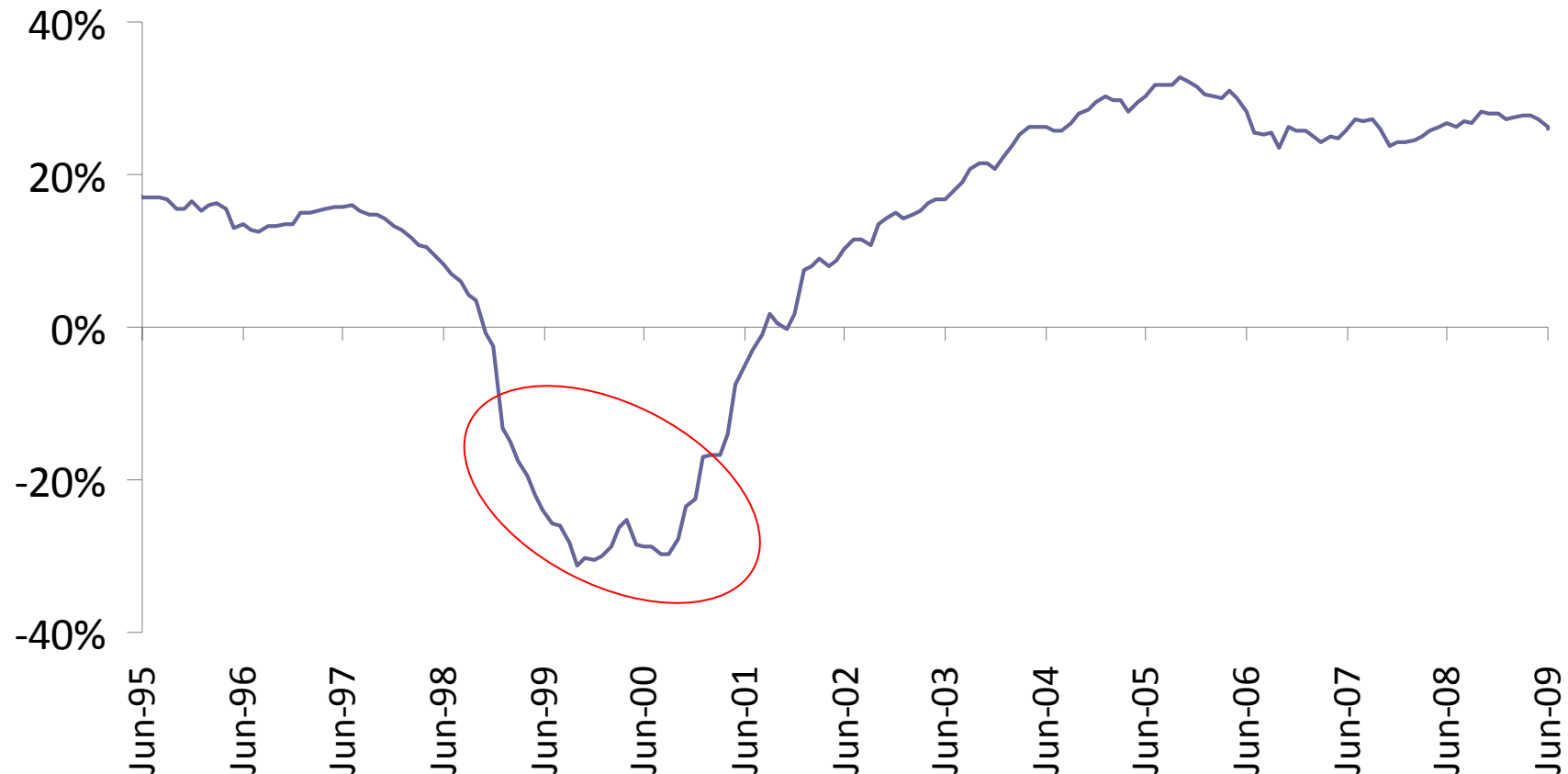
## Real Interest Rates in Colombia



## Current Situation

- Profits of the financial sector are healthy

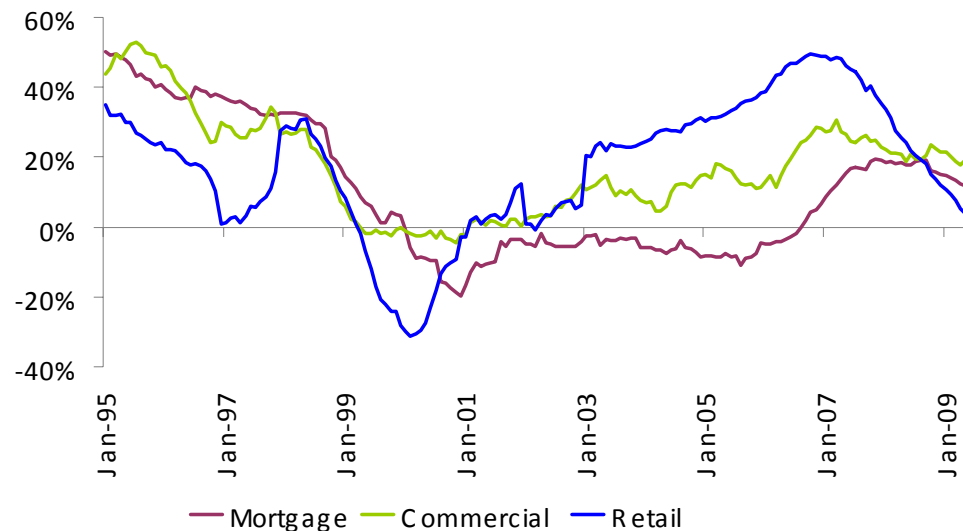
### Return on Equity



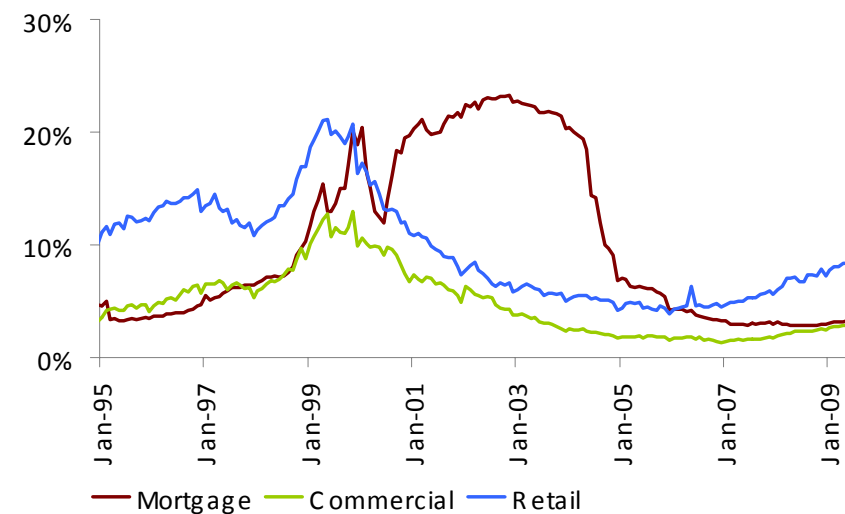
# Current Situation

- Credit has slowed down, but continues growing in real terms, and credit-default remains low

Real Credit Growth



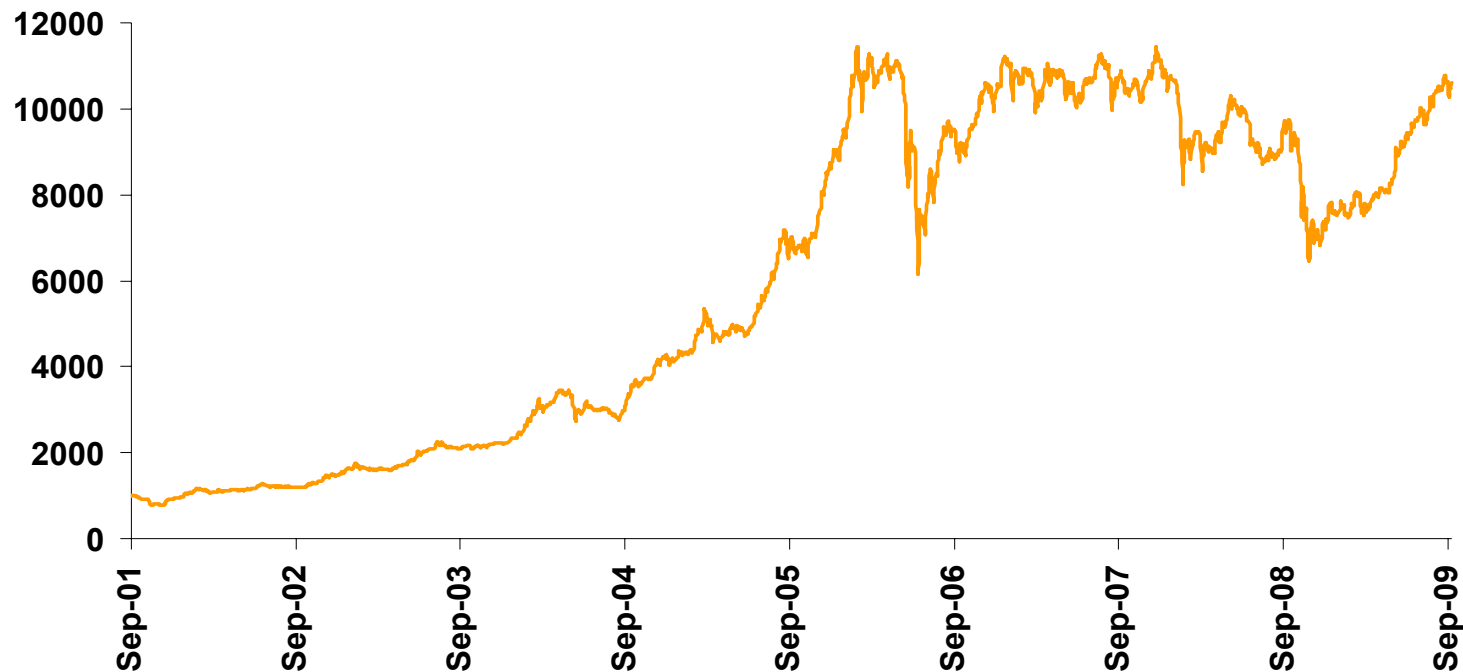
Non-performing / Gross Loan Portfolio



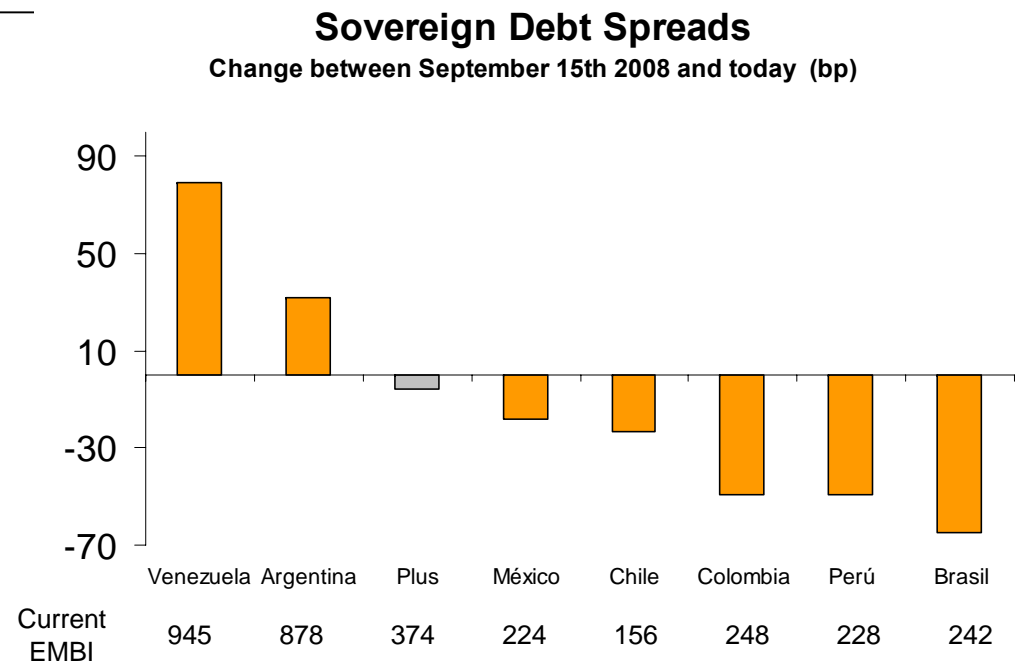
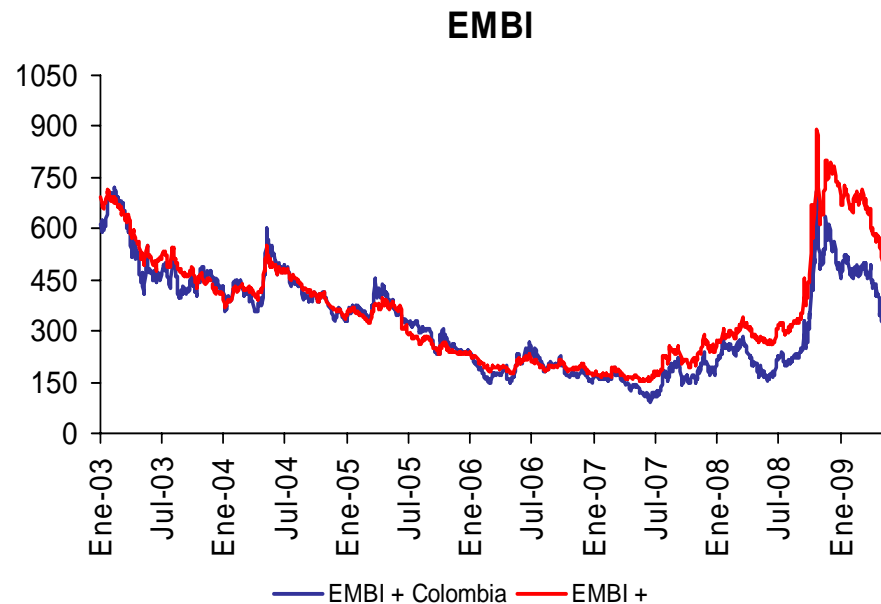
## Current situation

- **Following an acute decline in September 2008, stock prices are back to pre-crisis levels**

IGBC Index

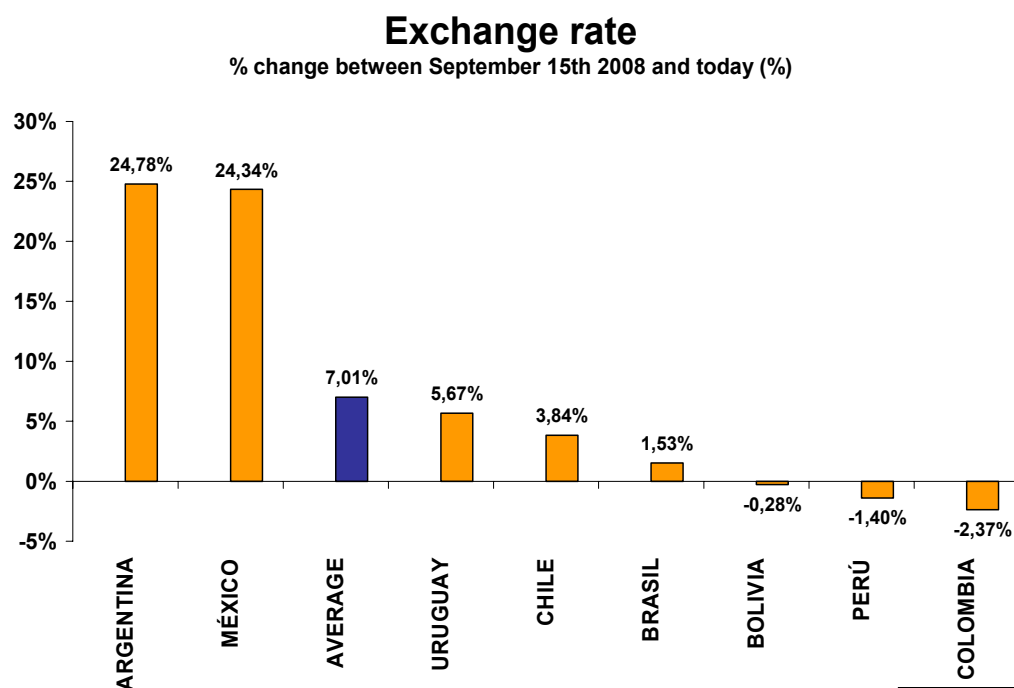


# Regarding risk perception, Colombia is among the most favored countries





# There has not been a sharp currency depreciation, and no loss of international reserves



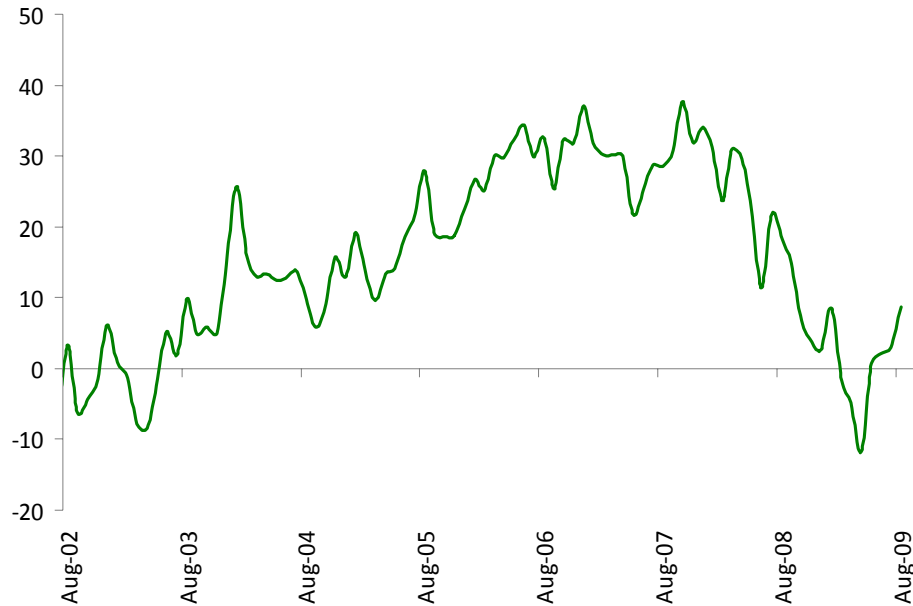
Last update on September 7 2009

International Reserves (US\$ m)			
Country	September	July	Δ%
BRASIL	206.494	207.363	0,4%
COLOMBIA	23.713	23.750	0,2%
ARGENTINA	47.121	46.047	-2,3%
CHILE	24.204	23.498	-2,9%
PERÚ	34.702	32.088	-7,5%
MÉXICO	83.313	73.269	-12,1%

Source: Bloomberg

# Following the initial downturn, consumers and investors confidence is progressively recovering

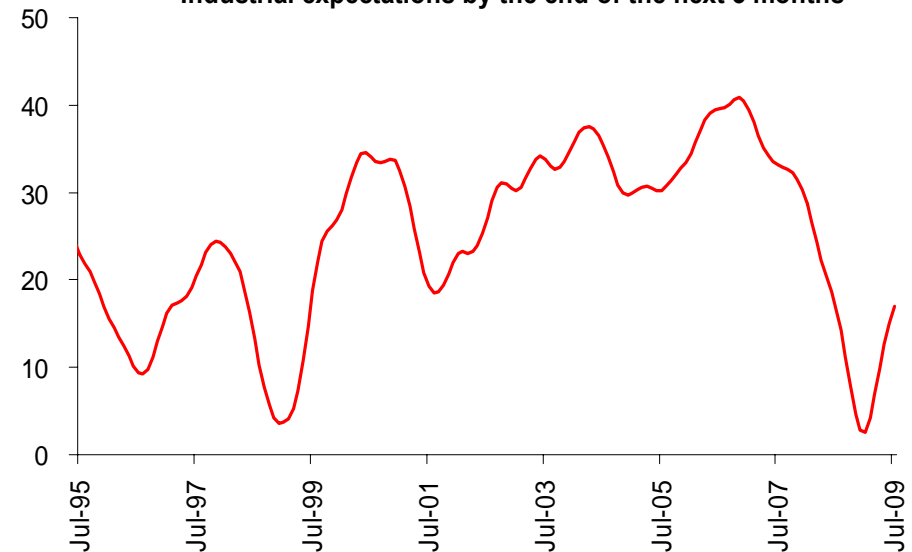
## Consumer Confidence



Source: FEDESARROLLO

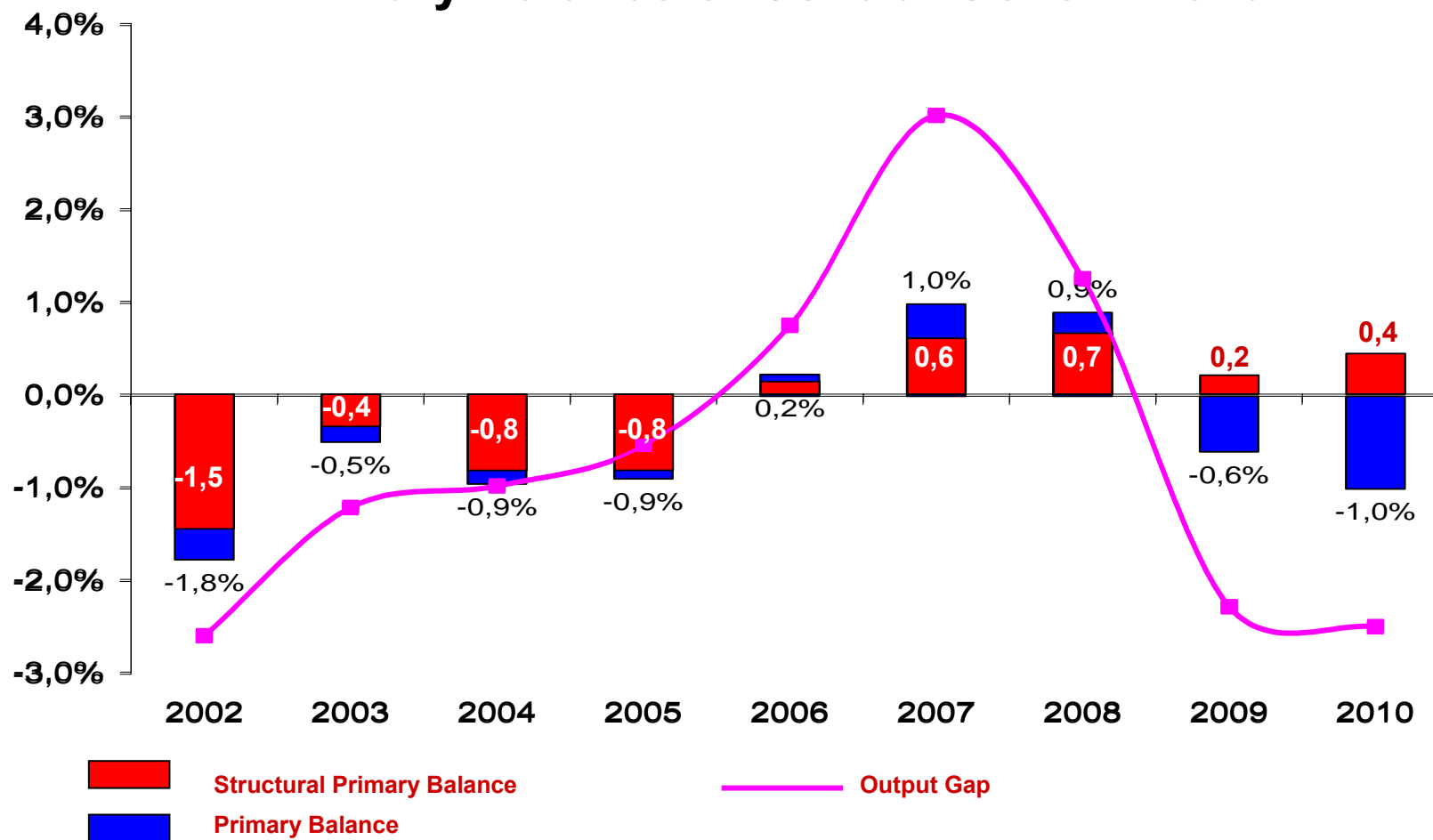
## Business Climate

Industrial expectations by the end of the next 3 months

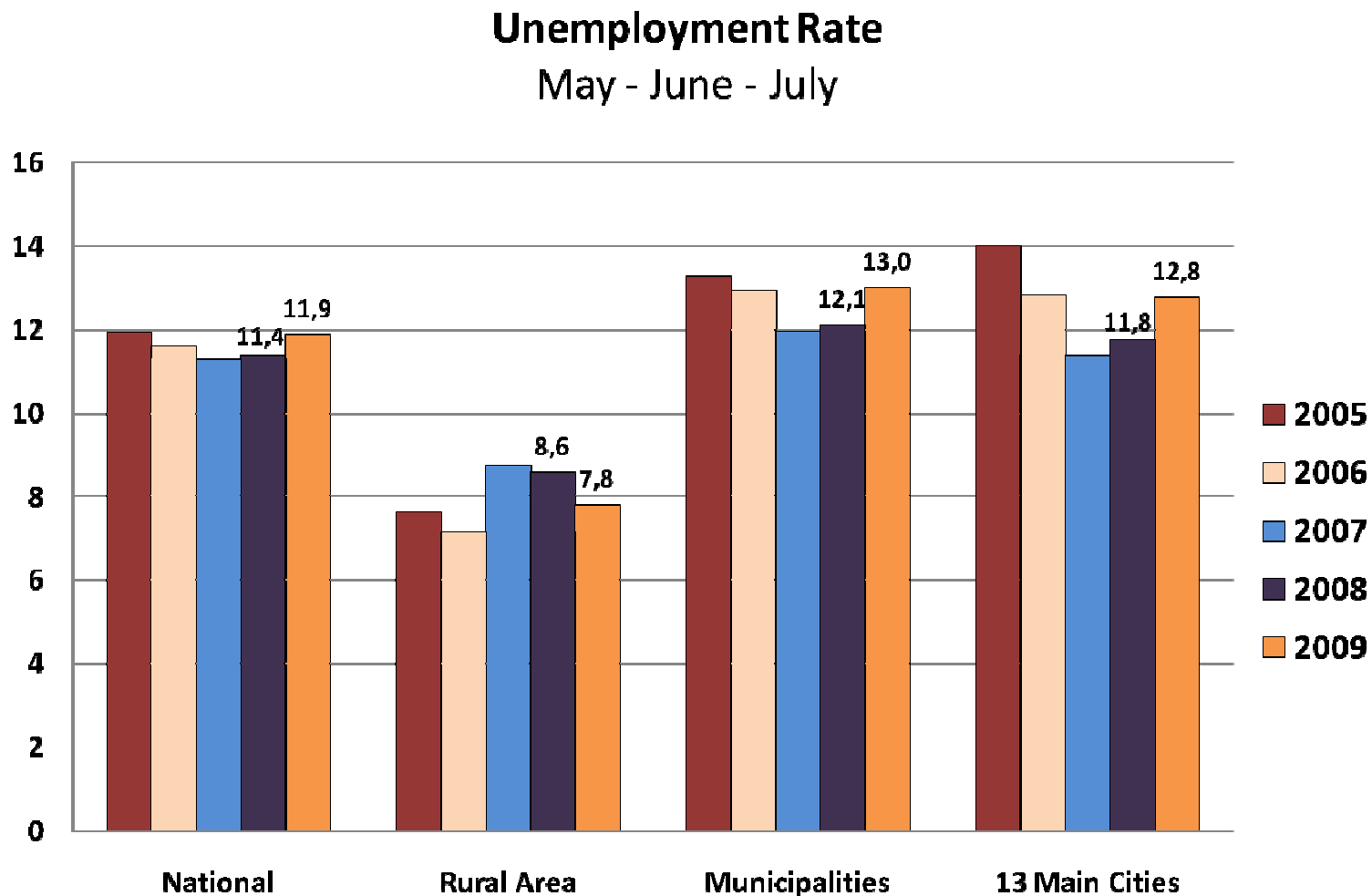


The Central Government's structural primary balance shows a countercyclical fiscal policy stance in 2009, which is currently supporting domestic demand and economic growth

## Primary Balance of Central Government

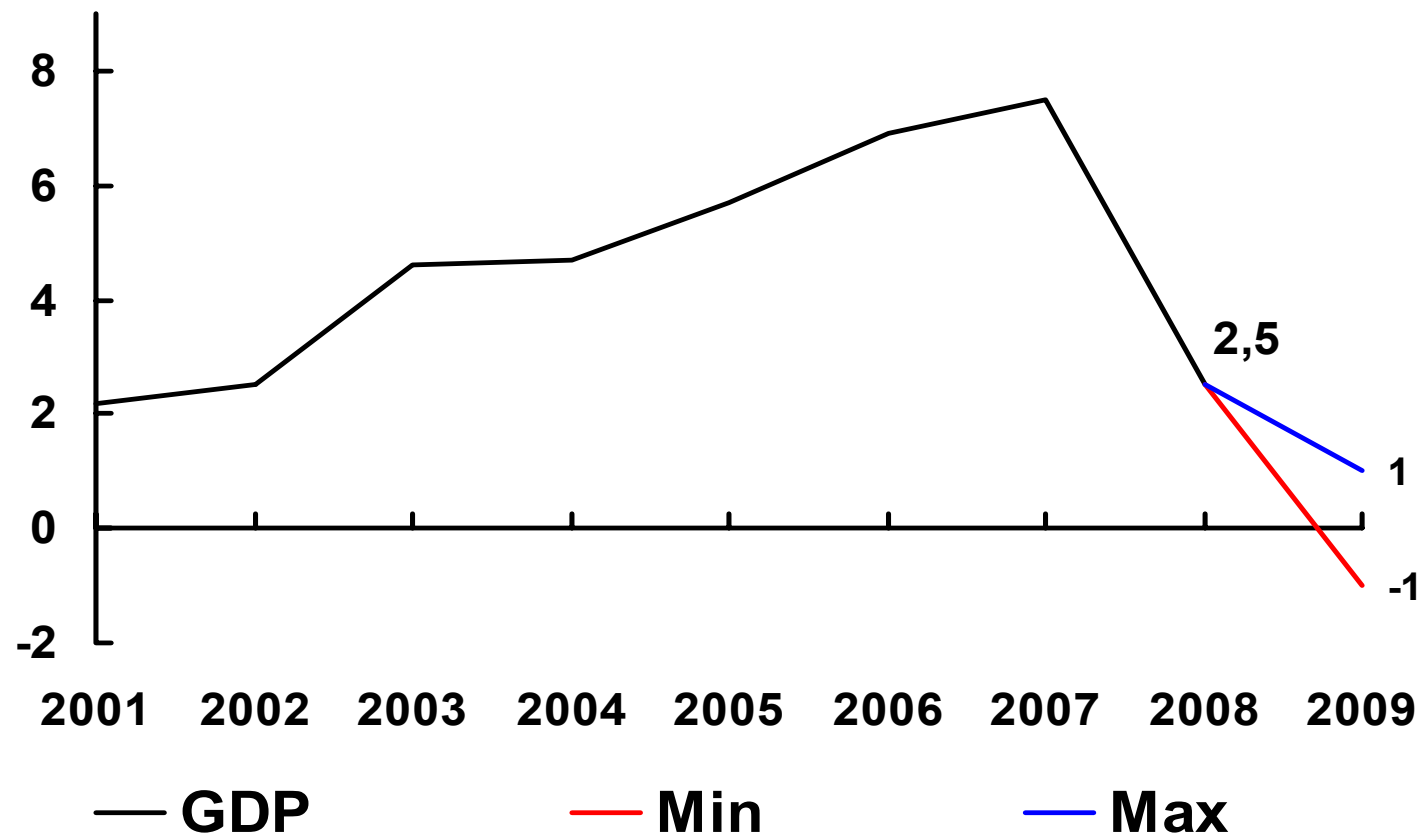


Unemployment has increased but rather moderately, and in any case, not as much as it did in 1999.



The outlook of economic growth for 2009, situates it within a range of -1% to + 1%, with a punctual forecast of 0% ..... likely to be revised upwards

### **GDP Growth Forecasts 2009 (%)**



## Some Final Thoughts...

- The crisis of the 90s in Colombia influenced policy makers to adopt monetary, financial and fiscal policies that strengthened economic fundamentals.
- **Monetary Policy** is evolving towards what some experts now call *Inflation Targeting Plus*
- **Financial policy** became more macro-prudential and precautionary, strengthening financial soundness
- **Fiscal Policy** became forward looking, taking care of debt sustainability, while supporting countercyclical efforts of monetary policy.

**THE END**