S&P Global Ratings (/en_US/web/guest/home)

Colombia 'BBB-/A-3' Foreign Currency Ratings Affirmed; Outlook Remains Negative

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Overview

In the context of the pandemic, Colombia is going through a severe economic contraction, resulting in an increase in the government's debt burden and a weak external profile.

The outlook for effective fiscal consolidation after the pandemic recedes is uncertain despite the government's commitment to tax reform and other budgetary measures.

We are affirming our 'BBB-/A-3' foreign currency and 'BBB/A-2' local currency sovereign credit ratings on Colombia.

The negative outlook reflects the risk of a downgrade because of potentially low economic growth and inadequate fiscal adjustment that fails to stabilize and then alleviate the sovereign's rising debt burden, thereby weakening its public finances.

Rating Action

On Oct. 28, 2020, S&P Global Ratings affirmed its 'BBB-' long-term foreign currency and 'BBB' long-term local currency sovereign credit ratings on Colombia. The outlook on our long-term ratings remains negative. We also affirmed our 'A-3' short-term foreign currency and 'A-2' short-term local currency ratings.

Outlook

The negative outlook reflects the risk that a sharp economic contraction this year and only moderate economic recovery in 2021 could erode the sovereign's financial profile. We expect that the government will take measures to contain future fiscal deficits as the impact of the pandemic recedes. However, the weakening of public finances may persist longer than we expect, resulting in a downgrade.

Downside scenario

We could downgrade Colombia over the coming year in the event of prolonged poor economic performance and inadequate fiscal adjustment that fails to stabilize and then alleviate the sovereign's rising debt burden. Net general government debt is projected to exceed 60% of GDP in 2021, up from around 44% in 2019. A persistently higher debt burden would raise Colombia's vulnerability to adverse external shocks that could worsen its external liquidity position.

Upside scenario

We could revise the outlook to stable within the next 12-18 months if the government undertakes steps to stabilize the economy, sustain GDP growth prospects, and strengthen fiscal policy. Under such a scenario, the recent rise in the sovereign's debt burden would be stabilized and then reduced to alleviate the recent worsening of public finances and to contain risks to external liquidity.

Rationale

Our ratings on Colombia reflect its stable democracy and political institutions that have sustained predictable economic policies and cautious macroeconomic management for many years, despite several economic shocks. We expect continued pragmatism in economic policies from both the Congress and the administration in handling the economic consequences of the pandemic, including steps to sustain long-term economic growth prospects and to address recent weakening of public finances.

Our ratings also reflect Colombia's flexible exchange rate and monetary policy flexibility, which remain a key economic buffer against external shocks. Our ratings on Colombia are constrained by its high external debt and volatile terms of trade. However, these risks are mitigated by the external assets of Colombia's private-sector pension funds, as well as the government's access to a recently extended credit line from the IMF.

Institutional and economic profile: A severe economic contraction and an important policy response

We expect the economy to contract by 8% in 2020 and then grow 5.5% in 2021.

There is a risk that the pandemic could lower the country's long-term growth prospects.
The administration's limited political room to maneuver amid the pandemic could constrain its ability to gain enough support in Congress to pass a meaningful tax reform in 2021.
We expect an economic contraction of 8% in 2020 due to the pandemic, economic lockdown, and lower oil prices. As demand recovers, we expect an economic rebound of 5.5% in 2021 and average growth of 4% during 2022-2023. As a result, Colombia is likely to regain its pre-COVID-19 output level only by late 2022. GDP per capita is likely to drop to US$5,500 in 2020 because of economic contraction and currency depreciation. As growth resumes and the exchange rate stabilizes, we expect GDP per capita will trend toward US$6,600 by 2023.

Colombia has used countercyclical fiscal and monetary policies to cope with the consequences of the pandemic. The government created an Emergency Mitigation Fund (FOME, Spanish acronym) and allocated 3% of GDP to it. The fund will provide resources to the health system, give cash transfers to the poorest segments of the population, and give payroll subsidies to companies. Colombia also capitalized its National Guarantee Fund (FNG, Spanish acronym) with 0.3% of GDP, which can be leveraged to 8% of GDP, in an effort to prevent credit disruption. The guarantees are mostly extended to small and midsize enterprises. The government is also providing value-added tax (VAT) refunds to around 1 million families in the poorest population segments.

The central bank cut its policy interest rates to historical lows and created new liquidity lines for the financial sector. The central bank also intervened briefly in the foreign exchange market to stabilize the movement in prices, and purchased some sovereign debt to stabilize domestic financial markets. Such interventions were temporary, and they did not seek to target the exchange rate or sovereign bond yields in the local market.

The Colombian political system has broadened in recent years to include a wider range of politicians and parties, including demobilized guerrilla members of the FARC. However, politics are anchored by relatively strong political parties, and by a history of stable economic policies. The coordinated fiscal and monetary policy response to the pandemic is consistent with the country's record of policy pragmatism and consensus across party lines.

The administration has become more effective recently in dealing with Congress, gaining more cooperation from political parties that had earlier felt excluded from the government's decision-making process and its patronage. However, the recession and pandemic may exacerbate latent social tensions in the country. That, plus the administration's limited political capital, could constrain its ability to muster enough support in Congress to pass an ambitious tax reform in 2021 (prior to national elections in 2022).

Flexibility and performance profile: Large fiscal deficits, a weakened external profile, and a gradual, but impactful, easing of monetary policy

We expect a large fiscal deficit in 2020-2021, with net general government debt peaking at 63% of GDP by 2021.
Growing external debt and the temporary decline in current account inflows translate into a weak external position.
Strong countercyclical monetary policy, including the use of unconventional policies, will alleviate the economic downturn.
The economic downturn will worsen Colombia's financial profile in 2020 and 2021, mainly because of higher sovereign debt. In response to COVID-19, the government decreed a severe and lengthy national lockdown. As a result, the loss of tax revenue and an increase in spending have led to large fiscal deficits. We expect Colombia's general government deficits at an average of 9% of GDP during 2020-2021. We expect government revenues to rise and spending to decline starting next year as the pandemic recedes. As a result, we expect a faster fiscal consolidation starting in 2022. Net general government debt is likely to rise by 13% of GDP in 2020 and by 8% in 2021 and then stabilize around 2.5% of GDP in 2022-2023.

Wider deficits, currency depreciation, and falling GDP will boost Colombia's net general government debt to 63% of GDP by 2023, compared with 44% in 2019. We expect the debt burden to decline only modestly in later years as the economy recovers. The government is likely to fund half of its fiscal deficit in 2020 in external markets, versus around 20% in 2018-2019. Higher debt will keep interest payments above 10% of general government revenues, on average, during 2020-2023.

The government acknowledges the need for additional tax revenues, but it has not presented a reform proposal. We believe that a new fiscal reform proposal will be sent to Congress in 2021 and may mostly target tax exemptions (8.7% of GDP as of 2019), mainly on the VAT. To mitigate the impact of higher consumption taxes, the government is planning to strengthen its VAT refund program that started in 2020 (as a result of the 2019 reapproval of the Financing Law), which has been significantly expanded as an additional measure to support the poorest segments of the population.

Government contingent liabilities are low. Public-sector companies are generally well run and had an adequate financial profile before the pandemic hit. The adjusted debt of Ecopetrol, the largest government-related entity (GRE) in Colombia, is low, below 6% of GDP. The company is expected to remain profitable even with low oil prices during 2020-2023.

Contingent liabilities from the financial sector are also limited. The banking sector, with estimated assets of 69% of GDP, was well-capitalized to weather the crisis, and the regulator has provided significant support. Nonperforming assets and profitability ratios are set to worsen in 2020, but an economic rebound in 2021 and the ongoing adoption of Basel III risk-management standards should result in a resilient sector in the long term.

Colombia's monetary policy response to the downturn has been gradual but significant. The deflationary nature of the current shock has allowed for a significant reduction in interest rates. The central bank has cut its policy rate seven times since March for a total reduction of 250 basis points to 1.75%. The financial sector regulator has also provided significant support by allowing borrowers to reschedule debt service without requiring banks to hold higher capital reserves, preventing credit disruption. The low policy interest rates have been effectively transmitted to bank lending to the private sector--which is estimated at 58% of GDP in 2020--and to debt markets. We expect the central bank's policy rates to remain low in 2021.

Through unconventional policies, the central bank helped ease market volatility during March and April. The central bank adhered to its long-standing policy of letting the Colombian peso (COP) exchange rate float freely but created foreign currency non-delivery forwards and SWAPS instruments to contain volatility, with a neutral impact on foreign reserves. The bank also bought sovereign debt and corporate debt (and accepted private-sector debt as collateral for its repo operations) to provide liquidity to the financial markets. We expect that Colombia's autonomous central bank will adhere to its inflation-targeting policies and maintain its price stability mandate. We expect inflation to average 2.7% during 2020-2023.

Persistent current account deficits, partly due to low oil prices in recent years, have weakened Colombia's external profile. We expect a current account deficit (CAD) of 3.9% of GDP in 2020, a marginal decline from 2019's 4.2%, as the fall in imports is likely to exceed the decline in oil exports (mainly because of lower prices). We expect the CAD to average 4% of GDP during 2021-2023. And FDI is likely to fund most of the CAD in these years.

In our base case, gross external financing needs are likely to be just below 100% of current account receipts (CAR) plus usable reserves during 2020-2023. Narrow net external debt is expected to reach 167% of CAR this year and average 160% during 2020-2023 as CARs would only recover gradually. Our narrow net external debt definition includes nonresident holdings of local currency-denominated debt, which, as of September 2020, totaled US$22 billion, similar levels to those during 2017-2019.

The external assets of Colombia's individual pension fund accounts, which we do not include in our external metrics, reached $30 billion (or 10% of GDP, or 52% of CAR) in September 2020. While these are private-sector external assets, they are regulated by the government and have helped stabilize the country's financial markets and boosted external liquidity. Moreover, Colombia's external liquidity is supported by the availability of a flexible credit line from the IMF, which was recently expanded to US$17.2 billion. The government will draw from the line for budgetary purposes but has stated that over two-thirds of the line will remain as an external liquidity buffer.

Key Statistics

Table 1

Colombia Selected Indicators

	2013	2014	2015	2016	2017	2018	2019	2020f	2021f	2022f	2023f
Economic indicators (%)											
Nominal GDP (bil. LC)	713,626.71	762,903.00	804,692.00	863,782.00	920,194.00	978,477.06	1,062,342.50	1,002,741.19	1,081,963.39	1,165,253.58	1,245,607.59
Nominal GDP (bil. $)	381.87	381.11	293.48	282.72	311.80	330.97	323.80	271.01	293.22	318.38	341.26
GDP per capita ($000s)	8.3	8.2	6.2	5.9	6.5	6.8	6.6	5.5	5.8	6.3	6.6
Real GDP growth	4.6	4.7	3.0	2.1	1.4	2.5	3.3	(8.0)	5.5	4.6	3.8
Real GDP per capita growth	3.4	3.5	1.8	0.9	0.1	1.4	2.2	(9.1)	4.3	3.4	2.6
Real investment growth	6.1	11.8	(1.2)	(0.2)	(3.2)	2.1	4.0	(16.0)	8.0	5.7	5.0
Investment/GDP	22.5	24.0	23.8	23.2	21.6	21.5	22.3	19.7	20.2	20.4	20.6
Savings/GDP	19.2	18.8	17.4	18.9	18.3	17.5	18.1	15.8	16.1	16.5	16.9
Exports/GDP	18.1	16.6	15.7	14.7	15.1	16.0	15.9	15.7	16.0	16.2	16.3
Real exports growth	4.7	(0.3)	1.7	(0.2)	2.6	0.9	2.6	(9.0)	7.5	5.5	4.5
Unemployment rate	9.6	9.1	8.9	9.2	9.4	9.7	10.5	15.4	14.5	13.6	12.7
External indicators (%)											
Current account balance/GDP	(3.3)	(5.2)	(6.3)	(4.3)	(3.3)	(3.9)	(4.2)	(3.9)	(4.1)	(3.9)	(3.8)
Current account balance/CARs	(16.2)	(26.8)	(32.7)	(22.5)	(16.7)	(19.0)	(19.9)	(18.9)	(19.3)	(18.2)	(17.2)
CARs/GDP	20.1	19.4	19.3	18.9	19.6	20.8	21.4	20.9	21.2	21.5	21.8
Trade balance/GDP	0.8	(1.2)	(4.6)	(3.2)	(1.4)	(1.6)	(2.6)	(3.4)	(3.6)	(3.0)	(2.9)
Net FDI/GDP	2.2	3.2	2.6	3.3	3.3	1.9	3.5	2.0	3.1	3.1	3.2
Net portfolio equity inflow/GDP	0.5	0.5	0.2	(0.1)	0.2	(0.2)	(0.4)	0.6	0.5	0.2	0.4
Gross external financing needs/CARs plus usable reserves	92.4	96.6	93.2	87.6	95.3	96.4	95.2	92.8	93.6	98.5	99.0
Narrow net external debt/CARs	50.6	66.2	97.6	123.8	117.5	113.5	114.5	166.6	165.9	158.5	152.6
Narrow net external debt/CAPs	43.5	52.2	73.5	101.0	100.7	95.4	95.6	140.0	139.1	134.1	130.2
Net external liabilities/CARs	133.8	153.5	211.8	253.4	242.6	225.0	245.9	319.7	309.8	297.0	289.3
Net external liabilities/CAPs	115.1	121.0	159.6	206.9	207.8	189.1	205.1	268.8	259.6	251.3	246.8
Short-term external debt by remaining maturity/CARs	20.6	26.3	37.4	40.7	50.4	43.5	41.3	60.3	60.6	59.8	54.9
Usable reserves/CAPs (months)	5.0	5.5	7.5	8.5	7.8	6.9	6.9	9.4	9.3	8.2	7.6
Usable reserves (mil. $)	43,158	46,807	46,223	46,174	47,133	47,888	52,650	57,286	55,197	55,108	55,019
Fiscal indicators (general government; %)											
Balance/GDP	(0.8)	(1.5)	(3.0)	(2.8)	(2.3)	(2.0)	(1.8)	(10.1)	(7.9)	(2.8)	(1.9)
Change in net debt/GDP	3.2	4.1	6.7	2.5	3.5	6.2	5.6	12.9	7.6	2.6	1.9
Primary balance/GDP	1.4	0.5	(0.4)	0.1	0.6	0.8	1.1	(6.3)	(4.0)	1.0	1.7
Revenue/GDP	25.3	25.4	23.9	22.4	23.4	25.3	26.5	24.5	25.6	26.3	26.8

Expenditures/GDP	26.1	27.0	26.9	25.2	25.7	27.3	28.3	34.6	33.5	29.0	28.7
Interest/revenues	8.7	8.0	10.7	13.1	12.4	11.1	11.0	15.4	15.4	14.5	13.7
Debt/GDP	35.7	38.8	43.7	44.4	45.3	48.7	50.3	65.3	68.2	65.9	63.5
Debt/revenues	141.0	152.7	183.1	198.3	194.1	192.2	190.2	266.2	266.4	250.6	237.0
Net debt/GDP	29.4	31.6	36.7	36.7	37.9	41.8	44.1	59.6	62.8	60.9	58.8
Liquid assets/GDP	6.3	7.2	7.1	7.7	7.4	6.9	6.2	5.7	5.3	5.0	4.7
Monetary indicators (%)											
CPI growth	2.0	2.9	5.0	7.5	4.3	3.2	3.5	2.6	2.3	3.0	3.0
GDP deflator growth	2.5	2.1	2.4	5.1	5.1	3.7	5.1	2.6	2.3	3.0	3.0
Exchange rate, year-end (LC/$)	1,922.56	2,392.46	3,149.47	3,000.71	2,971.63	3,250.00	3,277.00	3,700.00	3,675.00	3,650.00	3,650.00
Banks' claims on resident non-gov't sector growth	11.6	14.8	17.6	8.9	11.8	3.1	11.6	3.8	7.5	8.5	8.5
Banks' claims on resident non-gov't sector/GDP	41.4	44.4	49.5	50.3	52.8	51.1	52.5	57.8	57.6	58.0	58.9
Foreign currency share of claims by banks on residents	N/A	N/A	N/A	N/A	N/A	N/A	N/A	N/A	N/A	N/A	N/A
Foreign currency share of residents' bank deposits	N/A	N/A	N/A	N/A	N/A	N/A	N/A	N/A	N/A	N/A	N/A
Real effective exchange rate growth	(2.2)	(4.2)	(19.7)	(6.2)	3.2	0.5	(9.0)	N/A	N/A	N/A	N/A

Sources: None
Adjustments: None
Definitions: Savings is defined as investment plus the current account surplus (deficit). Investment is defined as expenditure on capital goods, including plant, equipment, and housing, plus the change in inventories. Banks are other depository corporations other than the central bank, whose liabilities are included in the national definition of broad money. Gross external financing needs are defined as current account payments plus short-term external debt at the end of the prior year plus nonresident deposits at the end of the prior year plus long-term external debt maturing within the year. Narrow net external debt is defined as the stock of foreign and local currency public- and private- sector borrowings from nonresidents minus official reserves minus public-sector liquid claims on nonresidents minus financial-sector loans to, deposits with, or investments in nonresident entities. A negative number indicates net external lending. N/A--Not applicable. LC--Local currency. CARs--Current account receipts. FDI--Foreign direct investment. CAPs--Current account payments. f--Forecast. The data and ratios above result from S&P Global Ratings' own calculations, drawing on national as well as international sources, reflecting S&P Global Ratings' independent view on the timeliness, coverage, accuracy, credibility, and usability of available information.

Ratings Score Snapshot

Table 2

Colombia Ratings Score Snapshot

Key rating factors	Score	Explanation
Institutional assessment	3	Stable democracy with continuity in economic policies across party lines. Policy implementation is strong. Our base case assumes policy pragmatism, backed by a professional and technical trained civil service, and ample checks and balances, including an active judiciary.
Economic assessment	4	Based on GDP per capita ($) as per Selected Indicators in table 1.
External assessment	6	Based on narrow net external debt and gross external financing needs as per Selected Indicators in table 1. The country is exposed to significant volatility in terms of trade due to its dependence on hydrocarbons.
Fiscal assessment: flexibility and performance	3	Based on the change in net general government debt (% of GDP) as per Selected Indicators in table 1. We exclude the transitory shock caused by the COVID-19 pandemic and related lockdowns.
Fiscal assessment: debt burden	4	Based on net general government debt trending below 60% of GDP by 2023 and general government interest expenditures trending below 15% of general government revenues as per Selected Indicators in table 1.
Monetary assessment	3	Colombia has a floating exchange-rate regime, but its currency is not actively traded. The central bank has a track record of independence and uses market-based monetary instruments. It has the ability to act as a lender of last resort for the financial system.
Indicative rating	bb+	As per Table 1 of "Sovereign Rating Methodology."
Notches of supplemental adjustments and flexibility	1	We expect relatively large and growing private pension funds' external assets to provide additional external flexibility. Colombia is one of few countries that has a flexible credit line from the IMF that would improve external liquidity under a stress scenario.
Final rating		
Foreign currency	BBB-	
Notches of uplift	1	Reflecting an independent monetary policy with a track record of floating currency. The sovereign has relatively adequate capital markets, as demonstrated by local currency fixed income and money market accounting for about 30% of GDP.
Local currency	BBB	

S&P Global Ratings' analysis of sovereign creditworthiness rests on its assessment and scoring of five key rating factors: (i) institutional assessment; (ii) economic assessment; (iii) external assessment; (iv) the average of fiscal flexibility and performance, and debt burden; and (v) monetary assessment. Each of the factors is assessed on a continuum spanning from 1 (strongest) to 6 (weakest). S&P Global Ratings' "Sovereign Rating Methodology," published on Dec. 18, 2017, details how we derive and combine the scores and then derive the sovereign foreign currency rating. In accordance with S&P Global Ratings' sovereign ratings methodology, a change in score does not in all cases lead to a change in the rating, nor is a change in the rating necessarily predicated on changes in one or more of the scores. In determining the final rating the committee can make use of the flexibility afforded by §15 and §§126-128 of the rating methodology.

Related Criteria

Criteria | Governments | Sovereigns: Sovereign Rating Methodology (/en_US/web/guest/article/-/view/sourceId/10221157), Dec. 18, 2017
General Criteria: Methodology For Linking Long-Term And Short-Term Ratings (/en_US/web/guest/article/-/view/sourceId/10011703), April 7, 2017
General Criteria: Principles Of Credit Ratings (/en_US/web/guest/article/-/view/sourceId/6485398), Feb. 16, 2011
General Criteria: Methodology: Criteria For Determining Transfer And Convertibility Assessments (/en_US/web/guest/article/-/view/sourceId/5402435), May 18, 2009

Related Research

Global Sovereign Rating Trends: Third-Quarter 2020 (/en_US/web/guest/article/-/view/sourceId/11696151), Oct. 16, 2020
Sovereign Risk Indicators (/en_US/web/guest/article/-/view/sourceId/11689747), Oct. 12, 2020
S&P Global Ratings Revises Oil And Natural Gas Price Assumptions (/en_US/web/guest/article/-/view/sourceId/11655632), Sept. 16, 2020
Global Sovereign Rating Trends Midyear 2020: Outlook Bias Turns Negative As Governments Pile On Debt To Face COVID-19 (/en_US/web/guest/article/-/view/sourceId/11594719), July 30, 2020
Colombia Outlook Revised To Negative On Increased Risks To External Liquidity, Debt, And Growth; Ratings Affirmed (/en_US/web/guest/article/-/view/sourceId/11395076), March 26, 2020
Banking Industry Country Risk Assessment: Colombia (/en_US/web/guest/article/-/view/sourceId/11181031), Nov. 1, 2019

In accordance with our relevant policies and procedures, the Rating Committee was composed of analysts that are qualified to vote in the committee, with sufficient experience to convey the appropriate level of knowledge and understanding of the methodology applicable (see 'Related Criteria And Research'). At the onset of the committee, the chair confirmed that the information provided to the Rating Committee by the primary analyst had been distributed in a timely manner and was sufficient for Committee members to make an informed decision.

After the primary analyst gave opening remarks and explained the recommendation, the Committee discussed key rating factors and critical issues in accordance with the relevant criteria. Qualitative and quantitative risk factors were considered and discussed, looking at track-record and forecasts.

The committee's assessment of the key rating factors is reflected in the Ratings Score Snapshot above.

The chair ensured every voting member was given the opportunity to articulate his/her opinion. The chair or designee reviewed the draft report to ensure consistency with the Committee decision. The views and the decision of the rating committee are summarized in the above rationale and outlook. The weighting of all rating factors is described in the methodology used in this rating action (see 'Related Criteria And Research').

Ratings List

	Ratings Affirmed
Colombia	
Sovereign Credit Rating	
Foreign Currency	BBB-/Negative/A-3
Local Currency	BBB/Negative/A-2
Transfer & Convertibility Assessment	BBB+
Senior Unsecured	BBB
Senior Unsecured	BBB-

Certain terms used in this report, particularly certain adjectives used to express our view on rating relevant factors, have specific meanings ascribed to them in our criteria, and should therefore be read in conjunction with such criteria. Please see Ratings Criteria at www.standardandpoors.com for further information. Complete ratings information is available to subscribers of RatingsDirect at www.capitaliq.com. All ratings affected by this rating action can be found on S&P Global Ratings' public website at www.standardandpoors.com. Use the Ratings search box located in the left column.

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