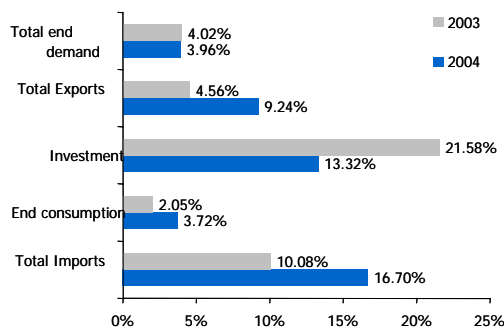


Medellín, Friday April 22, 2005

## 1. GROWTH

Recently, the DANE statistical agency revealed the 2004 growth rate for 2004, which exceeded market expectations, following the low growth recorded in the third quarter of last year. The reading for 2004 was 3.96%, whereas the average expectation had been 3.80%. Nonetheless, the growth rate was below the 5.53% Latin American average (not including Venezuela and Uruguay, which grew above 10%).

### GDP Growth According to Demand Components



Source: DANE

When breaking up the overall growth performance, the increase in consumption stands out, as it virtually doubled that of 2003 by expanding at 3.7% and thus exceeding the average since 1995: 2.8%. This result reflects the slack monetary conditions that the Central Bank has implemented and the now enhanced confidence among consumers. Investment also remained dynamic by growing at 13.3%, although it slowed its pace from last year's, when it expanded at 21.6%.

Meanwhile, the 14% appreciation in the local currency during 2004 left its traces on foreign trade, as imports expanded at a rate of 16.7%, while exports grew 9.2%. This difference had a negative contribution to the aggregate demand, and it poses a risk for 2005, given that demand for foreign products may displace domestic demand.

Separately, the national unemployment rate stood at 14% in February, a reading equivalent to a year-on-year reduction of 1.4%. In the meantime, for the thirteen largest cities, the jobless rate was 15%, falling 1.0%. The number of unemployed persons increased by 268 thousand, while underemployed decreased by 173 thousand.

Finally, it is worth mentioning that the good outlook remains in effect for 2005 economic growth in Colombia.

In recent days, the IMF revealed its growth expectation of 4% for 2005 and 2006, while the CEPAL projects 3.5% for the same years. CORFINSURA and SUVALOR maintain their outlook of 3.5% for the rolling year.

## 2. INFLATION

### Consumer Price Index (CPI)

Inflation ended the first quarter at 5.03% and thus it accumulated a 47-bp reduction since December 2004. In the year to date, the CPI records a 2.64% change, the lowest quarterly advance in history. This outcome increases the probability of meeting the Central Bank's specific target for this year at 5.0%.

Appreciation in the local currency continues to favor inflation through two different channels: 1) lower pressures on production costs as the growth in prices of imported raw materials slows down, and 2) the negative or barely positive change in prices for items such as home appliances, shoes, automobiles and other imported goods. In relation to this, it is worth noting that March's inflation in tradable goods stood at 4.12%, whereas the year-ago reading had been 5.62%.

As for the non-food inflation, it accumulated a 70-bp fall in the first quarter to end March at 4.82%, which is also the lowest level since November 2002. Rising pressures over inflation during the first quarter came from the transport and food groups, which contributed 1.74% of the 2.64% inflation accumulated during the period.

For April, CORFINSURA and SUVALOR project a monthly change in the CPI of 0.52%, and that would lead to a slight rebound of 7 bps in the 12-month inflation, from 5.03% to 5.10%. The average expectation for the monthly change, according to the survey of expectations that the Central Bank conducts, is 0.60%, which would mean an annual change of 5.18%.

### Producer Price Index (PPI)

Contrary to what happened with the CPI, the first-quarter PPI recorded a rebound, albeit moderate: 29 bps, to end March at 4.97%. Likewise, the 2.48% accumulated change in the first quarter was higher than that observed in the same period of 2004: 2.20%.

According to the use or economic destination of the goods that make up the PPI, a notable decline is observed in the annual growth rate of prices for construction materials, which fell from 6.15% in February to 4.87% in March. Nevertheless, deserving attention is the rebound in prices for end consumer goods, which stood at 5.05% annual, the highest level since April 2004.

### 3. FINANCIAL SECTOR

Recovery in the sector prevails. Proof of that is in the fact that for 2004, financial institutions reported earnings nearing COP\$3 trillion, and in the first two-month period of 2005, those earnings exceeded COP\$560 billion, by growing at a year-on-year rate of 12.7%.

Financial institutions have fulfilled their pledge to the government of increasing micro-sized loan granting. This portfolio now rises to COP\$1.8 trillion, an amount without precedents and much higher than expected.

Moreover, the rising trend in the financial system's loan portfolio remains throughout 2005, by accumulating an annual growth of 13.4% from the first quarter of 2004.

Hence, with partial data as of February, demand for consumer credits showed a real increase of 25% from the same period in the year ago, as an evidence of the good conditions of internal demand. The mortgage loan portfolio keeps declining, while the past-due loan indicators for the system remain stable.

This is considered good news for the economy. For as long as the economic system counts on a healthy financial sector, there are more possibilities of delivering credit. That should facilitate a more dynamic growth and greater possibilities for job generation.

### 4. INTEREST RATES

Good liquidity conditions characterized the overnight bank lending market throughout the first quarter of 2005, thereby favoring the stability observed in the cost of funding. The overnight bank-lending rate continues to decline at the rhythm of the ample cash availability, and remains at around 15 bps below the key interest rate of the Central Bank, which lingers at about 6.50%.

The aforementioned goes in line with the decision that the Board of the Central Bank made on Friday, April 22, of keeping its key short-term rates on hold, although it highlighted the minimum levels that inflation had reached.

In the first three months of 2005, the benchmark rate on 90-day borrowings has recorded a 46-bp drop. By the closing date of this report, the 90-day DTF had hit a new all-time low at 7.25%, although the amounts borrowed for all lengths did not show any major variations from the earlier month's average. The

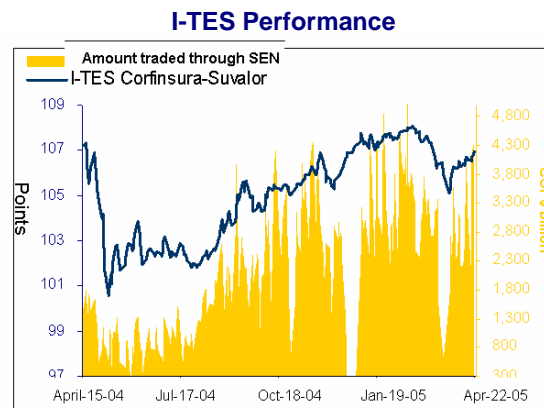
abundant liquidity available to the financial system has discouraged rises in borrowing rates for all terms, given the lower cost of resources.

Separately, the slack and stable monetary conditions prevailed throughout March. For a third consecutive month, the overnight bank-lending market ended with an ample supply of local cash. In fact, in the absence of rising pressures on the overall level of prices, no increases are expected either for Central Bank's rates or for those of the market in general.

### 5. GOVERNMENT DEBT PRICES

#### Domestic Government Debt

Even though the representative index of government debt by CORFINSURA and SUVALOR, the I-TES, recorded a 1.71% value loss in March, so far in April it has recovered to reach a 0.89% rebound. Consequently, in the year to date, the index has depreciated by 0.23%. When including the coupon, however, it accumulates a positive change of 2.27%. The volume of trades so far in 2005 stands at COP\$3.2 trillion on a daily average.



Source: SEN, CORFINSURA and SUVALOR.

As for the primary market, during March Public Credit issued TES totaling COP\$3.18 trillion, with the purpose of obtaining the necessary resources to perform the purchase of US\$1.25 billion in foreign reserves, resources that were used in paying in advance, on April 4, a loan that the IADB had granted to Colombia.

Between January and April, Public Credit was able to execute 46.2% of the placement target established for this year at COP\$27 trillion, including the COP\$3 trillion used in buying foreign reserves. As for the auctions, the placement stood at 38%, which is a very favorable outcome, considering that this result (COP\$3.6 trillion) was

obtained in only five auctions of fixed income TES and two of UVR TES.

From the local point of view, news developments in April continued to be favorable to the domestic government debt. Namely, it became known that the fiscal deficit of the central government had stood at 0.7% of GDP, after declining 0.1% from the result observed in January 2004, boosted by the 22% growth in tax collections.

Additionally, the decline in inflation during the first quarter, which allowed for maintaining a slack monetary policy, was also an upside. Finally, the passage of the pension reform bill through its fifth debate in Congress was also news that investors welcomed.

#### **External Sovereign Debt**

On average for the past month, prices for Colombian sovereign debt bonds declined by 0.8%. Meanwhile, the Colombia EMBI+ widened 4.4% to end April 21 at 404 points. It was, however, a month of high volatility, given the changing outlook for growth and inflation in the U.S.

Initially, on March 22, the Federal Reserve deployed another 25-bp hike in its key interest rate – raising it from 2.50% to 2.75%– and also it pointed out its concern about inflationary pressures building up within the near term. This circumstance led to a rise in yields on the 10-year U.S. Treasury, which climbed from 4.45% before the meeting to 4.64% after it had been held.

Separately, towards the middle of April, with the release of minutes from the Fed's meeting of March 22 and with disappointing earnings results of bellwether companies in the U.S., such as General Motors and IBM, which reported profits below expectations, fear resumed of a slowdown in the pace of growth in the U.S. Accompanied by a stronger inflation, such a slowdown would not be a good scenario for emerging economies. Consequently, yields on 10-year Treasuries declined to levels of 4.20%, but that did not reflect in a greater demand for Colombian bonds.

Notwithstanding those conditions, a favorable news development for Colombian bonds was the recommendation that JPMorgan issued, in which the said bank advised its clients increasing their exposure to Colombian bonds. Their rationale is that Colombian debt was more severely hit by March's price falls, and that it has not recovered at the same rhythm that other countries in the region have.

The latter contributed to the upbeat mood that the economic growth rate and the approval of the pension reform bill in its fifth debate (out of eight necessary for its congressional passage) generated, but during the past week, that had just started to reflect on prices of external sovereign debt.

## **6. FOREIGN EXCHANGE RATE**

After four consecutive months on a declining trend, the average foreign exchange rate recorded a 0.56% rebound in March to reach COP\$2,353.71. This situation is a reflection of the 2.06% depreciation in the local currency, recorded as the change observed between the closing quotations for March (COP\$2,377) and February (COP\$2,329). In the year to date, however, the dollar quotation shows a nominal appreciation of 0.56%.

Even though the local economic news items released during the month favored the continuation of appreciation in the Colombian peso, uncertainty abroad generated a currency-weakening pressure that prevailed throughout the third month of this year.

Despite the encouraging fiscal outcome for last year (deficit of 1.2% of GDP) and the fact that the 3.96% economic growth rate for 2004 outperformed expectations (3.8%), restlessness originating abroad in view of inflationary pressures building up in the U.S. favored the strengthening in the dollar against Latin American currencies in March. A surging inflation in the U.S. might promote a faster pace of increases in Fed's rates. This juncture fostered depreciation in major currencies of the region: the quotation against the dollar of the Brazilian real increased by 3.54%; of the Chilean peso, by 1.97%; and of the Mexican peso, by 0.71%.

The uncertainty reflected in the performance of the foreign exchange market in March led it to be a month of records: on March 16, the greatest intraday volatility for the year so far was observed: COP\$48; on the 28th, the dollar quotation against the Colombian peso hit its maximum level since 2005: COP\$2,407.20; and finally, on the 30th, the volume traded reached the largest figure in history: US\$919 million. Nonetheless, so far in April, fears concerning U.S. economic growth weakened the dollar and made its local price resume levels of COP\$2,340, more than COP\$30 below the closing rate for March.

In other news, early in April the Central bank revealed the results of the balance of payments for 2004.

Deserving mention in relation with the 2004 balance of payments is the fact that the current-account deficit totaled US\$1.11 billion, equivalent to 1.1% of GDP (US\$3,385 million). The change in gross international reserves was positive by US\$2,541 million.

Meanwhile, the trade balance recorded a US\$1,134-million surplus, while the foreign trade of

non-factorial services (i.e. transports and travels, insurance, financial and entrepreneurial services) reached a US\$1,725-million deficit. Likewise, the return on factors experienced a US\$4,185-million deficit, primarily explained by greater repatriation of earnings and dividends by companies with foreign capital. Nonetheless, the trade surplus and the inflow of foreign currency from remittances by workers living abroad totaling US\$3,170 million allowed offsetting the deficits in non-factorial services and in the return on factors.

Also deserving highlight is the US\$2,647-million growth in the capital and financial account to total US\$3,385 million, which allowed financing the current-account deficit. This outcome is mainly the result of the 53% growth in direct foreign investment, from US\$1,793 million to US\$2,739 million, and the decline in Colombian investment abroad, from US\$938 million in 2003 to US\$142 million in 2004.

Finally, between February 25 and April 01, an operation was conducted of selling US\$1.25 billion in foreign reserves from the Central Bank to the government. With the proceeds from this operation, advanced payment was performed of a US\$1.25-billion loan from the IADB, which had been contracted in 1998. This prepayment will allow for fiscal savings of US\$313 million in 2006, US\$625 million in 2007 and US\$313 million in 2008, on account of amortizations. This type of operations makes it possible for the country to reduce its vulnerability to sudden changes in the foreign exchange rate.

#### **Real Exchange Rate Index – ITCR (Trade-weighted)**

The trade-weighted competitive rate (ITCR) for March stood at levels of 116.32 points, equivalent to a 9.04% year-on-year appreciation. So far in 2005, the index continues to record the same trend of the nominal foreign exchange rate, so that it accumulates a 1.47% appreciation for the first quarter. Nevertheless, the exporting sector remains dynamic, providing evidence of the fact that the current competitiveness levels have not had any considerable impact on the overall performance of the exporting sector.

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