

SPECIAL REPORT

COLOMBIA'S FISCAL OUTLOOK HINGES ON THE ELECTION

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TABLE OF CONTENTS

EXECUTIVE SUMMARY	4
INTRODUCTION	6
METHODOLOGY	7
CONTEXT: EVOLUTION OF COLOMBIA’S MACROECONOMIC ENVIRONMENT & INSTITUTIONS	8
MACROECONOMIC ENVIRONMENT	8
ANNUAL INFLATION	9
UNEMPLOYMENT RATE	10
FOREIGN DIRECT INVESTMENT	12
COP PERFORMANCE	12
BOND ISSUANCE	13
STRONG, INDEPENDENT INSTITUTIONS	14
BANCO DE LA REPÚBLICA	14
FISCAL RULE	17
WHERE WE ARE TODAY: RISING FISCAL CHALLENGES	18
MEDIUM TERM FISCAL FRAMEWORK	18
MARKET REACTION	20
TAX REVENUE SHORTFALLS	22
GOVERNMENT EXPENDITURE	24
DEBT-TO-GDP	26
DEBT SERVICING COST	27
NATIONAL BUDGET PROPOSAL FOR 2026	28
POTENTIAL RISKS	30
UPCOMING ELECTIONS	30
EXTERNAL FUNDING SOURCES	31
DECERTIFICATION BY THE UNITED STATES	31
INTERNATIONAL MONETARY FUND’S FLEXIBLE CREDIT LINE	32
OTHER MULTILATERAL BANKS	32
ALTERNATIVE DEBT FINANCING OPTIONS	33
COMPETENCIES LAW	33
MINIMUM WAGE INCREASE	34
OIL EXPLORATION	35
VULNERABILITIES TO EXTERNAL SHOCKS	36
FURTHER DOWNGRADES	38
ELECTORAL GUARANTEES’ LAW	38
CASE SCENARIOS	39
BASE: STEP IN THE RIGHT DIRECTION, BUT LONG RECOVERY AHEAD	40
ADVERSE: PRO-SPENDING DRIFT, RULE SLIPPAGE, AND INTENSIFIED MARKET STRESS	40
FAVORABLE: TECHNOCRATIC LEADERSHIP, STRUCTURAL REFORM, AND CREDIBILITY RESTORED	41
CONCLUSION	43

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EXECUTIVE SUMMARY

There are two sides to Colombia’s economic outlook. The Petro administration highlights reduced inflation, steady GDP growth, and lower unemployment as evidence of sound economic policy. However, behind these seemingly solid headline numbers lies a deteriorating fiscal reality: government spending is surging, debt is climbing, and the fiscal rulebook has been tossed aside. In June 2025, the Petro administration suspended the fiscal rule by invoking the escape clause for up to three years, despite warnings from the Autonomous Committee for the Fiscal Rule. This decision signals the government’s unwillingness to cut costs and effectively grants it free rein to spend ahead of the 2026 presidential elections. Soon after, the government presented an overly expansive budget proposal, which is likely to further erode its credibility and perceived commitment to fiscal sustainability, already a source of concern for markets and credit rating agencies.

This report examines the growing fiscal and political risks that threaten Colombia’s economic trajectory and institutional integrity, particularly as the 2026 presidential and congressional elections approach. President Petro’s commitment to above-inflation minimum wage increases directly contradicts his public criticism of the Central Bank for maintaining tight monetary policy and not lowering interest rates at the pace he expected. Wage-driven inflation is likely to limit the Bank’s ability to reduce rates while it continues to combat inflationary pressures. As a result, this minimum wage policy is likely to prove counterproductive, worsening inflation and weakening conditions in the formal labor market.

In addition, Colombia remains highly exposed to external shocks due to its commodity-dependent export structure and reliance on external financial inflows. Oil and coal account for about half of total exports. A sudden drop in oil prices would likely reduce export revenues, weaken the Colombian peso, and strain the government budget.

At the core of Colombia’s fiscal challenges is a structurally rigid spending framework dominated by legally mandated and indexed expenditures. The proposed *Ley de Competencias* (Competencies Law), a bill aimed at regulating a larger share of resources administered at the regional level, is likely to strain this framework further. The administration’s consistent refusal to implement spending cuts exacerbates the problem and appears to be a deliberate political strategy rather than a policy oversight ahead of a highly contested electoral period. **This expansionary fiscal stance is likely to worsen Colombia’s fiscal outlook for 2026 and pose significant challenges for the incoming administration, which will almost certainly face strong public opposition to making the necessary adjustments.**

Despite mounting risks ahead of the elections, Colombia’s saving grace in turbulent times has consistently been its strong institutions, such as the Central Bank, that provide effective checks and balances. As this report examines the Bank’s independence and its commitment to its mandate, it is important to note that President Petro, after appointing three co-directors, has no remaining appointments to the Board, while the incoming administration will only be able to appoint new members in January 2027.

Lastly, we identify three forward-looking fiscal scenarios for the post-Petro landscape, each hinging on the policies and economic acumen of the next president. We built these scenarios from our extensive interview phase with experts, most of whom were pessimistic about the fiscal direction of the current administration, and building on Colombia Risk Analysis expertise and market relations. **While markets are cautiously optimistic that there is a high chance Colombia will return to a market-friendly administration with fiscally responsible leadership, we emphasize that the race remains open and cannot**

be called this early on. The political opposition faces a fragmented field, weakening its ability to deliver a decisive win despite the administration’s low approval and mounting macroeconomic headwinds. We invite readers to consult our August 2025 report, [Fragmentation and Polarization One Year Ahead of the Next Presidency](#), to learn more about the candidates and what to expect during the presidential campaign.

Ultimately, the next 12 months will be pivotal, as fiscal slippage, institutional tension, and political uncertainty are likely to define the landscape heading into 2026. This report provides an in-depth analysis of the fiscal path ahead, the likely implications of electoral outcomes, and the structural reforms needed to prevent further deterioration. For investors and decision-makers navigating Colombia’s complex environment, timely and well-grounded insight will be essential to cut through the noise. **We encourage readers to subscribe to Colombia Risk Monthly to anticipate the trends that will shape the political, economic, social, and security agenda during the upcoming electoral period and beyond.**

	Probability	Presidential Candidate	Market Reaction	Fiscal Impact	Social Impact
Base	High	Moderately market-aligned	Market Rally	Limited yet positive fiscal consolidation	Continued social protests, Congress imposes legislative constraints
Adverse	Low	Limited market alignment	Market Sell-off	Widening deficit, higher debt-to-GDP ratio, rising debt levels	Increased social spending, growing security concerns
Favorable	Medium	Market friendly	Market Rally	Strong fiscal consolidation, tax reform, and structural spending adjustments	Widespread social protests, low initial approval rating



INTRODUCTION

Colombia's current economic landscape presents a stark duality. On the surface, key macroeconomic indicators show resilience as GDP growth has gained momentum, inflation is trending downward, and unemployment has reached multi-year lows. However, beneath these positive signals lie deeply concerning fiscal challenges. The country's fiscal deficit continues to widen, public debt has reached its highest levels in over a decade, and structural rigidities in government expenditure limit the scope for meaningful fiscal adjustment. This imbalance poses significant risks for Colombia's long-term economic sustainability.

Historically, Colombia has distinguished itself in Latin America for effectively avoiding hyperinflationary and sovereign debt crises that have been endemic to the region. Strong institutional checks and balances, such as the country's Central Bank, have been strong anchors for macroeconomic stability. However, the current macroeconomic climate, rising populism, and recent threats by the executive branch to the country's institutional autonomy have threatened policymakers' ability to safeguard the fiscal outlook, as the fiscal deficit and debt levels approach historic highs.

After invoking the escape clause in June 2025, the Petro administration suspended the fiscal rule for three years. This decision has been heavily criticized by local and international experts, prompting credit rating downgrades by both [S&P Global Ratings](#) and [Moody's](#), further raising the country's risk premium. Given current conditions, it is unclear how the government will be able to comply with the fiscal rule again without a significant fiscal adjustment. This situation is critical given next year's presidential elections, as the next administration will inherit a complex fiscal landscape with a significant degree of inflexibility in government expenditures.

Most recently, the Petro administration presented its proposed budget for 2026, which mirrors the structural [shortcomings of the 2025 budget](#) enacted by decree after being [rejected](#) by Congress last year. Specifically, it lacks sufficient revenue backing, which implies that a tax reform will be necessary to finance the government's planned expenditures, even though the Petro administration also [failed](#) to pass a similar reform to fund this year's budget. **The administration's consistent refusal to implement spending cuts appears to be a deliberate political strategy rather than a policy oversight ahead of a contested electoral period. This expansionary fiscal stance, ahead of a highly contested electoral period, is likely to worsen Colombia's fiscal outlook for 2026 and pose significant challenges for the incoming administration.**

This report first outlines Colombia's macroeconomic environment and institutions, then identifies the political and fiscal risks for the Colombian bond market, and finally analyzes potential fiscal scenarios depending on the type of presidential candidate elected next year.

The purpose of this Colombia Risk Analysis report is to provide our audience, including investors and analysts, with a clear assessment of the extent to which the current administration can influence Colombia's fiscal position in the year leading up to the elections and the challenges the incoming administration will face.



METHODOLOGY

For this report, we interviewed 17 sources, including government and private sector experts, from Colombia, Chile, Brazil, and the U.S. Some interviews included prior finance ministers and presidential candidates. In addition to primary interviews, we drew on secondary sources and tapped into Colombia Risk Analysis' extensive knowledge base. These sources included reports, press articles, academic articles, databases, and public policy documents. This collaborative approach allowed us to understand the different perspectives on the political and economic landscape in Colombia.

We thank the experts for their time and contributions to this special report, provided under the principle of non-attribution.



CONTEXT: EVOLUTION OF COLOMBIA'S MACROECONOMIC ENVIRONMENT & INSTITUTIONS

MACROECONOMIC ENVIRONMENT

Despite pockets of resilience, Colombia faces a sluggish macroeconomic environment with growing fiscal pressures. While the economy has benefited from slow but moderate growth with [real GDP growth at 2.4%](#) for 2025, economic expansion has stabilized on the back of resilient [private consumption](#), a strong job market and services sector, and gradually improving real incomes as inflation decelerates. Nonetheless, price pressures remain above the Central Bank's 3% target, and core components of inflation have proven sticky.

Monetary policy is still restrictive in real terms, with the Central Bank's policy rate slowly easing from prior peaks. However, compared to other regional peers, Colombia has been slow in its cutting cycle due to persistent inflation and macroeconomic uncertainty. This restrictive stance has supported the peso, as Colombia's relatively high interest rates have attracted investment. More importantly, despite political pressure and public criticism from the government, Colombia's Central Bank has upheld its institutional independence and remains a credible actor, as it is likely to continue adjusting monetary policy in line with its constitutional mandate throughout the remainder of the Petro administration.

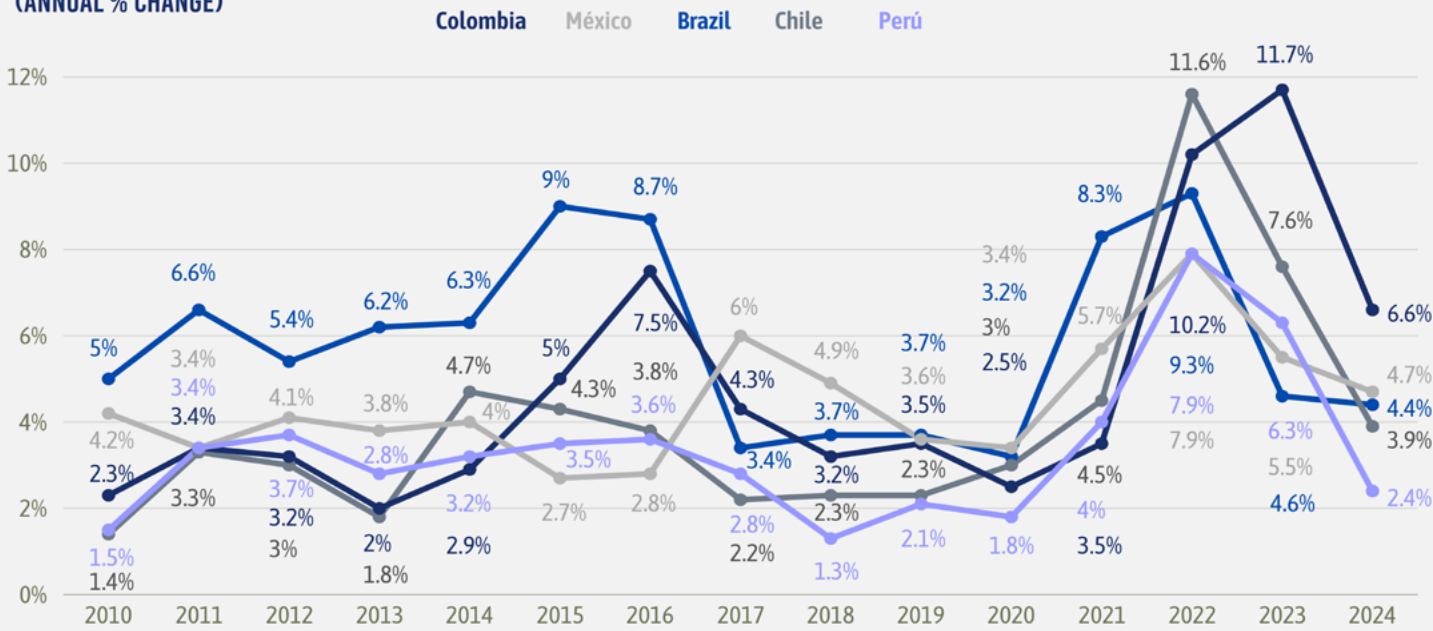
On the fiscal front, wider-than-planned central government deficits and lower-than-projected revenues have lifted financing needs, prompting the Ministry of Finance to issue bonds to finance its growing spending. The Petro administration has failed to present a convincing case for budgetary consolidation as it has refused to [make cuts to social spending](#). However, the government has had enough political leeway to make some cuts to subsidies, such as fuel and planned energy subsidies, that other governments would have been unable to deliver.

Ultimately, while the macroeconomic environment has improved since the lows of the pandemic, the outlook remains sensitive to the pace of global easing, domestic policy signals, particularly regarding fiscal rule credibility and the pace of monetary normalization, and, most importantly, next year's presidential elections. **This view is shared almost unanimously by the sources we interviewed and aligns with our own assessment.**

- ### ANNUAL INFLATION

Inflation has continued on its path of deceleration. Down from its [peak](#) of 13.3% in May 2023, Colombia's annual inflation rate has declined to [4.9% as of July 2025](#), mainly due to moderating food prices and the appreciation of the peso. However, the figure is still above the Central Bank's long-term target of 3%. The Central Bank forecasts that inflation for [2025 will reach 4.4%](#), with a gradual convergence toward target levels in 2026. As visible in the chart above, Colombia's inflation peaked after regional peers, and as such, has been slower to come down compared to other countries.

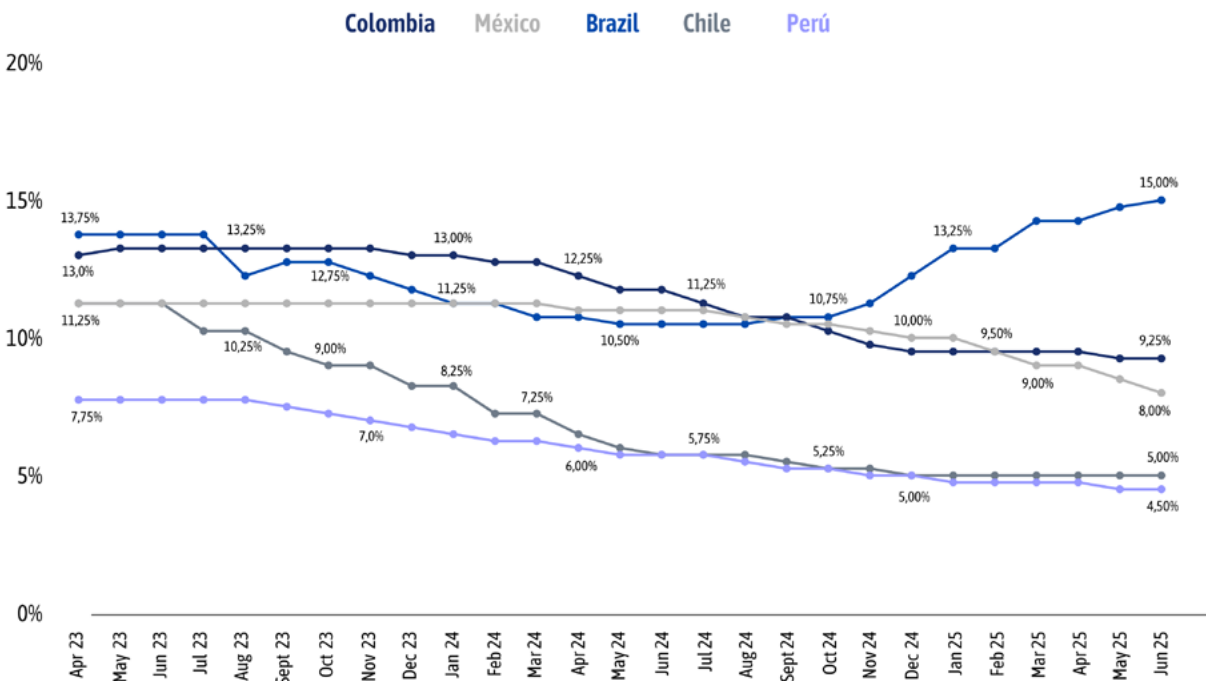
INFLATION RATE, AVERAGE CONSUMER PRICES
(ANNUAL % CHANGE)



Source: International Monetary Fund



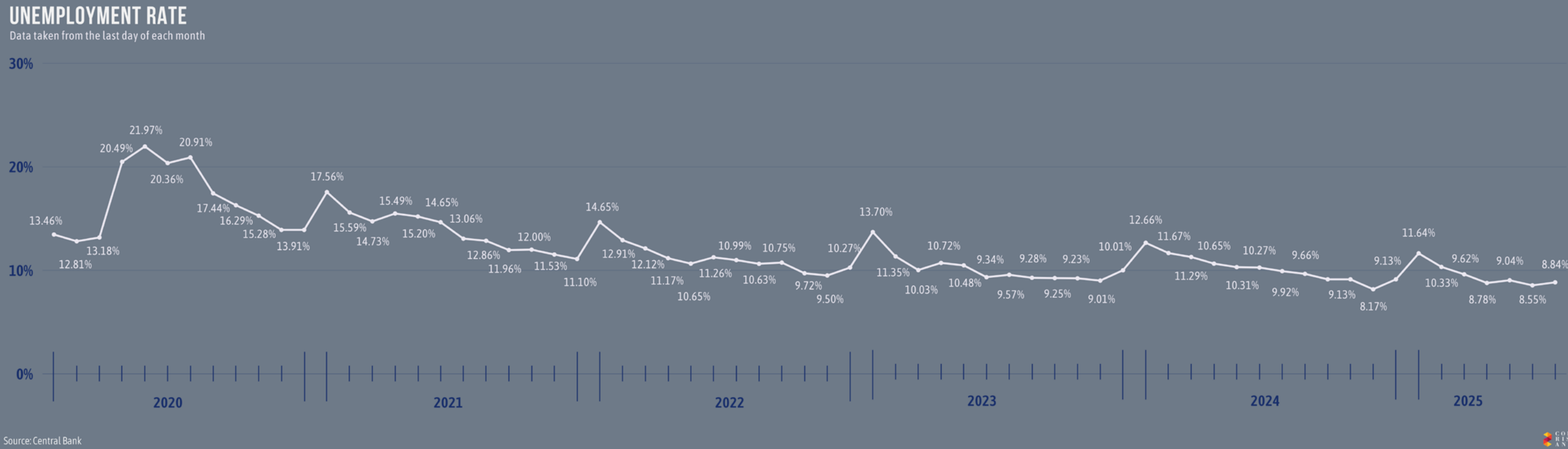
CENTRAL BANK INTEREST RATES



Given persistent inflation, monetary policy remains restrictive, reflecting the Central Bank’s commitment to price stability amid fiscal uncertainty. The chart above reflects the Colombian Central Bank’s comparatively more cautious stance in its cutting cycle compared to other central banks in the region. Most recently, the *Banco de la República* maintained its benchmark policy rate at [9.25% in July 2025](#), representing the Board’s cautious stance given current macroeconomic conditions. While further rate cuts are likely in the second half of 2025, the pace of normalization is expected to be gradual, with the Central Bank closely monitoring inflationary dynamics and fiscal developments.

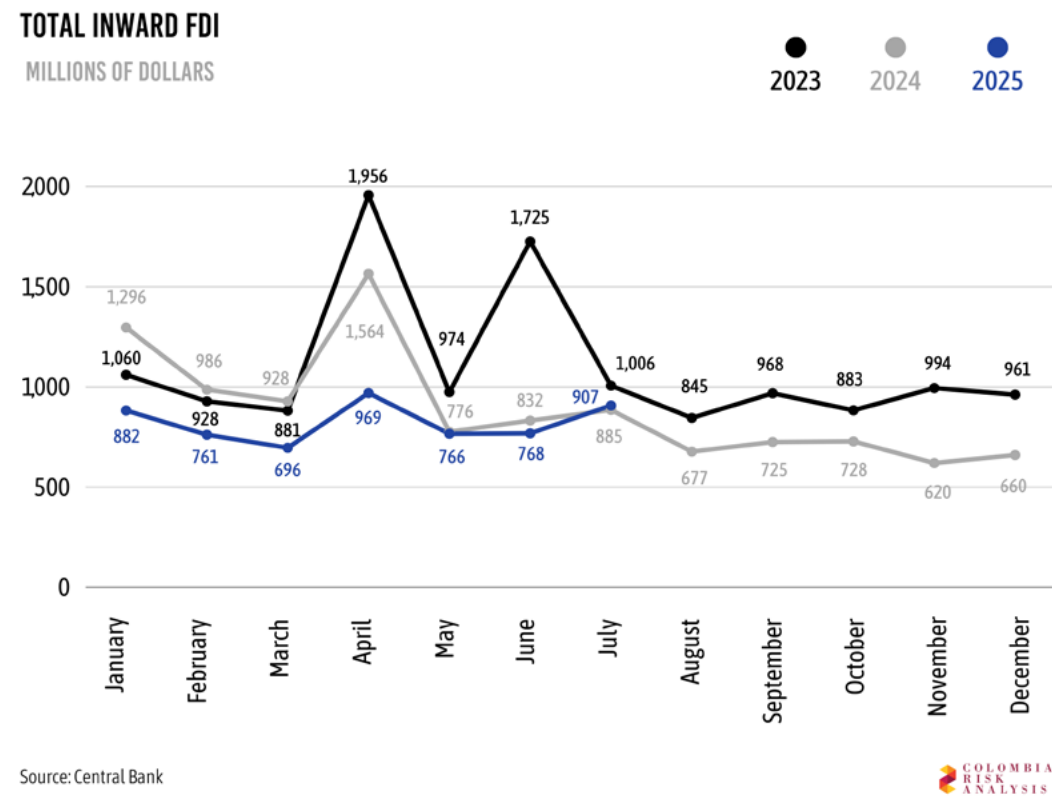
• **UNEMPLOYMENT RATE**

Over the last several years, Colombia’s unemployment rate has progressively declined, recently falling to [8.8% as of July 2025](#), a 1.1% decrease compared to the previous year. This rate marks the lowest level recorded for that month since 2001. In July, most job creation occurred in the hospitality and food services (186,000) and transportation and storage (172,000) sectors. The participation rate rose modestly to 64.6%, while the employment rate climbed to 58.9%. The drop in unemployment translated into approximately 766,000 more employed individuals and 230,000 fewer unemployed compared to the same month the previous year. In total during the [first semester of 2025](#), 842,000 new jobs were created. This strong labor market performance supports the government’s reluctance to reduce public spending. However, while rural areas can absorb labor, improving rural well-being will require transitioning these jobs into the formal sector.



• **FOREIGN DIRECT INVESTMENT**

According to the Central Bank, [Foreign Direct Investment](#) (FDI) into Colombia decreased by 15.2% in 2024, down by USD 2.5 billion from 2023. More recently, [FDI fell by 24.1%](#) in the first half of 2025 compared to the same period in 2024. This drop reflects business leaders’ perceived risk of the current administration and its unpredictability. According to business association [Fenalco](#), the business community lacks confidence in the government’s policies, failing to provide stability for investors. The major industries affected are mining and oil extraction, agriculture, and manufacturing.

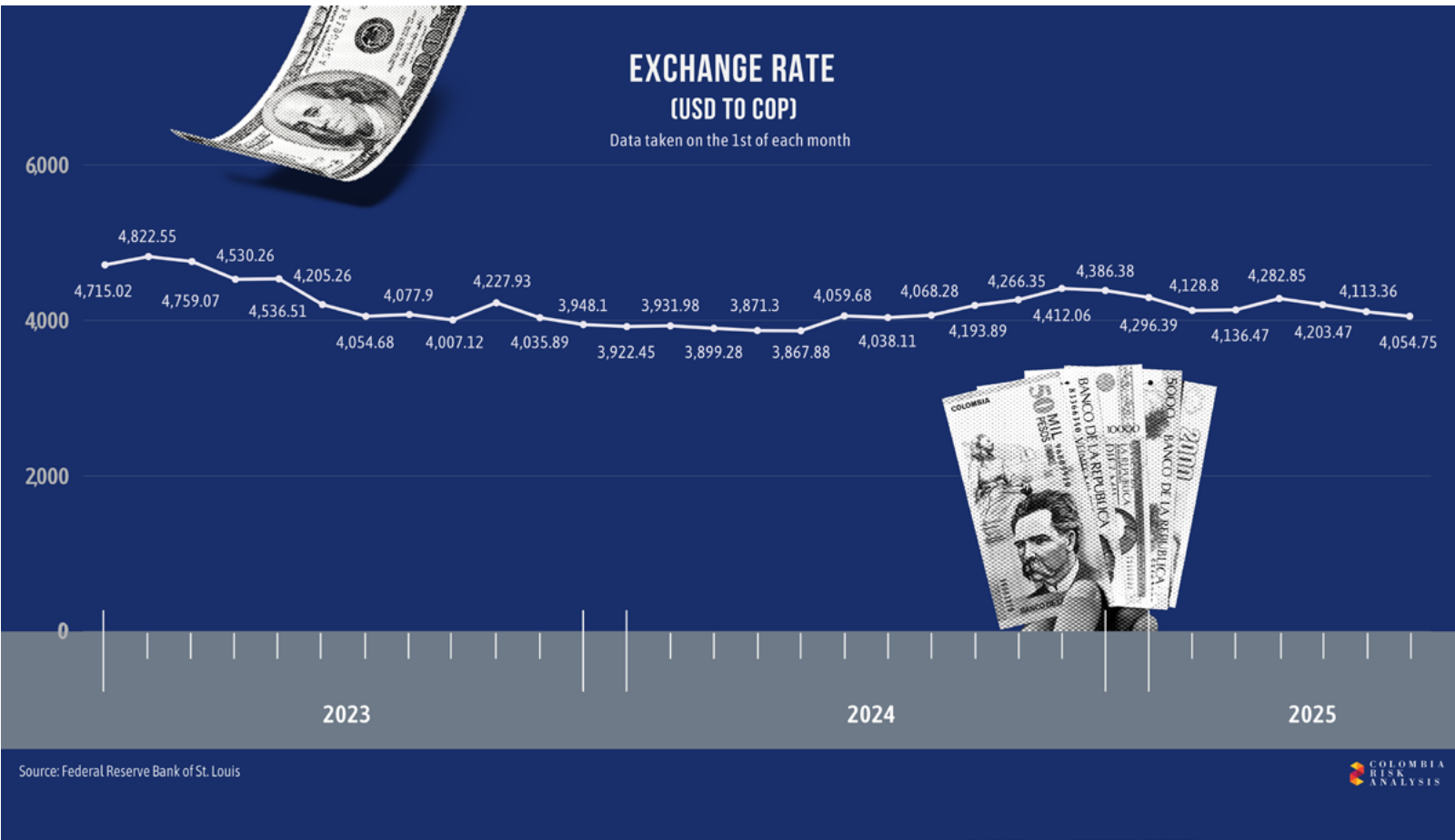


• **COP PERFORMANCE**

As of mid-August 2025, the Colombian peso (COP) had appreciated more than 8% versus the U.S. dollar compared to the start of the year. However, the appreciation of the COP does not primarily stem from the country’s strong fundamentals, but rather, it is due to the additional [yield pickup](#) versus the currencies of other emerging markets (EM) and the U.S. Colombia, currently rated BB by most credit rating agencies, is trading at a higher spread (i.e., cheaper) compared to countries that hold riskier ratings due to the Petro administration risk premium.

This interest-rate differential has made the COP one of the more lucrative EM currencies for investors looking for higher yields. A [currency carry trade](#) involves borrowing in a low-interest-rate currency, otherwise known as the funding currency (such as USD), converting it into a higher-yield local currency (such as COP), and investing in domestic assets that earn higher interest. The profit stems from the difference between the borrowing cost and the local return, plus any appreciation of the target currency, as long as exchange rates remain stable or move favorably. Given the rate differential, foreign investors [borrowing in USD to go long in COP](#) have earned positive returns in carry trades so far in 2025, reinforcing demand for the COP. This dynamic has artificially supported the value of the COP versus the USD.

However, according to key expert interviewees, the Colombian Central Bank now has to set monetary policy to not only reach its inflation target but also to carefully balance these carry trades so as not to lower rates too quickly, leading to rapid investor outflow, thus depreciating the COP. However, it is worth highlighting that the value of the COP is not solely in the control of the Central Bank or the administration; rather, it is highly contingent on external factors, such as the U.S. Federal Reserve’s policy interest rate, oil prices, and the basket of EM commodities. The volatile trade policy put forward by the Trump Administration further adds uncertainty and volatility to the value of the peso.



• **BOND ISSUANCE**

In comparison to the [2025 Financial Plan](#), the 2025 Medium-Term Fiscal Framework (MTFF) revealed a sharp rise in financing needs to address the wider-than-projected fiscal deficit through the issuance of both [local and external bonds](#). Specifically, the Petro administration plans to [boost local bond \(TES\) issuance](#) by COP 12 trillion and increase short-term treasury operations by COP 43 trillion in 2025. In late July 2025, the government executed a [large TES exchange](#) (~COP 26 trillion) to smooth amortization profiles and reported interest savings for 2025, a standard liability-management tool to ease near-term funding pressure. It also plans to continue similar strategies into 2026 with up to COP 60 trillion in local issuance and more treasury funding. Through this approach, the Ministry of Finance aims to lower borrowing costs but introduces higher refinancing risks.

For context, Colombia issues two main types of local bonds: COLTES (local currency fixed-rate bonds) and [TES UVR](#), which are local currency bonds indexed to the *Unidad de Valor Real* (UVR), a unit of account that tracks inflation and is certified by the Central Bank. UVR bonds, described as inflation-linked TES, transfer inflation risk to investors and



lower the sovereign’s real financing cost when inflation expectations are well-anchored. These bonds also broaden the investor base to institutions like pension funds and insurers seeking inflation-matched assets. However, a rising reliance on UVR bonds exposes the Colombian government to higher and less predictable debt servicing costs, as payments increase directly with inflation. With issuance quotas expanded in 2025, a prolonged period of above-target inflation amplifies fiscal pressures.

STRONG, INDEPENDENT INSTITUTIONS

In the eyes of markets and investors we interviewed for this report, Colombia’s saving grace through turbulent times is its strong institutions that provide effective checks and balances. During the Petro administration, many international actors have [expressed their concerns](#) regarding the erosion of institutionalality, questioning whether President Petro is attempting to sway institutions in his favor. However, the last few months have truly put the country’s institutional independence to the test.

• BANCO DE LA REPÚBLICA

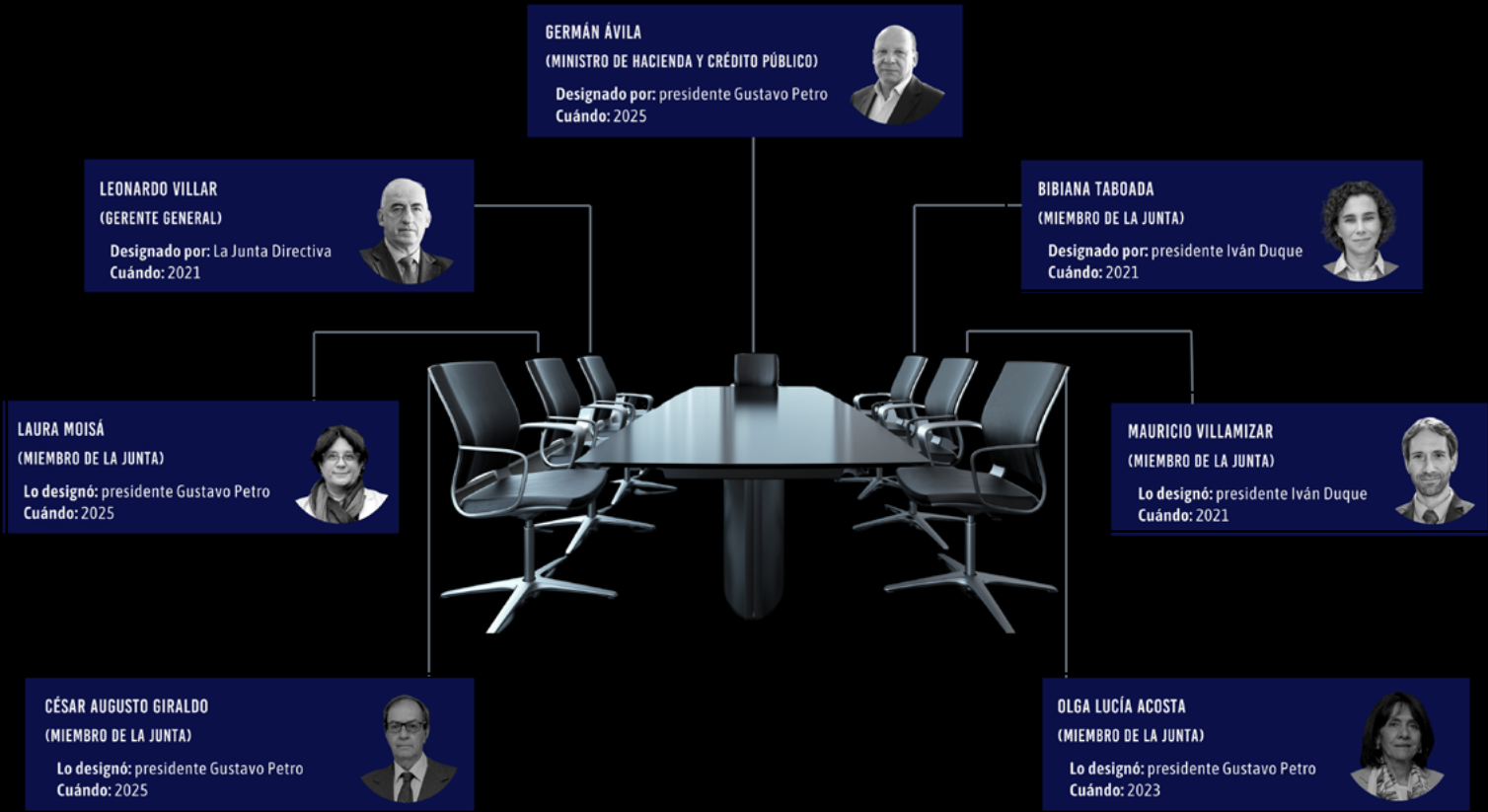
The 1991 Constitution firmly established the independence of Colombia’s Central Bank (*Banco de la República*), transforming the institutional framework of the country’s monetary policy and granting it constitutional autonomy. The granted independence marked a significant shift from the prior framework in which monetary policy was subject to political influence and was used to fund the government’s needs. For example, the constitution now states that any direct loan to the central government requires [unanimous approval](#) by the board members, precisely to avoid monetary financing. Up until now, the Central Bank has never granted any direct loans to the central government, thus maintaining its independence. [Article 371](#) of the constitution outlines the *Banco de la República*’s “[administrative, patrimonial, and technical autonomy](#)” from the executive branch. This article defines the institution’s primary [objective](#) as maintaining the currency’s purchasing power through an inflation-targeting strategy aimed [at the 3.0% target](#) as defined by the Central Bank’s monetary policy [since 2002](#).

The constitution also created the Central Bank’s Board of Directors, which has seven members. The Bank’s Governor is elected by the Board every four years and may serve up to two additional terms, allowing a maximum tenure of 12 years. A distinctive feature of the Colombian Central Bank, compared to others in the region, is that the Minister of Finance and Public Credit, whom the president appoints, is a voting member of the Board. The Minister also chairs Board meetings to coordinate the Bank’s decisions with the government’s overall economic policy, while respecting the institution’s autonomy and independence. The president appoints the remaining five Board members for fixed four-year terms, which can be extended twice. Every four years, the president can replace two members during the first month of each term. **President Petro has no further appointments to the Central Bank, while the incoming administration will only be able to appoint new Board members in January 2027.**

Since his election, President Petro has publicly criticized the Central Bank for its [high interest rates](#), as he claims it deters economic growth. His public shaming and [finger-pointing](#) towards members of the Central Bank have raised concerns over his potential to influence decisions. Worries about a loss of autonomy intensified in February 2025 as the current administration theoretically began to hold a majority in the Board, having chosen 4 out of 7 members.



MIEMBROS DE LA JUNTA DIRECTIVA



Fuente: Banco de la República

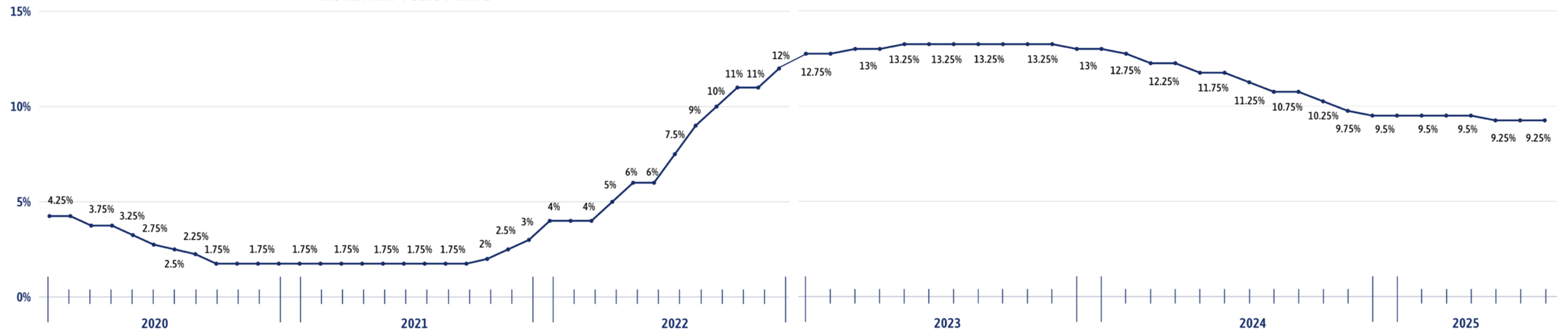


As mentioned in the *Colombia Risk Monthly #80* report, President Petro criticized the [Bank’s March 2025 decision](#) to keep rates steady, and suggested the Bank was aligned with the opposition and pointed to Co-Director Bibiana Taboada’s close family ties to a [campaign adviser of Victoria Dávila](#), a leading right-wing candidate. While this attack raised doubts on its ability to maintain independence, Central Bank Governor Leonardo Villar [publicly rejected claims of politicization](#), underscoring that, apart from the Finance Minister, Board Members do not represent political parties. Instead, the Bank’s decisions rest on technical analysis and the constitutional mandate to protect purchasing power.

The institutional record since January demonstrates that the Bank’s culture and decision-making framework continues to place price stability at its core. In [April 2025](#), the Board cut the policy rate unanimously by 25 bps to 9.25%. In [June/early July 2025](#), with inflation proving sticky and fiscal risks rising, the Board held the rate at 9.25% by majority vote, with the minutes highlighting slower-than-hoped disinflation, higher fiscal deficit projections, and tighter external conditions as reasons for caution. In the [July-end meeting](#), the Board again held rates at 9.25% due to above-target inflation and uncertain macroeconomic conditions. As in prior occasions, [President Petro](#) and his former [Chief of Staff Alfredo Saade](#) criticized the Central Bank for its July 2025 decision, claiming that this decision was politically motivated against the current administration to [influence the elections](#). The Board’s next meeting occurs at the end of September, and should the Board maintain interest rates steady, we can expect the President’s anger to be reflected on social media once again.



MONETARY POLICY RATE



Source: Central Bank



Market narratives often cast Olga Lucía Acosta as a centrist “swing” vote. However, the public record supports that she has voted in line with what the staff outlook and the inflation mandate require, even when that means disappointing easing advocates, including [President Petro, who appointed her](#). In late Q1 2025, with inflation still persistent, press coverage indicated a 4–3 vote to keep the rate at 9.50%, in which [Acosta’s stance was decisive](#), causing uproar from President Petro. On [his X account](#), the President publicly called Acosta out, questioning his decision in appointing her to the Board. Subsequent meetings continued to show split votes rather than a bloc aligned with the administration, and the [July 2025 press conference](#) revealed a 4–2–1 configuration (hold vs. 50 bps cut vs. 25 bps cut), again signaling nuanced, case-by-case judgments rather than a political line. During our interviews for this report, one source, who previously worked with Acosta, assured us of her professionalism, her unbiased views, and her adherence to her duties according to her mandate. **Through her independent votes, Acosta has proven her allegiance to the Central Bank’s mandate, ignoring any presumable political affiliation, which provides confidence in the institution’s autonomy and independence.**

This pattern (technical rationale + divided but disciplined votes) is consistent with what multiple local experts describe as the Central Bank’s strong internal culture of independence and institutionality, which has previously weathered episodes of political pressure.

• FISCAL RULE

In 2011, Colombia adopted a formal fiscal rule through [Law 1473](#) to enhance its fiscal discipline, given concerns about debt sustainability and rising deficits. It additionally included an escape clause that allows the government to temporarily suspend the fiscal rule in the face of extraordinary circumstances that threaten the country’s economy. If approved by the CONFIS (Colombia’s highest fiscal authority), the government can temporarily suspend the debt and deficit limits for up to three years. The only prior instance of suspension was during the COVID-19 pandemic to finance the emergency social and health spending under President Duque, thus increasing the deficit. In response, the government then revised the fiscal rule through [Law 2155 of 2021](#) to introduce a fiscal anchor based on the debt-to-GDP ratio to further strengthen the country’s fiscal sustainability. The rule also instituted various mechanisms for public debt control and transparency, including the annual updates through the MTFF. The MTFF is a key document for multilateral institutions, [credit rating agencies](#), and the markets as they examine the country’s fiscal sustainability and adherence to the fiscal rule.

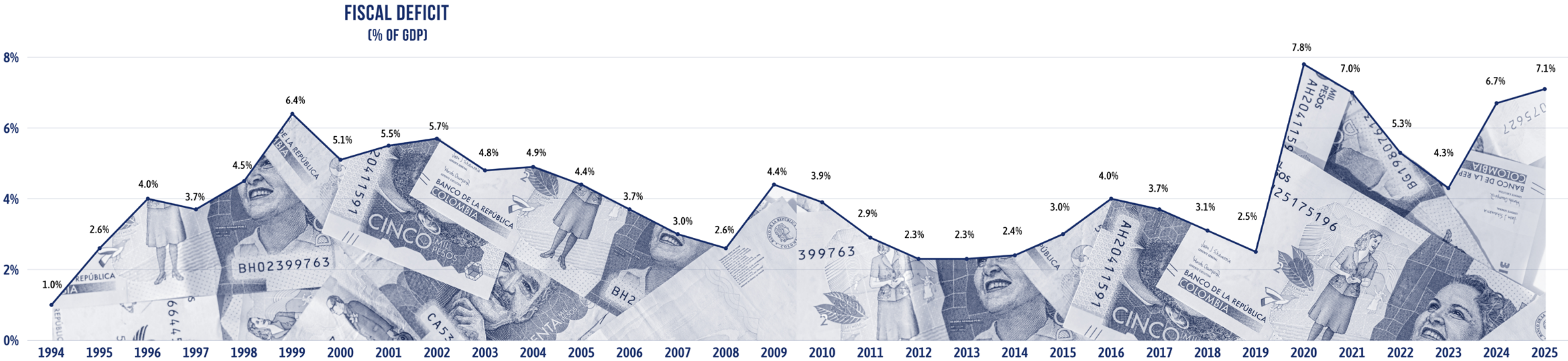
Colombia’s [Comité Autónomo de la Regla Fiscal \(CARF\)](#) is the country’s independent fiscal council, created by [Article 61 of the 2021 Social Investment Law](#) (which amended Law 1473 of 2011) as a technical, permanent, and independent body, which is formally attached to the Ministry of Finance but institutionally separate. Its purpose is to monitor compliance with the fiscal rule, assess the sustainability of public finances, and issue non-binding opinions on key documents, such as the MTFF. The CARF essentially acts as a consulting body to the country’s fiscal policies and provides investor confidence, given its technical and independent reviews. The institution recently asserted its independence when it criticized the government for activating the escape clause in June 2025 for up to three years, as further detailed in the subsequent section.



WHERE WE ARE TODAY: RISING FISCAL CHALLENGES

In 2024 and 2025, Colombia’s fiscal landscape deteriorated sharply, as the central government’s deficit increased by 2.4% from 4.3% of GDP in 2023 to 6.7% in 2024. Moreover, the 2024 deficit was 1.1% above the policymakers’ deficit target of 5.6% according to last year’s MTFF, reflecting both lower-than-expected tax revenues and higher-than-projected primary expenditures, despite spending adjustments in late 2024.

MEDIUM TERM FISCAL FRAMEWORK



Source: MHCP



For 2025, the government revised its fiscal deficit projection upward to 7.1% of GDP in [June’s MTFF](#). In response, the Ministry of Finance opted to [suspend the fiscal rule](#) by invoking the escape clause to accommodate elevated spending and lower-than-expected revenues. In its decision, the central government cited inflexible spending commitments as the main issue, in addition to insufficient tax collection and low economic growth. While the fiscal plan initially [targeted a 5.1% deficit](#) for this year, fiscal authorities claimed that achieving this goal was not feasible without significant corrective measures, like the proposed tax reform. However, it is unlikely that the reform will pass as is, given the little political will to assist the Petro government and the unpopularity of a tax reform ahead of Congressional elections.



Despite the activation of the escape clause, the government is required to detail the country’s fiscal projections over the next 10 years and to explain how it plans to return to the fiscal rule, [as outlined below](#):

Year	Key Measures and Actions
2025	• Tax Reform to initiate fiscal adjustment, which focuses on reducing inefficient indirect taxes and structural change. • Austere 2026 National Budget, safeguarding priority investments. • Establish a Fiscal Pact to frame structural public spending reforms. • Detailed expenditure monitoring to enhance efficiency. • Debt Strategy Revision to reduce financing costs through diversification, like Swiss franc-denominated bond issuance
2026	• Gradual reduction of fiscal deviation as tax reform takes effect. • Proposal of a comprehensive Public Expenditure Reform to address structural spending inefficiencies.
2027	• Significant improvement in public finances as fiscal reforms are fully implemented. • Restoration of the fiscal sustainability principle, aiming for full compliance with the Fiscal Rule.

In response to the government’s decision, the CARF issued [Press Release 17](#) on the same day the MTFF was published (June 13), in which it gave an unfavorable prior opinion on the activation as it did not deem it favorable to the health of the country’s public finances. The committee further argued that the legal framework does not contemplate using the clause for the circumstances invoked, which primarily cited government spending rigidity, and that the proposed budget adjustment was insufficient to shore up confidence or stabilize debt at a prudent level. Instead, it explicitly recommended pursuing alternative options, such as spending control and a stronger fiscal consolidation path to reduce the country’s debt and deficit levels. This stance, which directly goes against the central government’s decision, is a concrete demonstration of the CARF’s institutional autonomy.

• **MARKET REACTION**

On June 26, 2025, both [Moody’s](#) and [S&P Global Ratings](#) (S&P) lowered their credit ratings for long-term foreign currency Colombian debt to Baa3 and BB, respectively, on the back of the government’s decision to suspend the fiscal rule. A credit rating is an estimate of the country’s risk level. These downgrades push Colombia even further away from its prior investment grade status. In its report, [Moody’s cited](#) the country’s fiscal deterioration and the unnecessary use of the escape clause, given the absence of a major threat to the macroeconomic environment, as the primary reasons for the downgrade. The rating agency was aligned with the experts interviewed for this report that the government has once again overestimated its potential for revenue collection and is unwilling to make any significant efforts at cutting expenditures to help balance the budget. However, Moody’s has maintained its stable outlook, given the country’s strong system of checks and balances and its institutionality.

Meanwhile, S&P cited the likely further fiscal deterioration, which it believes could persist for several years, as a delicate situation exacerbated by the [increasing security challenges](#) that threaten institutional effectiveness. The credit rating agency also maintained a negative outlook due to concerns over the government’s ability to stabilize the fiscal and debt levels. It stated that it could further downgrade the sovereign debt rating in the next 12-18 months if proactive and effective measures are not implemented, which increases financing costs and the country’s risk profile for investors. It is worth highlighting that it took Colombia 12 years to regain investment grade status after losing it in 1999 due to rising debt levels. [In 2011](#), the government debt was upgraded given fiscal and political reforms and a crackdown on the security situation, which spurred investor confidence.

Credit Rating Agency	Long-Term Foreign Currency Rating	Long-Term Local Currency Rating	Outlook	Date of Most Recent Review
Moody’s	Baa3	Baa2	Stable	June 2025
S&P	BB	BB+	Negative	June 2025
Fitch	BB+	BB+	Negative	March 2025

Following these credit downgrades, foreign investors [sold an unprecedented volume](#) of Colombia’s peso-denominated government bonds (TES) in July 2025. Offshore holders sold approximately COP 13 trillion (USD 3.2 billion) worth of TES, the largest monthly sell-off since 2013, with net outflows of USD 1.56 billion. The bond activity in July marked the first whole month of trading since [S&P](#) cut Colombia’s local debt from investment grade to junk status in late June, which led to the removal of these bonds from certain global indexes that triggered forced sales by funds restricted to investment-grade only assets. In response, the Colombian government intervened in the market to absorb part of the excess supply and buy back some of the debt.

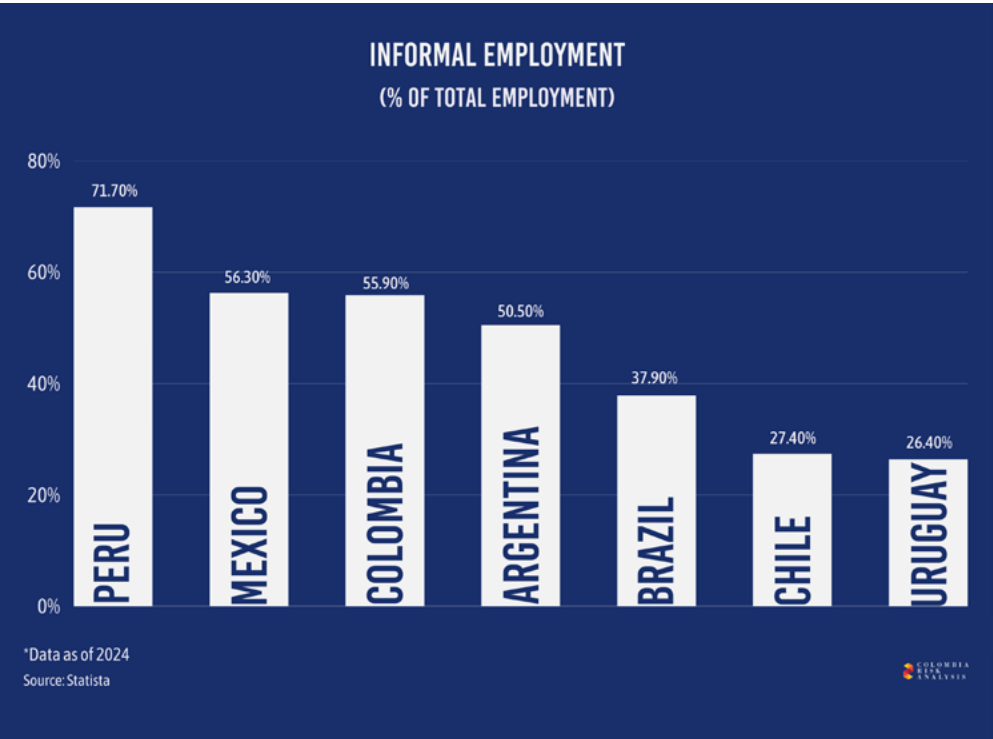
Unlike other countries in the region, Colombian government bonds continued losing value through the [first half of 2025](#), driven by persistent fiscal risks. Specifically, the peso-denominated TES lost the most value in medium-term maturities. This loss was partially because the government issued more bonds in this segment, pushing their yields higher. Longer-term yields stayed elevated due to ongoing uncertainty about the country’s fiscal position, while short-term yields remained high amid expectations that the Central Bank was likely to cut interest rates more slowly than previously thought. Inflation-linked TES (denominated in UVR) fell across all maturities, with yields rising even more than for peso-denominated TES, driven by a larger supply after the government increased its issuance quota this quarter, as well as seasonal factors affecting these instruments.



TAX REVENUE SHORTFALLS

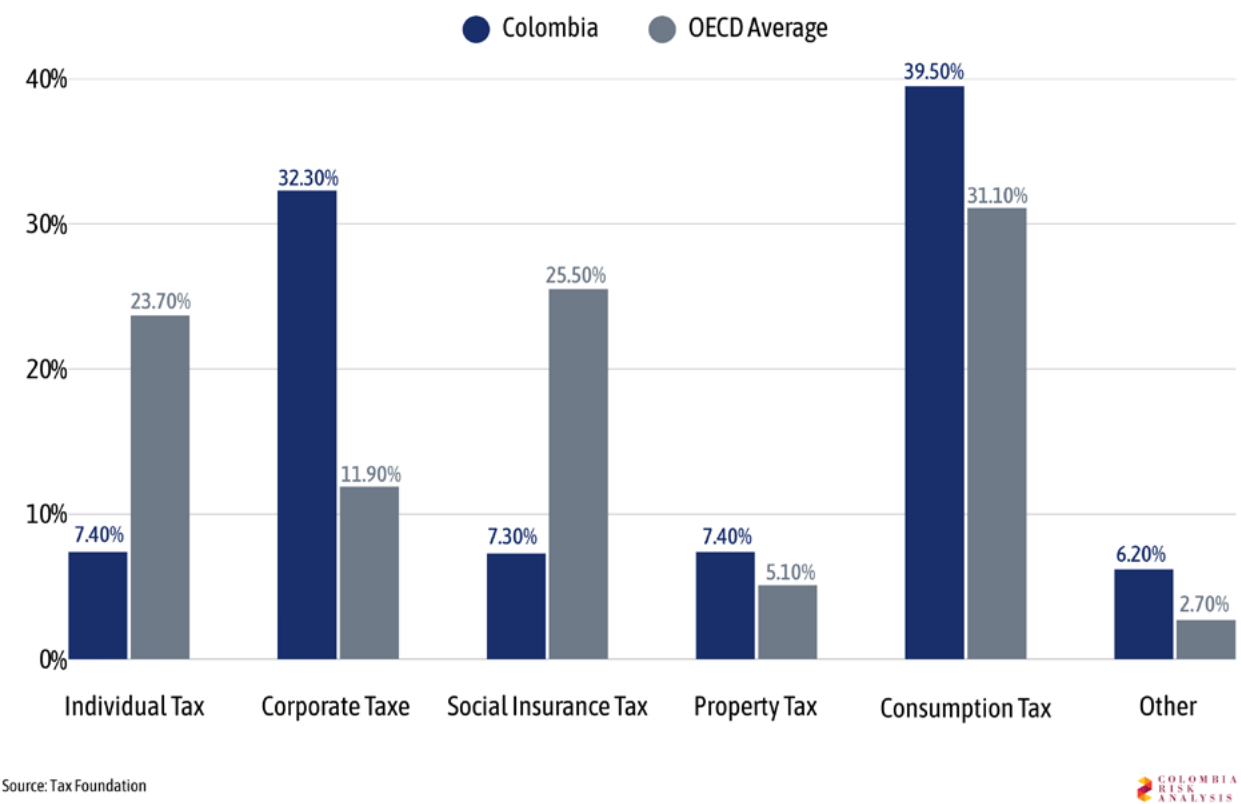
A consistent issue in Colombia’s widening deficit is the shortfall in tax revenue. Despite frequent tax reforms, Colombia collects less revenue relative to regional peers as a percentage of GDP. Hindered by a small tax base due to high informality rates, frequent evasion, and complex regulations, Colombia’s [tax-to-GDP ratio of around 20%](#) is significantly below the Latin American average.

One major driver behind this reality is the country’s prevalent informality rates in the labor market. [In 2023, 56%](#) of Colombia’s labor force operated in the [informal sector](#), which significantly limits the state’s capacity to collect income taxes, payroll taxes, or social security contributions from a majority of its citizens. Up to 1.4% of GDP annual revenue is foregone due to this structural issue. Notably, only around [10% of Colombians](#) file a personal income tax declaration, further highlighting the limited scope of direct taxation.



Consequently, the government’s tax strategy has historically relied heavily on corporate taxes and value-added tax (VAT), which are regressive and place disproportionate fiscal pressure on the formal sector and low-income populations. Colombia’s VAT sets a [standard rate of 19%](#) but it [only covers 41%](#) of final consumption, a figure well below the OECD average of 58%, revealing both policy and enforcement gaps. Because lower-income households spend a larger share of their income on consumption, they are more affected by the tax, thus accentuating the country’s [inequality issues](#). Although certain goods and services are exempt, these exemptions often end up benefiting higher-income groups more, while also creating significant gaps in tax collection. This weak performance further limits the government’s ability to raise funds for social programs and infrastructure. Several institutions have suggested [reducing exemptions](#) on certain products, eliminating VAT-free days, and replacing the current VAT refund mechanism with a VAT exemption for the [poorest 20% of households](#) to improve both fairness and revenue collection.

TAX STRUCTURES

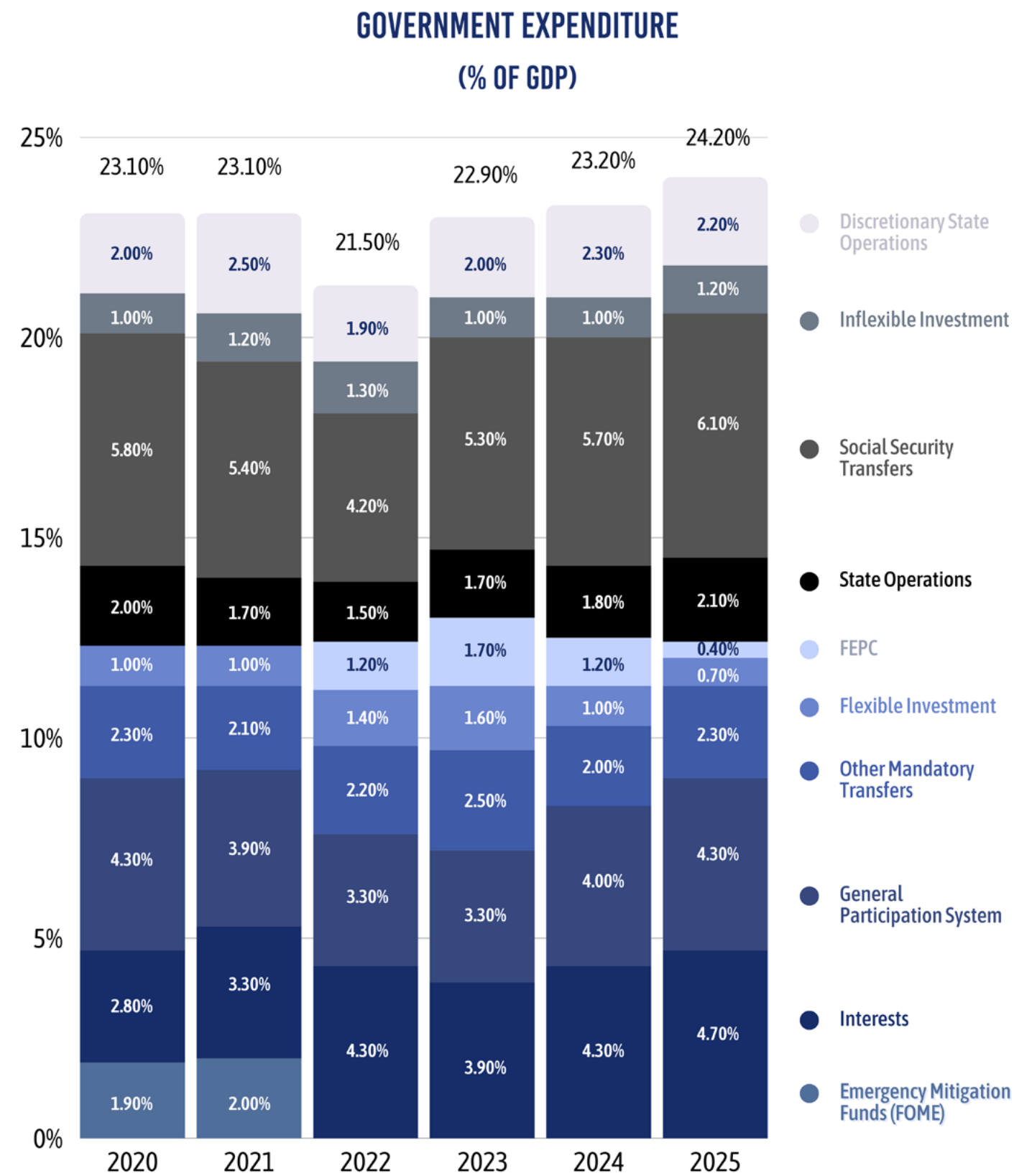


According to the “[International Tax Competitiveness Index 2024 Report](#),” Colombia has the least competitive tax system in the OECD. It is one of only four countries in the OECD to levy a net wealth tax and a financial transaction tax. In addition, Colombia has the highest corporate income tax rate, significantly above the OECD average, as visible in the graph above, which highly disincentivizes corporate investment in the country. It is one of the only OECD countries that applies a worldwide corporate tax system instead of a territorial system.

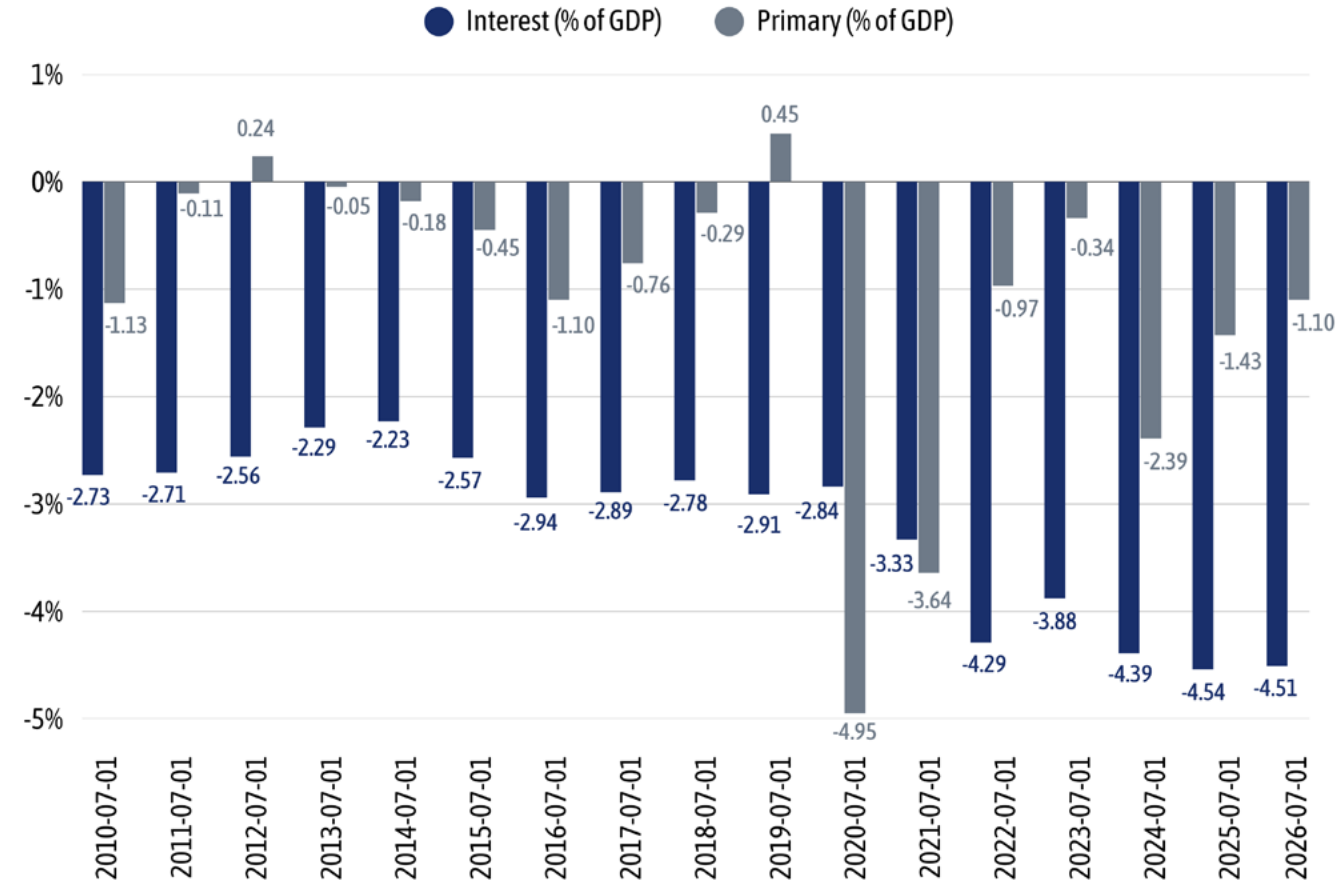
Further, the country’s current tax system and enforcement flaws easily allow for tax evasion and loopholes. Each year, Colombia loses around 8% of its GDP to tax evasion. [According to an Oxfam report](#), a person in the top 1% in Colombia paid an average of 17 cents on the dollar in taxes through 2021. Meanwhile, a person in the poorest 50% paid 21.1 cents in taxes on every dollar of income. As stated by [Luis Carlos Reyes, former DIAN director](#), if tax evasion reached lower levels like that of other OECD countries, which is around 2% of GDP, the additional six percentage points of potential collection could be allocated to create or strengthen social programs that benefit the poorest sector of the population. He estimates that the current levels of tax evasion, which have increased significantly under the Petro administration, are equivalent to around six tax reforms.

[Petro’s proposals](#) to further increase taxes on the wealthy will result in additional capital flight as nationals and corporations change their tax origination country, thus worsening the already-low tax revenue. According to [La Silla Vacía](#), after the 2022 tax reform, Colombia’s ultra-wealthy (those who earned over COP 100 million monthly) paid less in income taxes, due to accounting maneuvers and legal loopholes embedded in the tax code that allowed them to reduce their taxable income base, whilst thousands of others left the country, further reducing the tax base. Ultimately, without comprehensive reforms addressing informality and structural weaknesses in the tax system, Colombia will likely continue to struggle to expand its tax base and generate the revenue necessary to reduce its deficit.





Source: MHCP



Source: OECD



On the government expenditure side, Colombia’s recent fiscal deterioration is closely tied to rising and unusually high share of inflexible (non-discretionary) spending. The [2025 MTF](#) states that 86% of the total expenditure in 2025 is inflexible in nature, limiting the government’s ability to adjust without cutting investment. According to the report, 78% of this component is due to interest payments on existing debt obligations, transfers from the [General Participation System \(SGP\)](#), and healthcare and pension transfers.

A major source of rigidity in Colombia’s public expenditure stems from earmarked transfers and indexed expenditures, which severely limit the government’s ability to adjust spending in the short term. Earmarked transfers are resources that, by law or the Constitution, must be directed to specific purposes or entities and cannot be reallocated. The largest example is the SGP, through which a fixed percentage of central government current revenues is automatically transferred to subnational governments to fund education, health, and other social services. These transfers grow according to legal formulas tied to revenues or inflation, meaning the central government has little discretion to reduce them, even during fiscal stress.

Meanwhile, indexed expenditures are those whose amounts are automatically adjusted based on inflation or other reference variables, such as the minimum wage. These expenditures include pensions and health transfers, public sector wages, and a portion of legally mandated subsidies. Because these items rise mechanically each year, often at a rate that outpaces revenue growth, they place increasing pressure on the budget and force any fiscal adjustment to fall disproportionately on the small share of discretionary spending, typically capital investment. Together, earmarked transfers and indexed expenditures account for the bulk of the “inflexible” component of Colombia’s budget, making structural fiscal consolidation more difficult. These factors drive spending upward even when growth slows or revenues disappoint.



As identified by an economic expert interviewed, a significant rigid expenditure that this administration inherited is the [Fondo de Estabilización de Precios de los Combustibles \(FEPC\)](#), a fuel price-stabilization fund created during the Iván Duque administration to smooth domestic fuel price fluctuations. The FEPC [accumulates deficits](#) while domestic fuel prices are kept artificially low relative to international prices, requiring significant budget transfers to cover the gap. This mechanism has generated large contingent liabilities that must eventually be recognized in the national budget, a significant cost inherited by the Petro administration. In 2025, FEPC obligations continue to pressure the fiscal accounts, as payments to clear arrears reduce space for discretionary spending and compound the overall rigidity of expenditure. To partially reduce the subsidy and lower the deficit, the government first increased the [price of gasoline](#) in 2023 and then the [price of diesel \(ACPM\)](#) in 2024, particularly for enterprises that consume more than 20,000 gallons per month. Both of these decisions caused widespread protests across the country, led primarily by truckers.

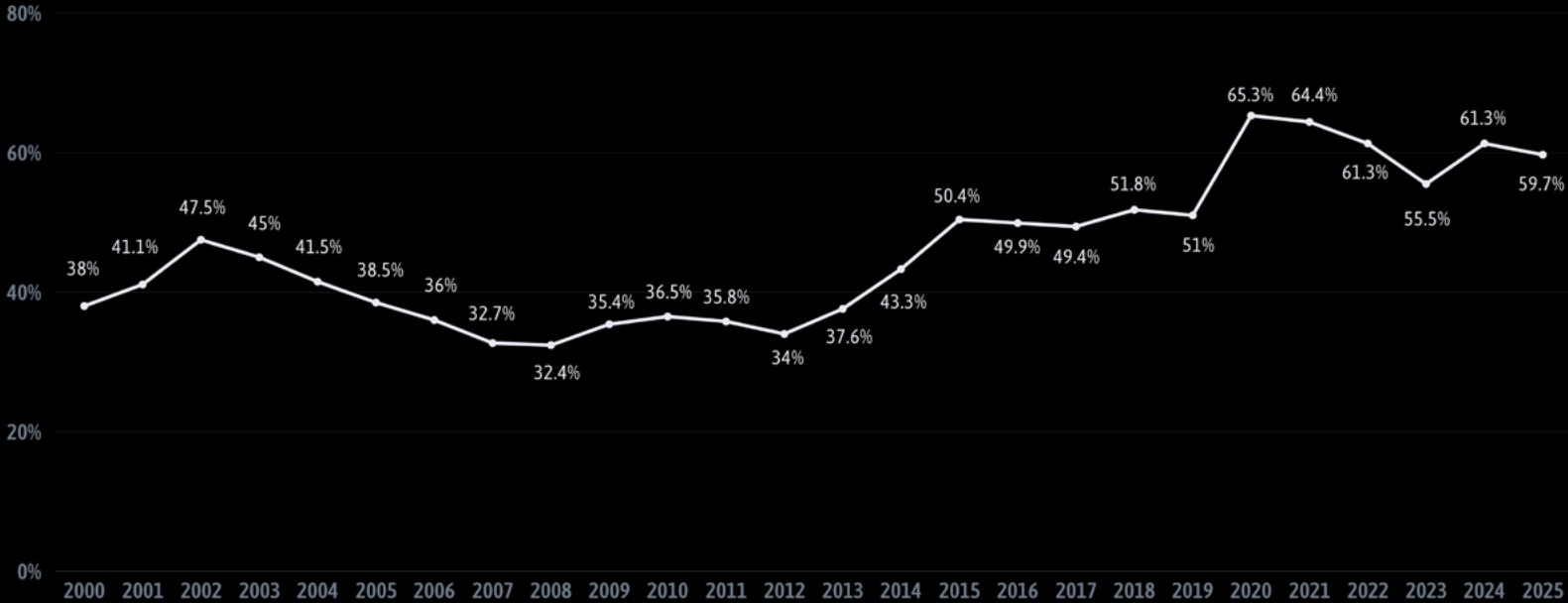
This high degree of inflexibility poses material macro-financial risks. First, it erodes fiscal-rule credibility and forces recourse to exceptional mechanisms, like the

escape clause, which rating agencies and multilateral lending institutions read as increasing fiscal uncertainty. Following the MTFF’s June 2025 revisions, Fitch warned that the widened deficit targets heighten uncertainty about the consolidation path. **In short, a spending profile dominated by legal and indexed commitments makes Colombia’s public finances less adaptable to shocks, raises risk premia, and can perpetuate a debt path in the low-60% of GDP unless structural rigidities are addressed.**

• **DEBT-TO-GDP**

After hovering in the 40–50%-of-GDP range pre-COVID, general government gross debt rose sharply and has remained elevated. Despite a decrease in post-pandemic highs, Colombia’s debt-to-GDP ratio climbed from 56% in 2023 to over 61% in 2024, reflecting a concerning trend. According to [IMF projections](#), the ratio will remain around 60% of GDP in 2024–2025 before stabilizing only under credible fiscal consolidation, a path complicated by wider deficits in 2024–2025. These rising debt levels are eroding investor confidence, as reflected in the credit rating downgrades by S&P and Moody’s.

GROSS GOVERNMENT DEBT
(% OF GDP)



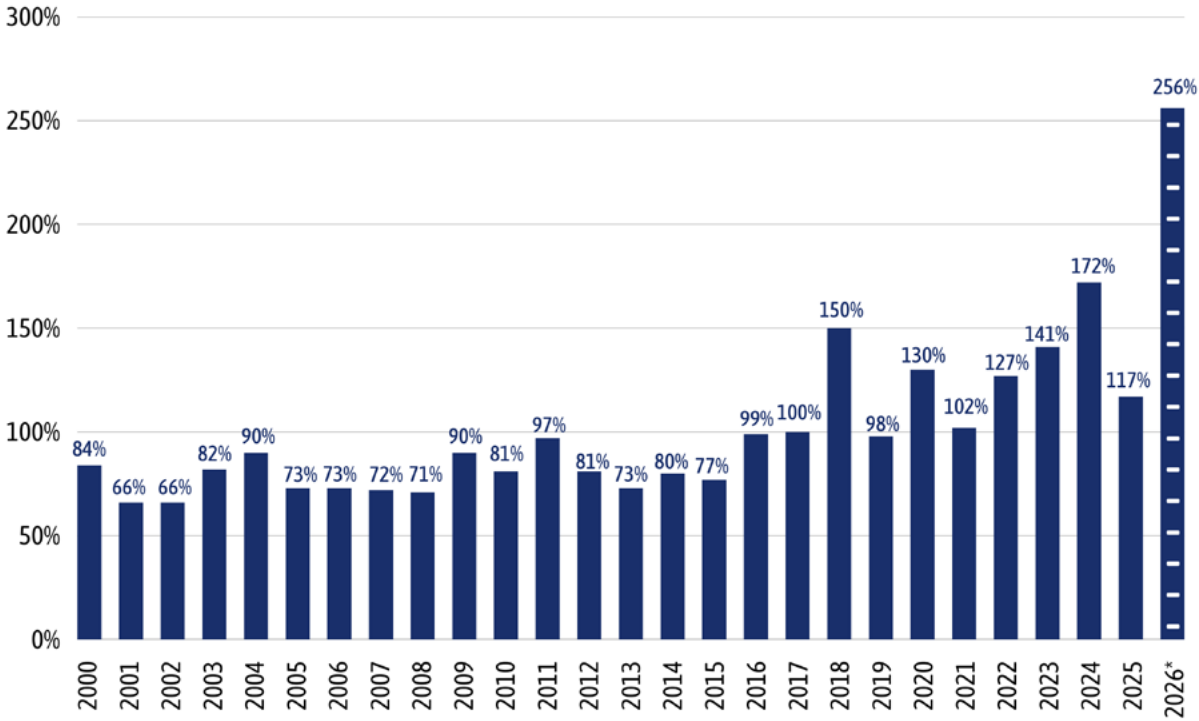
Source: IMF



• **DEBT SERVICING COST**

As an additional strain to the fiscal outlook, the ratio of interest payments to debt amortizations for 2026 is expected to reach a record 256%. This massive increase reflects both the rising cost of servicing debt and an unusually low level of amortization scheduled for that year. This imbalance is largely the result of previous decisions to reschedule debt payments, effectively postponing obligations originally due in 2026 to future years.

DEBT INTERESTS / AMORTIZATIONS (%)



*Estimates by DAVIVIENDA, based on the current budget allocations of the National General Budget (PGN) and the 2026 PGN proposal.

Source: MHCP



Based on recent estimates, [roughly COP 22 trillion](#) (USD 5.4 billion) in debt repayments have been deferred. While this provides short-term liquidity, it simply postpones the problem with higher debt burdens down the line, after the Petro administration’s term has ended. While this maneuver creates immediate fiscal space, it puts more pressure on future budgets and undermines long-term debt sustainability.

This situation underscores the original purpose of Colombia’s fiscal rule framework: to limit excessive spending in any given administration and avoid passing on disproportionate fiscal challenges to future governments. **The current strategy risks violating that principle by expanding the deficit today while accumulating obligations that will constrain future policy flexibility.**



NATIONAL BUDGET PROPOSAL FOR 2026

In late July 2025, the Ministry of Finance submitted a draft decree for the 2026 budget, which revealed that the government requires [COP 556.9 trillion](#) next year, representing 28.9% of the country’s GDP. The new budget proposal increased nearly 9% from the 2025 budget, double the expected inflation rate. Of that total, approximately 65% is earmarked for operational expenses, primarily salaries and administrative costs, representing an 11.1% increase compared to the prior year. Meanwhile, public investment spending will only rise by a modest 5.7%, signaling a reduced focus on long-term infrastructure and economic growth. According to former Finance Minister José Manuel Restrepo, social and productive investment has [suffered](#) an “alarming decline” compared to 2022, while bureaucratic expenses have increased by 40%. Further, contract-based personnel spending is set to rise by COP 4.8 trillion, as shown in the table below, without any corresponding reductions elsewhere in government expenditures. Overall, a [wide range of experts](#) immediately sounded alarm bells upon the budget’s release as they rejected the overwhelming increase in both the general budget and functional costs, especially given the country’s current fiscal deficit challenges.

A particularly controversial element of the proposal is that [COP 26.3 trillion](#) (USD 6.5 billion), or 5% of the total budget, in spending is currently unfunded, representing a red flag for analysts and credit rating agencies. Therefore, in September 2025, the Petro administration introduced its final tax reform to Congress, seeking to raise the remaining [COP 26.3 trillion](#) necessary to finance the 2026 budget and strengthen fiscal sustainability in the medium term. This reform, which is the [largest tax overhaul](#) in Colombian history, emphasizes progressivity, placing a heavier tax burden on high-income individuals, financial institutions, and select sectors.

[Key measures](#) include higher corporate tax rates for banks and insurers (up to 50%) and new surcharges on streaming platforms and online gambling. Also, the proposed tax hikes on petroleum derivatives and fuel consumption risk fueling additional inflationary pressure on the economy, which is counter to the Central Bank’s ongoing attempts to rein in prices while navigating other policy initiatives under the Petro administration. Notably, for the first time, the reform proposes taxing income generated by churches, a measure that is likely to add to the political friction surrounding the proposal. Ultimately, the reform reinforces the idea that the Petro administration has no desire to cut down on costs; instead, it has chosen to rely on increasing tax revenues solely.

Given its scope, the reform faces significant political and economic headwinds. With President Petro in his final year in office, congressional support for such a wide-ranging initiative remains low and uncertain, particularly given strained relations between the executive and legislative branches. Since congressional elections are also held next year, there will be reduced political will to approve such an expansive tax reform, which is unpopular for constituents, especially as it targets groups with significant political power. Congress is likely to pass a watered-down version of the reform or not pass it at all. However, markets are closely watching whether the government can credibly deliver fiscal consolidation, and failure to reach a consensus will likely raise the sovereign’s risk premium.

[According to Luis Fernando Mejía](#), director of the think tank Fedesarrollo, the budget exceeds a sustainable fiscal trajectory by about COP 20 trillion, especially when factoring in relatively low inflation and sluggish revenue growth. Mejía believes that a responsible budget should not exceed COP 531 trillion. The [CARF has also criticized](#) the budget for increasing the primary deficit from 1.4% to 2.0% of GDP, roughly COP 38.6 trillion, undermining Colombia’s compliance with its medium-term fiscal rule. Just a month ago, during the MTFF presentation, that shortfall had been [projected at COP 33 trillion](#), highlighting a worsening outlook and lack of control in fiscal management in a very short amount of time.

The COP 556.9 trillion national budget proposed in a pre-election year, combined with the suspension of the fiscal rule, suggests that reducing the fiscal deficit is not a government priority. **Ultimately, this budget proposal further erodes this administration’s credibility and commitment to fiscal sustainability.**

NATIONAL GENERAL BUDGET 2025-2026
*TRILLIONS OF PESOS

CATEGORY	2025* (COP) (1)	2026 PROJECTED (COP) (2)	PERCENTAGE DIFFERENCE (%) (2-1)	2025	2026
OPERATING EXPENSES	\$329,275	\$365,765	11.1%	18.1%	19.0%
PERSONNEL EXPENSES	\$61,890	\$66,788	7.9%	3.4%	3.5%
ACQUISITION OF GOODS AND SERVICES	\$17,540	\$18,888	7.7%	1.0%	1.0%
TRANSFERS	\$245,360	\$275,558	12.3%	13.5%	14.3%
COMMERCIALIZATION AND PRODUCTION EXPENSES	\$2,089	\$2,106	0.8%	0.1%	0.1%
ACQUISITION OF FINANCIAL ASSETS	\$758	\$760	0.2%	0.0%	0.0%
REDUCTION OF LIABILITIES	\$360	\$338	-6.1%	0.0%	0.0%
EXPENSES FOR TAXES, FINES, PENALTIES, AND LATE PAYMENT INTEREST	\$1,278	\$1,328	3.9%	0.1%	0.1%
DEBT SERVICE	\$112,605	\$102,450	-9.0%	6.2%	5.3%
PRINCIPAL	\$50,766	\$27,616	-45.6%	2.8%	1.4%
FRAMEWORK REMUNERATION AGREEMENTS	\$762	\$534	-29.90%	0.0%	0.0%
OTHER PRINCIPAL DEBT EXPENSES	\$50,004	\$27,082	-45.8%	2.8%	1.4%
INTEREST	\$59,435	\$70,765	19.1%	3.3%	3.7%
COMMISSIONS AND OTHER EXPENSES	\$497	\$1,404	182.4%	0.0%	0.1%
CONTINGENCY FUND	\$1,907	\$2,665	39.8%	0.1%	0.1%
INVESTMENT	\$83,966	\$88,760	5.7%	4.6%	4.6%
TOTAL	\$525,846	\$556,975	5.9%	29.0%	28.9%
TOTAL WITHOUT DEBT	\$413,241	\$454,525	10.0%	22.8%	23.6%

* Appropriation in force as of June 30, with year-end estimates, includes COP 12 trillion deferred through Decree 0069, as amended by Decrees 0494, 0571, and 0722 of 2025, and resources incorporated under the declaration of the State of Internal Disturbance.

** Includes COP 26.3 trillion in contingent financing.

Source: Dirección General del Presupuesto Público Nacional - Subdirección de Análisis y Consolidación Presupuestal



POTENTIAL RISKS

This section will identify the most consequential political and economic risks that will likely impact Colombia’s fiscal landscape in the short to medium term, according to our research and interviews with experts.

UPCOMING ELECTIONS

The most determinant event in the near future is the upcoming elections, both for the presidency and Congress. The [top three issues](#) that will be top of mind for voters during elections will be: healthcare, security, and corruption. The timeline below highlights the major milestones over the next year that will determine which parties will be at the forefront of policymaking decisions.

The three key dates to keep an eye on are:

- **October 31, 2025: First Results of Public Polls**

As recently approved by Congress, [Article 5](#) of the new law states that the results of election voting polls can only be published starting 3 months before the first day of candidate registration, which in this case is October 31. Therefore, this date will be vital as it will be the first indication of where the election is heading.

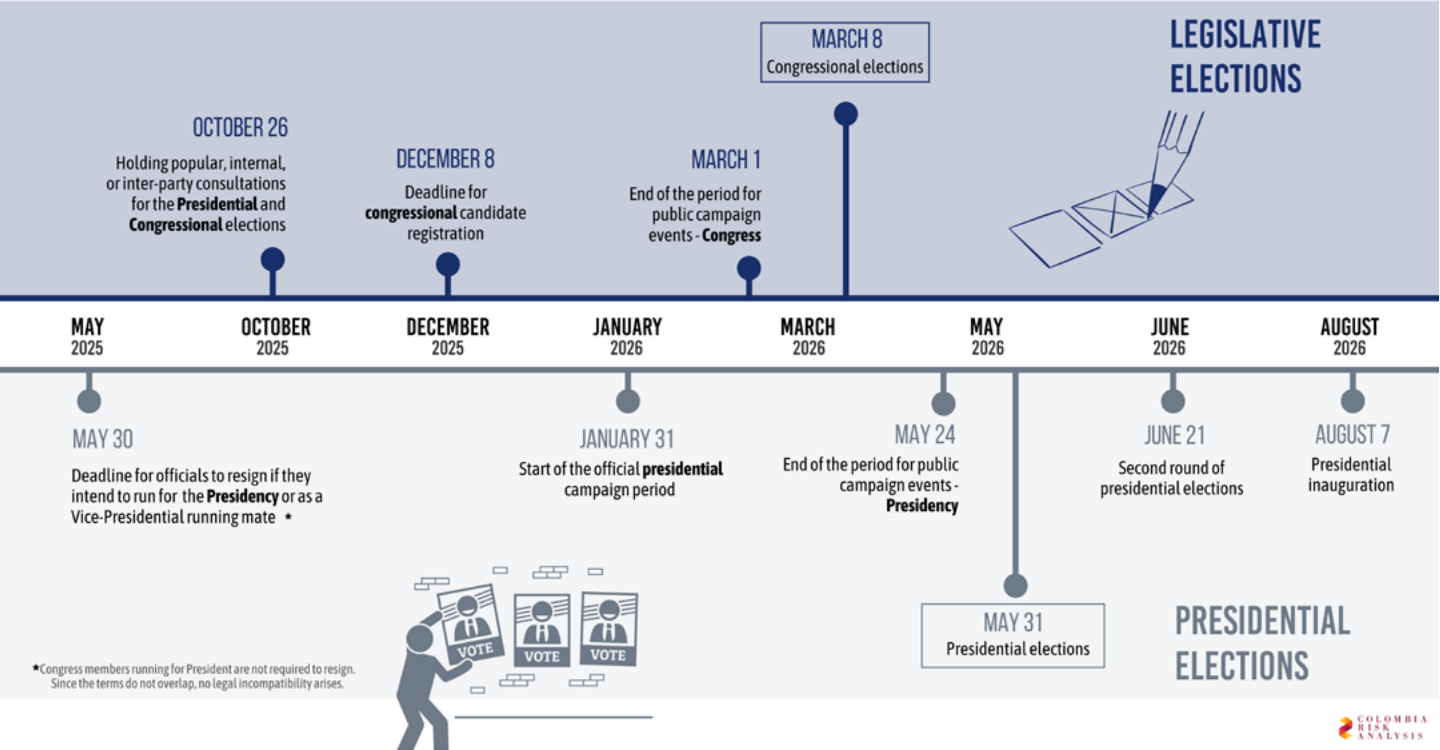
- **March 8, 2026: Start of Campaign Process for Congress**

Given recent developments regarding senator and candidate Miguel Uribe’s death, there is increased concern for the presidential and congressional candidates’ safety. Given the higher presence of armed groups in rural areas, it is probable that some candidates, mostly in rural areas, will form partnerships with these groups to receive their support, further institutionalizing their prominence, a situation akin to that in Mexico. If this materializes, this is likely to make legal governability more difficult, given the increased “legal” power held by the illicit groups.

- **May 31, 2026: Presidential Elections**

While it is still too early to predict the winner, there are a few major players that we believe we should keep an eye on. As detailed in our most recent report, [Fragmentation and Polarization One Year Ahead of the Next Presidency](#), published in August 2025, we provide a strategic analysis of the candidates, potential alignments, and narratives that will influence the upcoming electoral cycle, in addition to their potential impact on governance, institutional stability, and the investment environment. We also previously detailed what the left, center, and right parties must do to win in our Colombia Risk Monthly reports.

ELECTORAL CALENDAR



EXTERNAL FUNDING SOURCES

One major risk for Colombia at the moment is finding funding sources that do not solely rely on the U.S. or ones in which it carries less influence, as bilateral relations have become more [uncertain](#) in recent months. Specifically, with the decertification decision likely materializing in September 2025 and the International Monetary Fund (IMF) Flexible Credit Line being removed, Colombia has to consider alternatives to fill its funding gaps.

- **DECERTIFICATION BY THE UNITED STATES**

As outlined in the Foreign Assistance Act, the U.S. president conducts an annual assessment to determine whether a relevant country has taken active steps to cooperate with American counter-narcotic efforts. As we highlighted in our [The Future of U.S.- Colombia Partnership](#) report from September 2024, the threat of decertification by September 2025 is highly likely under the second Trump administration, especially given the historically high [increase in cocaine production](#). According to a crisis analyst whom we interviewed, the threat will definitely materialize this year. If Colombia is in fact [decertified](#), all U.S. assistance (except for certain humanitarian and counternarcotics assistance) to Colombia will likely be suspended unless President Trump waives these effects. Furthermore, the U.S. will have the obligation to vote against all loans and financial assistance to Colombia provided by multilateral development banks, like the International Monetary Fund and the Inter-American Development Bank. This scenario is likely to lead to fewer funding options for Colombia, in addition to potentially triggering another credit rating downgrade.

- **INTERNATIONAL MONETARY FUND'S FLEXIBLE CREDIT LINE**

The loss of access to international loans due to decertification is further exacerbated by the [International Monetary Fund's](#) decision to suspend the USD 8.1-billion Flexible Credit Line (FCL) in April 2025, given the country's fiscal challenges. The FCL is a key emergency financial instrument that signals confidence in the country's macroeconomic policy, which Colombia has held since 2009 to address fiscal or exchange rate crises. Market analysts warn that its loss erodes investor confidence, weakens Colombia's external insurance buffer, and will continue to raise sovereign borrowing costs amid rising fiscal deficits. The result of this loss was evidenced in a rise in borrowing costs for Colombia's local currency COP 1.5 trillion bond auction on May 28, in which it offered coupon rates substantially above similar regional peer issuances.

Prominent voices such as former [Finance Minister Mauricio Cárdenas](#), who is also a presidential candidate, warned that this move represents a gravely concerning message for financial markets as it leaves Colombia without its "spare tire" just as global uncertainty rises. Ultimately, the loss strips Colombia of a premium credibility tool used to reinforce market perceptions of fiscal strength and macroeconomic resilience. Restoring access, coupled with the accompanying confidence boost, will depend critically on delivering a credible fiscal consolidation plan and completing the [outstanding IMF reviews](#), likely targeted for the September–October 2025 mid-term check-in.

- **OTHER MULTILATERAL BANKS**

To reduce Colombia's reliance on the U.S. and U.S.-led multilateral institutions, Colombia has recently focused on exploring other avenues for financing. During President Petro's visit to China in May 2025, he formally submitted the country's [application](#) to join the New Development Bank (NDB), the BRICS' multilateral development institution. The [New Development Bank](#) was established in 2015 to offer alternative financing for sustainable development projects in emerging market economies. Compared to traditional Western financial institutions, it provides flexibility and lighter conditionalities, which were likely attractive to President Petro. This development seems like the natural next step to Colombia's decision to join the Belt and Road Initiative (BRI), with the NDB positioned to provide project-specific loans aimed at advancing the country's infrastructure agenda. Colombia has pledged to purchase 5,125 shares in the bank, amounting to an initial investment of USD 512 million. This move will likely unlock new funding options for large-scale initiatives.

When asked about Colombia's entry into the NDB, all experts interviewed were in favor of Colombia seeking alternative financing options. However, some expressed concerns about potentially straining the bilateral relationship with the U.S., yet believed this was a necessary step to take, especially given the current circumstances. However, a key distinction between NDB's financing options versus other institutions is that the former involve only project-based financing, rather than sovereign loans. Therefore, a gap will likely remain as institutions like the IMF and IDB reduce their financing to Colombia.

Another key financial institution is the Asian Infrastructure Investment Bank (AIIB). In March 2025, the Petro administration formally [submitted Colombia's application](#) to join the AIIB, which is now under internal review, and a membership vote is expected to conclude by September. Membership in the AIIB broadens Colombia's access to funding for environmentally sustainable and regionally integrated infrastructure projects, while also strengthening its ties to China-linked multilateral institutions. However, this step is likely to further strain Colombia's already delicate diplomatic relationship with Washington, fueling concerns about a strategic shift away from its traditional alliance with the U.S.

- **ALTERNATIVE DEBT FINANCING OPTIONS**

Colombia's new Director of Public Credit, Javier Cuellar, announced a [new strategy in July](#) to issue up to USD [10 billion bonds denominated in Swiss francs \(CHF\)](#), marking its first foray into this currency market. The primary purpose is to repurchase higher-cost COP and USD liabilities, as some are trading at deep discounts. In turn, the government aims to reduce near-term debt service costs by leveraging Switzerland's very low interest rate environment, thereby slightly trimming Colombia's annual interest burden as a share of GDP.

The strategy aims to not only diversify Colombia's external financing but also to build a broader currency curve, potentially including future issuance in euros. By replacing expensive fixed-rate TES and USD issuance with franc-denominated securities, Cuellar seeks to manage short-term rollover needs and benefit from [lower borrowing rates](#) amongst other major debt issuers.

However, this strategy carries significant risks. Since the Swiss franc tends to appreciate during episodes of global macroeconomic uncertainty as it is a safe-haven currency, any COP depreciation against CHF will sharply increase the peso value of future repayments, especially as investor sentiment deteriorates. Second, the initial CHF issuance features short maturities, exposing Colombia to refinancing risk if borrowing costs increase or credit ratings continue to deteriorate. Out of the experts consulted, the majority recognized the benefits of this alternative financing strategy as it reduced short-term costs but acknowledged the inherent exchange rate risks in issuing in a safe-haven currency.

COMPETENCIES LAW

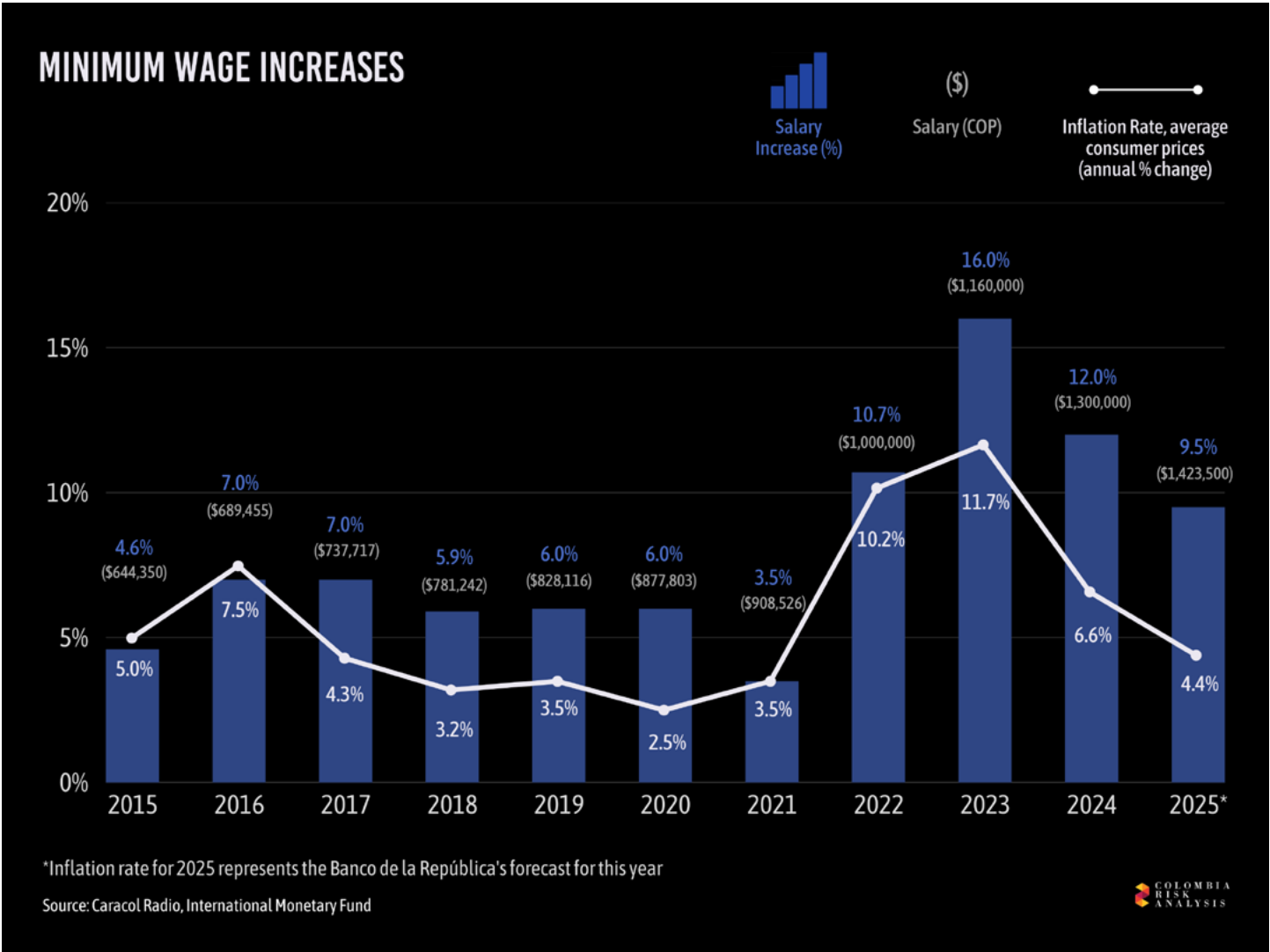
The *Ley de Competencias* (Competencies Law) is a proposed law in Colombia meant to operationalize the constitutional reform that changed the General System of Participations approved in late 2024, which modified [Articles 356 and 357](#) to gradually increase transfers from the national government to departments from about 25% of current revenues today to [39.5% by 2038](#). This law will determine which responsibilities, such as education, health, sanitation, and general-purpose funding, the departments and municipalities will have to assume in exchange for receiving more resources. Although the measure aims to strengthen decentralization and [increase the autonomy of regional governments](#), its implementation will likely place considerable strain on public finances, especially in a context of moderate economic growth, low spending efficiency, and a national budget that is becoming increasingly rigid. Furthermore, while the law defines how much income will be distributed to the departments, it is still uncertain how the debt payments would be distributed, thus placing additional fiscal pressure on the national government.

Fedesarrollo and other experts further caution that even if funds increase, the management efficiency of some departments is quite low. The think tank points to the [education sector](#) as an example, in which it has only achieved 79% of coverage, with quality at 86% with the resources allocated to it. This example implies that better results might be achieved with fewer resources if used more effectively.

Many of the experts interviewed warned of the fiscal risks that this new law is likely to pose if not executed correctly. Independent analysis from Fedesarrollo has been particularly cautionary. The think tank warns that without technical rigor and fiscal neutrality, the increase in transfers will likely lead to a fiscal deficit of around [5.2 % of GDP by 2038](#) and simultaneously push government debt to 66.9 % of GDP, approaching the 71 % ceiling established by the fiscal rule. These figures represent a heavy burden for a country with already fragile public finances. Ultimately, the high likelihood that the reform will be poorly structured and executed is poised to weaken central fiscal stability, drive up debt, and reduce transparency and effectiveness at regional levels.



MINIMUM WAGE INCREASE



The Petro administration has [recently indicated](#) its intention to push for another significant increase to the minimum wage by the end of the year. While framed as a measure to improve workers’ purchasing power and reduce poverty rates, a large wage hike will sharply increase labor costs for businesses, especially small and medium-sized enterprises (SMEs). As of 2024, micro and SMEs represented [99.5% of formal companies](#) in Colombia, which, given their size, will likely not be able to absorb the rise in labor costs.

As several experts have noted, a substantial rise in labor costs will likely lead to higher levels of informality. According to accounting and tax portal [Actualicese](#), although the legal minimum wage in 2025 is COP 1,423,500, the actual cost of hiring a formal worker is nearly [70% higher](#) once social security and benefits have been factored in. In response, companies will likely shift some jobs to the informal sector, where labor regulations are circumvented. Alternatively, companies will be forced to lower costs by reducing headcount. In turn, many of those who lose formal employment are expected to turn to the informal sector, where jobs are easier to access due to lower hiring costs and fewer regulatory constraints.

However, President Petro will likely claim that he was able to both increase the minimum wage and lower the unemployment rate. The unemployment rate only measures employees seeking employment and those working in the formal sector. As formal

hiring slows and more individuals take informal jobs, fewer will appear in official unemployment statistics because the formal labor metrics no longer capture them. Organizations, [like the ANDI](#), have questioned the government’s jobs report as most of the new jobs the government claims to have created are either informal or self-employed. This dynamic has the potential to produce the misleading idea of a falling unemployment rate, which, in reality, obscures a rise in informality, where workers lack legal protections, benefits, and job stability. These are ironically the very conditions President Petro claims to prioritize.

Simultaneously, a minimum wage increase will likely lead to a rise in inflation. During President Petro’s administration, Colombia’s minimum wage has [increased by 48%](#), while consumer prices have risen by 33% over the same period. **These above-inflation increases directly undermine Petro’s public criticism of the Central Bank for maintaining tight monetary policy, as wage-driven inflation likely limits the Bank’s room to lower rates as it combats inflationary pressures. In this sense, the policy further proves counterproductive as it worsens inflation while weakening formal labor market conditions.**

Ultimately, while the administration will likely claim this act as a political win, citing higher wages and lower unemployment, such figures obscure more concerning trends beneath the surface. As a result of this policy, there will likely be an erosion of formal employment, the weakening of labor protections, reduced competitiveness of Colombia’s environment for companies, and elevated inflation in the near term.

OIL EXPLORATION

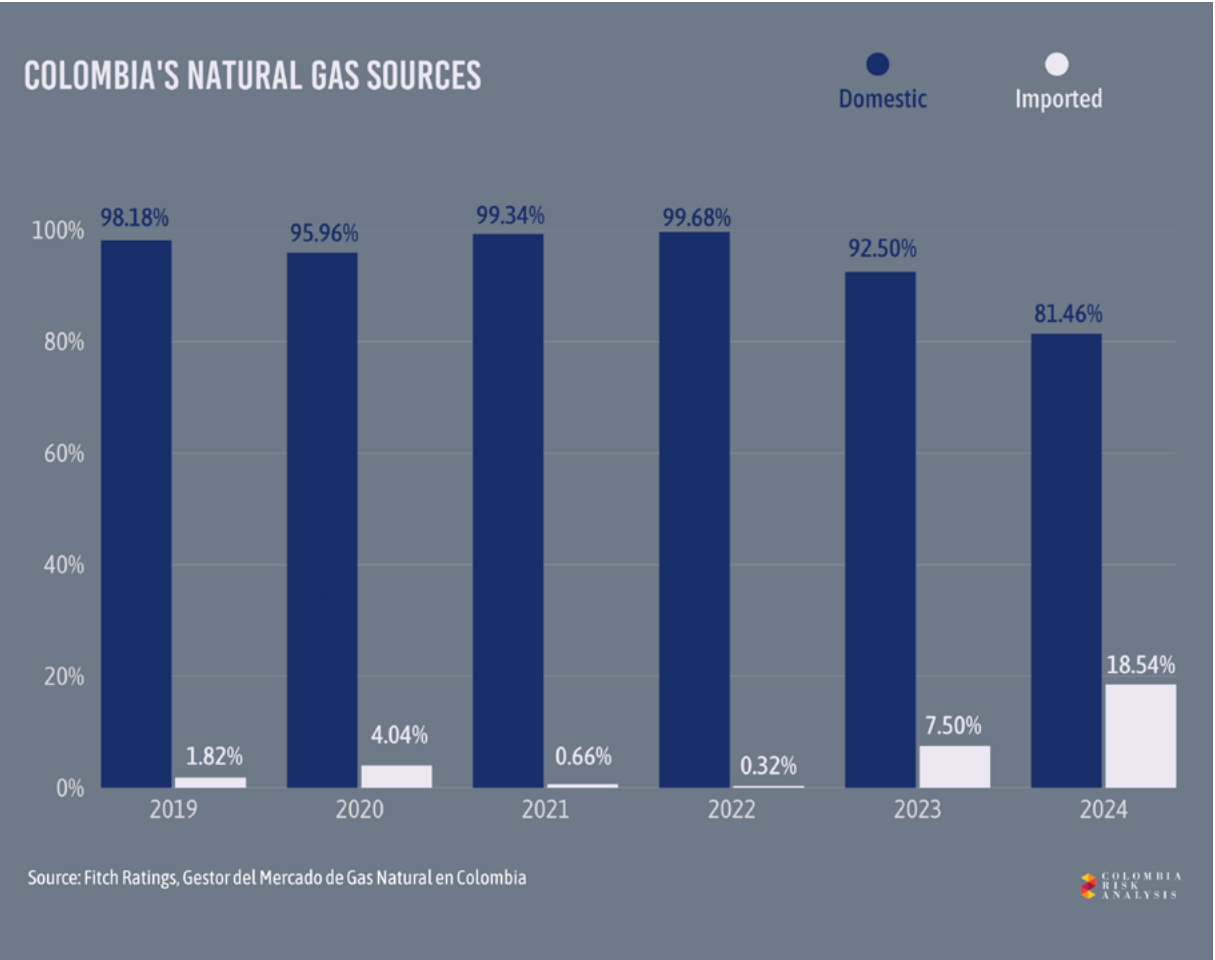
When President Petro assumed [office in 2022](#), he banned fracking and halted the [issuance of new permits for oil and gas exploration](#) as part of a broader effort to transition toward a more environmentally conscious economy. However, these policies have led to a sharp decline in proven oil and gas reserves. Oil reserves are now estimated at [around 7 years of consumption](#), and natural gas reserves at roughly 6 years, creating growing concerns around fiscal stability and energy security.

As [domestic production contracts](#) and demand rises, Colombia has moved toward costly gas imports. Earlier this year, President Petro announced that Colombia will begin to [buy gas from Qatar](#), which will likely lead to higher oil and gas import costs. These import deals are significantly more expensive than local production, raising concerns about fiscal burdens. Therefore, as reserves dwindle and output falls, Colombia will likely be forced to subsidize fuel prices to cushion the social impact or increase external borrowing to meet its energy needs, both of which likely raise the country’s already delicate fiscal burden.

Several experts interviewed for this report expressed concern over the fiscal implications of this shift, particularly given Colombia’s dependence on oil revenues and the inflationary pressures that will likely result from elevated import prices. With declining oil reserves, Colombia is left without its vital oil revenues. In 2023, Colombia exported USD 12.7 billion in crude oil and USD 2.9 billion in refined petroleum, accounting for approximately 30% of total exports ([USD 52.4 billion](#)). This data clearly indicates the sector’s continued significance in the national economy.

As highlighted in our recent [report](#), gas shortages are likely to result in [higher consumer prices](#), especially as current regulations allow companies to pass increased costs on to end-users. This risk is particularly acute for the 12 million Colombians who depend on natural gas, many of whom are socioeconomically vulnerable. As a result, energy access and affordability are likely to become increasingly relevant political issues ahead of elections, particularly in regions already experiencing electricity supply problems, such as the Caribbean coast.





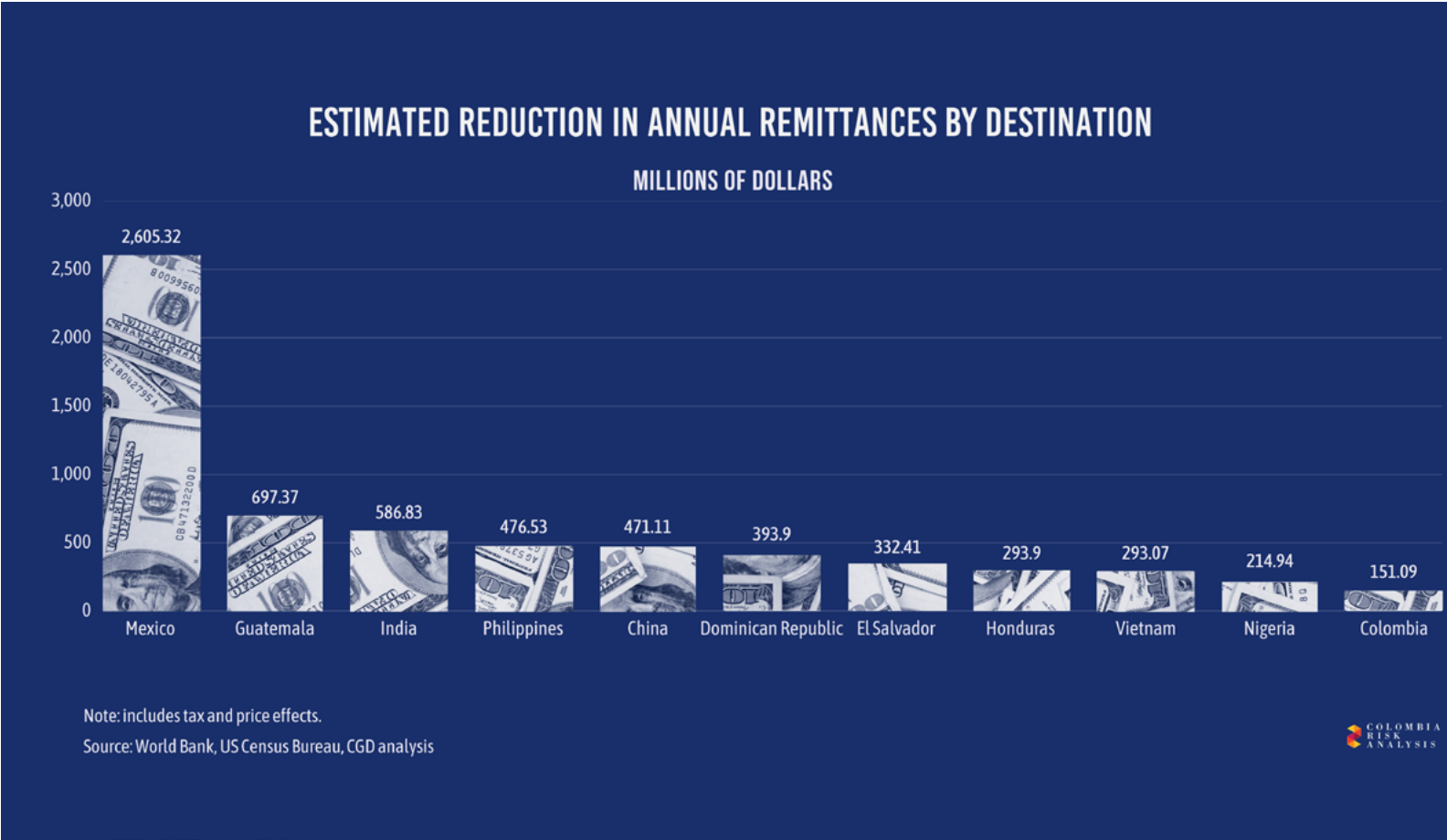
VULNERABILITIES TO EXTERNAL SHOCKS

Colombia remains highly exposed to external shocks given its export structure, which focuses on commodities, and its reliance on external financial inflows. Oil and coal currently make up about [half of total exports](#). Therefore, any sudden fall in oil prices swiftly reduces export revenues, weakens the peso, and strains the government budget.

Given the country's strong ties to the U.S., the peso is sensitive to U.S. trade policy and remittance flows, since the majority of Colombia's exports are [directed to the U.S.](#) In January 2025, announcements by U.S. officials about significant tariffs on Colombian exports (including oil, coffee, and flowers) after a public altercation between President Trump and President Petro triggered immediate volatility, with the peso [depreciating up to 1.8%](#) in a single day. Though tariffs were ultimately averted during a late-night deal, the episode underscored how quickly U.S. policy threats can undermine market confidence in the COP. After the de-escalation, the U.S. announced in April [a 10% tariff](#) on Colombian imports, which came into effect on [August 7](#). However, the tumultuous relationship between President Petro and President Trump increases the uncertainty between the two countries and opens space for future tariff increases if misunderstandings between the two leaders arise.

Of equal concern is a proposed U.S. remittances tax, a 3.5% levy on transfers from non-U.S. residents, that affects Colombia's second-largest source of dollar inflows. This tax is part of President Trump's "[big, beautiful bill](#)," which the House of Representatives passed on July 3, 2025. In 2024, remittances totaled [2.8% of Colombia's GDP](#), supporting 2.1 million families. The Center for Global Development estimated the effects of the proposed tax on formal remittances

for recipient countries, with a USD 151.09 million reduction in Colombia, as shown in the chart below. With lower household income due to lower remittances, there will likely be lower GDP growth, which naturally results in less tax revenue being collected. This chain of events worsens an already weak fiscal landscape in which tax revenues are low and below expectations.



These external risks feed directly into Colombia's fiscal constraints. A depreciated peso inflates the cost of servicing debt, raises inflation (especially through more expensive imports, which will likely push the Central Bank to tighten monetary policy), and erodes purchasing power. With the anticipated decline in oil revenues and remittances, fiscal authorities are likely to be further pushed into politically sensitive options, such as spending cuts or tax hikes amid reduced credibility. With gross debt already [near 62% of GDP](#) and a substantial fiscal deficit, Colombia has limited buffers to absorb such shocks.



FURTHER DOWNGRADES

According to the three major credit rating agencies, Moody’s, S&P, and Fitch, Colombia remains at risk of further credit downgrades if it fails to address its widening fiscal deficits and rising debt burden. [Moody’s](#) has explicitly warned that without credible fiscal consolidation, there will likely be another downgrade. The agency highlighted that stabilizing public debt and restoring compliance with Colombia’s fiscal rule are essential to maintaining the current rating, particularly after the government’s recent decision to activate the escape clause and widen its deficit projections.

[S&P](#) also pointed to persistent large deficits, unpredictable fiscal policy, and weak revenue performance as the primary sources of risk. The agency warned that another downgrade is likely to occur within the next 12-18 months, contingent on debt continuing to rise and confidence in Colombia’s fiscal management further eroding. It also highlighted that the invocation of the escape clause and Colombia’s growing vulnerability to external shocks amplify the risk of deterioration.

Another credit downgrade by any of the agencies is likely to have negative implications for Colombia’s economy and financial markets. Falling deeper into speculative-grade territory will likely raise sovereign borrowing costs sharply in both external and local markets and potentially reduce market access during periods of volatility. A downgrade is likely to trigger renewed pressure on the Colombian peso as capital outflows increase, compounding the fiscal challenges the country already faces. According to experts interviewed, falling further into junk bond territory is detrimental to Colombia’s standing with markets. When Colombia was last downgraded to junk, it took around a decade to restore investor confidence to achieve investment grade status with credit rating agencies, which in turn allowed its entry into investment grade indices and widened its investor base.

ELECTORAL GUARANTEES’ LAW

The [Ley de Garantías](#) (Electoral Guarantees’ Law) in Colombia refers to Law 996 of 2005, which restricts government actions that are likely to influence electoral outcomes to protect the fairness and neutrality of electoral processes. During this period, the law prohibits direct contracting by public entities, unless in cases of clear urgency, such as national disasters or public health emergencies. It also bars inter-administrative agreements between different levels of government and public entities, limits the modification of public-sector personnel (i.e., no new hires or promotions unless absolutely necessary), and restricts public officials from participating in campaign events or inaugurating government projects that are likely to favor any candidate. This law goes into effect on [November 8, 2025](#), as it starts four months before national elections, covering legislative and presidential campaigns.

Economically, the law creates short-term slowdowns in public investment and government procurement, which is likely to affect broader macroeconomic indicators, like GDP growth. As public entities are restricted from executing new contracts, especially infrastructure or service contracts, economic activity in affected sectors is likely to see a temporary drop. Analysts have noted an estimated [25% decline](#) in contracting volumes during the restricted period, often preceded by a [sharp increase in contracts](#) just before the law goes into effect, which will distort fiscal execution and planning cycles. Therefore, this contraction in public sector activity is likely to impact GDP, particularly in regions where public investment represents a significant share of local economic output.

CASE SCENARIOS

In the final year of the Petro administration, experts interviewed agree that most of the fiscal deterioration has already occurred, driven by the suspension of the fiscal rule, a widening fiscal deficit, rising debt levels, and an excessively expansive national budget proposal. Nonetheless, the fiscal deficit is likely to widen above the MTFF estimate of 7.1%, raising red flags for credit rating agencies closely monitoring Colombia’s commitment to return to fiscal discipline.

Additionally, spending pressures will likely intensify ahead of presidential elections next year, placing further strain on public finances. As a result, markets are likely to continue pricing in a significant risk premium amid persistent uncertainty. That said, Colombia’s strong institutional framework, particularly the independence of the Central Bank, represents the country’s most significant anchor for investor confidence and macroeconomic stability.

However, in the low likelihood that President Petro takes steps that threaten or undermine the institutional independence or fiscal credibility, investors (who currently maintain a cautiously optimistic forward-looking outlook ahead of the elections) will lose confidence. In this scenario, investors will likely divest from Colombian assets and turn to more stable regional peers for investment opportunities. With lower investor demand and higher risk premia, Colombia will face rising financing costs, limited market access, and greater volatility leading up to the political transition.

Building on our extensive list of interviewees for this report, as well as several years of experience speaking with market participants, most of whom have a pessimistic view of the Petro administration, we identified three potential scenarios that are hinged upon the policies and economic acumen of the candidates who stand to become Colombia’s next president. Based on a general candidate profile, we have outlined the potential outcomes for the country’s fiscal landscape and the potential effects that are likely to ensue as a result.

	Probability	Presidential Candidate	Market Reaction	Fiscal Impact	Social Impact
Base	High	Moderately market-aligned	Market Rally	Limited yet positive fiscal consolidation	Continued social protests, Congress imposes legislative constraints
Adverse	Low	Limited market alignment	Market Sell-off	Widening deficit, higher debt-to-GDP ratio, rising debt levels	Increased social spending, growing security concerns
Favorable	Medium	Market friendly	Market Rally	Strong fiscal consolidation, tax reform, and structural spending adjustments	Widespread social protests, low initial approval rating



BASE: STEP IN THE RIGHT DIRECTION, BUT LONG RECOVERY AHEAD

Our base case scenario hinges on the election of a pragmatic, market-friendly candidate, more specifically, one that does not promote continuity of the current government's policies. As the national government shifts back towards the right, we anticipate realignment with the U.S., potentially regaining certification in 2026, but likely at a concession on Colombia's behalf, such as reducing its trade ties to China or withdrawing from the BRICS development bank.

Per the experts interviewed, a more market-friendly candidate is likely to recognize the country's fiscal challenges and the need to implement a structural fiscal reform. This approach entails both a tax reform to increase revenue and a structural government spending overhaul to decrease costs. However, there is limited scope for radical measures and the ability to implement the necessary fiscal overhaul. Therefore, the government is likely to implement modest expenditure restraint, primarily by slowing the growth of current spending, with some reduction in costs.

Given Colombia's increasingly fragmented and polarized electorate, we do not foresee any candidate obtaining a working majority in Congress, suggesting that any substantial reform must be negotiated with a high potential of reforms being watered down. We also do not foresee a government having an expansive agenda on social reforms, political reforms, or fiscal reforms, but rather a government that narrows down its priorities, which will include the fiscal challenges. However, complications will arise due to the unpopularity of expanding the tax base, increasing the pension age, or cutting social spending and subsidies.

A gradual effort to strengthen tax compliance will likely be pursued with the broader tax reforms proposed. However, advancements are likely to be limited on this front, given potential Congressional stalling. The fiscal deficit is likely to narrow gradually, reaching levels close to the upper bounds of Colombia's historic averages, and debt-to-GDP will likely stabilize in the low-60% range before beginning to decline toward the end of the term. This path aims to avoid a sharp rupture with markets but involves a slower, incremental consolidation, with less politically costly measures prioritized early in the term. In response, markets are likely to view the government's willingness to publish a credible fiscal adjustment path favorably, although with some skepticism and at a higher risk premium given the incremental pace and political fragmentation.

Ultimately, out of the experts interviewed, when asked to describe their view on Colombia, the majority stated that they were "cautiously optimistic" in terms of the country's economic and fiscal future. One former Finance Minister described the view as fiscally pessimistic but economically optimistic.

The jump in risk premium is likely to be amplified by renewed departures from the fiscal rule, such as extending or normalizing the escape clause, as credibility erodes and fiscal anchors weaken. Rating agencies, already focused on wider-than-planned deficits and rising debt, will be poised to downgrade Colombia further, pushing it deeper into high-yield territory and raising funding costs across the curve. As previously mentioned, recent actions by S&P and Moody's underscore how quickly ratings adjust when fiscal targets are loosened and rule credibility is questioned.

Under this scenario, the headline deficit remains elevated and will likely set new historic highs, such as 10%, as current spending expands and the government potentially even expands its size in social spending. As financing needs rise, there will likely be heavier local issuance (including UVR-linked TES) at wider spreads. With the fiscal rule sidelined and costlier market access, authorities will likely be pushed toward an IMF stand by arrangement, or another lender of last resort, to restore policy credibility, especially since access to the IMF's Flexible Credit Line was already suspended. An IMF program will likely require a credible consolidation plan, guardrails on current spending growth, and a clear timetable for returning to rule parameters. These conditions will be costly and painful for the country, something potentially similar to the recent arrangements between Argentina and the IMF.

Heightened uncertainty (due to a continuation of current unfriendly market policies) and wider spreads are likely to weigh on capital flows into Colombia, as FDI and portfolio investors will shift from the current wait-and-see stance to reallocation. Until a more credible medium-term framework is presented, investors will likely reallocate to regional peers that show a more stable macroeconomic picture.

At the same time, institutional risks rise: pressure on fiscal guardrails (CARF and the fiscal rule) and renewed political attacks on the Central Bank will erode perceptions of autonomy. Contingent on the next president's alignment with the current administration, further appointments are likely to reshape the Board's center of gravity. Combined with sensitive inflation dynamics and fiscal slippage, additional aligned appointments signal a crack in the perception of independence and raise risk premia, even if formal autonomy remains unchanged. Recent coverage of new appointments and official statements illustrates why markets are watching governance signals closely.

Lastly, under a new left-wing administration, foreign policy will likely diverge further from the U.S. agenda during the Trump administration. This shift will likely cause geopolitical risk premia to widen at the margin, reinforcing outflows and alienating the potential for recertification in September 2026. In short, the election of a candidate closely aligned to Petro likely leads to persistent deficits, weaker anchors, higher risk premia, and institutional strain, creating a highly concerning macroeconomic and political situation for domestic and international investors.

ADVERSE: PRO-SPENDING DRIFT, RULE SLIPPAGE, AND INTENSIFIED MARKET STRESS

In this path, a candidate closely aligned with President Petro wins the presidency and secures enough legislative backing to continue a spending-forward agenda. Markets, which have largely priced in a market-friendly outcome this cycle, are likely to react with a significant sell-off across local rates, equities, and the peso, echoing the pattern seen after the 2022 election when the COP and local assets fell sharply in the immediate aftermath of President Petro's election.

FAVORABLE: TECHNOCRATIC LEADERSHIP, STRUCTURAL REFORM, AND CREDIBILITY RESTORED

This scenario hinges on the election of a technocratic leader who recognizes the severity of Colombia's fiscal challenges and prioritizes their resolution. Such a candidate is likely to build legislative coalitions and manage a broad base of support, even while advancing politically difficult reforms. As a former Finance Minister noted, this outcome requires a pedagogical shift during the campaign so that voters understand the stakes of Colombia's fiscal imbalances. Unlike Argentina, where the population was acutely aware of the economic crisis that the country was facing, since high inflation was affecting citizens' daily lives, most Colombians are not fully attuned to the gravity of the fiscal situation, as it is more complex and less visible in everyday life. It will therefore be critical for this candidate to frame fiscal consolidation as a national imperative, even if the campaign does not dive into the specifics of tax reforms or spending cuts, which are generally unpopular platforms.



Economists will likely tout these reforms as necessary to contribute to the stabilization of Colombia's debt dynamics by curbing the most rigid components of spending. However, the public (not to mention politicians in Congress) is unlikely to sympathize with a government intent on cutting subsidies, increasing taxes, and streamlining processes. This outlook suggests that any fiscal tightening proposal must be packaged as part of a larger deal, involving elements such as security or fighting corruption, to succeed.

Once in office, the new government is likely to adopt a comprehensive structural fiscal reform agenda, with an emphasis on expenditure control. Multiple sources emphasized the need for a full line-by-line review of government expenditure to identify duplicates, streamline programs, and increase efficiency. This position likely entails a multi-year expenditure rationalization process, targeting structural inefficiencies in pensions, transfers, subsidies, and public administration. In turn, the fiscal deficit is likely to return to average historic levels, and adherence to the fiscal rule is likely to be restored toward the end of the presidential period. As credibility improves, the debt-to-GDP ratio and interest payments are likely to fall as lower risk premia in the markets reduce Colombia's cost of borrowing. On the revenue side, the government is likely to restructure the tax system, not necessarily by raising rates, but by reducing complexity, broadening the tax base, and closing loopholes that facilitate tax evasion and high informality. Regardless, these reforms will be unpopular and are highly likely to generate social protests.

One source argued that a likely option is for the newly elected technocratic president to declare a national economic emergency to accelerate structural fiscal reforms. Under [Article 215 of Colombia's Constitution](#), the president, with the signature of all ministers, has the authority to declare a [State of Economic, Social, and Ecological Emergency](#) when grave and imminent disturbances to the economic or social order arise. Each declaration can last up to 30 days, with a maximum of 90 days per calendar year. During the emergency, the government issues decrees with the force of law strictly to conjure the crisis and prevent its extension. However, those measures must meet constitutional tests of necessity, proportionality, and direct connection to the emergency. All such decrees are subject to automatic and expedited review by the Constitutional Court, and Congress retains oversight powers. This framework, used recently during COVID-19 ([Decreto 417 de 2020](#)), provides a lawful channel to move quickly on targeted fiscal measures, while keeping judicial and legislative checks squarely in place.

This scenario marks a decisive return to fiscal discipline with clear communication and transparency from the government. Investors are likely to respond favorably to the renewed credibility with narrowing credit spreads and an appreciating peso. Credit-rating agencies are likely to stabilize outlooks to positive as the consolidation plan gains traction, setting Colombia on a path toward eventual investment-grade ratings. While protests and political resistance are likely to create episodic uncertainty, markets ultimately decide to reward the reforms, viewing Colombia as a regional example of early, technocratic adjustment rather than delayed crisis management.

CONCLUSION

The future of Colombia's fiscal landscape remains highly uncertain. Although there has been a rebound in specific macroeconomic indicators, the country faces an increasingly complex and concerning fiscal outlook with a widening fiscal deficit, growing debt, and increasingly rigid spending obligations. Further intensifying the strain on public finances, we expect spending pressures to increase ahead of the presidential elections next year. As a result, markets are likely to continue pricing in a risk premium for Colombian debt amid persistent uncertainty in the lead-up to the elections.

In the final year of the Petro administration, we do not anticipate a substantial further weakening of the fiscal landscape, as the fiscal rule was already suspended in June and the government still proposed an excessively expansive budget in July. However, we view the government's most recent fiscal deficit estimate of 7.1% for 2025 as overly optimistic, given a likely increase in government spending ahead of elections and little willingness for austerity. Along those lines, the administration's 2026 budget proposal mirrors the structural shortcomings of the 2025 budget, which was enacted by decree. Specifically, it lacks sufficient revenue backing, implying that a tax reform will be necessary to finance the government's planned expenditures, sounding alarm bells amongst experts and business leaders. Over the last 3 years, the Petro administration has caused significant harm to Colombia's fiscal credibility, as reflected not only in market sentiment and negative headlines, but also in the higher debt servicing costs that future governments and generations will be liable for.

That said, Colombia's strong institutions remain a critical anchor for investor confidence and macroeconomic stability. Despite attacks by the executive, the Central Bank has maintained its independence and autonomy. Market narratives often cast Olga Lucía Acosta as a centrist "swing" vote. However, through her independent votes, Acosta has proven her allegiance to the Central Bank's mandate, ignoring any presumable political affiliation, providing confidence in the institution's autonomy. Similarly, the CARF, Colombia's independent fiscal council, which issues non-binding opinions, has repeatedly asserted its independence when issuing unfavorable opinions on both the activation of the escape clause and the excessively expansive national budget proposal.

Ultimately, our view is that Colombia's fiscal outlook hinges upon the outcome of the presidential election. Through our case scenario analysis, we identify three potential scenarios that will determine whether fiscal slippage continues or fiscal discipline is restored. Our high probability, base-case scenario envisions a more pragmatic, market-friendly administration. While significant reforms are likely to be difficult to pass due to limited congressional support, we still expect moderate progress on government expenditure and tax reform. We do not foresee a government in this scenario to have an expansive agenda on social, political, and fiscal reforms, but rather a government that narrows down its priorities, including fiscal sustainability. However, complications will likely arise due to the unpopularity of expanding the tax base, increasing the pension age, or cutting social spending and subsidies. In this scenario, the fiscal deficit will narrow gradually, and debt levels will likely stabilize. This path aims to avoid a sharp rupture with markets but involves a slower, incremental consolidation, with less politically costly measures prioritized early in the term. Nevertheless, we expect that even moderate spending cuts and adjustments will be unpopular and provoke social unrest that a government will have to handle with care. Markets are likely to respond to this scenario with cautious optimism, but still demand a risk premium given the slower pace of fiscal consolidation.



Meanwhile, our adverse scenario assumes that a candidate closely aligned with President Petro wins the election and maintains a pro-spending agenda. This approach will likely lead to further fiscal slippage, persistently high deficits, and rising debt levels. Under this administration, institutional risks rise: pressure on fiscal guardrails (CARF and the fiscal rule) and renewed political attacks on the Central Bank erode perceptions of autonomy, with additional Board appointments likely to reshape its center of gravity. Market reactions are likely to be swift and negative, with Colombia likely facing further credit rating downgrades and capital flight by investors. While highly concerning for the economy and markets, we believe that this scenario has a low probability of occurring.

Lastly, in our favorable scenario, a technocratic leader wins the election and implements a structural fiscal reform. Multiple sources emphasized the need for a comprehensive, line-by-line review of government spending to identify and reduce inefficiencies, coupled with a more efficient tax system that widens the tax base. One option to fast-track these fiscal adjustments is for the next administration to invoke a constitutional economic emergency. Otherwise, any fiscal tightening proposal will likely be packaged as part of a larger deal involving elements such as security or fighting corruption to obtain public and congressional buy-in. However, these reforms will face steep political and social resistance in the form of widespread unrest and legal challenges. This shock plan has the potential to restore credibility, reduce the deficit, stabilize debt, and lower Colombia’s risk premium, pushing credit rating agencies to revise their outlooks positively. At the current juncture, this combination of events is very unlikely to occur.

In conclusion, Colombia’s next administration will inherit a complex and demanding operational landscape, one in which fiscal sustainability must compete with a crowded agenda of political, social, and security priorities. Advancing a comprehensive fiscal reform will require not only technical clarity but also political pragmatism and skill. Stabilizing markets and attracting investment will depend on credible efforts to restore fiscal order through structural reform on both the spending and revenue fronts, an issue for which no leading candidate is publicly advocating at the moment. In short, the incoming administration will need to rebuild credibility, both domestically and internationally, with fiscal responsibility as a key pillar of its mandate.

Colombia Risk Analysis hopes that this report provides valuable context and scenario analysis for decision makers and investors as they evaluate Colombia’s macroeconomic climate and fiscal landscape ahead of the elections.

