FitchRatings

RATING ACTION COMMENTARY

Fitch Revises Colombia's Outlook to Negative; Affirms IDR at 'BB+'

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Fitch Ratings - New York/Bogota - 06 Mar 2025: Fitch Ratings has affirmed Colombia's Long-Term Foreign-Currency Issuer Default Rating (IDR) at 'BB+' and revised its Outlook to Negative from Stable.

A full list of rating actions is at the end of this rating action commentary.

KEY RATING DRIVERS

Negative Outlook: Fitch revised the Outlook on Colombia's ratings to Negative from Stable on the deterioration in its fiscal position and uncertain prospects for corrective measures. The central government fiscal balance for 2024 came in at 6.7% of GDP, sharply underperforming Fitch's forecast of 5.6% of GDP, mainly due to revenue shortfalls and an inability to implement offsetting spending cuts.

As a result, general government (GG) debt to GDP jumped to an estimated 58% from 53% in 2023. Fitch believes that fiscal risks are tilted to the downside as the government will continue to struggle to meet fiscal targets and debt to GDP will continue to rise over the forecast period.

Colombia's ratings are supported by a track record of macroeconomic and financial stability, underpinned by an independent central bank with an inflation targeting regime and a free-floating currency. The ratings are constrained by high fiscal deficits and uncertain prospects for consolidation needed to stabilize debt/GDP, a high interest burden, and high commodity dependence.

Fiscal Uncertainties to Persist: Fitch envisages difficulties for the government to meet the revised fiscal rule target this year, given it projects tax administration efforts to yield 1.4% of additional revenues that Fitch expects is unlikely to be achieved.

Considering this revenue uncertainty and a worse-than-expected 2025 starting point, Fitch has upped its CG deficit forecasts for both 2025 and 2026 to 6.2% of GDP and 5.8%, respectively (from 5.1% and 4.7% previously). Fitch sees downside fiscal risks to even its revised forecasts from continued revenue underperformance as well as the reluctance of the Petro administration to sacrifice its spending priorities.

Mounting spending pressures and budgetary rigidities will make further deficit reduction difficult to achieve beyond 2026 without implementing tax reforms. Colombia has a good track record of implementing revenue-enhancing tax reforms amid fiscal pressures, but Fitch does not anticipate additional tax reforms during the rest of the Petro administration. Presidential elections are scheduled for May 2026.

Debt Burden to Rise: Fitch projects consolidated GG debt to continue to increase over the forecast period, reaching 62% of GDP in 2026, up from 57.8% in 2024, and continuing to diverge from the projected 2026 'BB' median of 55.4%. Colombia's GG interest/revenue ratio is expected to increase to 15.7% in 2025, above the 'BB' median of 10.1% and up from 14.9% in 2024. Fitch sees downside risks to the debt trajectory from further fiscal slippage, growth underperformance, or exchange-rate depreciation given that 35% of total debt is denominated in foreign currency.

Reforms Add to Fiscal Pressures: Last year, the Congress passed a pension reform that creates solidarity and semi-contributive pillars, with an estimated annual fiscal cost of 0.3% of GDP. It also redirects future pension contributions (up to 2.3x the minimum wage) to a public pension fund from individual private accounts, although current assets will be untouched.

Additionally, Congress passed a constitutional reform increasing CG transfers to local and regional governments to 39.6% of current revenues from 27.2%. A law redistributing competencies to local and regional governments will also be put in place. The increased transfers would be implemented gradually over a 12-year period beginning in 2027 (or once the law is in place). In Fitch's view, this will further increase the already significant budget rigidities (estimated at over 80% currently) in the medium term.

Growth To Accelerate: Fitch expects economic growth to accelerate significantly in 2025 to 2.7% from 1.7% in 2024 on the back of resilient consumer spending and recovering investment. However, uncertainties about trend growth persist since investment to GDP fell significantly during the pandemic and has only recovered to 17.1% in 2024. Fitch believes the ratio will remain below historic levels (averaging 22% of GDP from 2010 to 2020) throughout the forecast period.

Inflation Slowly Falls: Fitch expects inflation to continue declining and reach the upper band of the central bank's 3% (+/-1pp) target by end-2025 from 5.2% at end-2024. Widespread indexation and unwinding of fuel subsidies in 2023-2024 have led to a slower disinflation process than most countries in the region. The central bank has cut interest rates cumulatively by 375 bp since December 2023 to 9.5% in December 2024. Year-to-date, the central bank has been on hold. Fitch expects additional cuts reaching a terminal rate of 6.5% by YE 2026, but there is the risk of a more gradual pace from a slower-than-expected disinflation or stronger than expected peso depreciation.

Narrower Current Account Deficits: The current account deficit is expected to widen marginally in 2025 to 2.1% of GDP from 1.8% in 2024, well below its 2022 high of 6.1%. Foreign direct investment (FDI) has proven resilient to date despite political uncertainties, reaching an estimated USD10 billion in net terms in 2024 (3.1% of GDP). Fitch expects similar levels of net FDI in 2025-2026 that continue to fully cover the current account deficits.

The central bank has accumulated reserves to boost its external liquidity position to USD61.9 billion as of end-2024, with Fitch expecting further accumulation of nearly USD3 billion in 2025. In April 2024, the IMF approved a new two-year flexible credit line of USD8.1 billion for Colombia, which provides an additional buffer that the country has utilized in the past to manage external shocks.

ESG - Governance: Colombia has an ESG Relevance Score (RS) of '5' for both Political Stability and Rights and for the Rule of Law, Institutional and Regulatory Quality and Control of Corruption. Theses scores reflect the high weight that the World Bank Governance Indicators (WBGI) have in Fitch's proprietary Sovereign Rating Model (SRM). Colombia has a medium WBGI ranking at 42.9 reflecting a track record of violence but peaceful political transitions, a moderate level of rights for participation in the political process, moderate institutional capacity, established rule of law and a moderate level of corruption.

RATING SENSITIVITIES

Factors that Could, Individually or Collectively, Lead to Negative Rating Action/Downgrade

Public Finances: A continued deterioration in Colombia's GG debt-to-GDP ratio, for example from persistently high fiscal deficits and/or weak growth.

Macro: Deterioration of investment and medium-term growth prospects with adverse social ramifications, such as high unemployment and poverty levels.

Factors that Could, Individually or Collectively, Lead to Positive Rating Action/Upgrade

Public Finances: Achievement of fiscal consolidation that stabilizes the GG debt-to-GDP ratio.

Structural/Macro: Improvement in macro-policymaking that boosts fiscal and monetary credibility and/or growth-enhancing reforms.

SOVEREIGN RATING MODEL (SRM) AND QUALITATIVE OVERLAY (QO)

Fitch's proprietary SRM assigns Colombia a score equivalent to a rating of 'BB+' on the Long-Term Foreign-Currency IDR scale.

Fitch's sovereign rating committee did not adjust the output from the SRM to arrive at the final Long-Term Foreign Currency IDR.

Fitch's SRM is the agency's proprietary multiple regression rating model that employs 18 variables based on three-year centered averages, including one year of forecasts, to produce a score equivalent to a LT FC IDR. Fitch's qualitative overlay (QO) is a forward-looking qualitative framework designed to allow for adjustment to the SRM output to assign the final rating, reflecting factors within Fitch's criteria that are not fully quantifiable and/or not fully reflected in the SRM.

COUNTRY CEILING

The Country Ceiling for Colombia is 'BBB-', 1 notch above the Long-Term Foreign Currency IDR. This reflects moderate constraints and incentives, relative to the IDR, against capital or exchange controls being imposed that would prevent or significantly impede the private sector from converting local currency into foreign currency and transferring the proceeds to non-resident creditors to service debt payments.

Fitch's Country Ceiling Model produced a starting point uplift of +1 notch (above the IDR. Fitch's rating committee did not apply a qualitative adjustment to the model result.

REFERENCES FOR SUBSTANTIALLY MATERIAL SOURCE CITED AS KEY DRIVER OF RATING

The principal sources of information used in the analysis are described in the Applicable Criteria.

ESG CONSIDERATIONS

Colombia has an ESG Relevance Score of '5' for Political Stability and Rights as WBGIs have the highest weight in Fitch's SRM and are therefore highly relevant to the rating and a key rating driver with a high weight. As Colombia has a percentile rank below 50 for the respective Governance Indicator, this has a negative impact on the credit profile.

Colombia has an ESG Relevance Score of '5' for Rule of Law, Institutional & Regulatory Quality and Control of Corruption as WBGIs have the highest weight in Fitch's SRM and are therefore highly relevant to the rating and are a key rating driver with a high weight. As Colombia has a percentile rank below 50 for the respective Governance Indicators, this has a negative impact on the credit profile.

Colombia has an ESG Relevance Score of '4' [+] for Human Rights and Political Freedoms as the Voice and Accountability pillar of the WBGIs is relevant to the rating and a rating driver. As Colombia has a percentile rank above 50 for the respective Governance Indicator, this has a positive impact on the credit profile.

Colombia has an ESG Relevance Score of '4' [+] for Creditor Rights as willingness to service and repay debt is relevant to the rating and is a rating driver for Colombia, as for all sovereigns. As Colombia has track record of 20+ years without a restructuring of public debt and captured in Fitch's SRM variable, this has a positive impact on the credit profile.

The highest level of ESG credit relevance is a score of '3', unless otherwise disclosed in this section. A score of '3' means ESG issues are credit-neutral or have only a minimal credit impact on the entity, either due to their nature or the way in which they are being managed by the entity. Fitch's ESG Relevance Scores are not inputs in the rating process; they are an observation on the relevance and materiality of ESG factors in the rating decision. For more information on Fitch's ESG Relevance Scores, visitwww.fitchratings.com/topics/esg/products#esg-relevance-scores.

RATING ACTIONS

ENTITY / DEBT	RATING	PRIOR

Colombia	LT IDR BB+ Affirmed	BB+
	ST IDR B Affirmed	B
	LC LT IDR BB+ Affirmed	BB+
	LC ST IDR B Affirmed	B
	Country Ceiling BBB- Affirmed	BBB-
senior unsecured	LT BB+ Affirmed	BB+
Senior Unsecured-Local currency	LT BB+ Affirmed	BB+

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VIEW ADDITIONAL RATING DETAILS

Additional information is available on www.fitchratings.com

PARTICIPATION STATUS

The rated entity (and/or its agents) or, in the case of structured finance, one or more of the transaction parties participated in the rating process except that the following issuer(s), if any, did not participate in the rating process, or provide additional information, beyond the issuer's available public disclosure.

APPLICABLE CRITERIA

Country Ceiling Criteria (pub. 24 Jul 2023)

Sovereign Rating Criteria (pub. 24 Oct 2024) (including rating assumption sensitivity)

APPLICABLE MODELS

Numbers in parentheses accompanying applicable model(s) contain hyperlinks to criteria providing description of model(s).

Country Ceiling Model, v2.0.3 (1)

Debt Dynamics Model, v1.3.2 (1)

Macro-Prudential Indicator Model, v1.5.0 (1)

Sovereign Rating Model, v3.14.2 (1)

ADDITIONAL DISCLOSURES

Dodd-Frank Rating Information Disclosure Form