ESSAYS ON COLOMBIA’S ECONOMIC DEVELOPMENT

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Matrícula: XXXXXX

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INTRODUCTION

During the 1990s, the Colombian economy went through extreme points of the economic cycle: after growing at 5.1% (first part of the decade), economic growth collapsed registering negative growth rates (-4.2% in 1999). This represented the major fall in the last 100 years.

After a period of slow recovery, the Colombian economy presented growth rates above 5%. In 2005, GDP reached 5.2% and until the global slowdown GDP was growing at rates above 6%. When compared internationally, in the period 2002-2005, Colombia presented growth rates above the mean of the LAC region, and also above countries such as Brazil and Mexico. This can be explained by different factors, both internal and external ones. In the former ones, the role of household’s consumption stimulating effective demand and the confidence of investors, and improvements in labour productivity along historically low interest rates. In the case of external ones, the sustained growth of the main trading partners, the favorable terms of trade, and the increase in capital inflows (mainly foreign direct investment). By this, unemployment was reduced in 5.2% (from 15.6% to 10.4%) and poverty in 5% (from 54% to 49%) according to data of the Ministry of Planning.

During the 2000s, new challenges are present for policy makers regarding economic policy in order to boost inclusive growth in times of greater financial and economic integration but, with gloomy expectations about the economic performance of developed countries. In this sense, the main goal of economic policy is to consolidate sustained high growth rates of the Colombian economy in order to reduce poverty and unemployment levels. On this regard, it is necessary and crucial to identify the risks that will possibly affect negatively the growth performance in order to prevent them and suggest policy options.

Risks are diverse. From sudden changes in the international context such as changes in the terms of trade, financial collapse, crisis contagion or other that could reduce or reverse the flows of capital. In addition, excess aggregate demand over productive capacity would limit the accomplishment of inflation targets, or sudden changes of interest rates or exchange rates and their effects on the financial system. The 1999 crisis showed that a crisis in the real sector came along a crisis of the financial sector and both interact and reinforce each other. Another
associated risk, is the rapid growth in the value of some assets different from Government securities (treasury bills), particularly those of equities and real estate. Sudden negative (positive) changes would have negative (positive) wealth effects reducing (augmenting) households’ consumption, investment and the flow of capital. Finally, an excessive appreciation of the local currency (Colombian peso) would have certain impacts on growth and export competitiveness of the country, exposing local producers to an aggressive international competition.

This work is divided in two major parts. The first, explores the main features of recent developments of more elaborated theories to understand the functioning of modern economies regarding the close interaction of the nominal stock of money (and how the changes in the money stock are determined) with the rest of the economy, particularly on the economy’s real variables. The second, emphasizes on the understanding of how the Colombian economy works, their past developments and reforms, its structural changes and recent challenges that the economy face to boost sustained growth while reducing income inequality and poverty.

Structure of the thesis

The first chapter provides a literature review regarding Structuralism, Bastard-Keynesian, and Post-Keynesian theories. In the latter, is presented the theory of monetary production in its simplest model. Finally some issues are addressed regarding the Stock-Flow Consistent approach followed recently by many Post-Keynesians. Also is presented a review of the relevant literature regarding Computable General Equilibrium (CGE) models and in particular those applied models developed for Colombia.

The second chapter provides an initial overview of the performance of the Colombian economy in order to understand the major policy changes that generated structural changes in the economy. It considers the transition from a relatively ‘closed’ economy position to a more integrated one to international markets, which increased the vulnerability of the country to international fluctuations.
The third chapter takes into consideration the role of the financial sector in overall economy. It presents also the role of the Central Bank and its policy adoption of inflation targeting. It follows analyzing the role of the private banking system and ends up examining the different set of monetary policies adopted by the country.

Finally, the last chapter deals with the current situation of the Colombian economy in a period of gloomy expectations. The analysis draws on the differences with the 1999 crisis. It presents which are the main drivers of growth in the recent period and analyze the risks that the economy face despite the recent outstanding growth performance.