

**Colombia: First Review of the Extended Arrangement--Staff Report; News Brief on the Executive Board Discussion; and Statement by the Authorities of Colombia**

In the context of the first review of the Extended Arrangement with Colombia, the following documents have been released and are included in this package:

- the staff report for the first review of the Extended Arrangement, prepared by a staff team of the IMF, following discussions that ended on **July 15, 2000**, with the officials of Colombia on economic developments and policies. **Based on information available at the time of these discussions, the staff report was completed on August 23, 2000.** The views expressed in the staff report are those of the staff team and do not necessarily reflect the views of the Executive Board of the IMF.
- a News Brief summarizing the **views of the Executive Board as expressed during its September 7, 2000, discussion** of the staff report that completed the review.
- a statement by the authorities of Colombia.

The documents listed below have been or will be separately released.

Technical Memorandum of Understanding  
Letter of Intent sent to the IMF by the authorities of the member country

The policy of publication of staff reports and other documents by the IMF allows for the deletion of market-sensitive information.

**To assist the IMF in evaluating the publication policy, reader comments are invited and may be sent by e-mail to [Publicationpolicy@imf.org](mailto:Publicationpolicy@imf.org).**

Copies of this report are available to the public from  
International Monetary Fund • Publication Services  
700 19th Street, N.W. • Washington, D.C. 20431  
Telephone: (202) 623 7430 • Telefax: (202) 623 7201  
E-mail: [publications@imf.org](mailto:publications@imf.org) • Internet: <http://www.imf.org>

Price: \$15.00 a copy

**International Monetary Fund  
Washington, D.C.**

INTERNATIONAL MONETARY FUND

COLOMBIA

**Staff Report for the First Review  
Under the Extended Arrangement**

Prepared by the Western Hemisphere Department and  
the Policy Development and Review Department

(In consultation with the Fiscal Affairs, Legal,  
Monetary and Exchange Affairs, and Treasurer's Departments)

Approved by Miguel E. Bonangelino and Jesús Seade

August 23, 2000

	Contents	Page
Executive Summary.....		3
I. Introduction.....		4
II. Background and Recent Developments .....		4
III. Policy Discussions.....		16
A. Fiscal Policy .....		17
B. Monetary Policy .....		21
C. The Structural Reforms .....		22
D. External Policies.....		24
E. Financial Sector Restructuring.....		25
IV. Staff Appraisal .....		26
 Boxes		
1. The Fiscal Accounts.....		7
2. The Costs of Financial Sector Restructuring.....		8
3. Plan Colombia.....		18
4. The Revised Privatization Program .....		20

	Contents	Page
Tables		
1.	Performance Criteria .....	30
2.	Structural Benchmarks Under the Program .....	31
3.	Selected Economic and Financial Indicators .....	32
4.	Operations of the Combined Public Sector .....	33
5.	Operations of the Central Administration .....	34
6.	Summary Accounts of the Financial System .....	35
7.	Summary Balance of Payments, 1996-2002 .....	36
8.	External Debt and Debt-Service Projections .....	37
9.	Indicators of External Vulnerability .....	38
10.	Schedule of Purchases Under the Extended Arrangement .....	39
Figures		
1.	Selected Economic Indicators .....	6
2.	Banking Indicators .....	9
3.	Exchange Rate Development .....	11
4.	Interest Rates .....	12
5.	Monetary Indicators .....	13
6.	Trade Indicators .....	14
7.	External Indicators .....	15
Attachments		
I.	Fund Relations .....	40
II.	Letter of Intent .....	42
Annex		
	Technical Memorandum of Understanding .....	48

## EXECUTIVE SUMMARY

Colombia's economic performance deteriorated markedly in the last half of 1998 and during 1999 under the combined influence of external shocks and a weakening of confidence. The former included a worsening in the term of trade and the effects of the turbulence in international financial markets, and the latter was related to stepped-up guerrilla activity and uncertainty about the new government's policies in the face of a weakening fiscal position. In an effort to reverse the deterioration, the authorities in 1999 developed a multi-year stabilization and reform program based on fiscal consolidation, exchange rate flexibility (the peso was floated in September), bank restructuring, and structural reforms.

Following a 4.5 percent decline in 1999, real GDP grew by an estimated 3 percent in the first half of 2000 (compared with a year earlier); on a seasonally adjusted basis unemployment—still at around 20 percent—has shown a slight decline this year; and inflation remains below the 10 percent target for 2000. The prudential indicators of the financial system have improved since last year, but the public banks and the savings and loan institutions remain weak. The fiscal consolidation process has remained on track, and to help strengthen the fiscal outlook for 2001 and ensure that the objectives of the program are met, the authorities have announced that additional revenue measures will be proposed later in the year and that 23 government agencies will be closed.

Following the floating of the peso last year, the currency strengthened, and short-term interest rates came down to record low levels; the peso has since weakened and the central bank has raised its rates somewhat, but deposit rates remain low in real terms. The central bank is committed to the program's inflation target and it is closely monitoring inflationary trends to be ready to take corrective actions as needed.

The government has continued to pursue its structural reform agenda, albeit with some delays and modifications to the projects identified in the program. At the same time, new initiatives are being developed to strengthen the reform program; e.g., a fiscal responsibility law will be introduced in congress later this year. The privatization program will fall well short of projections in 2000, with the sale of enterprises in the electricity sector delayed due to guerrilla attacks on installations and because of the still low investor interest in the public banks. Nevertheless, the authorities are committed to their privatization program and expect to sell the remaining entities slated for privatization next year.

The peace negotiations with guerrilla groups continue, and in July the authorities announced a plan ("Plan Colombia") which integrates their strategies for settling the internal conflict, reducing the cultivation and trafficking of illicit drugs, and dealing with the social fall-out from these problems. Financial support for the plan is being sought from the international community. An initial consultative group meeting was held in Madrid in June with a follow-up meeting planned for Bogota in September.

## I. INTRODUCTION

1. The discussions for the first review under the extended arrangement were held in Bogota and Washington during four periods from April to July 2000; the last round of discussions was held with the new economic team, including the new minister of finance, that was appointed in July.<sup>1</sup> The three-year arrangement, in an amount equivalent to SDR 1.957 billion (84 percent of quota on an annual basis), was approved on December 20, 1999 (EBS/99/218). To date, the authorities have chosen not to make any of the purchases under the arrangement, and Colombia has no outstanding credit from the Fund.<sup>2</sup> In the attached letter to the Managing Director, dated August 22, 2000, the authorities describe developments under the program and the policies they intend to follow during the remainder of 2000.

2. All performance criteria for end-1999 and March 2000 were observed, except for a temporary excess over the ceiling on the central bank's net domestic assets (NDA) for December 1999 that reflected a sharp increase in the demand for liquidity by financial institutions at the end of the year related to the Y2K problem (Table 1). The performance criteria for end-June on the net international reserves and the net domestic assets of the central bank also were observed.<sup>3</sup> All structural benchmarks, except two, have been achieved, albeit with differences in the case of some of the reforms from what had been envisaged under the program (Table 2).

## II. BACKGROUND AND RECENT DEVELOPMENTS

3. Colombia's economic performance deteriorated markedly in the last half of 1998 and during 1999 under the combined influence of external shocks and a weakening of confidence. The external shocks included a deterioration in the terms of trade and the effects of the turbulence in international financial markets; the weakening of confidence was related to stepped-up guerrilla activity and uncertainty about the new government's policies in the face of a deteriorating fiscal position. These developments led to repeated episodes of pressure

---

<sup>1</sup> The staff participating in one or more rounds of the discussions were Messrs. Gronlie (Head), Gil-Diaz, Terrones (all WHD), Mongardini (PDR), de la Piedra (MAE), Mses. Daban (FAD), and Pinillos (Assistant—WHD). Messrs. Loser, Bonangelino (both WHD), and Junguito (Alternate Executive Director) participated in some of the discussions.

<sup>2</sup> The Fund's relations with Colombia are described in Attachment I. Colombia is subject to the safeguard assessment at the time of the next review of the extended arrangement.

<sup>3</sup> It is expected that the full set of data for measuring end-June compliance with the ceiling on the combined public sector deficit and the limits on the external public debt will be available before the Board consideration of the review.

against the peso despite a tightening of monetary policy that resulted in record high interest rates. In September 1999, Colombia eliminated the trading band for the exchange rate and allowed the peso to float. The currency had depreciated markedly in real effective terms during the preceding year, helped by two step-devaluations of the band and a fall in inflation; this largely reversed the real appreciation that had taken place since the mid-1990s (Table 3). Since the peso was floated, the central bank has participated in the foreign exchange market in a transparent manner through auctions held at pre-announced intervals with the objective of achieving the program targets for the net international reserves.

4. Following a notable increase in private sector debt (both external and domestic) over the course of several years, the sharp rise in real interest rates and the depreciation of the peso led to a marked increase in the debt service burden of the private sector in 1998, which, together with the weakening of confidence, contributed to a significant reduction in domestic demand, and real GDP growth fell to 0.5 percent in 1998 and was negative by 4.5 percent in 1999. Economic activity began to recover late last year, and in the first half of 2000 real GDP is estimated to have grown by 3.0 percent compared with a year earlier, based on a strong recovery of exports and some rebound in domestic demand.<sup>4</sup> Moreover, unemployment has declined from a peak of 20.5 percent at the end of the third quarter of 1999 to 19.2 percent in June 2000, on a seasonally adjusted basis. The 12-month rate of consumer price inflation rose from 9.3 percent in December 1999 to 10 percent in May on account of a sharp increase in certain food prices and the pass-through of higher fuel costs, before declining to the December 1999 level again by July (Figure 1).<sup>5</sup>

5. The nonfinancial public sector (NFPS) deficit was 5.5 percent of GDP in 1999, compared with 6.3 percent of GDP in the program, mainly because of lower expenditures than programmed, as explained in Box 1 (Tables 4 and 5, memorandum items). Data for the first quarter of 2000 show a surplus of 0.9 percent of annual GDP, which is a considerable improvement compared with a deficit of 0.1 percent of GDP for the same period last year, and a continuation of the overperformance with respect to the program's fiscal targets.<sup>6</sup> The improvement was mainly due to higher income of the state oil sector, the one-time effect

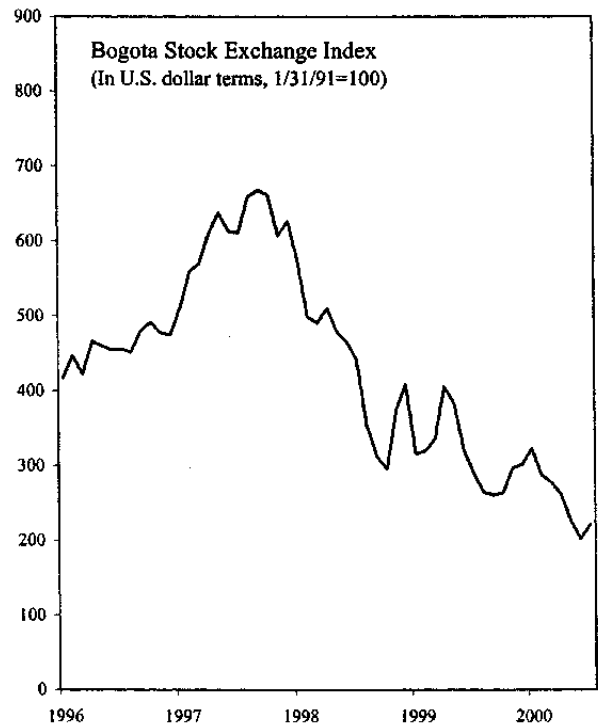
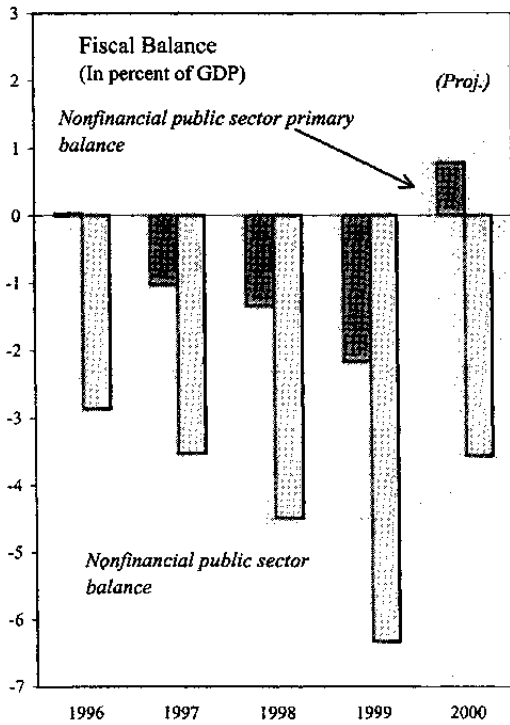
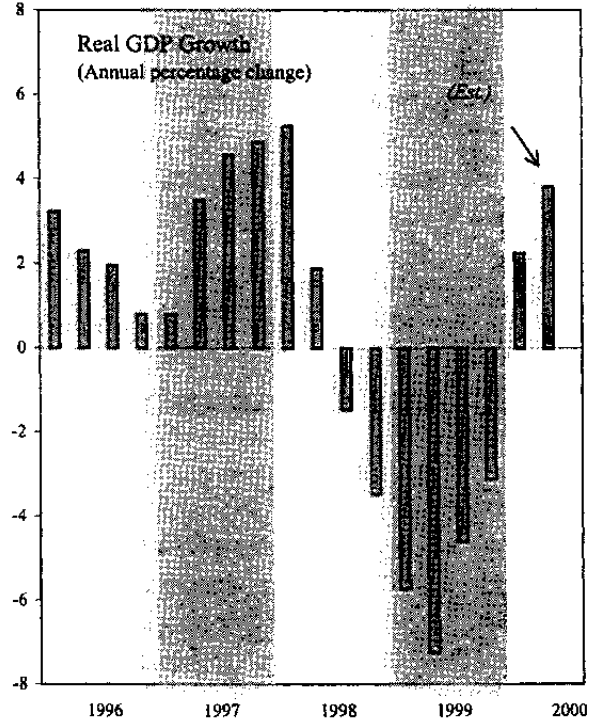
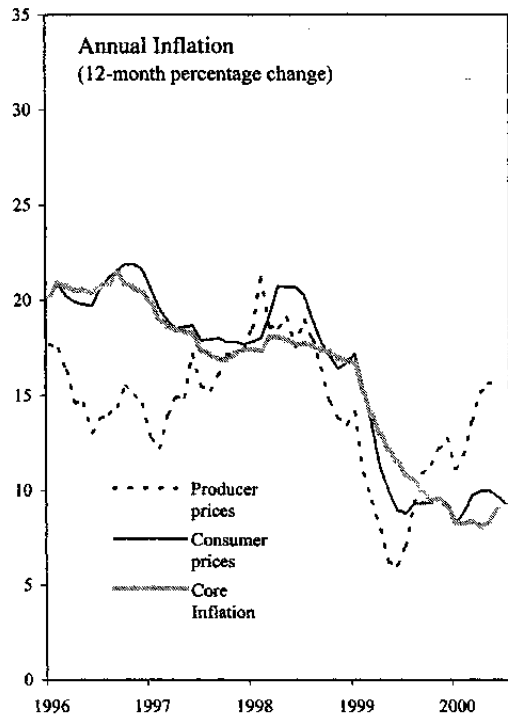
---

<sup>4</sup> In the first half of 2000, manufacturing output grew by 8.5 percent compared with a year earlier.

<sup>5</sup> In July the measure of core inflation rose because housing costs, which have a large weight and rose only slightly, were eliminated as an "outlier" from the calculation of core inflation for that month.

<sup>6</sup> The deficits referred to in this paragraph are on an "accrual basis," as defined under the program. The authorities have proposed that the fiscal deficit henceforth be monitored on a "commitments basis," as explained in Box 1.

Figure 1. Colombia: Selected Economic Indicators



Source: Banco de la Republica; Ministry of Finance; DANE; and Fund staff estimates.

## Box 1. The Fiscal Accounts

### The budget carry-over

The central administration's budget carry-over from one period to the next, *rezago*, is made up of two components: (i) unexecuted spending commitments (*reservas de apropiación*) and (ii) unpaid bills (*cuentas por pagar*). Both are subject to the same budgetary and accounting procedures and both are considered "obligations" from a budgetary point of view. The difference is that the former reflects commitments under which the goods or services have not yet been provided.

Over the recent past, each of the two components of the carry-over are estimated to have been of the same order of magnitude, but in 1999 the composition changed markedly as the unpaid bills were reduced by 0.2 percent of GDP, and the commitments carried over to 2000 increased by 0.8 percent of GDP. At the end of 2000, the total amount of the carry-over is projected to fall by about 0.2 percent of GDP, but the composition would change markedly again, with the share of commitments decreasing and that of unpaid bills rising. The amount of commitments would fall sharply on account of a provision in the 2000 budget law which provides that commitments carried over to the next year be subtracted from that year's budget appropriations (for the entity involved). Measuring the deficit for 2000 on an accrual basis, as defined in the program, where only cash transactions and unpaid bills are accounted for, the projected change in the composition of the budget carry-over would lead to a higher than programmed public sector deficit in 2000, just as the change in the composition the other way in 1999 provided for a considerable margin under the programmed deficit, as explained below.

### Redefinition of the fiscal deficit

The 1999 NFPS deficit was 5.5 percent of GDP when accounted for on an accrual basis. This lowering of the deficit relative to the program projection of 6.3 percent of GDP was achieved in large part because the execution of an unusually large amount of spending commitments was moved to 2000, as noted above. The 1999 ceiling on the combined public sector deficit (performance criterion) of 5.9 percent of GDP was observed with an even larger margin (1.3 percent of GDP) because it in addition takes account of the lower than projected fiscal costs of the bank restructuring operations. According to the authorities, a principal reason for the sharp increase in the carryover of commitments from 1999 to 2000 had to do with suppliers not obtaining credit under the recent "credit crunch" in Colombia. In an effort to improve fiscal management by making the commitments subject to the program, the authorities are proposing that the fiscal deficit henceforth be monitored on a commitments basis (i.e., by accounting for the commitments in the period in which they are incurred). Measured this way, the NFPS deficit was 6.3 percent of GDP in 1999, while the combined public sector deficit was 5.4 percent of GDP; for 2000 the deficits would be 3.6 and 3.7 percent, respectively, as discussed below in the text (Table 4).

The authorities explained that the change in the definition also would help with fiscal legislation that is before congress, and that it will strengthen the ministry's hand in dealing with spending requests that are made after the budget has been approved, which in the past often have been accommodated by postponing their execution and payment to the subsequent year. This has been a source of the widening deficits in recent years. An FAD technical assistance mission visited Bogota in May 2000 to assess if commitments could be monitored adequately on a quarterly basis. It found that, as in the case of the unpaid bills, the commitments can be reliably monitored and reported, so that both components of the budget carry-over can be considered in calculating the combined public sector deficit for the purpose of the program. To further strengthen the reporting procedures, the authorities are taking steps to ensure that the data on budget carry-overs reported by the central budget office and the national accounting agency are always reconciled.



of shortening the transit period of taxes through the banking system, a slow execution of investment projects, and a lower wage bill that reflects a nominal wage freeze in 2000 for 70 percent of public employees. Interest payments on both external and domestic debt rose.

6. The Colombian financial system was showing clear signs of distress by the second half of 1998. To head off a system-wide crisis, the government introduced several measures late in the year and in 1999 (Box 2). The most acute phase of the banking crisis would since appear

### **Box 2. The Costs of Financial Sector Restructuring**

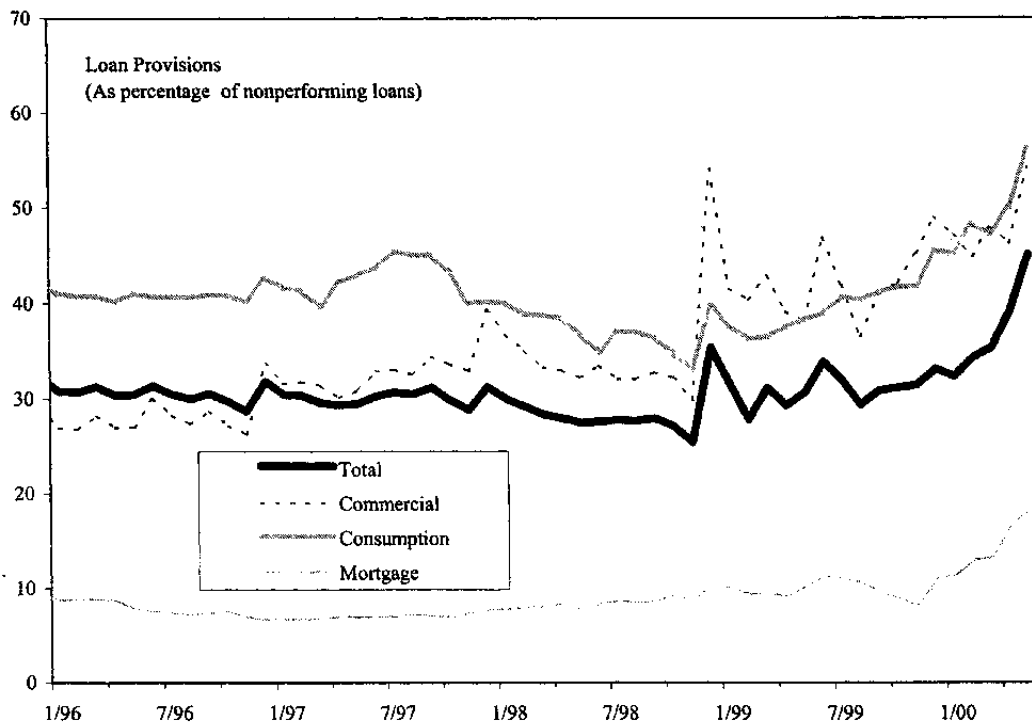
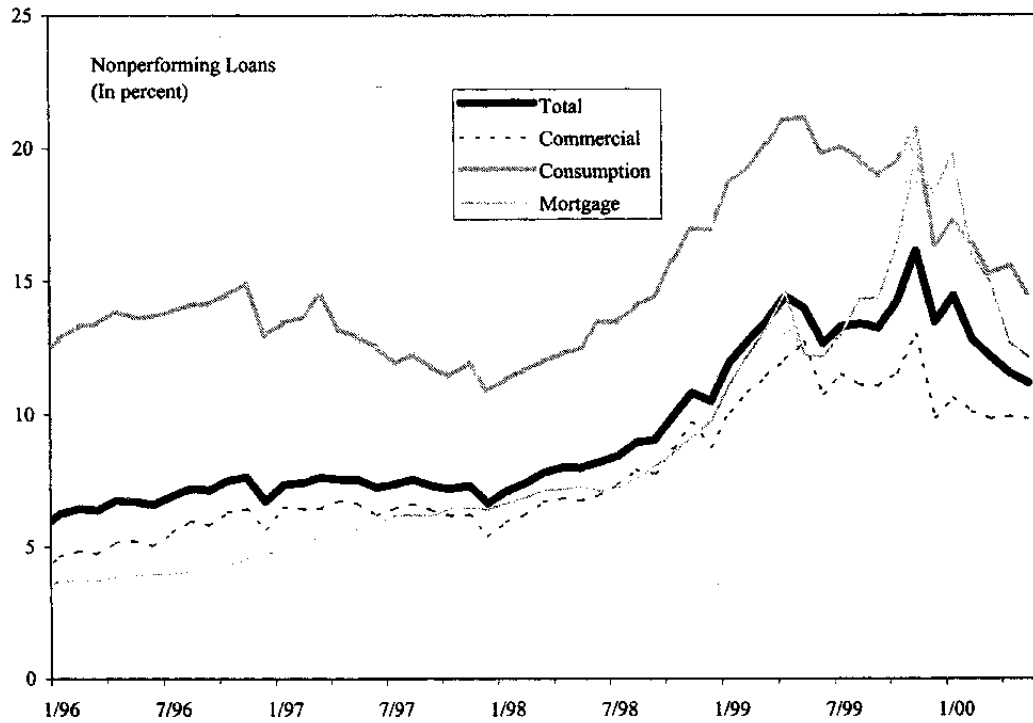
Since mid-1998 the Colombian financial system has undergone a period of substantial stress. Rapid credit expansion, inadequate regulation, and poorly managed public banks were at the root of the difficulties, which were exacerbated by the softening and collapse of the real estate market and the worst recession on record. The problems were manifested by a rise in nonperforming loans, large losses, and a significant deterioration in solvency.

To address these problems, the authorities introduced several measures in late 1998 and in 1999 (see EBS/99/218, Appendix III). Steps were taken to alleviate the debt burden for mortgage holders (debt reduction) as widespread delinquencies were threatening the savings and loan institutions; recapitalize viable private financial entities; and restructure the public banks to restore their solvency in preparation for divestment. A tax (0.2 percent) on financial transactions and obligatory investment requirements by the financial sector in government securities (at below market interest rates) were introduced to help finance some of these programs. The Colombian deposit guarantee fund, FOGAFIN, was designated as the agency responsible for managing the financial sector restructuring programs.

The net present value of the fiscal cost of the financial sector restructuring operations has been estimated at about 8½ percent of GDP. The recapitalization of state banks account for about half of this, while the mortgage debt relief operations account for one-fifth. The cost could decline to around 5 percent of GDP depending on the value that can be recovered from the acquired assets. In terms of annual flows, the net cost borne by the combined public sector was virtually nil in 1999, but is projected to rise to 0.6 percent of GDP in 2000 as a result of (i) the assumption of the debts of the state-owned agricultural bank, Caja Agraria, and (ii) the interest costs, including the capitalization of interest on bonds to recapitalize public banks. In addition to these two items, the higher than projected cost of the mortgage debt-reduction plan after it was extended to include delinquent loans imply that the financial sector restructuring costs would increase relative to the program, by 0.3 percent of GDP in each of 2001 and 2002.

to have subsided and financial conditions in the private banking sector are improving. Most financial institutions are highly liquid and the use of the central bank's liquidity support windows has become concentrated in banks under state-sponsored recapitalization programs, particularly the public banks, which have continued to incur losses; as a result of the latter, the cost of the restructuring required to proceed with their liquidation or privatization will be somewhat higher than anticipated, as discussed in Box 2. The nonperforming loans (NPLs) of the private banks have declined as a proportion of total loans, to 8.3 percent in June 2000 from 10 percent a year earlier, while the provisioned share of their NPLs has risen from 30 to 52.7 percent (prudential indicators for the financial system are shown in Figure 2). The

Figure 2. Colombia: Banking Indicators



Source: Superintendencia Bancaria de Colombia.

restructuring and recapitalization programs, as well as the decline in short-term interest rates and the incipient economic recovery contributed to the improvement.

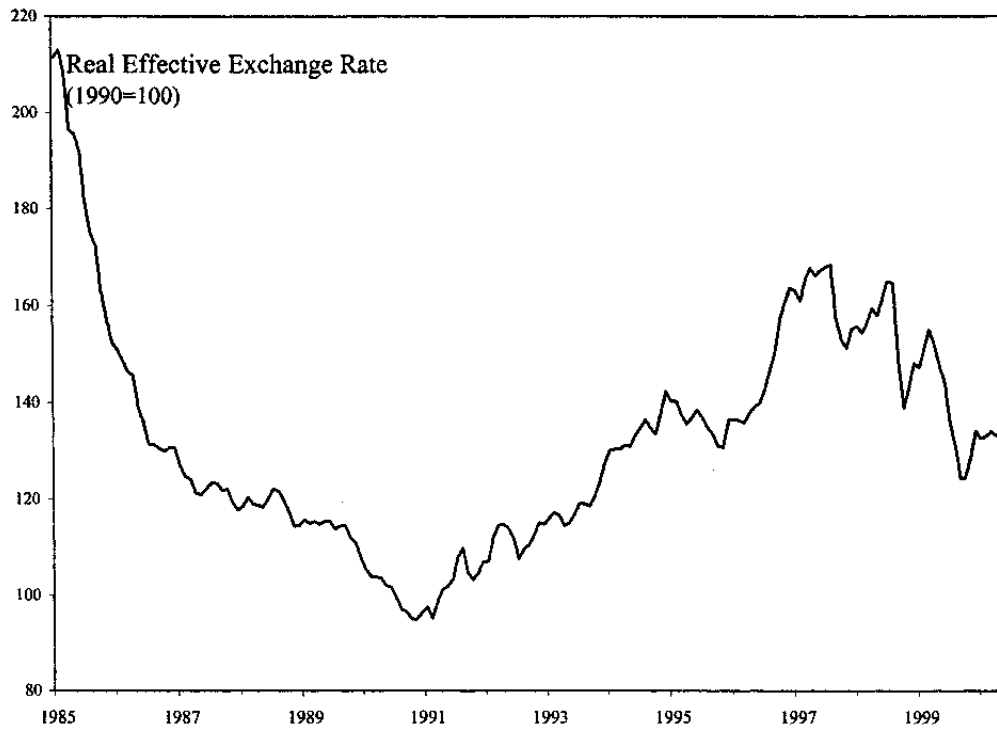
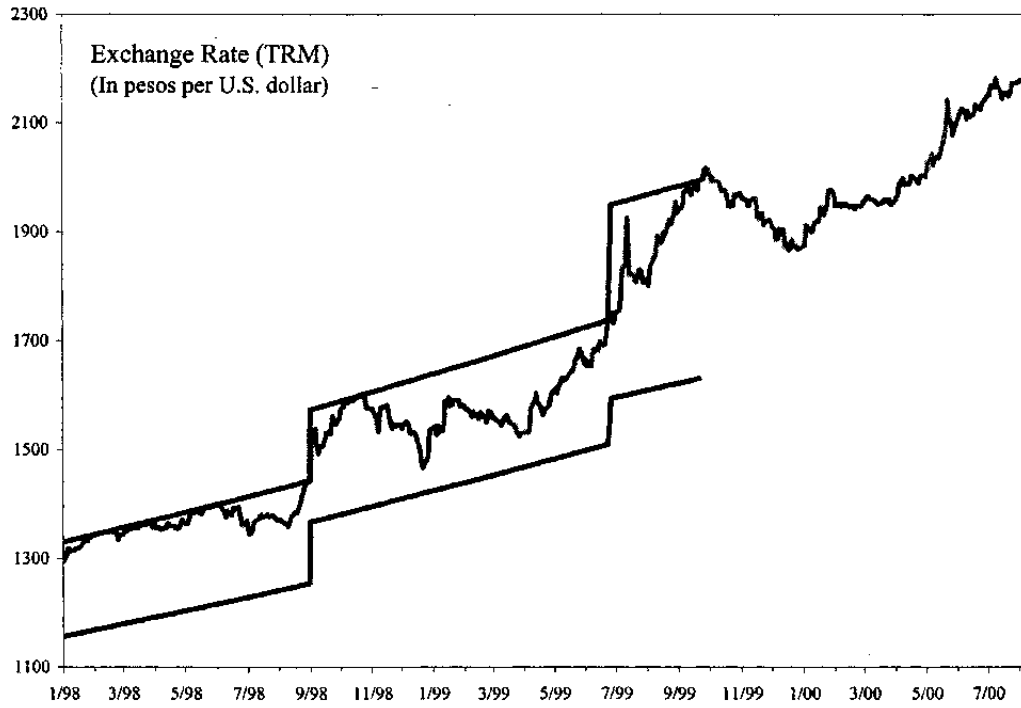
7. The broad money supply has shown a 12-month growth of 3–5 percent in recent months, while base money has grown by around 20 percent as a result of a strong demand for currency in the wake of the problems faced by the banking system, the fall in interest rates, and the widening of the base for the financial transactions tax earlier this year. Reflecting not only the recession, but also the difficulties faced by the financial system and private debtors, credit to the private sector declined throughout 1999 (Table 6), but in recent months, the stock of such credit has shown a 12-month growth rate of 3–6 percent.<sup>7</sup> In light of their recent experience, and faced with the reduction in the value of most collateral assets, particularly real estate, financial institutions have been reluctant to lend, and with rising debt service obligations and widespread mortgage defaults, the private sector has sought to reduce its debt burden, both foreign and domestic. In an effort to help spur lending, legislation has been passed to facilitate the voluntary restructuring of private debt. Following the floating of the peso in September 1999 and the concurrent announcement of an agreement on the main parameters of a Fund-supported program, the currency strengthened, allowing the central bank to reduce its interest rates substantially in the last months of 1999 (Figures 3, 4, and 5).

8. Despite the fiscal deterioration in 1999, the external current account deficit declined to 1.1 percent of GDP (from 5.3 percent of GDP in 1998), as private consumption contracted and investment plummeted, with imports falling by 26 percent in U.S. dollar terms (Table 7, Figure 6). Subsequently, in the first five months of 2000, imports recovered by 13 percent compared with the same period in 1999, and in the first half of the year exports grew 21 percent, mainly reflecting higher oil prices, but nontraditional exports also rose, by 13 percent. The capital account weakened substantially in 1999 as both foreign direct investment and debt-creating flows declined. Following a loss of net international reserves (NIR) in the first three quarters of the year when the central bank sought to defend the peso within its trading band, there was a gain of reserves through the foreign exchange auctions that were instituted in November 1999, as the peso strengthened after it was floated (Figure 7; see Figure 3). Thus, the loss of NIR in 1999 was limited to US\$443 million (compared with a loss of US\$725 million allowed in the program), followed by an increase of US\$220 million, to US\$8.3 billion, in the first half of 2000.

---

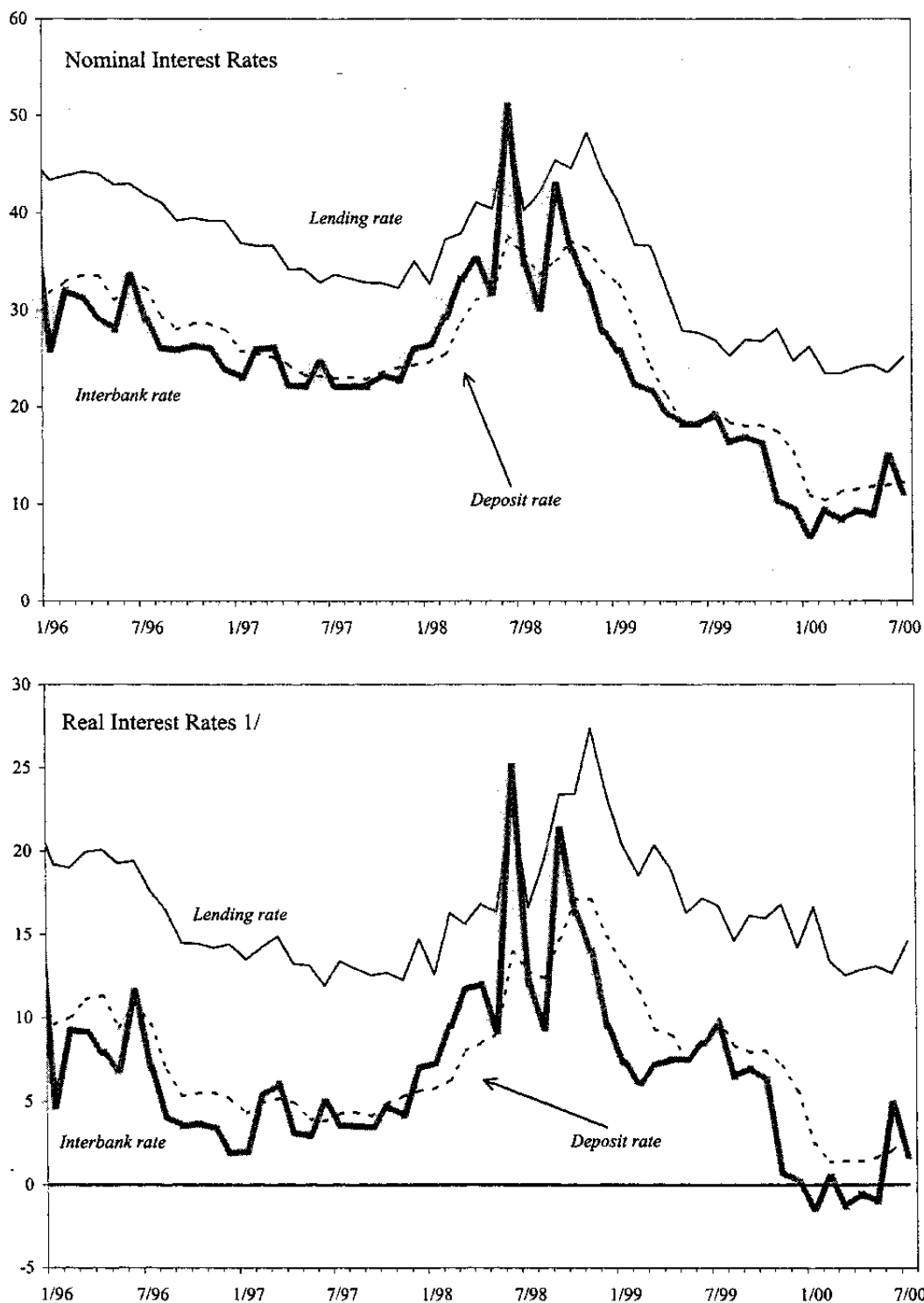
<sup>7</sup> The official statistics show a decline in financial sector credit to the private sector also for this period because of loans that have been written off under the mortgage reduction and bank restructuring programs. The figures quoted are based on estimates that exclude the effect of these write-offs.

Figure 3. Colombia: Exchange Rate Developments



Sources: Banco de la Republica; and Information Notice System.

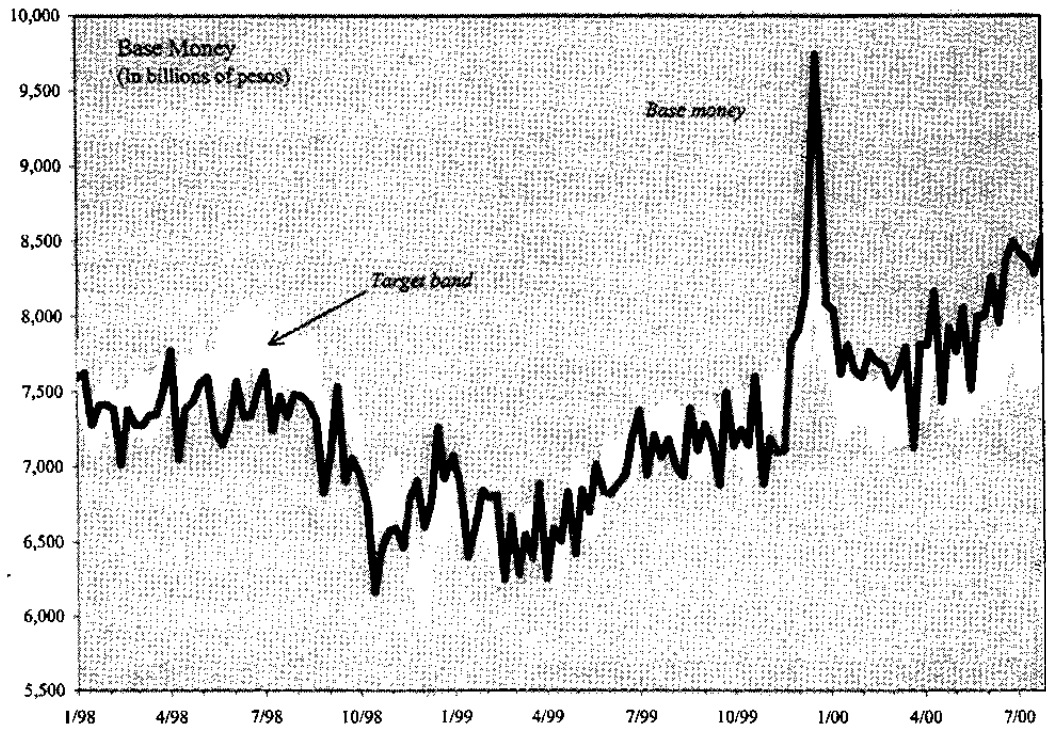
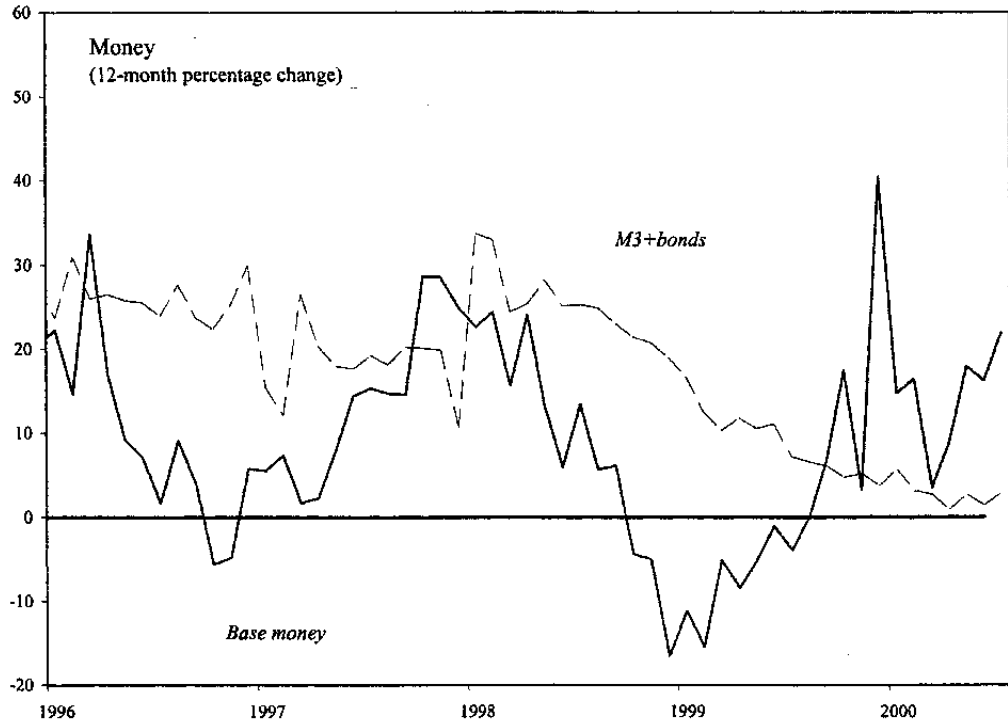
Figure 4. Colombia: Interest Rates  
(In percent per annum)



Source: Banco de la Republica.

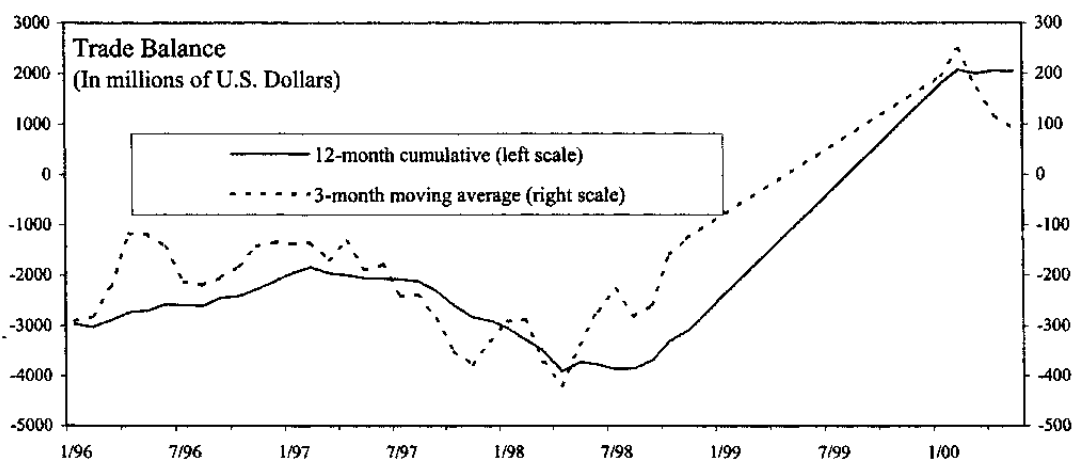
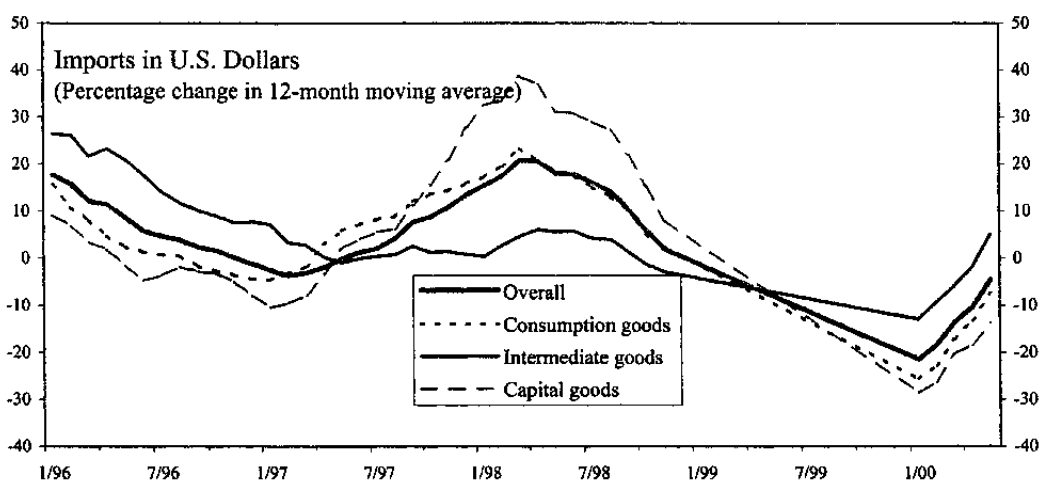
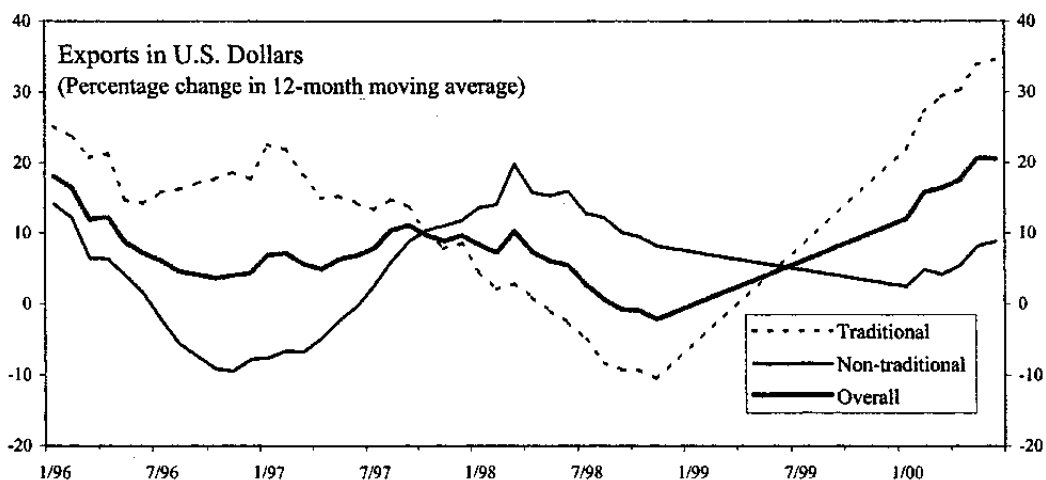
1/ Based on the change in the consumer price index over the preceding twelve months.

Figure 5. Colombia: Monetary Indicators



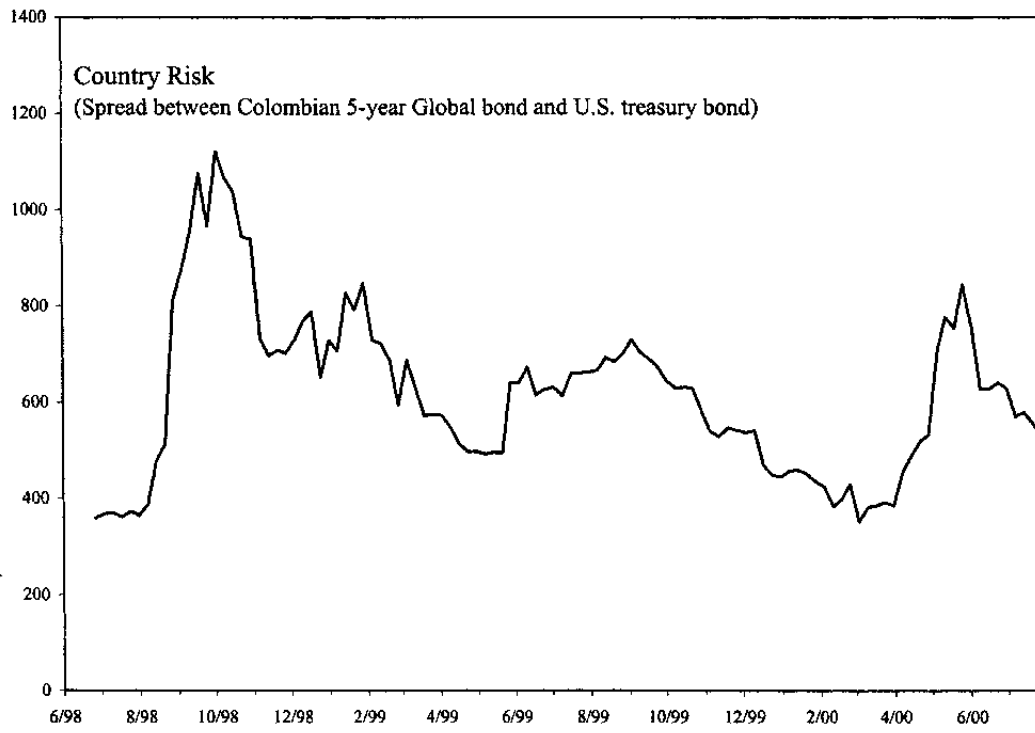
Source: Banco de la Republica.

Figure 6. Colombia: Trade Indicators



Source: Banco de la Republica.

Figure 7. Colombia: External Indicators



Sources: Banco de la Republica; and Bloomberg.



9. The government has made advances on its structural reform agenda after its three-year development plan was approved in May 1999; later in the year legislation was passed to set up funds to support the territorial governments' pension obligations, and to control the establishment of new universities. Legislation subsequently has been enacted to strengthen the territorial government finances by limiting their current expenditures and halt the creation of new municipalities, and a bill to organize lottery and gaming activities to contribute resources to the new pension funds is currently before congress. Also before congress is a proposal to change the system of revenue transfers to territorial governments, as well as a tax package that would yield 0.3 percent of GDP a year, based on a reduction in the income tax rate from 35 to 32 percent over three years; measures to strengthen tax enforcement; and the creation of a simplified tax regime for small businesses.<sup>8</sup> The package also calls for making permanent the 0.2 percent financial transactions tax; under the program it had been envisaged that this tax would be extended only to the end of 2002.

10. A political reform initiative announced by the government in March 2000 sparked a controversy that raised doubts about its ability to keep together the congressional alliance on economic issues, and in response the peso depreciated markedly again in April/May and the spread on Colombian sovereign bonds widened (see Figure 7). The initiative, which was announced in the wake of allegations of misuse of funds by the congress, called for a number of political reforms. In the context of subsequent negotiations between the two main political parties to settle the controversy and seek understandings on the reforms, it would appear that support for the economic policy agenda has been largely preserved, and in July members of the opposition Liberal party were appointed (in a personal capacity) to key positions in the cabinet, including the ministry of finance.

### III. POLICY DISCUSSIONS

11. The discussions for the review were held mainly with the outgoing economic team, but staff also met with the new minister of finance at the end of July, shortly after he had been appointed. The discussions focussed on policies for the remainder of 2000 amid signs that the economic recovery is taking hold and that the macroeconomic objectives of the program can be achieved. Looking beyond 2000, the talks centered on the achievement of the program targets, particularly the fiscal objectives for 2001 and the initiatives underway to sustain the momentum of the government's structural reform program. The authorities also outlined to the staff the "Plan Colombia" which integrates their strategies for settling the internal conflict,

---

<sup>8</sup> The simplified regime (*Régimen de Impuestos Simplificado*—RIS) would replace the income and value-added taxes for small- and medium-size tax payers. The tax itself would be levied on the basis of presumed annual income. It is estimated that the RIS will be applied to some 500,000 taxpayers.

reducing the cultivation and trafficking in illicit drugs, and dealing with the social fall-out from these problems (Box 3).

#### A. Fiscal Policy

12. Reflecting the deeper than anticipated recession in 1999, the authorities have revised downward the projection of non-oil tax revenue in 2000, and the contributions to the social security system also have been revised downward. However, with average oil prices now expected to be US\$25.9 per barrel (compared with US\$17.7 in the program), this shortfall would be more than offset by additional oil revenue, despite somewhat lower than projected oil production, and a one-time increase in tax collections from a shortening of the transit period of taxes through the banking system.<sup>9</sup> On this basis, total revenue of the NFPS would exceed the program projection by 1.5 percent of GDP, but the overall deficit of the NFPS would remain as envisaged at 3.6 percent of GDP, as new spending programs are being introduced to help deal with several critical problems, including the internal conflict and the associated social problems, the financial difficulties of some territorial governments, and unemployment (see Tables 3 and 4).<sup>10</sup> The authorities explained that the additional spending would be temporary, for the most part, and would be concentrated on low cost housing construction, additional electricity subsidies for the lowest income groups following the rise in fuel costs, security related outlays, and support for the pension obligations of some territorial governments. The deficit of the combined public sector would be 3.7 percent of GDP,

---

<sup>9</sup> This shortening—from 22 days to 14 days—took place in the first quarter of 2000, providing a one-time revenue gain of about 0.2 percent of GDP this year.

<sup>10</sup> The new spending programs will give rise to a larger than projected deficit on the part of the central administration, which will execute the programs, offset by a higher surplus in the rest of the public sector, mainly accounted for by the principal recipients of petroleum revenue.

### **Box 3. Plan Colombia**

For decades, violence has imposed a heavy burden on the Colombian society. In recent years, the actions of guerrillas, private justice groups, and drug producers and traders have increased. In some regions of the country, these groups have virtually displaced the state. The social support system has become overtaxed and poorly able to deal with the fall-out from the mounting insecurity; as a result, the number of internally displaced persons has risen.

The administration of President Pastrana has made peace its first priority. Reflecting this, a set of strategies, policies, and projects has been developed and presented as the "Plan Colombia." The plan calls for building peace through negotiations, protecting human rights, enhancing the presence of the state, securing economic recovery, reducing the production and trade of drugs, and safeguarding the environment. Colombia has sought to involve the international community as a political facilitator and a provider of financing for the plan.

Negotiations with armed groups is a main element of the plan; the authorities will seek to reach peace agreements and build consensus on reforms needed to eliminate the causes of the conflict. Negotiations have started with the two guerrilla groups, and agreements have been reached on procedures, the agenda, and the mechanisms for participation by additional parties.

The drug related activities have intensified the violence and led to a serious deterioration of the country's social fabric. The aim of the plan is to halt the expansion of the illegal crops and reduce the production of narcotics by 50 percent over the next six years. This will require stepped-up drug interdiction, further strengthening of control of money laundering, support for small farmers to develop alternative crops, provision of personal security, and the building of physical and social infrastructure.

To promote institutional strengthening and social development, public institutions and NGOs will allocate resources to improve physical and human capital. The plan calls for the development of viable economic activities through investment in physical capital, especially in remote areas, and for improvement in the quality of life through investment in basic services. It also seeks to improve the environment in regions where, as a result of the armed conflict and drug related activities, water sources and woodlands have suffered. Investment in social capital will focus on training and humanitarian assistance to the victims of violence, with special emphasis on the most vulnerable groups, such as women and children.

The total cost of the plan is US\$6.9 billion (some 8 percent of annual GDP) over three years. The most important item is related to the fight against drugs, which accounts for 55 percent of the total. Colombia has requested international support of US\$2 billion. Recently, the United States Congress approved US\$1.0 billion in support of the plan, and a consultative group meeting was held in Madrid in June, with a follow-up meeting planned for Bogota in September, to help secure funding for the plan.

The plan envisages that public entities, private firms, NGOs, community organizations, universities, and international agencies, among others, will execute the projects, and the National Planning Department has drawn up a list of qualified agencies. A Peace Investment Fund (FIP) has been created to manage the collection and use of the plan's resources, including those that come from the budget, and ensure transparency and accountability. A unit in the presidency will manage the FIP under the direction of a board composed of members of nongovernmental groups, the private sector, and senior officials.

0.2 percent of GDP higher than indicated earlier, due to higher costs of the financial sector restructuring programs (see Box 2).<sup>11</sup>

13. The staff questioned the temporary nature of some of the new spending programs and cautioned against allowing the increase in oil revenue to be translated into spending commitments that would be difficult to reverse if oil prices fall. In response, the authorities explained that the oil prices used in their most recent fiscal projections for 2000 correspond to those indicated by the latest WEO projections, and noted that there are margins in the program, reflected in the strong fiscal performance in the first quarter of 2000; they also noted that the collection of non-oil revenue continued to exceed projections through June. The authorities reiterated their strong commitment to reducing expenditures, if necessary, to stay within the deficit limits of the program, and assured the staff that the planned strengthening of the underlying fiscal structures would be accomplished through the pursuit of the structural reform agenda, which they plan to strengthen further, as discussed below.

14. The staff expressed support for the authorities' proposal to monitor fiscal developments under the program on a commitment basis (see Box 1), and noted that a recent FAD mission had found the present reporting and monitoring system for budget carry-overs to be of high quality. It urged the authorities to ensure that the reporting will remain accurate.

15. In presenting the "Plan Colombia" to the staff, the authorities explained that the public sector's contribution to the plan—some two-thirds of the total cost of US\$6.9 billion over three years—is being incorporated within the fiscal program (see Box 3). They emphasized the need to also accommodate the expenditures to be financed with the external assistance that is being secured for the plan, a large part of which would be spent on equipment purchases abroad. To this end, they proposed that the disbursements of concessional loans be facilitated through the inclusion of an adjustor in the program ceilings on the fiscal deficit and the public external debt. It is not expected that significant loan disbursements will take place in 2000.

16. Under the program it was envisaged that the large number of privatization projects that was being prepared for 2000 would provide the resources necessary to finance the combined public sector deficit, and that a small increase in external debt would be matched by a reduction in domestic indebtedness. In the event, the privatization program is now expected to fall well short of expectations, with some projects being postponed to 2001, mainly due to the recent security problems facing the electricity sector and the present lack of investor interest in the public banks (Box 4). The shortfall this year is likely to be equivalent to

---

<sup>11</sup> The projected deficit of the combined public sector in 2000 that was presented with the program was 3.5 percent of GDP. Nonetheless, the proposed ceiling on the combined public sector deficit (performance criterion) for end-2000 is well within the limits of the cumulative financing of the deficit for the period 1999–2000 indicated in the original program.

1.9 percent of GDP, a part of which would be compensated with the use of financial assets held abroad by the public sector and by additional domestic credit; the rest would be made up with additional external borrowing, which is being secured through accelerated preparation and disbursement of some sector loans from the multilateral lending institutions and by additional bond placements. (Colombia's most recent bond issue, for €300 million, in June 2000 was oversubscribed and carried a 596 basis point spread.) To allow for the additional external borrowing, the end-2000 ceiling on the public sector's medium- and long-term external debt would be set US\$300 million higher than the indicative ceiling suggested in the program; this amount corresponds to about half of the value of the large electricity company, ISA, which would be privatized in 2001 instead of in 2000.

#### **Box 4: The Revised Privatization Program**

The government's economic program included a bold privatization plan for 2000. It envisaged the privatization of a large electricity distribution company ISA; the electricity generating company ISAGEN; fourteen regional electricity distribution companies; the coal mining company CARBOCOL; and all state-owned banks except one. The government also expected to sell telephone concessions, and the city of Bogota planned to sell its telecommunications company, ETB. In total, the privatization program would yield about US\$2.8 billion (3.5 percent of GDP) in net proceeds.

As it turns out, the privatization plan for this year cannot be fully implemented. Mainly as a result of the worsening security situation and the risks associated with investing in Colombia (reflected in the loss of investment grade rating on sovereign debt last year and the negative outlook still reported by most rating agencies), the government has extended the timetable and revised downwards the projected proceeds. ISA has been the target of guerrilla attacks on its main transmission lines and the needed repair is likely to delay its privatization. Following a more detailed valuation analysis, the government also has decided to privatize the regional electricity distribution companies by inviting private ownership participation through capital injections which is expected in 2001 but is unlikely to provide any net cash proceeds. Moreover, the sale of telephone concessions will not take place as a result of the deregulation of the industry that took effect this year. Finally, the state-owned banks have suffered additional losses, and the ongoing restructuring process is likely to delay their sale.

Privatization of the remaining companies is proceeding, and it is expected that the sales will be completed in the second half of this year. In the case of ISAGEN and CARBOCOL, the closure of the bid process is expected shortly, with the final sale to be completed in the fourth quarter. Two European telecommunications companies have expressed strong interest in ETB, and that sale also should be completed this year. Net proceeds from these divestitures are projected to be about US\$1.4 billion in 2000. In 2001 net proceeds are projected to increase by US\$0.8 billion as a result of the delay in the privatization of ISA and the state-owned banks.

17. Looking ahead, the authorities explained that the budget for 2001 that was introduced in congress in late July was consistent with the program's NFPS deficit target of 2.5 percent of GDP, based on tight spending policies (including wage increases below projected inflation),

the elimination of government agencies, and a capital spending plan that will be executed fully only to the extent additional revenue for 0.8 percent of GDP can be mobilized. To this end, they undertook to introduce a set of revenue measures later in the year, complementary to the tax package that is currently before congress. They also have announced the closure of 23 government agencies, involving more than 5,000 employees, to be effected by decree with severance payments charged to the 2000 budget.<sup>12</sup> Notwithstanding the additional revenue effort and the fact that the tax revenue of the NFPS would increase as the economic recovery gains momentum, total revenue of the NFPS would decline in 2001 as oil prices are projected to fall and the combined operating surplus of the public enterprises declines due to privatization. The latter, and the reduced role of the state oil company in exploration and operations, would be reflected in lower investment spending by the NFPS. The staff encouraged the authorities to proceed with the planned strengthening of the revenue effort, recommending that it be based on the measures contemplated in the program (mainly a widening of the base for the income and value-added taxes), and cautioned that the fiscal adjustment envisaged for 2001 and 2002 would be difficult to achieve and sustain if it were to rely mainly on expenditure compression, particularly further wage concessions and cutbacks in public investment. The fiscal program for 2001, its financing, and the revenue package to be introduced later this year will be focal issues during the second program review (scheduled for consideration by the Executive Board in December 2000).

18. The further fiscal consolidation required to bring the NFPS deficit to the programmed 1.5 percent of GDP in 2002 would be achieved, in part, through the adoption of a territorial government tax reform to be introduced in congress in early 2001; the effect of the proposed reform (constitutional change) of the revenue sharing system that is currently before the congress; reforms of the health system (noted below), and through application of a fiscal responsibility law, which the authorities expect will take effect next year (noted below).

### **B. Monetary Policy**

19. In light of the stronger than projected demand for currency, the authorities are proposing that the ceiling on the central bank's net domestic assets (NDA) for the second half of 2000 be set somewhat higher than suggested by the indicative targets presented with the program, while the target for the net international reserves would remain unchanged. The central bank considers that the higher holdings of liquid assets reflect a permanent shift in the composition of money demand following an expansion of the financial transactions tax base in early 2000, and in recognition of that it has shifted upward by 3 percent its reference corridor for base money (intermediate target for its inflation control policy). While recognizing that an upward shift of the base money corridor would not be inflationary as long as the stronger

---

<sup>12</sup> This downsizing action follows sizeable staffing reductions in the territorial governments and public banks over the past two years.

preference for liquid assets is permanent, the staff nevertheless expressed caution about the downside risks of facilitating a more rapid growth of base money. In response, the authorities indicated that they would be prepared to reverse the decision on the base money corridor should the shift to higher demand for base money turn out not to be permanent.

20. The staff cautioned that the upward shift in the base money corridor and the depreciation of the peso so far this year could heighten the risk of reigniting inflationary pressures. The authorities maintained that the objective of keeping price increases to 10 percent during 2000 will be achieved, noting that the sharp rise in some important food prices would be reversed as more ample crops come to market in the last half of the year. They also pointed to the recent pass-through of higher fuel prices; the fact that core inflation remains below the target; and the moderation of wage demands over the past 12 months.<sup>13</sup> They believe that the pass-through of the depreciation of the peso so far this year will have relatively little impact on the general price level, but indicated that they remain prepared to take action as required to achieve the inflation objective of the program. In this regard, they pointed to the interest rate hikes by the central bank in January and June, and noted that the decline in retail interest rates had stopped, and that some rates—particularly deposit rates—had shown an upward trend in recent months.

### C. The Structural Reforms

21. With regard to the structural reforms, most of the actions contemplated in the program have been executed, while some have been delayed or weakened somewhat. At the same time, new projects are being introduced as the authorities continue to develop and strengthen their structural reform agenda.

22. The staff noted that the tax package that is currently before congress is weaker than envisaged, not only in terms of revenue mobilization but also in terms of structural content, and welcomed the government's intention to seek a strengthening of the tax reform later in the year. In this context, the staff urged the authorities to proceed with the elimination of the financial transactions tax by the end of 2002 as contemplated in the program, pointing to the commonly held view that the introduction of this tax and the widening of its base earlier this year had contributed to financial disintermediation, as reflected in the increased demand for currency.

23. A proposal to de-link the transfers to territorial governments from government revenue was introduced in congress in late 1999 as provided in the program, but it was withdrawn and amended to allow the transfers to increase by 1.5 percent a year in real terms in order to ensure that the provision of health and education services keep pace with

---

<sup>13</sup> Wages in the manufacturing sector have risen in real terms so far in 2000; unit labor cost, on the other hand, has declined due to a notable increase in productivity.

population growth; the original proposal had called for freezing the transfers in real terms at a level corresponding to 46.5 percent of the government's current revenue in 2001. The impact on the central government's finances of the change would be small, less than 0.1 percent of GDP per year initially, rising to less than 0.3 percent of GDP by the fifth year. The amended proposal was re-introduced in March 2000, with the first of two readings by consecutive congresses (required for a constitutional change) expected in the fall session of 2000.

24. Under the program, the presentation to congress of the second generation reform of the social security pensions had been scheduled for last December (a program benchmark), but it was postponed in order to provide time for a technical strengthening of the proposal (including on advice from the World Bank) and to build public consensus on the contents of the reform. In an attempt to achieve the latter, the government has invited political parties, labor unions, employers, experts, and others to "round table discussions" on the pension reform. The authorities informed the staff that it was proving difficult to reach agreement on the reform through these discussions, but they noted that even if a workable compromise cannot be found, the government's proposal would be presented to congress before the end of the year; the corresponding program benchmark would be changed to reflect that.

25. All but one of the regulations needed to implement the provisions of the 1999 financial reform law have been issued. The authorities already have published the pending regulations for comments and are working with MAE on the final version, which is expected to be adopted and issued shortly (issuance of the regulations by June 2000 was a program benchmark). The pending regulation defines a set of early warning indicators that will allow the authorities to require quick action on the part of the institution concerned to correct potential prudential problems.

26. Since the approval of the EFF last year, the authorities have continued to develop and strengthen their structural reform agenda by adding new initiatives. In particular, action will be taken before the end of 2000 to close 23 government agencies, as noted above. In addition, the government has advanced on the drafting of a fiscal responsibility law to supplement and reinforce the structural reforms already on the government's agenda. The provisions of the law would be applicable to both the central administration and the territorial governments, and would help to achieve the programmed fiscal consolidation for 2001 and 2002 and ensure that the public finances remain viable also beyond the period of the program. The presentation to congress of the fiscal responsibility law by December 2000 would be a structural benchmark under the program. Also, the financial deterioration of the health system under the social security institute (ISS) points to a need for restructuring the way health services are provided. To this end, the authorities have been studying various options and expect to bring forth proposals for reform before the end of the year. Both the fiscal responsibility law and any reforms of the health system would be discussed in the context of the second review of the program.



#### D. External Policies

27. Under the program, it was expected that last year's recession-induced narrowing of the external current account deficit would be partly reversed in 2000, as aggregate demand recovered. The revised projections suggest that while a recovery is in progress, the deficit would remain about unchanged from 1999 due to the higher than projected prices of oil exports (see Table 7). Other exports, except coffee which has suffered declining prices for the past three years, grew rapidly in the first half of 2000, as volumes increased in the wake of the real depreciation of the peso that has taken place since mid-1998.

28. The Colombian trade regime continues to be liberalized within the framework of the WTO agreements. The authorities confirmed that the performance requirements for foreign investment in the automotive sector were eliminated as scheduled at end-1999 and that Colombia would soon be in full compliance with the WTO agreement on intellectual property rights which is being implemented at the level of the Andean Community.<sup>14</sup> However, performance requirements in the agricultural sector are still in place pending a global agreement under the WTO, which has granted an extension to April 2003 of the deadline to eliminate the remaining official minimum prices in this sector.

29. The net capital inflow to Colombia in 2000 is projected to fall well short of the program projections, mainly on account of the difficulties in executing the privatization program. Low domestic interest rates also have been providing incentives for shifting out of peso denominated assets, as evidenced by the deterioration of net short term flows in the first five months of 2000.<sup>15</sup> In response to concerns expressed by the staff about the effect on capital flows of the interest rate differential, the authorities stated that central bank rates have been raised somewhat since the beginning of the year, as noted above, and that the nonremunerated deposit requirement on external loan proceeds was reduced to zero in May, and they saw little need for a stronger move to raise interest rates as long as inflationary pressures remain subdued.<sup>16</sup> With the stronger than projected current account balance, the authorities remain confident that the NIR target for end-2000 will be achieved.

---

<sup>14</sup> Performance requirements are rules that require foreign investors to meet certain criteria that are different from those applicable to national producers, e.g., domestic contents requirements.

<sup>15</sup> Taking the depreciation of the peso into account, the returns obtained by investing in U.S. dollar deposits would have exceeded investments in peso deposits by 15–20 percentage points for most of the past year.

<sup>16</sup> The nonremunerated deposit requirement is described in SM/98/251 (Colombia—Selected Issues and Statistical Appendix), chapter IV.

30. Colombia's external debt is now projected to rise to 45.2 percent of GDP at the end of 2000, compared with 43.1 percent of GDP under the program (Table 8). The increase reflects, in part, the additional borrowing by the public sector to make up for the delays in privatization. With the delayed privatizations expected to take place in 2001, both the public external debt and Colombia's total external debt can be expected to remain about unchanged in terms of GDP from 2000 to 2001.<sup>17 18</sup>

### **E. Financial Sector Restructuring**

31. The situation of the Colombian financial sector remains delicate despite the recent improvement in most prudential indicators. In the last year and a half, financial institutions have been burdened with taxes, forced investments, and quasi-fiscal responsibilities. The staff urged the authorities to avoid burdening these institutions further, and underscored the importance of eliminating the tax on financial transactions. They agreed that additional burdens should not be placed on the banks and shared the concern that part of the financial system remains vulnerable, particularly the public banks and the savings and loan institutions. The latter have required considerable support after the softening and collapse of the real estate market, and while their prudential indicators have improved, they remain vulnerable. At the same time, the authorities underscored that the financial sector has been strengthened considerably in the recent past, helped by the restructuring and recapitalization programs, noting also that the economic recovery that is underway would further benefit the sector.

32. Despite the steps already taken to restructure the public banks, their operations have continued to be hampered by low efficiency and continued losses. In an effort to boost their value prior to their privatization, the authorities have been seeking to merge and liquidate some of the remaining banks.<sup>19</sup> Because of the need to proceed with the provisioning of their

---

<sup>17</sup> The ratio of Colombia's total external debt to GDP would exceed the program projection by nearly 2 percentage points of GDP both in 2000 and 2001, reflecting not only higher debt in U.S. dollars, but also the lower than projected nominal GDP and the strengthening of the U.S. dollar.

<sup>18</sup> The outlook for Colombia's external debt will be presented in the context of a medium-term projection of the balance of payments at the time of the second review, when the program for 2001 is considered by the Executive Board (scheduled for December 2000).

<sup>19</sup> A large portion of the assets and liabilities of the Banco Central Hipotecario (BCH) were transferred to Granahorrar in January 2000 and BCH is expected to be closed in the second half of 2000. Uconal and Banco del Estado were merged in August 1999; a large part of the assets and liabilities of the resulting entity, Banco del Estado, are expected to be transferred to Bancafé in the second half of 2000. Granahorrar and Bancafé are expected to be divested in 2001.

bad loan portfolio, FOGAFIN is expected to inject the equivalent of about 1 percentage point of GDP in additional equity capital in 2000. The staff urged the authorities to complete the restructuring of the state banks as soon as possible, including by improvements in the provisioning of bad loans and continuing efforts to reduce operational expenses.

#### IV. STAFF APPRAISAL

33. Early indications suggest that economic activity in Colombia is recovering about as envisaged, and the program supported by the extended arrangement remains on track. The staff welcomes the authorities' reaffirmation of the strategies and policies underlying the program, focussed on fiscal consolidation, structural reform, financial sector restructuring, and exchange rate flexibility. Their recent efforts to sustain the political support for this strategy appear to have been successful.

34. Nevertheless, the authorities face considerable challenges to achieve the objectives of their three-year program. Most important is the need to make progress toward settlement of the internal conflict, curb the production and trafficking in illicit drugs, and address the social fall-out from these problems. Advances on these fronts would help strengthen confidence and facilitate the longer term commitments that would be required for a timely recovery of private investment. To this end, the authorities have developed a comprehensive, multi-year strategy, presented as the "Plan Colombia," for which they are seeking support from the international community.

35. As regards the public finances, the fiscal consolidation called for in the program for 2000 had been based—to a large extent—on tight spending policies, but subsequently the authorities decided to use the oil revenue windfall to boost their efforts to deal with four major problems: the internal conflict, high unemployment, weaknesses in the public banks, and the financial problems faced by some territorial governments. They have explained that most of the associated spending increases will be temporary. The staff understands the importance of addressing these problems in view of the delicate security situation and the continued weaknesses of the public banks; nevertheless, caution needs to be exercised in making new spending commitments that may be difficult to reverse if oil prices were to fall.

36. The staff considers prudent the authorities' downward revision of the forecast for non-oil revenue for 2000. That, together with the indications of strong fiscal performance so far this year and the government's firm commitment to introduce spending cuts should revenue collections fall short of the projection, provides comfort that the fiscal objectives for 2000 can be achieved.

37. The tax package currently before congress is weaker both in terms of resource mobilization and structural contents than envisaged in the program, and given the uncertainties of oil prices, the fiscal adjustment planned for 2001 could be difficult to achieve, especially if the government were to rely mainly on expenditure compression. The staff

therefore welcomes the recent decision to strengthen the revenue effort by introducing tax measures later in the year that will complement the current tax proposals. The staff will urge the authorities to reconsider the proposal to make the financial transactions tax permanent, as this tax contributes to disintermediation and, if used at all, should be used only as a temporary expedient in the face of fiscal pressures, as indicated in a study prepared by the Fund. The decision to reduce the number of government agencies also would support the fiscal consolidation effort in 2001 and beyond.

38. The staff concurs with the authorities' views that the fiscal adjustment in Colombia should be measured by taking account of the changes in the full budget carry-over. Hence, and given the assurances about its monitorability, the staff supports their proposal to change the definition of the combined public sector deficit for the purpose of monitoring the fiscal program.

39. On monetary policy, the staff notes that the exchange market has remained orderly since the peso was floated, and that the foreign exchange auction system introduced last year is transparent and has been functioning well. However, the recent stance of monetary policy—which has provided for record low real interest rates—may risk rekindling inflationary pressures, and the staff will urge the authorities to stand ready to tighten monetary policy to ensure that the inflation objective of the program is attained. Also, the authorities may need to make adjustments should the shift to higher demand for currency turn out not to be permanent, but to also reflect transitory factors, such as the public's response to the recent problems faced by the banking system and the adjustment of portfolios to the fall in interest rates. The staff supports the lowering to zero of the deposit requirement on external borrowing.

40. The staff welcomes the measures proposed by the authorities to strengthen the structural reform program, particularly the plan to present a fiscal responsibility law to congress later this year and the decision to close a large number of government agencies. The staff will encourage the authorities to proceed with the proposed reforms intended to enhance revenue efficiency, and will strongly recommend that a broadening of the income and value-added taxes be part of the reform. In view of the difficulties faced by some territorial governments, the staff will urge that a strong territorial tax package be introduced in early 2001.

41. The staff is encouraged by the authorities' commitment to the privatization program, and supports their proposal to set the ceiling on medium- and long-term external debt for the rest of 2000 somewhat higher than had been indicated in the program in order to accommodate the delay of some sales to 2001.

42. The staff also welcomes the reported strengthening of the financial system's prudential indicators. The public banks remain a cause for concern, and the staff will encourage the authorities to move swiftly to either sell or liquidate those public banks that have been slated

for privatization. The financial position of the savings and loan institutions also warrants close monitoring.

43. Overall, the staff is of the view that the authorities have made a strong initial effort to implement their program and to ensure that it receives political support. The ground has been laid for the program's success, as suggested by the economic recovery, the easing of the banking crisis, and the early fiscal adjustment. The authorities should continue to strengthen their structural reform agenda through the development of new initiatives. While some of the risks to the program pointed out by the staff have been reduced, others have been borne out, such as the excessive reliance on privatization proceeds to finance the fiscal deficit. Other risks remain; in particular, the prospects for peace are uncertain, although the "Plan Colombia" holds out encouraging prospects.

44. Notwithstanding the risks, the staff recommends completion of the first review under the extended arrangement on the basis of good performance so far and the authorities' firm commitment to the policies and the measures required to attain the objectives of the program. The staff also supports the authorities' proposal to (i) set the program ceiling on external debt somewhat higher than indicated earlier; (ii) introduce an adjustor to the ceilings on the fiscal deficit and external public debt to allow disbursement of concessional loans in support of the "Plan Colombia"; (iii) change the definition of the fiscal deficit for the purpose of monitoring the program; and (iv) set the ceiling on the central bank's net domestic assets somewhat higher than indicated earlier, consistent with the recent lifting of the base money corridor.

## V. PROPOSED DECISION

The following draft decision is proposed for adoption by the Executive Board:

1. Colombia has consulted with the Fund in accordance with paragraph 3(c) of the Extended Arrangement for Colombia (EBS/99/218, Supplement 1) and paragraph 3 of the letter dated December 3, 1999 from the Minister of Finance and Public Credit and the General Manager of the Bank of the Republic, in order to review the implementation of the program and to establish performance criteria for September 30 and December 31, 2000.

2. The letter from the Minister of Finance and Public Credit and the General Manager of the Bank of the Republic of Colombia dated August 22, 2000, with its attached Technical Memorandum of Understanding (the "Memorandum"), shall be attached to the Extended Arrangement for Colombia, and the letter dated December 3, 1999 and its annexed Memorandum of Economic Policies shall be read as supplemented and modified by the letter dated August 22, 2000 and its attached Memorandum.

3. Accordingly, the performance criteria referred to in paragraphs 3(a)(i), (ii), (iii), (iv), and (v) of the Extended Arrangement for September 30 and December 31, 2000 shall be as specified in Section I (A), Section II (A), and Sections III (A), (B), and (C), respectively, of the Memorandum.

4. The Fund decides that the first review contemplated in paragraph 3(c) of the Extended Arrangement for Colombia is completed.

Table 1. Colombia: Performance Criteria 1/

	Dec. 31 1999	Mar. 31 2000	Jun. 30 2000
Cumulative flows from January 1, 1999 (In billions of Col\$)			
<b>Overall balance of the combined public sector</b>			
Floor	-9,150	-11,550	-13,300
Outcome	-6,871	-5,903	-7,570
Margin or deviation (-)	2,279	5,647	5,730
Outstanding stock (In billions of Col\$)			
<b>Net domestic assets of the Banco de la Republica</b>			
Ceiling	-7,650	-8,950	-9,050
Adjusted ceiling	-7,650	-8,655	-7,205
Outcome	-6,901	-9,789	-8,718
Margin or deviation (-) 2/	-749	1,135	1,513
(In millions of US\$)			
<b>Net international reserves of the Banco de la Republica</b>			
Target	7,850	8,150	8,350
Adjusted target	7,850	8,006	7,450
Outcome	8,116	8,254	8,335
Margin or deviation (-)	266	248	885
Cumulative net disbursement from January 1, 1999 (In millions of US\$)			
<b>Net disbursement of medium- and long-term external debt by the public sector</b>			
Ceiling	2,450	2,600	2,750
Adjusted ceiling	2,450	2,793	3,383
Outcome	1,768	2,291	2,248
Margin or deviation (-)	682	502	1,135
<b>Change in the outstanding stock of short term external debt of the public sector</b>			
Ceiling	382	70	70
Outcome	368	56	56
Margin or deviation (-)	14	14	14

Sources: Ministry of Finance, Banco de la Republica, and Fund staff estimates.

1/ Definitions of concepts and adjustments to the performance criteria are explained in the Annex to Attachment II.

2/ The end-1999 deviation (excess) in net domestic assets reflected excess liquidity demand at the end of the year related to the Y2K problem.

Table 2. Colombia: Structural Benchmarks Under the Program

	<b>Benchmark</b>	<b>Status</b>
<b>By December 31, 1999</b>	Present to congress a proposal for a second generation social security reform. (Modifying Law 100 of 1993).	Postponed to December 2000.
	Present to congress a proposal for the creation of the territorial government pension funds.	Done. Approved by congress in December 1999.
	Present to congress a constitutional reform which delinks transfers to territorial governments from current income of the central government.	Done in March 2000. Reform proposal somewhat different from envisaged in program.
	Present to congress a proposal for the fiscal strengthening of territorial governments by means of limiting their current expenditures.	Done. Approved by congress in June 2000.
	Present to congress a proposal to organize lottery activities to help boost public revenue.	Done. Currently before congress.
<b>By March 31, 2000</b>	Present to congress a proposal for widening the base of the income tax, tackling "loopholes" in the VAT (national tax reform). The reform of the income tax/VAT will be designed to yield a total of 0.6 percent of GDP per year on an annual basis starting in 2001 with additional 0.2 percent of GDP in 2002.	Done, but proposal different from that envisaged in program. Currently before congress.
<b>By June 30, 2000</b>	Regulations issued to implement the provisions of the financial reform law enacted in July 1999.	All but one have been issued. The pending regulation has been published for comments and is expected to be issued shortly. The authorities are consulting with MAE on the final version.
<b>By September 30, 2000</b>	Present to congress the 2001 budget consistent with a nonfinancial public sector deficit of at most 2.5 percent of GDP	Done. Presented to congress in late July.
<b>By December 31, 2000</b>	Present to congress a draft fiscal responsibility law.	
	Present to congress a proposal for a second generation social security reform (modifying law 100 of 1993).	Postponed from December 1999.
<b>By March 31, 2001</b>	Present to congress a proposal on territorial tax policy, granting more fiscal autonomy to territorial governments (territorial tax reform).	
<b>By December 31, 2001</b>	Full disinvestment of all remaining public banks, excluding Banco Agrario.	
<b>By September 30, 2002</b>	Complete process of bringing provisioning standards of the financial institutions to international levels.	
	Latest date for accepting the obligations of Article VIII, Sections 2, 3, and 4 of the Fund's Articles of Agreement.	



Table 3. Colombia: Selected Economic and Financial Indicators

	1996	1997	1998	1999		2000		Rev. Proj.	
				Prog.	Prel.	Prog.	Rev. Proj.	2001	2002
(Percentage changes, unless otherwise indicated)									
<b>National income and prices</b>									
Real GDP	2.1	3.4	0.5	-3.5	-4.5	3.0	3.0	3.8	4.8
GDP deflator	16.9	16.8	15.9	11.6	12.2	11.5	10.8	8.8	7.0
Consumer prices (average)	20.8	18.5	18.7	11.3	10.9	11.2	11.2	8.8	7.0
Consumer prices (end of period)	21.6	17.7	16.7	11.0	9.2	10.0	10.0	8.0	6.0
<b>External sector (on the basis of U.S. dollars)</b>									
Exports (f.o.b.)	4.0	10.1	-5.8	8.9	4.8	9.2	16.3	3.0	-2.5
Imports (f.o.b.)	-0.6	12.8	-5.2	-29.8	-26.4	20.2	9.0	9.9	5.0
Export volume	-2.3	6.6	5.4	5.1	0.1	6.0	3.8	1.1	0.4
Import volume	2.0	21.7	-1.4	-28.9	-26.7	18.4	7.8	4.3	2.4
Terms of trade (deterioration -)	9.2	11.4	-7.0	5.0	4.2	1.5	10.7	-0.7	-5.3
Nominal exchange rate to U.S. dollar 1/2/ (depreciation -)	-12.0	-9.1	-20.1	...	-18.8	...	-20.0	...	...
Real effective exchange rate 1/2/3/ (depreciation -)	7.0	11.3	-4.7	...	-9.6	...	-11.9	...	...
<b>Central administration</b>									
Revenue	23.0	27.9	9.8	9.2	8.1	20.7	21.3	21.8	13.0
Expenditure 4/	34.7	15.6	31.2	18.4	15.7	5.7	10.6	7.1	13.0
<b>Money and credit 5/</b>									
Broad money	30.0	24.5	10.3	12.8	8.7	18.2	11.4	13.1	12.2
Private sector credit	25.7	25.6	11.9	5.9	6.1	16.7	8.6	12.3	13.3
Income velocity of money	2.8	2.7	2.8	2.7	2.8	2.6	2.9	2.9	2.9
Interest rate (90-day time deposits) 6/									
Nominal	27.9	24.3	34.1	...	15.4	...	...	...	...
Real	5.0	5.6	14.9	...	5.6	...	...	...	...
Broad money (as ratio to net international reserves)	3.6	3.5	3.9	3.7	3.6	3.6	3.3	3.3	3.3
(In percent of GDP)									
Central administration balance 4/	-4.9	-3.4	-6.0	-7.1	-7.5	-5.0	-6.1	-4.2	-4.0
Public sector savings 4/ 7/	6.2	5.7	4.3	3.0	3.4	4.8	5.1	5.4	5.0
Nonfinancial public sector balance 4/	-2.8	-3.6	-4.4	-6.3	-6.3	-3.6	-3.6	-2.5	-1.5
Combined public sector balance 4/	-2.8	-3.6	-3.7	-5.9	-5.4	-3.5	-3.7	-2.6	-1.5
Foreign financing	0.9	0.6	1.8	1.6	1.3	0.4	1.4	0.6	1.0
Domestic financing 8/ 9/	1.2	1.7	1.8	3.6	3.4	-0.5	0.7	0.8	0.7
Privatization	0.8	1.3	0.1	0.7	0.7	3.5	1.6	1.2	-0.2
Public debt	24.6	24.2	27.5	34.5	35.6	34.4	35.5	34.2	33.8
Gross domestic investment	22.2	20.9	19.8	15.3	14.5	18.4	16.6	21.0	22.0
Gross national savings 7/	17.2	15.3	14.5	14.0	13.4	16.0	15.5	19.0	19.3
Current account (deficit -)	-5.0	-5.6	-5.3	-1.3	-1.1	-2.4	-1.1	-2.0	-2.7
External debt 10/	31.6	31.5	35.8	41.1	42.6	43.1	45.2	45.4	46.2
Of which: Public sector 10/	17.0	15.8	18.9	23.3	23.8	24.8	26.0	26.2	26.9
Total short-term external debt to reserves 11/	49.9	47.8	52.7	72.0	72.0	57.2	57.2	66.4	58.4
(In percent of exports of goods, services and income)									
External debt service 10/	39.3	45.3	47.9	50.0	47.7	49.0	45.9	56.0	57.2
Of which: Public sector	21.7	24.0	23.0	22.6	23.2	21.1	21.0	27.2	27.1
Interest payments 10/	15.1	17.1	17.8	16.9	17.6	16.4	17.6	19.2	18.3
Of which: Public sector	8.0	8.4	8.5	8.9	8.8	9.3	9.2	10.9	3.3
(In millions of U.S. dollars)									
Overall balance of payments	1,754	280	-1,388	-750	-423	744	458	326	323
Gross official reserves 12/	9,938	9,908	8,741	8,215	8,215	9,458	8,611	8,936	9,260
Gross official reserves (in months of imports of goods and services)	6.2	5.5	5.2	5.8	5.9	5.9	5.6	5.4	5.4

Sources: Colombian authorities; and Fund staff estimates and projections.

1/ Annual average.

2/ For 2000, first six months average.

3/ Based on the Information Notice System.

4/ According to the new definition of floating debt (=unpaid bills plus outstanding commitments).

5/ All annual changes in foreign currency stocks valued at constant exchange rate.

6/ End of period.

7/ Excluding privatization proceeds. Public saving is defined as the sum of the NFPS saving and the central bank cash profits.

8/ Includes the balance of the quasi-fiscal operations of Banco de la Republica.

9/ Includes residual differences between items above and below the line, as well as sales of assets and extension of phone licenses.

10/ Includes short-term debt.

11/ Short-term debt is defined by its remaining maturity from 1999 onward.

12/ Assuming no purchases under the current EFF arrangement.

Table 4. Colombia: Operations of the Combined Public Sector 1/

(In percent of GDP)

	1996	1997	1998	1999		2000		2001		2002	
				Prog.	Prel.	Prog.	Rev.	Prog.	Rev.	Prog.	Rev.
							Proj.		Proj.		Proj.
<b>Total revenue</b>	<b>27.0</b>	<b>27.4</b>	<b>26.5</b>	<b>27.3</b>	<b>27.6</b>	<b>27.5</b>	<b>29.0</b>	<b>27.5</b>	<b>28.1</b>	<b>27.6</b>	<b>27.4</b>
<b>Current revenue</b>	<b>27.0</b>	<b>27.4</b>	<b>26.5</b>	<b>27.3</b>	<b>27.6</b>	<b>27.5</b>	<b>29.0</b>	<b>27.5</b>	<b>28.1</b>	<b>27.6</b>	<b>27.4</b>
Tax revenue 2/	16.8	17.7	17.3	16.5	17.0	18.1	17.9	19.3	18.7	19.8	19.3
Nontax revenue	10.1	9.8	9.1	10.8	10.6	9.4	11.2	8.2	9.5	7.9	8.1
Property income	0.8	0.9	0.9	0.9	1.1	0.9	1.0	1.0	1.0	1.0	1.0
Operating surplus of public enterprises	4.7	3.7	3.3	4.0	4.0	4.0	4.9	3.5	4.1	3.2	3.4
<i>Of which</i> : Ecopetrol	2.0	1.7	1.6	2.4	2.5	2.6	3.5	2.3	3.0	2.0	2.2
Other 3/	4.6	5.2	5.0	5.8	5.5	4.5	5.4	3.8	4.4	3.7	3.7
<b>Total expenditure and net lending 2/</b>	<b>29.7</b>	<b>31.0</b>	<b>31.1</b>	<b>33.6</b>	<b>33.6</b>	<b>31.1</b>	<b>32.5</b>	<b>30.1</b>	<b>30.7</b>	<b>29.1</b>	<b>28.9</b>
<b>Current expenditure</b>	<b>20.8</b>	<b>21.6</b>	<b>23.0</b>	<b>24.7</b>	<b>24.6</b>	<b>23.2</b>	<b>24.4</b>	<b>22.6</b>	<b>23.2</b>	<b>22.1</b>	<b>22.9</b>
Wages and salaries	6.6	6.7	7.0	7.5	7.8	7.0	7.2	6.5	6.7	6.2	6.5
Goods and services	3.5	3.7	3.4	3.4	3.7	3.0	3.3	2.9	3.0	2.8	2.9
Interest	2.7	2.6	3.3	4.0	3.8	4.2	4.2	4.0	4.2	4.0	4.1
Transfers and other 4/	8.0	8.6	9.3	9.7	9.4	9.0	9.6	9.1	9.3	9.1	9.3
<i>NFPS saving</i>	6.2	5.9	3.5	2.6	3.0	4.3	4.7	5.0	4.9	5.5	4.5
<b>Capital expenditure</b>	<b>8.9</b>	<b>9.5</b>	<b>8.1</b>	<b>8.6</b>	<b>8.8</b>	<b>7.9</b>	<b>8.1</b>	<b>7.5</b>	<b>7.5</b>	<b>7.0</b>	<b>6.0</b>
Net lending	0.0	0.0	0.0	0.3	0.1	0.0	0.0	0.0	0.0	0.0	0.0
Statistical discrepancy 5/	-0.2	0.1	0.1	0.0	-0.4	0.0	0.0	0.0	0.0	0.0	0.0
<i>NFPS primary balance</i>	-0.1	-0.9	-1.2	-2.3	-2.5	0.6	0.7	1.5	1.7	2.5	2.6
<b>Nonfinancial public sector balance</b>	<b>-2.9</b>	<b>-3.5</b>	<b>-4.5</b>	<b>-6.3</b>	<b>-6.3</b>	<b>-3.6</b>	<b>-3.6</b>	<b>-2.5</b>	<b>-2.5</b>	<b>-1.5</b>	<b>-1.5</b>
Quasi-fiscal balance (BR cash profits)	0.0	-0.1	0.8	0.4	0.4	0.5	0.5	0.5	0.5	0.4	0.5
Fogafin balance	...	...	...	0.3	0.6	-0.2	-0.1	0.1	0.2	0.1	0.2
Net cost of financial restructuring 6/	...	...	...	-0.2	0.0	-0.2	-0.6	-0.4	-0.7	-0.3	-0.6
<b>Overall balance</b>	<b>-2.9</b>	<b>-3.6</b>	<b>-3.7</b>	<b>-5.9</b>	<b>-5.4</b>	<b>-3.5</b>	<b>-3.7</b>	<b>-2.4</b>	<b>-2.6</b>	<b>-1.3</b>	<b>-1.5</b>
<b>Overall financing</b>	<b>2.9</b>	<b>3.6</b>	<b>3.7</b>	<b>5.9</b>	<b>5.4</b>	<b>3.5</b>	<b>3.7</b>	<b>2.4</b>	<b>2.6</b>	<b>1.3</b>	<b>1.5</b>
Foreign, net	0.9	0.6	1.8	1.6	1.3	0.4	1.4	1.3	0.6	1.0	1.0
<i>Of which</i>											
Changes in assets held abroad (-increase)	-0.4	-0.6	0.1	-0.6	-0.9	-1.3	-1.0	0.4	0.4	0.1	0.1
Domestic, net	1.2	1.7	1.8	3.6	3.4	-0.5	0.7	0.6	0.5	0.5	0.7
Financial system and bonds	0.3	2.0	0.7	3.1	2.8	-0.4	0.9	0.6	1.0	0.5	0.7
Change in floating debt, net	0.9	-0.3	1.1	0.5	0.6	0.0	-0.2	0.0	-0.3	0.0	0.0
Privatization (including concessions) 7/	0.8	1.3	0.1	0.7	0.7	3.5	1.6	0.5	1.5	-0.2	-0.2
<b>Memorandum items: (accrual basis as defined in the program)</b>											
NFPS saving 8/	6.3	5.8	4.8	2.7	3.9	4.4	...	...	...	...	...
NFPS primary balance 8/	0.4	-1.1	-0.6	-2.3	-1.4	0.6	...	...	...	...	...
NFPS balance 8/	-2.5	-3.6	-3.8	-6.3	-5.5	-3.6	...	...	...	...	...
Combined public sector balance 8/	-2.6	-3.7	-3.0	-5.9	-4.6	-3.5	...	...	...	...	...

Sources: Ministry of Finance; Banco de la Republica; and Fund staff estimates.

1/ New program definition of fiscal balance: commitment basis (see Box 1).

2/ Excludes proceeds of financial transaction tax in 1999 from revenue and expenditure.

3/ Includes local fees and penalties.

4/ Includes expenditure on an accrual basis not included in other outlays

5/ Includes residual differences between items above and below the line.

6/ Transfer to Caja Agraria in 1999, interest payments on public banks restructuring bonds and mortgage debt relief related costs.

7/ Includes nonrecurrent fees from telecommunications licensing

8/ Original program definition of fiscal balance (see Box 1).

Table 5. Colombia: Operations of the Central Administration 1/  
(In percent of GDP)

	1996	1997	1998	1999		2000		2001		2002	
				Prog.	Prel.	Prog.	Rev.	Prog.	Rev.	Prog.	Rev.
<b>Total revenue</b>	<b>11.8</b>	<b>12.6</b>	<b>11.8</b>	<b>11.9</b>	<b>12.1</b>	<b>12.6</b>	<b>12.8</b>	<b>13.3</b>	<b>13.8</b>	<b>13.7</b>	<b>13.8</b>
Current revenue	11.8	12.6	11.8	11.9	12.1	12.6	12.8	13.3	13.8	13.7	13.8
Tax revenue 2/	10.1	10.8	10.4	10.1	10.1	11.0	11.0	11.9	12.2	12.4	12.4
Net income tax and profits	3.8	4.4	4.3	4.2	4.3	4.0	4.3	4.4	4.7	4.5	4.6
Goods and services	5.3	5.3	4.9	4.9	4.9	5.2	5.1	5.7	5.8	6.0	6.1
Value-added tax	4.7	4.8	4.5	4.4	4.4	4.6	4.6	5.0	5.1	5.4	5.3
Gasoline tax	0.6	0.5	0.5	0.5	0.5	0.6	0.5	0.7	0.8	0.7	0.9
International trade	0.9	1.0	1.2	0.9	0.9	1.2	1.0	1.2	1.0	1.3	1.0
Financial transaction tax	0.0	0.0	0.0	0.0	0.0	0.6	0.6	0.6	0.6	0.6	0.6
Stamp and other taxes	0.0	0.1	0.0	0.0	0.0	0.0	0.1	0.0	0.1	0.0	0.0
Nontax revenue and transfers	1.7	1.8	1.4	1.9	2.0	1.6	1.8	1.4	1.6	1.3	1.5
Property income	0.3	0.3	0.3	0.2	0.3	0.3	0.3	0.3	0.4	0.3	0.3
Other	1.4	1.5	1.1	1.7	1.6	1.3	1.5	1.1	1.2	1.1	1.2
<b>Total expenditure and net lending</b>	<b>16.7</b>	<b>15.9</b>	<b>17.8</b>	<b>19.0</b>	<b>19.6</b>	<b>17.5</b>	<b>19.0</b>	<b>17.5</b>	<b>18.0</b>	<b>17.0</b>	<b>17.9</b>
Current expenditure	11.9	12.2	14.2	15.1	15.1	14.4	15.3	14.3	14.4	13.8	14.2
Wages and salaries	2.5	2.5	2.7	2.9	2.9	2.7	2.8	2.6	2.5	2.5	2.4
Goods and services	1.3	1.6	1.4	1.3	1.4	1.1	1.2	1.1	1.0	1.1	1.2
Interest	1.1	1.2	1.9	2.3	2.1	2.7	2.7	2.6	2.9	2.7	2.8
Other expenditure 3/	0.3	0.1	0.9	0.1	0.1	0.0	0.0	0.0	0.0	0.0	0.0
Current transfers 4/	6.7	6.8	7.4	8.5	8.6	7.9	8.6	8.0	8.0	7.5	7.8
Capital expenditure	4.4	3.6	3.4	3.4	4.0	2.9	3.1	2.9	3.3	3.0	3.7
Fixed capital formation	2.3	1.4	1.3	1.1	1.7	0.9	1.1	0.7	1.3	0.7	1.3
Capital transfers	2.1	2.2	2.0	2.3	2.3	2.0	2.0	2.3	2.0	2.3	2.4
Net lending	0.4	0.2	0.2	0.5	0.6	0.2	0.6	0.2	0.3	0.2	0.0
<b>Overall balance</b>	<b>-4.9</b>	<b>-3.4</b>	<b>-6.0</b>	<b>-7.1</b>	<b>-7.5</b>	<b>-5.0</b>	<b>-6.1</b>	<b>-4.2</b>	<b>-4.2</b>	<b>-3.3</b>	<b>-4.0</b>
<b>Memorandum items:</b>											
Current transfers to local governments 5/	4.0	4.0	4.3	4.6	5.1	4.3	4.6	4.2	0.0	4.1	4.3
Current account balance, original definition of fiscal balance 6/	0.0	0.3	-1.8	-3.1	-2.9	-1.8	...	...	...	...	...
Overall balance, original definition of fiscal balance 6/	-4.6	-3.5	-5.3	-7.1	-6.7	-5.0	...	...	...	...	...

Sources: National Department of Planning, CONFIS; and Fund staff estimates.

1/ New program definition of fiscal balance: commitment basis (see Box 1).

2/ Excludes proceeds of financial transaction tax in 1999 from revenue and expenditure.

3/ Expenditures on an accrual basis not included in other outlays.

4/ Includes interest payment to the rest of the nonfinancial public sector.

5/ After 2001, annual increase of 1.5 percent in real terms.

6/ Original program definition of fiscal balance (see Box 1).

Table 6. Colombia: Summary Accounts of the Financial System

	1996	1997	1998	1999		2000		Rev. Proj.	
				Prog.	Prel.	Prog.	Rev. Proj.	2001	2002
(Annual percentage changes) 1/									
<b>I. Financial System 2/</b>									
Net foreign assets	7.0	-0.7	-2.5	-2.0	2.8	2.1	1.5	0.2	0.0
Net domestic assets	24.8	22.9	12.7	14.6	5.8	16.1	9.6	12.9	12.2
Credit to public sector (net)	1.1	-0.3	7.3	8.2	3.7	4.6	8.7	2.1	1.1
Quasi-fiscal deficit (surplus -)	0.0	0.2	-2.4	-1.2	-1.2	-1.7	-1.7	-1.8	-1.6
Credit to private sector	28.4	20.9	8.9	2.4	-5.3	13.6	-2.9	12.1	13.0
Other (net)	-4.6	2.1	-1.1	5.2	8.6	-0.4	5.5	0.5	-0.3
Liabilities to private sector	31.8	22.2	10.2	12.6	8.6	18.2	11.2	13.1	12.2
<b>II. Banco de la Republica (BR) 3/</b>									
Net international reserves	51.4	0.1	-33.2	-21.5	-13.1	18.1	10.1	6.4	5.6
Net domestic assets	-45.7	24.9	16.6	43.2	54.1	-3.8	-2.6	6.6	6.5
Credit to public sector (net)	0.7	-3.2	6.3	15.2	20.6	0.4	-9.0	-6.7	-5.6
Credit to financial system	-14.1	10.4	6.7	13.0	24.2	-0.7	3.1	14.9	11.6
Credit to private sector (net)	-7.1	14.4	7.2	2.7	2.5	-0.3	0.4	-0.6	-0.5
Other (net)	-25.3	3.3	-3.6	12.4	6.7	-3.3	3.0	-1.0	0.9
Monetary base	5.7	25.0	-16.6	21.7	40.9	14.3	7.5	13.0	12.1
<b>Memorandum items:</b>									
(Flows in millions of U.S. dollars)									
Net official international reserves 4/	1,572.3	4.2	-1,341.3	-725.0	-442.9	744.3	478.0	326.0	323.5
Broad money 5/	30.0	24.5	10.3	12.8	8.7	18.2	11.4	13.1	12.2
Money (M1)	15.8	20.6	1.8	1.3	27.8	16.3	13.6	13.1	12.1
Quasi-money and other	34.1	25.4	12.3	15.4	4.6	18.6	10.8	13.1	12.2
Private sector credit 6/	25.7	25.6	11.9	5.9	6.1	16.7	8.6	12.3	13.3
Base money	5.7	25.0	-16.6	21.7	40.9	14.3	7.5	13.0	12.1
(Annual percentage changes in real terms)									
Broad money 5/	6.9	5.7	-5.5	1.7	-0.5	7.5	1.2	4.7	5.8
Money (M1)	-4.7	2.5	-12.8	-8.7	17.0	5.7	3.2	4.7	5.8
Quasi-money and other	10.3	6.6	-3.7	3.9	-4.3	7.8	0.7	4.7	5.9
Private sector credit 6/	3.4	6.7	-4.1	-4.6	-2.8	3.7	-1.3	4.0	6.9
Base money	-13.0	6.2	-28.5	9.7	29.0	3.9	-2.3	4.6	5.7
(Nominal GDP/broad money)									
Velocity of broad money	2.8	2.7	2.8	2.7	2.8	2.6	2.9	2.9	2.9
(Interest rates) 7/									
<b>90-day deposit rates</b>									
Nominal	27.9	24.3	34.1	17.5	15.4	...	12.0	...	...
Real	5.0	5.6	14.9	7.5	5.6	...	2.1	...	...
<b>Lending rates</b>									
Nominal	38.7	33.2	44.6	26.2	26.4	...	23.9	...	...
Real	14.1	13.2	23.9	15.4	15.7	...	12.9	...	...

Sources: Banco de la Republica; and Fund staff estimates.

1/ All annual changes in foreign currency stocks valued at a constant exchange rate.

2/ Changes in relation to private sector liabilities at the beginning of the period. Rates of growth of money and quasi-money are with respect to themselves.

3/ Changes in relation to monetary base at the beginning of period.

4/ The NIR are equal to the BOP concept of NIR excluding *causaciones* (accrued, but unpaid, interest on reserve assets).

5/ M3 plus bonds issued by financial institutions.

6/ The figures for 1999-2002 have been adjusted for loan write-offs resulting from the mortgage debt reduction and bank restructuring programs.

7/ End of period annual rates. The 1999 program interest rates correspond to September, 1999. The 2000 revised projection interest rates correspond to June, 2000.

Table 7. Colombia: Summary Balance of Payments, 1996-2002

	1996	Rev.		1999		2000		Rev. Proj.	
		1997	1998	Prog.	Prel. Act.	Prog.	Rev. Proj.	2001	2002
(In millions of U.S. dollars)									
<b>Current account balance</b>	<b>-4,827</b>	<b>-5,952</b>	<b>-5,271</b>	<b>-1,159</b>	<b>-963</b>	<b>-2,087</b>	<b>-948</b>	<b>-1,756</b>	<b>-2,464</b>
Trade balance	-2,140	-2,712	-2,511	2,542	1,733	1,696	2,761	2,397	1,435
Exports, f.o.b.	10,951	12,060	11,494	12,377	12,044	13,519	14,002	14,429	14,067
Coffee	1,577	2,259	1,893	1,409	1,324	1,516	1,240	1,464	1,477
Petroleum products	2,895	2,707	2,329	3,673	3,757	3,649	5,128	4,064	2,934
Other	6,480	7,094	7,272	7,296	6,963	8,355	7,635	8,901	9,656
Imports, f.o.b.	13,092	14,772	14,006	9,836	10,311	11,823	11,241	12,032	12,632
Services (net)	-1,188	-1,500	-1,470	-1,628	-1,370	-1,658	-1,499	-1,522	-1,506
Income (net)	-2,090	-2,350	-1,735	-2,618	-2,122	-2,631	-2,769	-3,202	-2,974
Interest (net)	-1,432	-1,754	-1,738	-1,827	-1,886	-1,786	-2,055	-2,315	-2,059
Of which: public sector	-582	-597	-604	-913	-802	-971	-1,001	-1,282	-1,112
Other services (net)	-657	-597	3	-791	-236	-845	-715	-887	-915
Current transfers (net)	591	610	446	545	795	506	559	570	581
<b>Capital and financial account balance</b>	<b>6,715</b>	<b>7,092</b>	<b>4,542</b>	<b>332</b>	<b>317</b>	<b>2,831</b>	<b>897</b>	<b>2,082</b>	<b>2,788</b>
Financial account balance	6,715	7,092	4,542	332	317	2,831	897	2,082	2,788
Public sector (net)	810	529	1,515	1,358	970	-122	901	405	1,250
Nonfinancial public sector	881	839	1,823	1,236	1,359	100	1,199	750	1,298
Medium- and long-term (net)	1,330	1,268	1,989	2,065	2,071	1,514	2,078	1,358	1,141
Disbursements	2,742	2,955	3,589	3,887	3,817	3,192	3,700	3,770	3,905
Amortization	1,412	1,687	1,601	1,822	1,746	1,678	1,622	2,412	2,765
Short term	-449	-429	-166	-829	-712	-1,413	-879	-608	157
Financial public sector	-71	-310	-307	122	-388	-223	-298	-345	-48
Private sector (net)	5,905	6,563	3,027	-1,026	-653	2,954	-4	1,677	1,538
Nonfinancial private sector (net)	5,892	6,419	3,922	-412	475	2,540	-34	1,537	1,373
Direct investment	2,795	4,830	2,432	249	933	3,460	1,453	1,412	1,268
Of which: Privatization	443	2,998	513	0	0	2,785	1,443	1,330	0
Leasing finance	278	401	348	127	80	127	124	95	62
Long-term loans	2,599	1,735	368	-448	-58	-1,829	-277	426	242
Short term (including portfolio invest)	221	-548	774	-340	-480	782	-1,334	-396	-198
Financial private sector (net)	13	144	-895	-614	-1,128	413	30	140	166
Net errors and omissions	-161	-859	-659	78	223	0	529	0	0
Changes in NIR	1,754	280	-1,388	-750	-423	744	478	326	323
(In percent of GDP)									
Current account balance	-5.0	-5.6	-5.3	-1.3	-1.1	-2.4	-1.1	-2.0	-2.7
Changes in NIR	1.8	0.3	-1.4	-0.9	-0.5	0.9	0.6	0.4	0.4
(In months of imports of goods and services)									
Gross international reserves 1/	6.2	5.5	5.2	5.8	5.9	5.9	5.6	5.4	5.4

Sources: Banco de la Republica; and Fund staff estimates and projections.

1/ Not including Fund purchases under the current EFF arrangement.

Table 8. Colombia: External Debt and Debt-Service Projections

	1996	1997	1998	Prel. 1999	Proj.		
					2000	2001	2002
(In millions of U.S. dollars)							
Total debt outstanding	30,674	33,575	35,794	36,777	38,013	39,841	41,478
Medium- and long-term 1/	25,713	28,840	31,185	32,618	34,131	35,642	37,002
Short term	4,961	4,734	4,609	4,160	3,882	4,199	4,475
Public sector debt outstanding	16,505	16,820	18,840	20,540	21,846	22,939	24,111
Medium- and long-term 1/	15,336	15,916	17,972	19,916	21,697	22,709	23,802
Short term	1,169	904	867	623	149	229	309
Private sector debt outstanding	14,169	16,755	16,954	16,238	16,167	16,903	17,367
Medium- and long-term 1/	10,377	12,924	13,212	12,701	12,434	12,933	13,200
Short term	3,793	3,831	3,742	3,537	3,733	3,970	4,167
Total debt service	5,443	6,836	6,930	7,043	7,816	9,877	9,935
Public sector	3,012	3,620	3,323	3,416	3,564	4,790	4,707
Amortization	1,910	2,359	2,098	2,114	1,995	2,874	2,924
Interest	1,103	1,261	1,225	1,302	1,569	1,916	1,783
Private sector	2,431	3,216	3,608	3,627	4,252	5,087	5,228
Amortization	1,438	1,897	2,259	2,332	2,825	3,608	3,826
Interest	993	1,319	1,349	1,294	1,427	1,479	1,402
(In percent of GDP)							
Total debt	31.6	31.5	35.8	42.6	45.2	45.4	46.2
Public sector	17.0	15.8	18.9	23.8	26.0	26.2	26.9
Private sector	14.6	15.7	17.0	18.8	19.2	19.3	19.3
(In percent of exports of goods, services, and income)							
Total debt stock	221.5	222.6	247.4	249.3	223.5	225.9	238.8
Total debt service	39.3	45.3	47.9	47.7	45.9	56.0	57.2
Public sector	21.7	24.0	23.0	23.2	21.0	27.2	27.1
Private sector	17.6	21.3	24.9	24.6	25.0	28.8	30.1
Interest	15.1	17.1	17.8	17.6	17.6	19.2	18.3
Public sector	8.0	8.4	8.5	8.8	9.2	10.9	10.3
Private sector	7.2	8.7	9.3	8.8	8.4	8.4	8.1
Amortization	24.2	28.2	30.1	30.1	28.3	36.8	38.9
Reserves to total short-term external debt	2.0	2.1	1.9	1.9	2.2	2.1	2.1

Sources: Banco de la Republica; and Fund staff projections.

1/ Includes leasing.

Table 9. Colombia: Indicators of External Vulnerability

(In percent of GDP, unless otherwise indicated)

	1996	1997	1998	1999		2000			Rev. Proj.		
				Prog.	Prel. Act.	Latest Obs.	Date of Obs.	Prog.	Rev. Proj.	2001	2002
<b>Financial indicators</b>											
Public sector debt (domestic and external)	24.6	24.2	27.5	34.5	35.6	...	...	34.4	35.5	34.2	33.8
Broad money (percent change, 12-month basis)	29.9	24.5	10.3	12.8	8.7	4.6	6/30/00	18.2	11.3	13.1	12.2
Private sector credit (percent change, 12-month basis)	24.9	25.6	11.9	5.9	6.1	3.5	3/31/00	16.7	8.5	12.3	13.2
90-day time deposit rate	27.9	24.3	34.1	17.5	15.4	12.0	6/30/00	...	...	...	...
90-day time deposit rate (real)	5.2	5.6	14.9	7.5	5.7	2.1	6/30/00	...	...	...	...
<b>External indicators</b>											
Exports (percent change, 12-month basis in U.S. dollars)	4.0	10.1	-4.7	8.9	4.8	19.8	06/00	9.2	16.3	3.0	-2.5
Imports (percent change, 12-month basis in U.S. dollars)	-0.6	12.8	-5.2	-29.8	-26.4	-7.7	05/00	20.2	9.0	7.0	5.0
Terms of trade (percent change, 12-month basis)	6.1	10.7	-6.2	5.0	4.2	7.5	Q1/00	1.5	10.7	-0.7	-5.3
Current account balance	-5.0	-5.6	-5.3	-1.3	-1.1	-0.4	Q1/00	-2.4	-1.1	-2.0	-2.7
Capital and financial account balance	6.9	6.6	4.6	0.4	0.4	0.0	Q1/00	3.3	1.1	2.4	3.1
<i>Of which</i>											
Inward short-term portfolio investment (debt securities, etc.)	-0.3	0.0	0.4	-0.5	-1.6	0.2	Q1/00	-1.9	-2.0	-1.0	0.3
Other investment (loans, trade credits, etc.)	0.1	-0.8	-0.1	-0.8	-0.5	-0.2	Q1/00	0.1	-0.3	0.1	-0.1
Inward foreign direct investment and long-term flows	7.1	7.5	4.2	1.7	2.4	0.0	Q1/00	5.1	3.4	3.2	2.9
Gross official reserves (in U.S. dollars) 1/	9,938	9,908	8,740	8,215	8,116	8,439	7/26/00	9,458	8,611	8,937	9,260
Central bank short-term foreign liabilities (in U.S. dollars)	6	-2.4	36.5	334.3	0.2	0.0	8/16/00	832.4	62.7	62.7	62.7
Short-term net foreign assets of the financial sector (in U.S. dollars)	6,254	6,128	5,536	5,051	6,229	6,552	3/31/00	5,642	6,618	6,673	6,674
Official reserves in months of imports of goods and services 1/	6.2	5.5	5.2	5.8	5.9	6.0	Q1/00	5.9	5.6	5.4	5.4
Broad money to reserves 1/	3.4	3.6	3.8	3.5	3.5	3.2	3/31/00	3.3	3.2	3.3	3.4
Total short-term external debt to reserves 1/2/	49.9	47.8	52.7	72.0	51.3	46.6	Q1/00	57.2	67.5	73.1	64.8
Total external debt	31.6	31.5	35.8	23.3	42.6	42.2	Q1/00	43.1	45.2	45.4	46.2
<i>Of which</i>											
Public sector debt	17.0	15.8	18.9	22.3	23.8	23.8	Q1/00	24.8	26.0	26.2	26.9
Total external debt to exports of goods, services, and income	221.5	222.6	247.4	224.7	249.3	247.0	Q1/00	223.0	223.5	225.9	238.8
External interest payments to exports of goods, services, and income	17.6	17.1	17.8	18.0	17.6	17.0	Q1/00	16.4	17.6	19.2	18.3
External amortization payments to exports of goods, services, and income	15.1	28.2	30.1	29.0	30.1	26.6	Q1/00	29.7	28.3	36.8	38.9
Exchange rate (per U.S. dollar, period average)	1,037	1,141	1,426	1,737	1,756	2,174	7/28/00	...	...	...	...
Real effective exchange rate appreciation (+) (end of period) 3/	19.9	-5.1	-4.5	-15.4	-9.4	-13.1	06/00	...	...	...	...
<b>Financial market indicators</b>											
Stock market index	847	1,417	1,086	916	998	791	8/17/00	...	...	...	...
Foreign currency debt rating 4/	...	BBB-	BBB-	BB+	BB+	BB	7/28/00	...	...	...	...
Spread of benchmark bonds (basis points, end of period) 5/	...	...	728	650	445	529	7/28/00	...	...	...	...

Sources: Ministry of Finance and Public Credit; Banco de la Republica; and Fund staff estimates and projections.

1/ Not including purchases under the current EFF arrangement.

2/ Short-term debt is defined by its remaining maturity from 1999 onwards.

3/ Source: INS.

4/ Standard &amp; Poors.

5/ Consists of the spread on a US\$500 million global five-year note issued in June 1998.

Table 10. Colombia: Schedule of Purchases Under the Extended Arrangement

Date	In millions of SDRs	Conditions
December 1999	150.5	Board approval.
February 2000	150.5	Observance of end-December 1999 performance criteria.
May 2000	150.5	Observance of end-March 2000 performance criteria.
August 2000	150.5	Observance of end-June 2000 performance criteria and completion of the first review. 1/
November 2000	150.5	Observance of end-September 2000 performance criteria.
February 2001	150.5	Observance of end-December 2000 performance criteria.
May 2001	150.5	Observance of end-March 2001 performance criteria.
August 2001	150.5	Observance of end-June 2001 performance criteria.
November 2001	150.5	Observance of end-September 2001 performance criteria.
February 2002	150.5	Observance of end-December 2001 performance criteria.
May 2002	150.5	Observance of end-March 2002 performance criteria.
August 2002	150.5	Observance of end-June 2002 performance criteria.
November 2002	150.5	Observance of end-September 2002 performance criteria.
<b>Total</b>	<b>1,957</b>	

Source: Fund staff estimates.

1/ It is expected that program reviews will be held on six-month cycle.



**COLOMBIA: FUND RELATIONS**  
(As of July 31, 2000)

I. Membership Status:  
Joined: 12/27/45  
Status: Article XIV

	<b>SDR Million</b>	<b>Percent of Quota</b>
II General Resources Account Quota	774.00	100.0
Fund holdings of currency	488.20	63.1
Reserve position in Fund	285.80	36.9

	<b>SDR Million</b>	<b>Percent Allocation</b>
III SDR Department: Net cumulative allocation	114.27	100.0
Holdings	100.68	88.1

IV. Outstanding Purchases and Loans: None

V. Financial Arrangements:

<u>Type</u>	<u>Approval Date</u>	<u>Expiration Date</u>	<u>Amount Approved (SDR Million)</u>	<u>Amount Drawn (SDR Million)</u>
EFF	12/20/1999	12/19/2002	1,957.00	0.00

VI. Projected Obligations to Fund: None

VII. Exchange Rate Arrangement:

In January 1994, the Banco de la Republica (BR) adopted a managed float of the exchange rate vis-à-vis the U.S. dollar within a 14 percentage point band. The band was widened to 20 percentage points and the slope reduced from 13 to 10 percent in June 1999. In September 1999, the BR eliminated the band, floating the peso. Multiple currency practices that result from taxes on profit remittances from direct investment in Colombia and on foreign exchange earnings from personal services and transfers, and export tax credit certificates (CERTs) have not been approved under Article VIII. In April 2000, the BR reduced to zero the deposit requirement on external loans. At end-July 2000, the exchange rate was Col\$2,172.8 per U.S. dollar.

VIII. Last Article IV consultation and recent contacts:

The 1999 Article IV consultation was concluded by the Executive Board on December 20, 1999. At that time, Directors also approved Colombia's request for an extended arrangement. Staff discussed the first review of the EFF with the authorities during four periods during April-July 2000.

IX. Recent Technical Assistance:

<b>Dept.</b>	<b>Purpose</b>	<b>Time of Delivery</b>
MAE	Advise on financial sector reform	July 1997
STA	Multisector mission	November 1997
FAD	Advise on customs administration	November 1997
FAD	Advise on tax administration	February 1998
STA	Advise on national accounts statistics	March 1998
STA	Advise on government finance statistics	May 1998
MAE	Financial sector stability assessment (FSSA)	May 1999
STA	Advice on government finance statistics	August 1999
STA	Advise on banking statistics	October 1999
FAD	Advise on tax policy	November 1999
FAD	Advise on tax administration	December 1999
MAE	Advise on the deposit insurance system	March 2000
FAD	Advise on the measurement of the deficit of the nonfinancial public sector	May 2000
FAD	Follow up mission in customs administration	June 2000

X. Resident Representative: None.

XI. Colombia has not yet accepted the Fourth Amendment to the Articles of Agreement.

Bogotá, Colombia  
August 22, 2000

Mr. Horst Köhler  
Managing Director  
International Monetary Fund  
Washington, D.C. 20431

Dear Mr. Köhler:

1. In the period since December 1999, when the extended arrangement was approved, the recovery of economic activity in Colombia has been confirmed, based on strong and broad based growth of both exports and domestic demand, and the central bank's disinflation policy has remained on track to achieve the objectives set for 2000. Despite the strong signs of recovery, the number of Colombians that are out of work remains unacceptably high, and the government will take steps to ensure that the unemployment rate will decline. The external current account is stronger than projected, helped by higher oil prices, and the foreign exchange market has functioned well under the floating rate system. The fiscal consolidation plan is progressing as envisaged under the program, and the financial system has responded well to the restructuring programs, showing significant improvements in prudential indicators. The authorities are pursuing their structural reform agenda which will continue to be developed and evolve over the three-year period of the program. Most important for Colombia is the achievement of peace, and to enhance the near-term prospects for peace and social cohesion, the government recently presented to the nation and the international community its comprehensive plan to achieve this, the "Plan Colombia."

2. Notwithstanding that the decline of the Colombian economy in 1999, as measured by a GDP growth rate of -4.5 percent, was more pronounced than projected in the program (-3.5 percent), all performance criteria established for end-1999 and March 2000 were observed, except as discussed below. In addition, the external current account deficit declined to 1.1 percent of GDP in 1999 (compared with 1.3 percent of GDP in the program), and inflation fell to 9.2 percent (compared with a target of 11 percent). Despite the negative impact on tax collections of the deeper than expected recession, the combined public sector deficit was 5.4 percent of GDP, well below the projected level of 5.9 percent of GDP.

3. In terms of performance criteria, the net international reserves at the end of 1999 and March 2000 were above the minimum levels set in the program, and the overall fiscal deficit was below the ceilings for these dates. The performance criterion on net disbursement of medium- and long-term public sector external debt for end-1999 was observed with a considerable margin that in large measure reflected the lower than projected fiscal deficit; the ceiling established for March 2000 also was observed. The public sector's short-term external debt was below the ceiling both in December and March. The outstanding stock of net domestic assets (NDA) of the central bank at the end of 1999 was above the ceiling, reflecting demand for base money that was temporarily in excess of the projected level

related to the Y2K problem, a possibility foreseen in the program. The NDA was below the established ceiling again in March 2000.

4. The Colombian authorities confirm the program objectives of seeking to restore real GDP growth in 2000 to 3 percent and maintain the annual inflation target of 10 percent. Despite a projected shortfall in non-oil revenues, a deeper than expected recession in 1999, and the need to attend to some unforeseen expenditures in 2000, the authorities reaffirm their commitment to meet the program target of an overall deficit for the nonfinancial public sector (NFPS) of 3.6 percent of GDP in 2000, with a combined public sector deficit of 3.7 percent of GDP. Central government expenditures will be 1.4 percent of GDP higher than originally expected due to unforeseen, mostly nonrecurrent, requirements stemming from the need to address problems in three areas: the internal conflict; the high level of unemployment; and the fiscal problems of some territorial governments. Nevertheless, the program's fiscal target will be achieved due to public sector wage increases below projected inflation, higher than expected oil revenues (0.7 percent of GDP), expenditure measures introduced in May, and the impact of savings in other areas. If revenue were to fall below current projections, the authorities will make the necessary expenditure cuts to ensure that the fiscal target is fully met.

5. The authorities are proposing that the overall deficit of the central administration be measured on a commitment basis for the purpose of monitoring the program. This will help fiscal management in Colombia by fully reflecting all budgetary commitments in the year in which they are incurred. It also will allow the executive to better control expenditure requests that come late in the year; such requests have often been accommodated in the past by pushing their execution to the next fiscal year, giving rise to budgetary carryovers that have been difficult to control. A deficit on a commitment basis also will make the budgetary process more transparent and efficient by abandoning the hybrid accrual and cash basis that has been used in the past. The government has worked with Fund staff to ensure that the mechanisms are in place to guarantee accurate reporting of all budgetary commitments.

6. At present, the authorities do not expect that the plans drawn up for privatization of public enterprises and banks in 2000 can be fully executed, as explained below. Lower than projected privatization receipts will have implications for the financing of the public sector deficit. According to the provisions in the program, the government will seek compensatory external financing in an amount of up to 50 percent of the shortfall in privatization proceeds. Additional financing also would be required, which the authorities have sought to secure in the international financial markets and by accelerating program lending operations that are under preparation by the multilateral lending institutions. To allow for the additional financing the authorities are proposing that the program ceiling on medium- and long-term external debt for the end of 2000 be set US\$300 million higher than the indicative ceilings presented in the program. This increase would correspond to about half of the amount of privatization receipts expected from the sale of the main electricity transmissions company, whose privatization is being shifted from 2000 to 2001. If opportunities arise to pre-finance the needs for the year 2001 during the last half of 2000, the government will discuss with the

Fund the necessary changes in the external indebtedness ceilings; the proceeds of any such financing would be kept in foreign exchange abroad until they are needed in 2001.

7. Significant progress has been made in recent months in the peace process. The discussion methodology now contemplates the possibility of implementing partial peace agreements, which may require a temporary increase in the NFPS deficit in order to ensure their adequate implementation. While the government expects that progress on the peace front will strengthen the underlying fiscal position, the authorities will discuss with the Fund any budgetary changes that may be required should the need arise.

8. The Colombian government recently has made public its multi-year project entitled "Plan Colombia" which integrates its strategies for ending the internal conflict, reducing the scope of narco-trafficking, and dealing with the serious social consequences of these problems. A number of bilateral donors and lenders have indicated that they will support the "Plan Colombia," and the Colombian authorities are proposing that the program ceilings on the fiscal deficit and the net disbursement of medium- and long-term debt be adjusted upwards, by the amount of concessional loans disbursed in support of this plan. The domestic contributions to the plan are being incorporated into the government budget as part of its fiscal program.

9. With respect to monetary policy, the central bank continues to follow a strategy of inflation targeting, with the growth of base money as an intermediate target. The monetary authorities consider that the inflation targeting strategy is compatible with the use of an intermediate target, as long as the latter is subordinate to the inflation goal. Substantial effort is being devoted to improving the inflation forecast capability and the knowledge of the transmission mechanisms of monetary policy. At present, the projections of the central bank indicate that inflation will be on target by the end of the year and that the 8 percent target for 2001 also will be achieved. However, an increase in inflation has been registered during the first part of 2000 due to a temporary rise in some food prices and higher domestic fuel prices. In fact, all four measures of annual core inflation calculated by the central bank have remained below the target in recent months, and the central bank's forecasts of core inflation point to levels well below the official target for December 2000.

10. So far this year, cash balances held by the public have grown more than projected in the program. Since the authorities consider that the shift to higher holdings of liquid assets is permanent, related to exogenous shocks to money demand (e.g., to the expansion of the financial transactions tax base earlier this year), the reference monetary base has been raised somewhat for the rest of 2000; this would not impede the achievement of the inflation goals for 2000 and 2001. Accordingly, the authorities propose that the performance criterion on NDA for September and December 2000 be set somewhat higher than the indicative target presented in the program, while the target for the net international reserves would remain as indicated earlier.

11. Since September 1999, the Colombian peso has been allowed to float against the dollar. The transition to the floating system was smooth and the exchange rate has since

remained relatively stable. The central bank has introduced an auction system under which market participants (banks and the treasury) bid for options to transact foreign exchange with the central bank. The experience with this system has been successful and helped the bank exceed the NIR targets in December 1999 and March 2000. Presently, Colombia exhibits a strong international reserves position, and given the balance of payments projections, the central bank expects to be able to meet the NIR target for 2000. To ease the access to external financing, the central bank in May reduced to zero the nonremunerated deposit requirement (at the central bank) on external loan proceeds.

12. Since the middle of 1999, there has been a positive evolution in both liquidity and solvency indicators in the Colombian financial system. The average capital adequacy ratio in June was 11.2 percent, approximately 1.2 percentage points higher than the observed figure in August 1999, when it was at its lowest. Capital strengthening has been achieved primarily due to the implementation of programs under the financial institutions guarantee fund (Fogafin), both in public and private financial intermediaries. The nonperforming loan indicator, though still at undesired levels, has improved from 16.1 percent in November 1999 when it was at its highest level to 10.5 percent in June 2000, while provisions have increased as a percentage of past-due loans. The former result was due to the combination of the process of loan restructuring required under Fogafin recapitalization programs and the recovery in economic activity, while the latter is mainly the result of more stringent provisioning rules imposed by the banking superintendency. The authorities plan to increase the capitalization of the public banks by an additional 1 percent of GDP (with an annual fiscal carrying cost of some 0.1 percent of GDP) to prepare them for sale on the schedule envisaged in the program.

13. Most of the structural reform actions to be completed by June 2000 have been implemented. The proposal for the creation of a territorial government pension fund was approved through Law 549 at the end of 1999. Most of the regulations to implement the provisions of the financial sector reform law enacted in July 1999 have been issued, with the final regulation to be issued shortly. The draft legislation to organize lottery and gaming activities to help boost the territorial governments' pension reserves was presented to congress as scheduled and legislation to strengthen territorial government finances by means of limiting their current expenditures has been passed. The proposal for a constitutional reform which delinks revenue transfers to territorial governments from the current income of the central government was submitted to congress last fall as envisaged under the program, but it was withdrawn after initial discussions. The government agreed to restructure the proposal and it was re-submitted in March 2000. Regarding the tax reform, a proposal was presented to congress in March 2000, as envisaged in the program. The presentation to congress of the proposal for a second generation social security reform, originally scheduled for December 1999 has been postponed to provide for technical improvements in the proposal and to allow time to build public consensus on the contents of the reform. The government now intends to present it to congress before the end of the year.

14. The Colombian authorities confirm their determination to pursue and deepen the structural reform process over the three-year period of its program. To that end several reform proposals are currently before congress (as noted above) or under preparation.

15. The tax package currently before congress proposes a gradual lowering of the marginal income tax rates from 35 to 32 percent, and the creation of a unified income and value-added tax for small business (to help prevent tax evasion), as well as other measures to close loopholes in the income and value-added taxes.

16. With the purpose of protecting the viability of the public finances, while increasing the coverage in the provision of education and health services, the government has submitted a constitutional amendment to the congress aimed at modifying the present scheme for revenue transfers to territorial governments (*situación fiscal and participaciones municipales*). The proposed reform delinks the transfers from the current revenue of the government, so as to guarantee their stability and allow more flexibility of the central government finances. Under the government's proposal, the transfers would increase by 1.5 percent annually in real terms in order to allow for the need to expand services, notably in education and health.

17. In regard to the pension reform, the government will present to congress before the end of the year its proposal to eliminate the sources of future deficits of the social security institute in order to guarantee its financial viability in the medium term.

18. In regard to the privatization program, significant advances have been made in bringing several major enterprises near the point of sale. However, it is likely that the original schedule will be affected by the intensification of attacks on strategic locations of the electricity network. As a result, the sale of the main electricity distribution company, ISA, would be postponed to 2001, but the government expects that the sale of the electricity generating firm, ISAGEN; the large coal mine, Carbocol; and the regional telephone company in Bogota, ETB, will be completed before the end of 2000. The government continues to pursue its efforts to privatize the public banks, as noted above, and bring them to the point of sale by the end of the year. On the other hand, the sale of the other electrical distribution companies is less advanced than expected and is likely to bring less revenue than anticipated.

19. In addition, the government is seeking to build a stronger partnership between the executive and congress in the area of fiscal policy. To this end, it will propose to congress before the end of the year a fiscal responsibility law to promote the long-run sustainability of the public finances, both at the central and territorial (departmental and municipal) levels of government. More fundamentally, the structural reform policies regarding substantive economic and social issues, as well as employment, are currently the subject of political discussions in Colombia; mainly through round table discussions (*mesas de concertación*) among representatives from congress and wide segments of society. The government expects that concrete proposals will emerge from these roundtable fora in the last half of the year.

20. The government is committed to the fiscal adjustment path agreed under the program. On this basis, the authorities submitted to congress in late July 2000 a budget for 2001 that is consistent with a nonfinancial public sector deficit of at most 2.5 percent of GDP and a combined public sector deficit that is consistent with the program.

21. The Colombian authorities reaffirm their policy commitments under the program supported by the EFF arrangement approved by the IMF Executive Board last December, request completion of the first review thereunder, and will conduct the second review with the Fund under the three-year EFF arrangement by December 20, 2000.

Sincerely yours,

---

Juan Manuel Santos  
Minister of Finance  
and Public Credit

---

Miguel Urrutia  
General Manager  
Bank of the Republic



**COLOMBIA—TECHNICAL MEMORANDUM OF UNDERSTANDING**

1. This memorandum sets out the definition of concepts, specific performance criteria (PCs) for September and December 2000, the structural benchmarks defined to date for the remaining period of the program (SBs), and assumptions that apply under the first-year program supported by extended arrangement.

**I. FISCAL TARGETS**

**A. Performance Criterion on the Overall Balance of the Combined Public Sector 1/**

	Floor 2/ (In billions of Col\$)
Overall balance of the combined public sector, from January 1, 1999 to:	
September 30, 2000 (performance criterion)	-13,700
December 31, 2000 (performance criterion)	-14,550

1/ As measured by the net financing requirement defined below. Combined public sector as defined below.  
2/ Minimum cumulative balance of the combined public sector.

2. The overall balance of the **combined public sector (PS)** is defined as the sum of the overall balances of the nonfinancial public sector (NFPS), the operating cash result (quasi-fiscal balance) of the Banco de la República (BR), the overall balance of Fondo de Garantías de Instituciones Financieras (FOGAFIN), and the net fiscal costs borne by the central administration related to financial sector restructuring. The NFPS consists of the general government and the public enterprises; the general government includes the central government, the territorial governments, and the social security system; the central government includes the central administration and the national decentralized agencies as indicated below. The net fiscal costs borne by the central administration related to financial sector restructuring are defined to include interest payments and amortization of the bonds used to compensate financial entities for the mortgage debt reductions approved by the congress in December 1999, the interest payments on the bonds used to recapitalize public banks, and the costs of closing Caja Agraria.

**The Combined Public Sector**

PS = NFPS<sup>1/</sup> + FOGAFIN + quasi-fiscal BR + net fiscal costs borne by the CG related to bank restructuring  
 NFPS = general government (GG) + public enterprises (PE)  
 GG = central government (CG) + territorial governments (TG) + social security  
 CG = central administration + national decentralized agencies  
 TG = territorial government + territorial decentralized agencies

1/ Excludes net fiscal costs borne by CG related to bank restructuring.

3. For any given calendar quarter, the overall **PS balance** is measured, in Col\$, as the sum of: (i) its net domestic financing, (ii) its net external financing, and (iii) privatization proceeds, as defined below. Items denominated in foreign currency will be converted into *pesos* at the actual exchange rate.
4. The **PS net domestic financing** comprises (i) the change in its net credit from the financial system, excluding bonded debt; (ii) the change in its bonded debt (including domestic bonds denominated in or indexed to foreign currencies) net of valuation changes; (iii) the change in the budget carry-over (*rezago presupuestario*, which includes *cuentas por pagar* and *reservas de apropiación*) of the central administration and, from March 2000, the change in the floating debt (*cuentas por pagar*) of the social security system (Instituto de Seguro Social, Cajanal, and Caprecom) and main public enterprises; Ecopetrol, Carbocol, Telecom, the national electricity companies (ISA, ISAGEN, and the national electricity distributors), and the national coffee fund; (iv) the change in the amount of public funds administered by *Fiduciarias*; and (v) the operating cash result of the BR. Any capitalization of interest on new issues of government bonds from September 1, 1999 and the accrual of the inflationary component of indexed bonds will be included as (interest) expenditure for the purpose of measuring the PS deficit.
5. The **financial system** comprises the banking sector, saving and loan institutions (*corporaciones de ahorro y vivienda*), finance corporations (*corporaciones financieras*), FEN, IFI, finance and leasing companies (*compañías de financiamiento comercial*), Bancoldex, Finagro, and Findeter. The banking sector includes the BR, the commercial banks, and BCH.
6. The **PS net external financing** is defined as the sum of (i) disbursements of project and nonproject loans, including securitization; (ii) proceeds from bond issues abroad; (iii) the net changes in short-term external debt; (iv) any change in arrears on external interest payments; minus (v) cash payments of principal on current maturities for bonds and loans; (vi) cash payment to settle any external arrears; (vii) any prepayment of external debt; and (viii) changes in financial assets held abroad by the PS.
7. **Privatization** proceeds are defined as the cash payments received by the PS, converted to Col\$ at the actual market exchange rate of each transaction. Nonrecurrent fees for concessions of public services, such as in the telecommunications sector, are treated as privatization proceeds. For purposes of the program, such fees will be accounted for over the concession period distributed in equal annual amounts. Proceeds from decapitalization of public enterprises will be considered as privatization. To the extent the purchasers of public enterprises assume their debts, the net financing used by these enterprises during the program period until their sale will be deducted from the net financing of the PS; if the PS assumes the debt, the net financing used by the enterprise during the program period before the sale will remain outstanding as part of the financing of the PS.
8. **Adjustments.** The ceiling on the overall combined public sector deficit will be adjusted upwards, and the ceiling on net disbursements of medium- and long-term external debt of the public sector will be adjusted upward (see below), by the full amount of any

concessional loan disbursements in support of the Plan Colombia. A loan will be defined as concessional if it has at least a 35 percent grant element using the commercial interest reference rate (CIRR) as discount rate.

## II. MONETARY TARGETS

### A. Performance Criterion on the Net Domestic Assets (NDA) of the BR

	Ceiling 1/ (In billions of Col\$)
Outstanding stock of net domestic assets as of:	
September 30, 2000 (performance criterion)	-8,500
December 31, 2000 (performance criterion)	-7,100

1/ Maximum level of end-of period outstanding stock of net domestic assets of the BR. This level is calculated as the difference between the upper band of the central bank's monetary base corridor and the floor of the NIR established in Section III below.

9. The NDA of the BR are defined as the difference between the monetary base and its net international reserves (NIR) valued in Col\$ at an accounting exchange rate. The monetary base consists of currency in circulation, including cash-in-vaults at financial institutions, and the sight deposits of the financial system at the BR.

10. The NIR of the BR (*reservas de caja*) are equal to the balance of payments concept of net international reserves excluding *causaciones* (accrued, but unpaid, interest on reserve assets) and are the U.S. dollar value of gross foreign reserves of the BR minus gross reserve liabilities.

11. Gross foreign reserves of the BR comprise (i) gold, (ii) holdings of SDRs, (iii) the net position in the FLAR, and (iv) all foreign currency-denominated claims of the BR. Gross foreign reserves exclude participation in international financial institutions (including Corporación Andina de Fomento (CAF), IDB, IBRD, IDA, and the Caribbean Development Bank), the holdings of nonconvertible currencies, and holdings of precious metals other than gold. The *pesos andinos* are considered to be part of Colombia's gross foreign reserves. Gross reserve liabilities of the BR are defined as the sum of (i) all foreign currency-denominated liabilities of the BR with an original maturity of one year or less, (ii) liabilities to the Fund, (iii) any net position on foreign exchange derivatives with both residents and nonresidents undertaken directly by the BR or by other financial institutions on behalf of the BR, (iv) any purchases from the Latin American Reserve Fund (FLAR), (v) any increase in medium-and long-term external debt of the BR over and above US\$125 million, which is the level of the outstanding debt on October 1, 1999, and (vi) any foreign currency deposits in the BR by residents, including financial institutions. Options to sell foreign exchange to the central bank acquired by financial institutions and the treasury at the monthly auctions to

build the central bank's reserves (*mecanismo para acumular reservas internacionales*) will be added to reserves when they are exercised.

12. **Adjustments.** Adjustments to the ceiling on the NDA of the BR are described in Section III (13) below.

### III. EXTERNAL TARGETS

#### A. Performance Criterion on NIR of the BR

	Target 1/ (In millions of U.S. dollars)
Outstanding stock as of:	
September 30, 2000 (performance criterion)	8,250
December 31, 2000 (performance criterion)	8,570

1/ Minimum level of NIR of the BR. NIR as defined in Section II above.

#### 13. Adjustments

(a) The quarterly NIR targets may be adjusted downward by US\$500 million, as necessary, to help secure orderly currency market operations after the September 1999 floating of the peso. The amount of any overperformance on the adjusted NIR target for December 31, 1999, up to US\$500 million, can be carried forward into 2000 as follows: the adjusted NIR target for March will be subject to an additional downward adjustment of one-half of the overperformance; the adjusted target for June of one-quarter of the overperformance; and the adjusted target for September of one-eighth of the overperformance. In case of such adjustments to the NIR, the NDA ceilings established above in Section II. A will be raised using the following marginal adjustments:

Loss of NIR Relative to Baseline (In US\$ million)	Marginal Increase of NDA Ceilings <sup>1/</sup> (In percent of observed NIR loss)
Between 0 and 200	100 percent
Between 200 and 300	90 percent
Between 300 and 400	80 percent
Between 400 and 500	70 percent
More than 500	60 percent

1/ These refer to the marginal adjustment of the NDA ceiling for each successive US\$100 million loss of NIR relative to the baseline. For example, a loss of US\$300 million relative to the baseline would imply an upward adjustment of the NDA ceiling by the equivalent in Col\$ of US\$290 million.

(b) In case there is a shortfall from the amount of net external financing of the combined public sector programmed for 2000 (the sum of privatization proceeds and changes in external debt, as defined in Section I, paragraphs 6 and 7 above and shown in the attached

Table 1), the quarterly targets for the NIR in 2000 will be subject to a further downward adjustment of any shortfall up to a cumulative US\$600 million through March, and up to a cumulative US\$900 million for the rest of the year. The ceilings on the NDA of the BR will be raised by the equivalent in Col\$ of any downward adjustments in the NIR targets.

(c) In the case of an excess in the amount of net external financing of the combined public sector with respect to the baseline (Table 1), the quarterly targets for NIR will be adjusted upward by the full amount of the excess less US\$50 million (such excess could be avoided by increasing the public sector's assets abroad, as indicated in paragraph 6 (viii) above). The ceiling on the NDA of the BR will be lowered by the equivalent in Col\$ of any such adjustment in the NIR target.

**B. Performance Criterion on the Net Disbursement of Medium- and Long-Term External Debt by the Public Sector 1/**

	Ceiling (In millions of U.S. dollars)
Cumulative net disbursement of external debt by the public sector from January 1, 1999 to	
September 30, 2000 (performance criterion)	3,200
December 31, 2000 (performance criterion)	3,500

1/ The public sector includes the PS as defined above and the financial public sector, including second-tier banks.

14. This ceiling applies to the net disbursement (gross disbursement minus amortization/redemptions) of debt of the public sector (financial and nonfinancial) of nonconcessional external debt of maturity of over one year. The changes in the external debt will be valued in U.S. dollars at the exchange rate prevailing at the time of each transaction.

15. **Adjustments.** To the extent there is a shortfall in privatization proceeds relative to the program baseline shown in the attached Table 1, the ceiling will be adjusted upward by 50 percent of the shortfall.

16. **Guarantees.** The government will maintain the policy of not guaranteeing private sector external debt.

**C. Performance Criterion on Change in the Outstanding Stock of Short-term External Debt of the Public Sector 1/**

	Ceiling (In millions of U.S. dollars)
Cumulative net disbursement of short-term external debt of the public Sector from January 1, 1999 to:	
September 30, 2000 (performance criterion)	70
December 31, 2000 (performance criterion)	70

1/ Short-term debt defined as all debt with an original maturity of one year or less, excluding normal trade financing. Public sector includes the PS as defined above and the financial public sector except transactions that affect the reserve liabilities of the BR.

**IV. STRUCTURAL BENCHMARKS**

17. **To be completed by September 30, 2000**
  - Present to congress the 2001 budget consistent with a nonfinancial public sector deficit of at most 2.5 percent of GDP.
18. **To be completed by December 31, 2000**
  - Present to congress a draft fiscal responsibility law.
  - Present to congress a proposal for a second generation social security reform (modifying law 100 of 1993).<sup>1</sup>
19. **To be completed by March 31, 2001**
  - Present to congress a proposal on territorial tax policy, granting more fiscal autonomy to territorial governments (territorial tax reform).
20. **To be completed by December 31, 2001**
  - Full disinvestment of all remaining public banks, excluding Banco Agrario.
21. **To be completed by September 30, 2002**
  - Complete process of bringing provisioning standards of the financial institutions to international levels.
  - Latest date for accepting the obligations of Article VIII, Sections 2, 3, and 4 of the Fund's Articles of Agreement.

<sup>1</sup> This was expected to be completed by December 31, 1999 in the original program.

Table 1. Colombia: Baseline Assumptions for  
Net External Financing of Combined Public Sector

	Mar. 2000	Jun. 2000	Sep. 2000	Dec. 2000
(In millions of U.S. dollars)				
<b>Net external financing of combined public sector</b>				
<b>(cumulative in 2000) 1/</b>	<b>1,218</b>	<b>2,087</b>	<b>2,452</b>	<b>3,197</b>
Cumulative privatization proceeds	385	1,265	2,235	2,785
Cumulative net external financing of the combined public sector 2/3/	833	822	217	412

1/ Includes only external sources.

2/ Including concession revenues.

3/ For purposes of the program the net external financing for the first quarter of 2000 includes the US\$500 million of prefinancing obtained in November 1999 that is being held abroad until the first quarter of 2000.

**NEWS**  **BRIEF**

**FOR IMMEDIATE RELEASE**

EDITORIAL DIVISION  
ROOM IS 7-1200 0493

News Brief No. 00/82  
FOR IMMEDIATE RELEASE  
September 7, 2000

International Monetary Fund  
700 19th Street, NW  
Washington, D. C. 20431 USA

**IMF Completes First Colombia Review**

The Executive Board of the International Monetary Fund (IMF) today completed the first review under the Extended Arrangement for Colombia (see Press Release 99/63).

In commenting on the Executive Board discussion of the review, Stanley Fischer, First Deputy Managing Director, made the following statement:

“The Executive Board welcomed the continuation of the recovery of Colombia’s economic activity, despite the challenges posed by the political and security situation, and fact that the the program supported by the Extended Arrangement is being implemented as planned.

“Essential elements for the restoration of confidence and recovery of private investment are the continued commitment on the part of the authorities to the objectives of their three-year economic program, further progress toward resolution of the internal conflict, progress in curbing the production and trafficking in illicit drugs, and addressing the social fall-out from these problems.

“Executive Directors welcomed the fiscal consolidation that has taken place under the program. Nevertheless, they urged that caution should be exercised to ensure that the new spending plans that had been introduced earlier this year and financed with the oil revenue windfall do not become entrenched and can be reversed if oil prices fall. In this regard, the authorities’ commitment to introduce spending cuts, if necessary, should help ensure that the fiscal objectives for 2000 will be achieved. The recent decision to strengthen the fiscal effort by introducing additional tax measures later this year, will help the fiscal adjustment while allowing

EXTERNAL RELATIONS DEPARTMENT

Washington, D.C. 20431 • Telephone 202-623-7100 • Fax 202-623-6772 • [www.imf.org](http://www.imf.org)



adequate budgetary resources to key social priorities on a more permanent basis. Executive Directors urged the authorities to eliminate the financial transactions tax which contributes to financial disintermediation by the end of 2002 as envisaged in the program.

"Executive Directors noted that the exchange market has remained orderly since the peso was floated and the foreign exchange auction system introduced last year is transparent and has been functioning well. To prevent a rekindling of price pressures, they encouraged the authorities to stand ready to tighten monetary policy if that becomes necessary to attain the inflation objective of the program.

"The strengthening of the financial system's prudential indicators is encouraging. Moreover, the authorities' plan to privatize or liquidate public banks should limit the scope for quasi-fiscal spending. The financial position of the savings and loan institutions continue to warrant close monitoring.

"The authorities' were encouraged to press ahead with the privatization program despite recent delays, as well as to work towards achieving a broad consensus on strengthening their structural policies by adding new reform initiatives to the program, especially those aimed at easing social tensions and improving investors' confidence", Fischer said.

**Statement by Murilo Portugal, Executive Director,  
and Roberto Junguito, Alternate, for Colombia  
September 7, 2000**

**Introduction**

The Colombian authorities have asked us to convey their appreciation for the professional competence and collaborative spirit shown by staff in the discussions held in Bogota and Washington for the preparation of the First Review Under the Extended Arrangement. The dialogue with the IMF also included fruitful discussions with Colombian congressmen, non-governmental organizations and the private sector, which contributed to enhance the credibility of the program and offered an opportunity to stress the significance of policies and reforms being proposed and undertaken by the government.

**Recent Developments**

As indicated by the staff, despite a complex political situation and serious domestic insecurity, the Colombian economy has performed well under the program. Economic activity began to recover late last year and, in the first half of 2000, real GDP is estimated to have grown by 3.0 percent on an annual basis, which is consistent with projected growth in the program. However, in the view of the authorities, the number of Colombians who are out of work remains unacceptably high and the government is undertaking additional steps to ensure that the unemployment rate declines. On the other hand, inflation has been kept well under control and the monetary authorities are confident that its annual 10 percent inflation target will be met. Over the past three months, the inflation rate has continuously declined, reaching an annual 9.1 percent increase by end-August.

On the external front, the current account deficit, which had shown a sharp reduction in 1999, has remained low, helped by the increases in oil export revenues and a strong export response. Besides, international reserves have increased according to the program and have been maintained at a comfortable level equivalent to near six months of imports of goods and services. More importantly, the flexibilization of the exchange rate regime adopted last September was smooth and has worked very well.

The non-financial public sector deficit was 5.5 percent of GDP in 1999, below the 6.3 percent expected in the program. As staff indicates, lower than programmed expenditures alongside higher revenues from the oil sector contributed to the overperformance. Fiscal performance for the first half of 2000 is also encouraging as it indicates that public finances have shown substantial improvements from 1999 and the fiscal deficit has remained well within the program.

As to the financial sector, it is important to note that critical conditions evident last year have subsided and a major banking crisis has been averted. Financial conditions in private sector banks are improving. Capital adequacy has strengthened; reserves for past due loans have increased and non-performing loans as a proportion of total loans have declined.

The government has carried out a thorough restructuring and capitalization of public banks. Of the six major public banks, existing in mid 1999, three have suspended banking operations and will be closed. The authorities are committed to privatize the two remaining public banks (except the Banco Agrario) before the end of 2001 and all the necessary steps are being taken to have them ready for sale by year-end.

In sum, as has been indicated in the staff report, all performance criteria for end-1999, as well as March and June, have been met, except for an exclusively end-of-year excess over the ceiling on the central bank's net domestic target related to the Y2K problem, a possibility that had been foreseen in the program. The NDA has been below the established ceiling since then.

Also, all but two of the structural benchmarks were achieved. The circumstances and motivations for the two postponements were discussed on a timely fashion and at length with staff. One is the pension reform law, a draft proposal of which has been subject to technical review by the World Bank and is now in consultation and consensus building before being submitted to Congress before year-end. The second has to do with one remaining regulation regarding indicators of financial sector performance associated with the financial sector reform law. Its content is being analyzed by a financial sector mission from the Fund presently in Colombia.

### **Policy Discussions**

Policy discussions, as noted by staff, were undertaken both with the outgoing and the new Minister of Finance. The main aspect to point out is that, notwithstanding the change, there has been full continuity of policies on major issues and the new Minister of Finance has expressed his full commitment to the program. We should point out that not only Fund staff traveled to Colombia to discuss issues with the new economic team, but also that the Minister very recently came to Washington and held meetings with staff and Management to express his support for the program and indicate his views on the content and passage of structural reforms.

The major current fiscal policy items discussed, well covered in the staff report, referred to the use of additional oil revenue in 2000, which helped to compensate a shortfall in revenues and to finance non-recurrent spending programs; the decision of the Colombian authorities, supported by staff, to monitor fiscal development on a commitment rather than cash basis; the characteristics of the 2001 budget submitted to Congress by the authorities, which is consistent with the program's fiscal targets; and the fiscal implications of the project known as "Plan Colombia", a government strategy to deal with the internal conflict and narco-trafficking, widely supported by the international community.

Another policy issue discussed was privatization. As pointed out in the Letter of Intent, the authorities do not expect that the plans drawn for the privatization of public enterprises in 2000 can be fully executed. Despite difficulties linked both to lack of investor interest and security problems, the government is going ahead in 2000 with the privatization

of the coal company, Carbocol, the electricity generating firm, Isagen, and the Bogota telephone company, ETB. To facilitate additional external borrowing, in light of the delay in the privatization program, the authorities have asked for the end-2000 external debt indicative ceiling of the public sector to be raised by US\$300 million. Additionally, as noted by the authorities, if opportunities arise to pre-finance the needs for the year 2001 during the coming months, the government would tap the markets after discussing with the Fund the changes that may be required in the external indebtedness ceilings, and would maintain the foreign exchange abroad until it is needed.

As shown in the staff report, the Colombian monetary authorities are proposing that the ceiling on the central bank's net domestic assets (NDA) for the second half of 2000 be raised on account of an increased demand for currency, with the target for net international reserves remaining unchanged. The analysis by the Colombian authorities indicates that on account of the reduction in inflation and the presence of the financial transaction tax, there has been a permanent shift in the composition of broad money demand and an increase in the demand for base money. Regarding the risk of reigniting inflationary pressures, the authorities wish to reiterate that the principal objective of monetary policy in Colombia is to control inflation and that the authorities remain prepared to take action to achieve the inflation target set annually by the Central Bank staff. The authorities would also like to inform that progress has been made in the implementation of the inflation targeting framework and that substantial effort is being devoted to improving the forecast capability and the understanding of the transmission mechanisms of monetary policy.

### **Structural Reforms**

As indicated by staff, a tax package was submitted to Congress last March, which differed somewhat from that originally envisaged in the program both in terms of expected revenues and the reform content. The tax proposal submitted reflected the appreciation by the authorities of what then appeared as an adequate second best and politically acceptable tax reform. The new Minister of Finance has indicated the government's intention of strengthening the tax package submitted to Congress, both in terms of expected revenues and structural content. The revised reform will aim to simplify the tax structure, reduce exemptions, and widen the VAT and income tax base. The final decision on the fiscal reform corresponds to Congress and the government expects the tax package to be approved by year-end.

Progress was made in the approval of structural reforms. Legislative initiatives have been approved for the creation of a territorial government pension fund, which was approved through Law 549 at the end of 1999, as well as the strengthening of local public finances. Other proposed structural reforms include a constitutional amendment regarding the transfers to the territorial governments, which modifies the revenue transfers from the central government, and a second generation reform of social security pensions, which is expected to eliminate the sources of future deficits of the social security institutions to guarantee their financial viability in the medium term. The proposed reforms are currently being subject to discussion and consensus building through round-table discussions. The authorities'

expectation is that by year's end both reforms make progress in Congress so as to have them approved next year as programmed. In addition to the structural reform package originally agreed, the government has advanced on the drafting and will submit to Congress a fiscal responsibility law in order to establish fiscal rules and facilitate fiscal consolidation both at the central administration and territorial government levels.

## **Conclusions**

The Colombian authorities appreciate the staff's recommendation for completion of the first review under the extended arrangement on the basis of good performance and express, once again, their firm commitment to the policies and the measures required to obtain the objectives of the program. We thank the Board for the support it has given to the Colombian program and ask Directors for their approval of the authorities' proposals to raise the program's ceiling on external debt; to change the definition of the fiscal deficit to a commitment basis for improved monitoring; to set the ceiling on the central bank's domestic assets at a higher level in view of the permanent shift in the composition for the demand for money; and to introduce adjusters to the ceiling of the fiscal deficit and external public debt to allow future disbursements of concessional loans that may be forthcoming in support of Plan Colombia.

We would like to close this statement emphasizing that, in the view of the Colombian authorities, the support to the program by the IMF has contributed significantly to its credibility and provided potential access to IMF resources, which the authorities have not considered necessary to draw. Following a long-standing tradition of the country in support of transparency, the Colombian authorities are interested in having the staff report, this Buff statement, as well as the LOI and the Technical Memorandum placed in the web and published. The Board, on this account, should recall that Colombia participated, with a very positive experience, in the pilot project for the release of the Article IV staff report and that it is also engaged in the Standard Data Dissemination Standards, SDDS.