Minutes of a Meeting of the Board of Directors of the Central Bank of Colombia on April 30, 2009

A regular meeting of the Board of Directors of the Central Bank of Colombia was held in the city of Bogotá on April 30, 2009.

Present:
Mr. Óscar Iván Zuluaga, Minister of Finance and Public Credit
Mr. José Darío Uribe, Governor of the Central Bank of Colombia

Full-time Directors:
Mr. Carlos Gustavo Cano
Mr. Juan José Echavarría
Mr. Cesar Vallejo
Mr. Pablo Zárate.

Inflation and the economic situation with respect to growth and prospects for the future were discussed, and monetary-policy decisions were reached. Mr. Fernando Tenjo's absence was justified. The following is a summary of the principal topics addressed during the meeting.

1. BACKGROUND

a. Recent Developments in Inflation

Annual consumer inflation in March was 6.14%, having dropped for the fifth month in a row. Most of the core inflation indicators declined, resuming the downward tendency observed since November 2008, which was interrupted in February.

Annual food inflation declined from 9.5% in February to 8.7% in March, thanks to processed foods. Perishables increased.

Regulated price inflation went from 9.0% in February to 8.1% in March, mainly because of public utilities, residential natural and gasoline.

Non-tradable inflation, without food and regulated prices, was 5.36%. This is similar to the rate observed the month before and was due to certain indexed prices, such as those for education, health and rentals.

Tradable inflation, without food and regulated prices, increased from 2.4% in February to 2.5% in March.

The various inflation-expectation indicators measured on the basis of local government bonds at 1, 5 and 10 years were between 3.5% and 4.7% at the start of April. This is the lowest level since mid-2006.

The annual variation in producer prices (PPI) rose from 6.2% in February to 6.8% in April.

b. Internal Growth

Available figures show internal economic activity continued to slow faster than was anticipated the quarter before by the Central Bank's technical team.

- The industrial production figures released by DANE signal an annual drop of 12.8% by January.

- Despite somewhat of a recovery and 5% growth, the demand for energy, after being adjusted by the number of work days, registered a decline of 5.1%.

- According to Fedesarrollo, industrial orders and inventory continued to deteriorate during the first two months of the year.

- The Fedesarrollo indicator of consumer sentiment dropped again in March.

- The Fenalco commercial sales survey showed some recovery during the month, but from a low level. The economic expectation indicator resulting from the survey conducted by that trade association is at historically low levels.

- The February retail sales figures reported by DANE were off by an annual rate of 4.1%, abiding by the downturn begun in mid-2008.

- Building permits continued to decline, as did cement production.

With respect to external demand, total exports in dollars were down by 13.2% in January compared to the same month in 2008. The drop in non-traditional exports (14.8%) was slightly larger than the decline in traditional exports (13.6%). Coal was the only traditional export item to register an increase (88% annual), thanks to larger volumes sold. The lower export values for other products (oil and ferronickel) were the result of price declines.

As to non-traditional exports, by destination, sales to Venezuela were less dynamic in every aspect, compared to the same month the year before. In all, they registered an annual decline of 20% in January Exports to Ecuador increased at an annual rate of 1.7%, bolstered by the industrial sector, particularly food and beverages, transport material and graphic arts. The other major buyer, the United States, also performed poorly (-43% by January 2009, excluding gold), with cutbacks in all sales, except bananas. Non-traditional exports to the rest of the world rose by 0.4%.

Imports in dollars fell by 11.7% between January and February 2009, compared to the same period in 2008. An analysis by product (CUODE classification) shows the drop was led by intermediate goods (-26.9% annual). The annual rate for consumer goods was -9.5% in February, while capital goods were up by 4.0%.

With the monthly figures for March, unemployment nationwide and in the 13 major urban areas rose in annual terms: 12.0% total unemployment nationwide and 13.5% in the 13 urban areas. These figures represent respective increases of 0.8 pp and 1.5 pp compared to those registered for the same period in 2008. As was the case in February, the expansion witnessed during March is due largely to growth in the labor supply (measured by the global participation rate).

c. The External Context

The economy and commerce worldwide contracted sharply during the first quarter of 2009, adding to the drop witnessed in the fourth quarter of 2008. This outcome confirms the fears of a pronounced and larger-than-expected recession in the global economy.

By March 2009, the annual decline in industrial production in the United States was 12.8%, reaching the levels observed in 1999. Industrial production in the other developed economies has fallen off sharply as well. Japan is the most dramatic case. By February, it annual rate of industrial production was down by more than 45% and the level that month was lower than any other registered during the last two decades.

World commerce has been hard hit as well. The annual variation in nominal exports, in dollars, declined at annual rates of 25% in January and February, both in the Euro zone and the United States, respectively. The drop in this variable is particularly dramatic in Japan, where the annual decline was around 48% in February. In terms of impact, the collapse has caused a sharp GDP reduction in the developed economies.

In short, the current situation in the developed economies is characterized by a generalized loss of consumer and investor confidence, which has lowered spending levels dramatically and been reinforced by a noticeable increase in restrictions on loans. The first quarter of 2009 saw no change in this respect, as suggested by the additional decline in consumer confidence indicators. Business confidence indicators have been slightly less negative in the last two months, although the perception of the economic situation is still very pessimistic. This being the case, the forecasts for growth in the United States and the other development economies were reduced.

The emerging economies also have been seriously affected. In Latin America, the drop in industrial production is a fact, as is the reduction in exports. Growth and inflation forecasts for the region have been revised downward as a result. Yet, despite fewer prospects for growth, exchange rates in the Latin American countries did not continued to weaken. On the contrary, most Latin American currencies appreciated last month. Risk perception, viewed from the standpoint of both EMBI + and five-year CDs, is down.

d. Financial Variables

During the seven weeks ended April 10, the growth in monetary aggregates slowed as a result of the increase in treasury deposits with the Central Bank. During the first week of the month, the annual increase in M3 was nearly 17%. Practically the same was true of liabilities subject to reserve requirements. The financial system continues to place a priority on deposits in the form of certificates of deposit (CDT in Spanish) and bonds, which are growing at annual rates of 40%.

As to credit, the slowdown in the total gross loan portfolio in domestic currency ceased during the last month and a half. In early April, annual growth was 15.2%. In real terms, the increase in the total portfolio comes to 9.4%, which is more than the average witnessed since 1970 (6.4%).

With respect to types of loans, the build-up in the commercial loan portfolio (from 17.0% to 18.4%) was a high point during the last six weeks and was accompanied by a reduction in the consumer loan portfolio. At the beginning of April, the annual increase in consumer lending was 6.5%. The mortgage loan portfolio continued to grow at an annual rate of around 14%.

External borrowing in the private sector was down by US$259 million in January and February. This was due a reduction in the foreign-currency denominated portfolio of exchange market intermediaries. Direct borrowing rose slightly (by US$63 million), but not enough to offset the drop in the foreign-currency portfolio.

Interest rates continued to decline quickly, following the Central Bank's benchmark rate. Compared to December 19, the date of the first adjustment in that rate, and up until April 17, the rate on certificates of deposit had dropped by 324 bp in all, while the DTF fell by 283 bp. As to lending rates, the cumulative reductions for commercial loans are significant as well: 342 bp for preferential lending and 298 bp for the treasury rate. The rates on household loans have declined less, in the midst of more volatility: 85 bp for home purchase, 65 bp for consumer financing and nearly 100 bp in the case of credit card lending.

The drop in nominal rates allowed for a reduction in real rates during recent months, including March. The real rates on preferential and treasury lending remain above their historic averages (calculated since 1998 and 2001). Those on commercial loans already are below average, and those on consumer lending have fluctuated around average.

2. DISCUSSION AND POLICY OPTIONS

The following points were emphasized during the Board's deliberations:

i. Price increases at rates that continue to exceed the targets for inflation set by the Board, but have shown a tendency to decline.
ii. The absence of signs of a reduction in non-tradable inflation, excluding food and regulated prices.
iii. The decline in international prices for food, raw materials and oil compared to the high level in 2008, which could have a major impact on total inflation, depending on the country's trade policy and the exchange rate.
iv. The drop in international oil prices, which is not reflected in domestic gasoline prices.
v. The continued decline in economic activity, which is occurring faster than the Bank's technical team had anticipated.

vi The end to the slowdown in the total loan portfolio in the financial system, and the fact that most interest rates in the market declined quickly in response to cuts in the Bank's benchmark rate.
vii Negative growth in the United States and less growth in Ecuador and Venezuela
viii The effect of the exchange rate on inflation and growth in the tradable sectors
ix The downturn in government bond prices
x Intermediate and long-term expectations for inflation, which are within the target range set by the Board of Directors.

The main points of the discussion among Board members centered on: (i) the effect of monetary-policy measures, given the time it takes them to work through to the economy; (ii) the elements that affect inflation forecasts for 2009 and 2010, and particularly the indexing mechanisms incorporated into some prices; (iii) the uncertainty the world financial crisis has generated on international markets and its impact on the Colombian economy; (iv) the region's access to external financing and the reasons for less momentum in the financial system's loan portfolio; (v) the risk balance between growth and inflation in a context where the economy is slowing faster than anticipated and inflation expectations have declined; and (vi) the need to bolster the monetary authority's credibility and to anchor inflation expectations.

The Board members highlighted the fact that consumer inflation was down for the fifth month in a row. The decline in inflation and expectations of inflation ratifies the fact that weak internal and external demand and the drop in international commodity prices are bringing less pressure to bear on inflation.

The Board also emphasized the faster-than-expected deterioration in the world economy during the first quarter of 2009. Despite signs of stabilization in some of the industrialized countries, the negative effects of the world crisis are expected to continue throughout the year. In Latin America, the generalized drop in industrial production is a reality, as is the decline in inflation. It was noted that the sharp devaluation in Latin American currencies at the start of 209 has been corrected.

Available figures show similar performance for the Colombian economy, with a slowdown in exports and subsequently weaker growth. The latest information on industry and commerce signals sharp cutbacks. However, the financial system continues to perform well. Under these conditions, and considering the low level of capacity utilization, one would expect inflation in Colombia to continue to decline in the months ahead. In fact, it might end the year below the mid-point of the target range.

In view of the foregoing, the members of the Board unanimously agreed to lower the Central Bank's intervention rate to 6%. This is a reduction of 100 bp. The cumulative 400 bp reduction in the intervention interest rate since December 2008 bolsters economic growth. Recent developments in Colombia and throughout the world make for a low risk balance in terms of economic activity and inflation. This allows the Board to continue to implement a policy designed to reduce the Central Bank's intervention rates.

Finally, the Board reiterated the need to continue to monitor the international financial situation, so monetary policy measures needed to address its impact can be adopted without delay.

3. POLICY DECISION

The Board of Directors agreed to reduce the Central Bank's intervention interest rate by 100 bp, placing it at 6%.

Bogotá D. C., Colombia
May 15, 2009