Euler Hermes Economic Research

Country Risk Analysis

Colombia

Commodity-led

General Information

GDP	USD333,4bn (World ranking 31, World Bank 2011)
Population	46.93 million (World ranking 27, World Bank 2011)
Form of state	Republic
Head of government	Juan Manuel SANTOS Calderon
Next elections	2014, presidential

Strengths

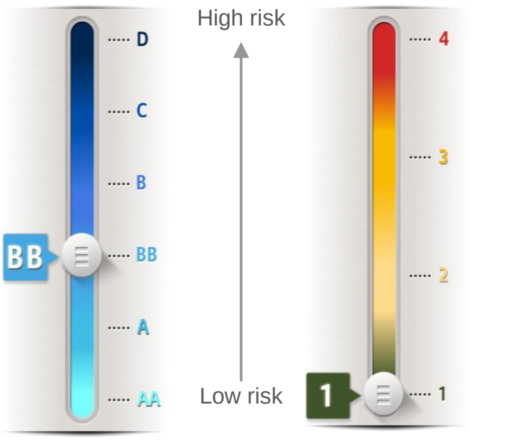
- Natural resource base (agricultural, energy and minerals)
- Strong medium-term growth
- Pro-business, sound macro-policy framework.
- Strong external balance
- Support from IFIs very likely if needed
- Structural Business Environment above average
- Durable political framework, with stable handovers of power

Weaknesses

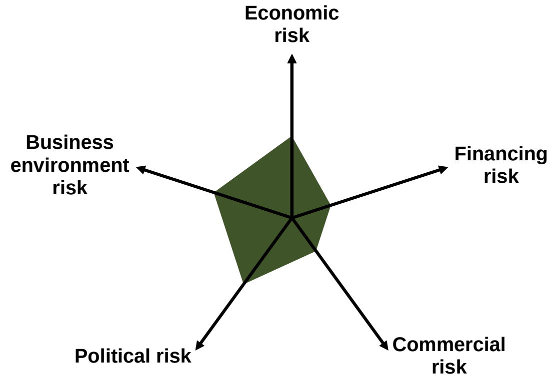
- Sensitive to commodity price fluctuations and US business cycle
- ST pressure on real exchange rate from capital inflows
- Difficult security situation with long running domestic insurgency and drug trafficking (frequently interlinked)
- Skewed income distribution, high poverty levels
- Rule of Law and control of corruption are below average

Country Rating BB1

Country Grade **Country Risk Level**



Risk Dimensions



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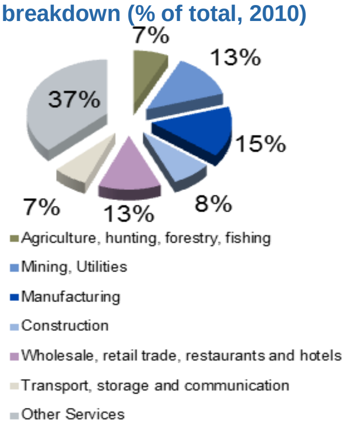
Economic Structure

GDP breakdown (% of total, 2010)



Trade structure (% of total, 2010)

By destination/origin

Exports		Rank		Imports
United States	40%	1	29%	United States
Other America	9%	2	12%	China
China	5%	3	9%	Mexico
Ecuador	5%	4	6%	Brazil
Venezuela	4%	5	4%	Germany

By product

Exports		Rank		Imports
Crude Oil	34%	1	7%	Refined Petroleum Products
Coals	14%	2	6%	Cars And Cycles
Other Edible Agricultural Prod	9%	3	5%	Basic Organic Chemicals
Refined Petroleum Products	6%	4	4%	Plastic Articles
Non-Monetary Gold	4%	5	4%	Construction Equipment

Sources: Chelem, UnctadStat, IHS Global Insight, Euler Hermes

Economic Forecast

	Average 2000-08	2009	2010	2011	2012	2013f	2014f
GDP growth (% change)	4.2	1.7	4.0	6.6	4.0	5.0	5.5
Inflation (%, end-year)	2.6	0.3	2.1	4.7	2.4	2.5	3.0
Fiscal balance (% of GDP)	-1.7	-2.8	-3.3	-2.0	0.2	-1.0	-0.9
Public debt (% of GDP)	38.7	36.1	36.5	35.8	32.8	32.0	31.2
Current account (% of GDP)	-1.3	-2.1	-3.0	-2.8	-3.1	-3.2	-3.3
External debt (% of GDP)	31.0	23.1	22.6	22.6	21.3	21.0	21.4

Sources: IHS Global Insight, National sources, Euler Hermes

Economic Growth

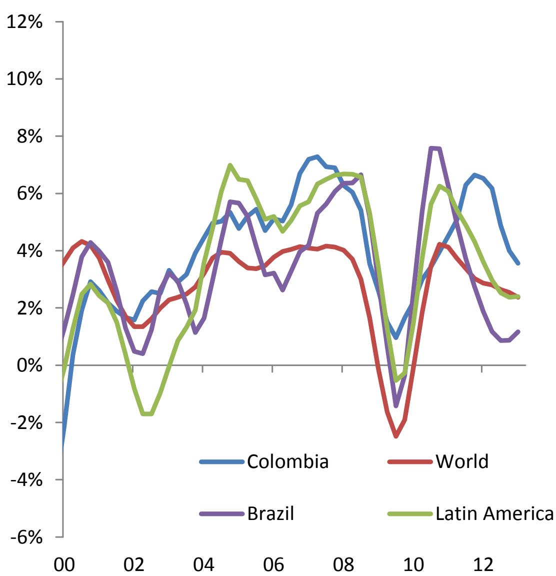
Commodity based growth

Medium-term growth has been strong over the past ten years with an annual average increase in per capita GDP of 3.5%. Long a commodity producer, with the development of oil, petroleum and coal together account for 65% of exports. Coffee, ferro-nickel, gold and flowers account for another 12%. While sensitivity to commodity prices has boosted economic growth in recent years, it also leaves the economy vulnerable to falling prices. As 40% of exports go to the US, the economy is also sensitive to the US business cycle. Although per capita GDP has increased strongly, poverty levels remain high, income distribution poor and unemployment is above 10%.

More moderate but still robust gains in 2013-14

Annual growth will moderate in 2013 to 3.5% before picking up to 4% in 2014, though most of the slowdown came in H2 2012 and Q1 2013. Near-term growth will continue to be driven by domestic demand, as both private consumption and fixed investment remain robust. The net export contribution will remain negative, reflecting a strong increase in imports, though this is mirrored by buoyant FDI inflows, underpinning overall economic expansion. The risk to growth, however, is to the downside as commodity prices adjust to weaker demand growth.

GDP growth (y/y, 4 qtrs cumulated %)



Sources: IHS Global Insight, Euler Hermes

Economic Policies

Policies are generally prudent reflected in moderate fiscal deficits, lower inflation in recent years and a strong external balance. Overall sound policies have been reflected in Colombia's eligibility for an IMF FCL, another of which is currently under discussion. This precautionary credit line, which is free of conditionality, is granted only to the strongest economies. Medium-term policy continues the Productive Transformation Programme, a public-private initiative that seeks to promote growth and competiveness in higher value-added sectors. More specifically the current administrations' policies focus on infrastructure, agriculture, mining, housing construction and technological innovation.

Inflation easing, cautiously accomodative monetary policy

Monetary policy is framed against inflation targeting, currently set at 2-4%. Inflation eased steadily through 2012 falling below the lower bound of the target range in February and March 2013 and was 2% y/y in April. While inflation is likely to pick up, it should end 2013 around the mid-point of the target range. With quarterly GDP growth slowing, inflation also easing and amid exchange rate appreciation, the central bank began to ease monetary policy in mid-2012, cutting the policy interest rate from 5.25% in July to 3.25% in March 2013. The policy rate was left on hold in April. Credit expansion remains very strong. The real effective exchange rate also remains overly strong, as capital inflows have strengthened the nominal exchange rate despite official intervention and measures to stem short term inflows.

Bank lending to the private sector remains very strong, but banking system indicators are robust. Tier 1 capital ratios are 15%, non-performing loans are 3% and fully covered by provisions and the net open FX position is not threatening.

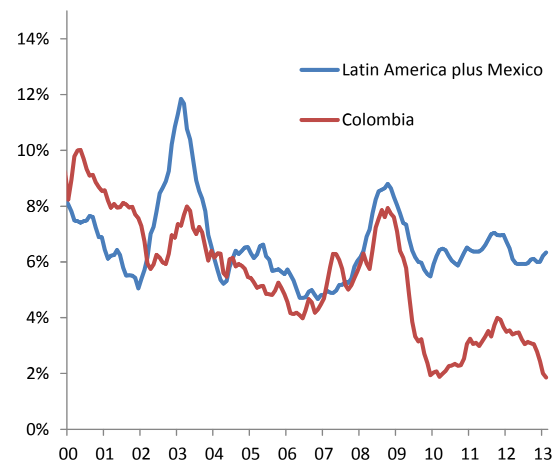
Sound near-term fiscal position, strengthened sustainability

The general government balance swung into small surplus of 0.2% of GDP in 2012 with a primary surplus of 1.9%. Importantly, revenues of the non-financial public services increased by 1.75pps of GDP during 2010-2012 and expenditures were flat. The overall balance will probably return to small, but manageable deficit of around 1% of GDP in 2013.

The central government, however, has a deficit and the overall surplus is generated by public sector entities. In order to strengthen fiscal sustainability the government has passed a number of important measures including a Fiscal Responsibility law, to improve management of "windfall" gains from booms and control expenditure and a reform aimed at improving revenues from mining royalties.

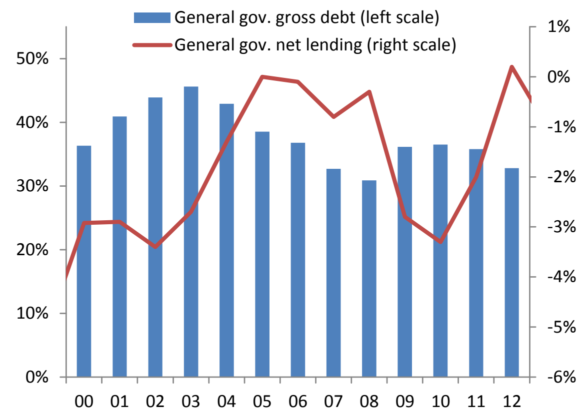
The public debt-GDP ratio is low at 32.8% at end-2012 and is on a downward trend.

Inflation (% y/y)



Sources: IHS Global Insight, Euler Hermes

Fiscal balance and debt (% of GDP)



Sources: IHS Global Insight, Euler Hermes

External Sector

Moderate current account deficit and strong FDI flows

The current account balance is in moderate deficit, at -3.1% of GDP in 2012 (after -2.8% in 2011 and -3.1% in 2010. The deficit is likely to widen slightly in 2013 and 2014 to -3.2% and -3.4% of GDP, as commodity prices stabilise. Inflows of services and transfers are relatively small, but outflows of profits and dividends have risen markedly.

FDI inflows have strengthened, particularly with the development of the oil sector (58% of FDI) and in 2012 net flows were 60% higher than before the global financial crisis. Net FDI flows more than covered the current account deficit in 2012 and are likely to do so in 2013-14 as well, limiting the need for debt financing.

Importantly from a financing perspective Colombia has had access to an IMF FCL, a precautionary credit line given only to economies with sound policies and sustainable debt indicators. The government is close to concluding another FCL.

Moderate external debt

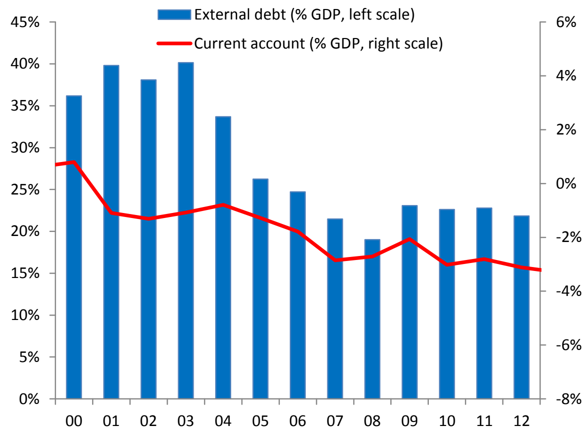
External debt is moderate. External debt is 21% of GDP, 109% of exports of goods and services and interest payments are 5.8% of exports of goods and services.

Foreign exchange reserves increase

Foreign exchange reserves have increased steadily and cover a comfortable 6.5 months imports of goods and services and 180% of external debt falling due (including ST) in 2013. M2 as a proportion of FX reserves, however, is on the high side.

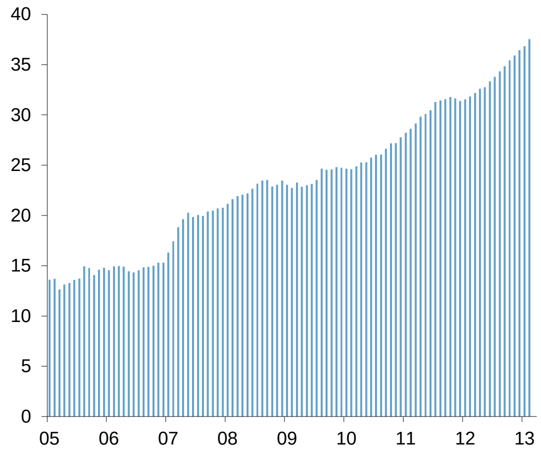
Overall, the external balance is sound.

Current account and external debt (% of GDP)



Sources: IHS Global Insight, Euler Hermes

FX reserves (USDbn)



Sources: IHS Global Insight, Euler Hermes

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