

Editorial

Economic growth in Colombia

In all countries, economic policy goals are very important. Undoubtedly, economic growth is very important because economic activity influences many aspects, including employment creation, poverty reduction, and government revenue. Moreover, as Amartya Sen notes, growth is not the same as economic development, but it is a means to achieve it.

Growth in Colombia has been declining, even before the coronavirus pandemic. In 2020 it fell substantially to -7.2%; while, in 2021 and 2022, it rose considerably to reach rates of 10.7 and 7.5%, respectively. In these last two years, the high growth is explained, in large part, by expansive monetary and fiscal policies, as well as by the favorable terms of trade and the increase in remittances. However, growth in 2023 was just 0.6%.

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The Bank of the Republic estimated a growth of 1.4% for this year. On the other hand, the government, in accordance with the Fiscal Plan 2024, predicted a growth of 1.5%, but in the Medium Term Fiscal Framework, a document presented on June 14th by the Minister of Finance, Ricardo Bonilla, it was revised upwards and placed at 1.7%. This latter figure, according to him, can be achieved with a gradual reduction in inflation, a more flexible monetary policy and an economic reactivation program to be implemented in the second half of the year.

For its part, the Organization for Economic Cooperation and Development (OECD) believes that Colombia's economic growth will be 1.2% in 2024; the International Monetary Fund (IMF) forecasts 1.1% and the World Bank (WB) 1.3%. This last institution, when reviewing the projections in the first days of June, considered that the 2.2% growth that Latin America achieved in 2023 will be lower this year and it is possible that it could reach 1.8%, to recover in 2025 and reach 2.7%. As for Latin America, this organization argues that these low levels of growth this year and the rebound in 2025 can be achieved to the extent that inflation falls, and interest rates normalize.

The World Bank considers that the world economy will grow at a rate of 2.6%, 0.2 points higher than its estimate at the beginning of the year and expects to reach a growth of 2.7% in 2025.

The figures on economic growth show that the low performance of said variable does not only occur in Colombia but is a global phenomenon. Of course, the case of Colombia is more urgent, which shows that the fact that the Colombian economy will grow by only 0.6% in 2023 is somewhat worrying, given that the most pessimistic forecasts considered that the economy would grow by 1.1%.

According to the National Administrative Department of Statistics (DANE, by its acronym in Spanish), the economy grew by 0.7% in the first quarter of 2024. The sectors most affected in the first quarter were: manufacturing (-5.9%), financial activities and insurance (-3%), information and communication (-1.6%), mining and quarrying (-1.5%), trade, transport and accommodation (-0.8%) and professional and scientific activities (-0.2%). The sectors with notable growth were agriculture (5.5%), public administration, education and health (5.3%) and arts and entertainment (5.2%).

In fact, the low growth in 2023 and in the first half of this year is a cause for concern for both the government and the manufacturing unions. For this reason, Bruce Mac Master, president of the National Business Association of Colombia (ANDI, by its acronym in Spanish), raises the need to join forces to stimulate the economy: “We have reached the point where we must propose a National Pact for Employment, Reactivation, Investment and Prosperity, in which we commit ourselves to do everything in our power to create more jobs, to create equity and job opportunities, and to create the conditions for the economy to function.”

As previously stated, low growth is a global phenomenon, but in Colombia, this situation is more pronounced. The causes of this phenomenon are subject to various explanations. For example, some analysts, including Mauricio Cárdenas, Marc Hofstetter, and Carlos Caballero, among others, attribute the situation to “the lack of confidence that has greatly affected investment.” Cárdenas asserts that investment in Colombia was previously 24% of GDP but has since declined to 17%. He attributes this decline in investment to the government’s persistent rhetoric of reform and change, as well as its criticism of the private sector’s role in various sectors, including infrastructure, electrical energy, health, and pensions. This, he argues, has led to a reduction in private sector investment in these sectors and others that contribute significantly to the creation of formal employment.

In the view of José Antonio Ocampo, the inaugural Minister of Finance of the Petro administration, the decline in investor confidence is essentially attributable to the repercussions of the political crisis. To summarize, the private sector perceives the government’s policies as inadequate. “That is the element of trust.”

Other analysts, including Kalmanovitz, González, and Ocampo, concur that the elevated interest rates set by the Bank of the Republic have had a considerable impact on investment, affording it a greater degree of significance than other factors. Ocampo asserts that the interest rate is a significant factor that affects investment. The other factor is the slowdown in demand, which has been substantial in recent years, particularly in 2021 and 2022. This is due to the expansionary monetary and fiscal policies that have been in place. However, in 2023, this pressure begins to subside.

In light of the undeniable reality of the Colombian economy's deceleration, it is of paramount importance to implement an efficacious economic reactivation program that is capable of achieving the projected growth potential of the economy, which is estimated to be 2.7%. To achieve this, it is essential to establish a national consensus involving the government, academic institutions, the private sector, social organizations, and other key stakeholders. A crucial aspect of this objective is the reduction of interest rates set by the Bank of the Republic. Given the considerable increase in these rates, from 1.75% in August 2021 to 13.25%, it is essential to consider a reduction. By May 2023, that is, in less than two years. This last figure was maintained until December 2023. It is important to note that throughout 2023, the interest rate remained above 12%, with a gradual and relatively slow decrease. In December 2023, the issuing bank reduced the interest rate to 13%. It was only in May of this year that the bank set the interest rate at 11.75%.

It is evident that a high interest rate exerts a considerable influence on both investment and consumption, with the sectors most affected being construction, industry, and commerce. The Board of Directors of the Bank of the Republic posits that, despite the decline in inflation, the rate of decrease has not been sufficient to warrant a more rapid reduction in the interest rate. It would be interesting to ascertain whether inflation in Colombia is determined by demand or supply factors. It is our contention that, in the context of a relatively low level of economic growth and an increase in the unemployment rate, inflation is primarily driven by supply-side factors, with a significant international component.

The need to lower the interest rate in order to stimulate investment and consumption has been a topic of concern not only for the government but also for various production unions, including ANDI, the Society of Farmers of Colombia (SAC, by its acronym in Spanish), the National Federation of Merchants (FENALCO, by its acronym in Spanish), and ASOBANCARIA, among others. At the most recent union convention, bankers were among those who made a statement to this effect. Luis Carlos Sarmiento Gutiérrez, who serves as the president of the Board of Directors of Grupo AVAL, made the following statement: "The Bank of the Republic, of which I have been a respectful observer, is taking an excessive stance in not lowering interest rates." In the event of an inflationary shock, it would be prudent to raise the interest rate once more should the need arise.

Thus, to reactivate the economy, it is necessary to implement a reduction in interest rates and to encourage the production of goods and services in sectors that are intensive in the use of labor. One such sector is construction, which encompasses both buildings and civil works. Construction is a leading sector that promotes other activities, and therefore represents an important area for economic stimulus. It is similarly important to promote plans and programs that stimulate industry, commerce, and tourism, given the potential of these sectors to generate employment and added value.

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How to cite:

Vallejo-Zamudio, L. E. (2024). Economic growth in Colombia. *Apuntes del Cenes*, 43(78). Págs. 11 - 14. <https://doi.org/10.19053/uptc.01203053.v43.n78.2024.17963>



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Economic growth in Colombia

El crecimiento económico en Colombia

Apuntes del Cenes

vol. 43, no. 78, p. 11 - 14, 2024

Universidad Pedagógica y Tecnológica de Colombia (UPTC),

ISSN: 0120-3053

ISSN-E: 2256-5779

DOI: [https://doi.org/10.19053/
uptc.01203053.v43.n78.2024.17963](https://doi.org/10.19053/uptc.01203053.v43.n78.2024.17963)