Capital inflows to Emerging Markets

XV Meeting of Monetary Policy Managers
CEMLA-September 2019
Santo Domingo
Higher global uncertainty and lower GDP growth

World Trade Uncertainty index (weighted by GDP-PPP)

[Diagram showing the World Trade Uncertainty index with data points from 1996q1 to 2018q4.]

Source: IMF and own calculations.

World GDP forecast (2019-2020) (percentage of change)

[Bar chart showing GDP forecast for 2014 to 2019 with data for 2019q1 to 2019q4.]

Source: IMF
A more expansionary monetary policy in advanced economies

Fed fund rate (Forecast –September 2018)

Fed fund rate (Forecast –September 2019)

Capital inflows to emerging markets

Higher liquidity and lower interest rates in AE

Idiosyncratic factors in EM

Higher uncertainty

Foreign Investment Flows
Emerging markets (Billions of U.S. dollars)

Source: IIF.
Volatility of the international financial markets have affected some emerging economies. However, investors have recognized the soundness of Colombian macroeconomic policy framework and the orderly adjustment to shocks in previous years.

Source: Bloomberg
Capital inflows to Colombian economy have remained broadly stable. Foreign direct investment (FDI) has been the main source of external financing.

Composition of foreign capital inflows
(Percentage of GDP)
Colombian Policy Framework

XV Meeting of Monetary Policy Managers
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Policy Framework affords to cushion external shocks

Inflation targeting

- Maintaining a low and stable inflation rate
- Reducing the gap between GDP growth and its “potential” level.

Flexible exchange rate.

- Independence of monetary policy
- Mitigates the response of economic activity to external shocks

Exchange rate flexibility is the first line of defense. The successful of “floating” is due to:

- Limited currency mismatches
- A credible monetary regime
- External buffers (international reserves)
- Sound and robust financial sector

Nominal exchange rate
COP/USD

- Sep-13
- Mar-14
- Sep-14
- Mar-15
- Sep-15
- Mar-16
- Sep-16
- Mar-17
- Sep-17
- Mar-18
- Sep-18
- Mar-19
- Sep-19

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<th>2500</th>
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 Colombian external funding has been mostly FDI. Portfolio investment has increased but mainly in public debt (LCU). Aggregate currency mismatches in Colombia are lower than the average of countries with negative NFA*.

**Total net foreign assets**

<table>
<thead>
<tr>
<th>Year</th>
<th>Colombia (NFA)</th>
<th>All countries (Average of total NFA) a/</th>
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</thead>
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**Total net foreign assets excluding direct investment**

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<th>Year</th>
<th>Colombia (NFA excluding DI)</th>
<th>All countries (Average of NFA excluding DI) a/</th>
<th>Countries with negative NFA excluding DI (Average) b/</th>
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</table>

*Source: IMF*

b/ 76 emerging and advanced economies reporting NFA excluding DI (around 100% of GDP to -100% GDP)
Well anchored Inflation Expectations in Colombia

Expectations Implicit in Government Bonds (TES of 2 years)
(Percentage)

Source: Banco de la República.
A sufficient level of external buffers provides another safeguard against external shocks. The Flexible Credit Line (FCL) by the IMF has complemented the accumulation of international reserves.
Discussion topics

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What is the impact on MP in EM of lower natural interest rate in AE and lower premium risks in EM?

Natural Rate of Interest
(percentage)

CDS Emerging Markets


Source: Bloomberg
What is the impact of lower international interest rate on macroeconomic imbalances in EM?

### External Debt
**Latin America and the Caribbean**
(percentage of GDP)

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### Fed fund rate
(Forecast –September 2019)

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<th>Futuros</th>
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