Economic Research Department

BBVA

Colombia

GDP Observatory

September 30, 2009

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Economy shrinks 0.5% yoy in first half of the year

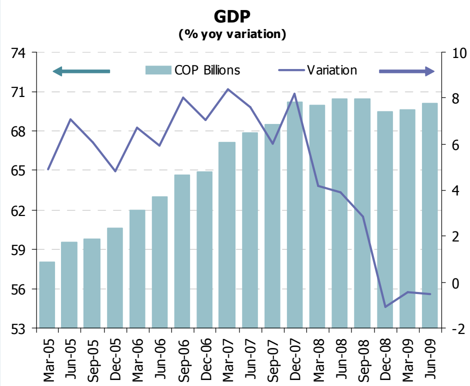
- 2Q09 GDP growth was in line with latest market forecasts (-0.5% yoy).
- There was a major adjustment in domestic demand, especially in investment, compensated by a fall in imports.
- The fall in exports sharpened in the 2Q09, especially due to the worse performance in leather goods, textiles and transport equipment.
- The construction sector and mining continued to be the engines of economic activity.
- The performance of public spending in investment for the first half of the year was better than expected by the BBVA ERD, eliminating one of the main sources of uncertainty.

According to recent DANE data on second quarter GDP growth, Colombia's economy saw a 0.5% yoy fall for the period. Recent market and BBVA ERD forecasts had anticipated the result by taking into account the better performance in civil works in June, but the figure was a positive surprise in comparison to earlier forecasts. Over the year, output saw positive qoq changes in March and June after seeing a 1.4% qoq fall between September and December 2008.

The lower present economic output is mainly linked to the adjustment in domestic demand resulting from lower private investment levels. Gross fixed capital formation not including civil works decreased 14.7% yoy in 2Q09, with major falls in machinery and transport equipment purchases. Investment in civil engineering increased 40.6% yoy as a result of the advances in roads, ports and mining related construction. Taking this increase in investment into account, the fall in fixed investment comes in at only 2.2% yoy.

Private consumption continued to see modest falls, sustained in part by the moderate growth in real public spending. The monetary policy which cheapened credit and limited growth in the debt burden of households lessened the effects of the external shock on consumer confidence and the impact the worsening labor market had on disposable income.

Weak domestic demand was also part of the major reduction in imports, seeing a larger than expected fall over the quarter. In this sense, the fall in investment demand corresponded to a lower external purchase rate for capital goods and transport equipment. In turn, exports accelerated their fall in the 2Q09 (but at a lower rate than imports), mainly as a result of the lower sales of non-traditional products (leather, textiles, clothing and cars). In this way, net foreign demand contributed positively to quarterly growth (1.8%), offset in part by the major fall in domestic demand (-2.1% yoy) leading to a negative contribution of the latter (-2.3%).



GDP per demand (%, Year on year variation)			
	1Q09	2Q09	1S09
Final Consumption	-0.3	-0.3	-0.3
Private Consumption	-0.5	-0.7	-0.6
Public Consumption	0.3	0.9	0.6
Gross investment	-3.7	-7.3	-5.5
Fixed investment	-1.9	-2.2	-2.0
Domestic demand	-1.1	-2.1	-1.6
Exports	2.0	-5.7	-1.8
Imports	-1.5	-9.7	-5.6
GDP	**-0.4**	**-0.5**	**-0.5**

Source: DANE BBVA ERD

GDP per supply (% Year on year variation)			
	1Q09	2Q09	1S09
Agriculture	-0.7	-1.8	-1.2
Mining	11.0	10.2	10.6
Energy	0.3	0.1	0.2
Manufacturing sector	-7.6	-10.2	-8.9
Construction	-1.4	16.8	7.7
Trade	-2.6	-3.9	-3.3
Transport	-1.0	-1.2	-1.1
Financial	4.9	4.3	4.6
Social services	1.1	0.5	0.8
Taxes	-4.3	-5.2	-4.7
GDP	**-0.4**	**-0.5**	**-0.5**

Source: DANE BBVA ERD

The manufacturing output and commerce sectors saw the biggest falls over the quarters in both yoy and qoq terms. These two sectors represent 26% of national production and contributed -2.0% yoy to the second quarter growth figure.

In turn, civil engineering construction and mining continued to be the most dynamic sectors, thanks to higher public investment and the increase in extraction capacity, the fruits of growing overseas investment in recent years. These two sectors contributed 1.6% yoy to second quarter growth.

Colombian economy bottoms out in the first half of the year

Public spending in investment over the first half was better than anticipated by the BBVA ERD, eliminating one of the main sources of uncertainty in our growth scenario for 2009. The increase in civil engineering led to positive qoq growth over the period. If this trend continues into the second half of 2009, there could be major yoy growth in December, especially in comparison to the low-end statistics for output seen in the fourth quarter of 2008.

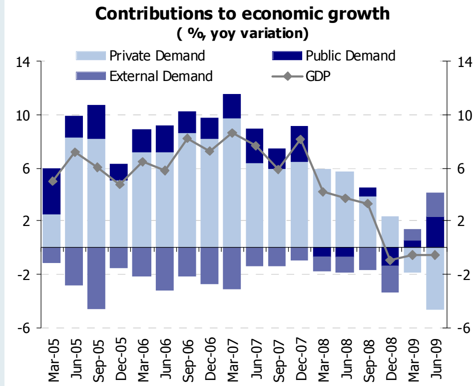
In turn, household consumption will recover slowly as the labor market continues its downward march over the coming quarters due to its characteristic lag behind economic output. In addition, the full impact of the interest rate reductions by the BanRep will only be felt in 2010, when transmission to market rates finalizes. In turn, public spending has major fiscal limits this year and next due to lower tax receipts. This means real consumption will remain at similar levels to those at present.

The economic investment rate stabilized over the last two quarters at around 26% of GDP, almost two points below the previous year's level. Nonetheless, in the 2Q09 investment saw positive qoq growth (1.1%) above that reported for GDP (0.7% qoq) due to the advance in civil engineering. The adjustment in machinery and equipment investment will continue in the second half of the year, although recovery in business confidence levels and the fall in inventories may coincide with better investment performance in the first quarter of 2010.

Manufacturing and commercial output shows signs of recovery. For the first time since 2007, manufacturing output in July saw growth at 0.2% mom (seasonally adjusted). This could lead to positive yoy changes for manufacturing in the second half of the year. In turn, although they continue to decline (mom, seasonally adjusted) retail sales are close to presenting zero-change rates (mom); this points to better retail performance in the second half of the year.

However, commercial restrictions in Ecuador and Venezuela, growth results and the impact on the country's overseas sales continue to be the greatest risks for commerce. This will mean a slow recovery in non-traditional and manufacturing exports for the rest of the year.

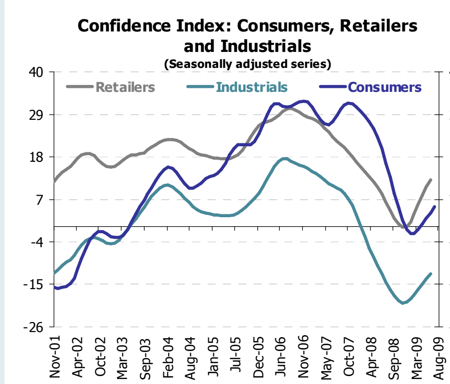
In short, the good growth results over the first half of the year and the forecasts for civil engineering advances, the second half of 2009 point to this year's growth coming in above our earlier forecast (-0.5% yoy) at a near-zero level.



Source: DANE and BBVA ERD calculations BBVA ERD

Consumption and Investment (Year on year variation %)			
	1Q09	**2Q09**	**1S09**
Final household consumption	**-0.4**	**-0.7**	**-0.6**
Nondurable goods	-1.5	-2.0	-1.7
Semi-durable goods	-2.5	0.4	-1.1
Services	1.9	1.1	1.5
Durable goods	-7.3	-7.2	-7.2
Gross fixed capital formation	**-1.9**	**-2.2**	**-2.0**
Machinery and equipment	2.9	-18.4	-8.1
Transport eq.	-17.3	-16.0	-16.7
Construction and buildings	-14.3	-10.8	-12.5
Civil engineering	9.7	40.6	25.3
Other	0.9	-0.2	0.4

Source: DANE BBVA ERD



Source: Fedesarrollo BBVA ERD