Macro scenario -Colombia

August 15, 2025

Narrowing scope for monetary policy cuts

- Amid robust domestic demand, we revised our GDP growth forecast upward to 2.9% for 2025 and 2.6% for 2026 (from a previous estimate of 2.5% for both years).
- We maintained our year-end inflation forecast at 5.1%, but revised our 2026 projection up to 4.0% (from 3.6%), incorporating risks from a significant minimum wage increase next year.
- Facing elevated inflation and upside risks, in the context of pressure on the fiscal accounts, we revised our year-end policy rate forecast upward to 9.25% (from 8.75%) and to 8.25% by end-2026 (from 7.75% in the previous scenario).

Resilient activity accompanied by labor market tightness

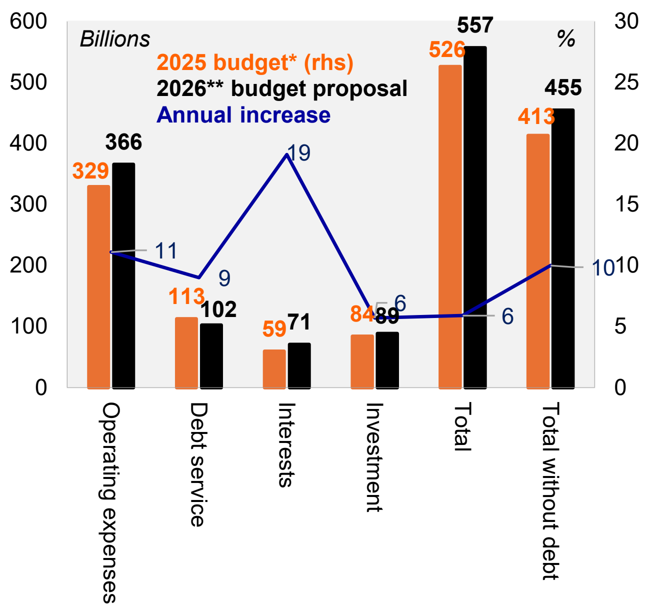
Private consumption is driving recovery of economic activity. Private consumption remains one of the main drivers of economic activity, while the agricultural, commercial, and entertainment sectors are leading the path to recovery. In parallel, the labor market remains tight with the unemployment rate (SA) at 8.4%, well below BanRep's 10.2% NAIRU estimate. In this context, business confidence was mixed in June, with questions related to the outlook improving, but order levels weakening.

Fiscal accounts still under pressure, even as revenues rise significantly

Another large monthly deficit. The monthly fiscal balance in May reached 0.3% of GDP (stable from the previous year), leading to a cumulative fiscal deficit of 3.1% of GDP, 0.8pp above the same in period in 2024. Tax revenues continued to increase in June, rising nominally by 13% YoY, leading to a cumulative increase in the year of 9.7% YoY, still below the year's official forecast of 14.8%.

Fiscal Council flags concerns over the 2026 budget. The government presented the 2026 budget to Congress, reaching 28.9% of GDP. Part of the funding is reliant on the eventual approval of a new tax reform (1.4% of GDP). Spending is projected to rise by 9% in nominal terms with respect to the final 2025 budget. The Fiscal Council (CARF) raised concerns over the budget's consistency with the Medium-Term Fiscal Framework (MTFF), noting that the 2026 primary deficit forecast was revised up by 60bps to 2% of GDP. CARF estimates that the additional resources needed to meet 2026 fiscal targets have increased to 2.0% of GDP, up from 1.7% in the MTFF. These discrepancies highlight the stress on the fiscal accounts and reduce the likelihood of Colombia reinstating the fiscal rule by 2028. The deadline for congressional approval is October 20.

Budget depends on financing bill approval



Source: Minister of Finance; Itaú

Inflation rebounded in July

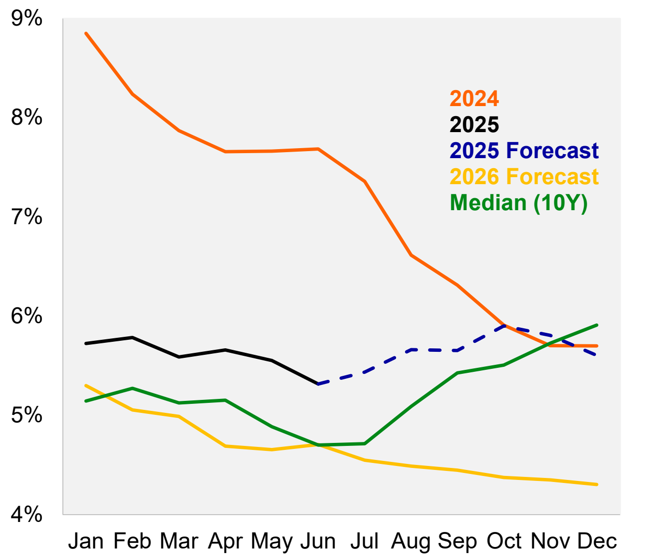
Monthly inflation surprised consensus to the upside. Consumer prices rose by 0.28% MoM in July, driven by food prices and housing and utilities. On an annual basis, headline inflation increased by 8bps from June to 4.90% in July, while core inflation fell slightly by 3bps to 5.34%. Services inflation remained broadly stable at 6.5% (9.51% peak in September 2023). At the margin, we estimate that inflation accumulated in the quarter reached 5.5% (SA, annualized; +5.7% in 2Q25). Core inflation remains elevated at 5.3%, from 5.4% in 2Q25 (SA, annualized).

Inflation concerns keep BanRep cautious

As in June, a majority of the BanRep Board favored holding the policy rate at 9.25% for a second consecutive meeting. The Board remained divided along June lines with four members voting for a pause, one member opting for a 25bp cut and two members favoring a 50bp cut. Governor Villar highlighted that although headline inflation fell from 5.1% to 4.8% between May and June, it was driven by volatile prices, and inflation expectations remained above the target. Additionally, core inflation was steady at 4.8%, interrupting its downward trend.

Inflation, economic activity, and neutral rate revised upward by BanRep's technical staff. In its quarterly Monetary Policy Report, the central bank raised its year-end inflation forecast by 30 basis points to 4.7% (Itaú: 5.1%; 5.2% in 2024), while the projection for 2026 was also revised upward by 20 basis points to 3.2%. Regarding monetary policy, the central bank staff's baseline scenario suggests a policy rate trajectory that, on average for 2025 and 2026, remains above market expectations (8.6% in Q4 2025 and 7.0% in Q4 2026). Additionally, the neutral rate estimate for 2025 remained unchanged at 2.7%, while the 2026 projection was revised upward to 3.1% (from 3.0% in the previous IPoM).

CPI rebound is likely



Source: DANE, Itaú

Strong domestic demand supports upward growth revisions

Amid robust domestic demand, we revised our 2025 GDP growth forecast up to 2.9% and 2.6% for 2026 (from a previous estimate of 2.5% for both years). This adjustment reflects a faster-than-anticipated recovery in the commerce sector, supported by strong private consumption. Additionally, the agricultural sector has maintained solid momentum, bolstered by favorable coffee prices.

Higher remittances and favorable COP dynamics continue to support a low current account deficit (CAD). Although the trade deficit is widening, stronger GDP growth and a resilient exchange rate are expected to partially offset this pressure. We now forecast a CAD of 2.7% of GDP for this year (up from 2.6% in the previous scenario, 1.8% in 2024). Meanwhile, we continue to expect the exchange rate to end both this year and next at COP 4,100/USD, consistent with a weakening global dollar trend.

Inflation is expected to remain elevated in the second half of the year. A low statistical base compared to H2 2024, along with persistent risks from higher gas prices, will likely limit further disinflation. We maintain our year-end inflation forecast at 5.1%, but revised our 2026 estimate upward to 4.0% (from 3.6%), incorporating risks from another significant increase in the minimum wage next year, amid strong domestic consumption and a resilient labor market.

Tighter monetary policy. Following BanRep's July decision to hold rates steady, reflecting concerns over stubborn inflation expectations and strong domestic demand, we see limited room for further cuts this year. We expect inflation to remain elevated or even rise in H2, leading us to revise our year-end rate forecast upward to 9.25% (from 8.75%) and to 8.25% by end-2026 (from 7.75%).

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Colombia | Forecasts and Data

	2020	2021	2022	2023	2024	2025F		2026F	
						Current	Previous	Current	Previous
Economic Activity									
Real GDP growth - %	-7.2	10.8	7.3	0.7	1.7	**2.9**	2.5	**2.6**	2.5
Nominal GDP - USD bn	270	322	345	364	420	**423**	421	**462**	458
Population (millions)	50.9	51.4	51.8	52.2	52.7	**53.2**	53.2	**53.5**	53.5
Per Capita GDP - USD	5,312	6,272	6,657	6,972	7,968	**7,956**	7,909	**8,639**	8,554
Unemployment Rate - year avg	16.7	13.8	11.2	10.2	10.2	**9.0**	9.6	**9.2**	9.8
Inflation									
CPI - %	1.6	5.6	13.1	9.3	5.2	**5.1**	5.1	**4.0**	3.6
Interest Rate									
Monetary Policy Rate - eop - %	1.75	3.00	12.00	13.00	9.50	**9.25**	8.75	**8.25**	7.75
Balance of Payments									
COP / USD - eop	3,433	3,981	4,810	3,822	4,409	**4,100**	4,100	**4,100**	4,100
Trade Balance - USD bn	-10.1	-15.3	-14.5	-9.7	-10.8	**-12.4**	-12.0	**-11.0**	-11.0
Current Account - % GDP	-3.4	-5.6	-6.1	-2.4	-1.8	**-2.7**	-2.6	**-3.1**	-3.1
Foreign Direct Investment - % GDP	2.8	3.0	5.0	4.6	3.4	**3.5**	3.6	**3.7**	3.7
International Reserves - USD bn	58.5	58.0	56.7	59.1	61.9	**62.5**	62.5	**63.0**	64.0
Public Finances									
Primary Central Govt Balance - % GDP	-5.0	-3.6	-1.0	-0.3	-2.4	**-2.7**	-2.7	**-2.5**	-2.5
Nominal Central Govt Balance - % GDP	-7.8	-7.1	-5.3	-4.2	-6.7	**-7.5**	-7.5	**-6.8**	-6.8
Central Govt Gross Public Debt - % GDP	65.0	63.0	60.8	56.7	63.3	**65.0**	65.0	**66.5**	66.5

Source: IMF, Bloomberg, Dane, Banrep, Haver and Itaú

Macro Research – Itaú

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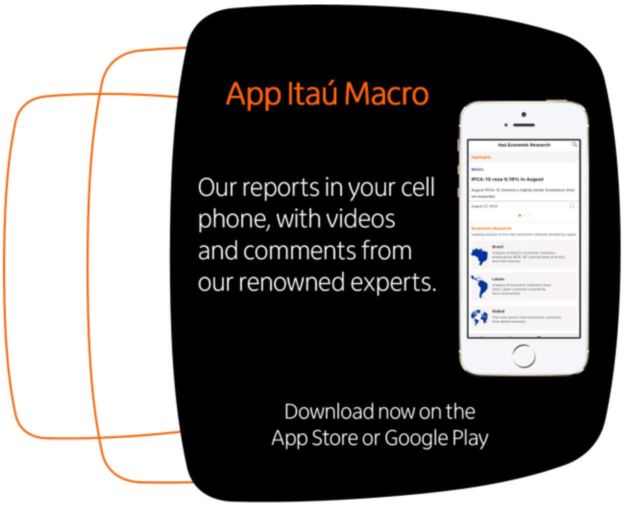

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