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## Country Profile: Colombia

Thomas White Global Investing

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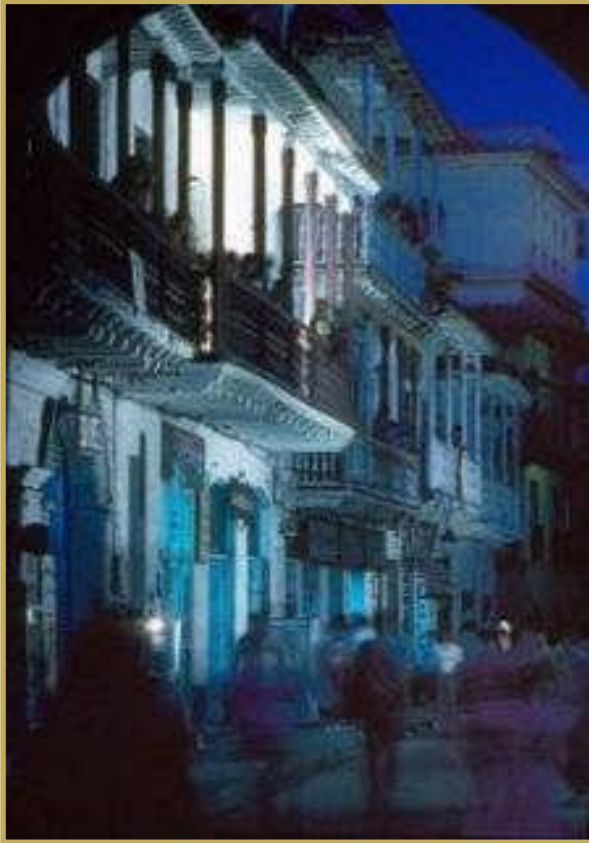
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*The Thomas White organization was founded in 1992 with the goal of bringing the benefits of globalization to investors around the world. We believed that once investors understood that globalization was a positive force, they would also see the advantages of adding international equities to their portfolios. It only makes common sense that professional investors would begin searching the globe for the most attractive opportunities. Researching a wider universe of companies should improve long-term performance. Moreover, broad diversification typically lowers return volatility. Multinational corporations have been using this global strategy for years; why shouldn't investors do the same?*

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A handwritten signature in dark blue ink that reads "James S. White, Jr." The signature is written in a cursive style with a large, stylized initial 'J'.

# Colombia: Recasting its Image in the World



Balconies dominate the streets in Cartagena, Colombia. The city, located on the northern coast of Colombia, is a tourism hotspot.

To most people, Colombia is now known for some of the finest coffee in the world, as well as emeralds, and swinging salsa. And, the small Latin American country, which borders Venezuela and Brazil in the east, Ecuador and Peru in the south, and Panama in the northwest, has registered moderate GDP growth over the recent years.

Indeed, Columbia has come a long way from the images of a country torn apart by murderous conflicts between powerful drug cartels, where kidnappings and extortions for money were the order of the day.

It has been a long and troublesome turnaround journey for a country aspiring to be counted among Latin America's resurging economies. Political stability and restoration of peace were instrumental in bringing about the transformation.

## Leaving a Troubled Past Behind

During the time before the arrival of Christopher Columbus, the country's namesake, nomadic tribes such as hunters and farmers used to inhabit the geographical region, which later came to be known as Colombia. Most of these people were taken as slaves on farms and in the mines, when the Spaniards invaded the territory. These European conquerors established the Viceroyalty of New Granada, comprising Venezuela, Ecuador, and Panama, making Santa fe de Bogota their capital.

But the Spanish were hardened masters and soon an independence movement gained momentum. In an attempt to establish social equality for the people of the region, Venezuelan general Simon Bolivar, a patriot and military mastermind, led the region's quest for independence from Spain, which was won in 1819. The new Republic of Greater Colombia (Gran Columbia) comprised all the regions formerly ruled by the Spanish Viceroyalty. Simon Bolivar, together with fellow patriot Francisco de Paula Santander, were elected as the republic's first president and vice

president respectively. But with the secession of Venezuela and Ecuador, the republic of Gran Colombia was dissolved in 1830, and the two remaining countries, Colombia and Panama, were now collectively named the Republic of New Granada.

With the establishment of New Granada began Columbia's long tradition of political disorder and violence. Political parties founded in the mid-1800s, namely the Conservative and Liberal parties, began a clash that exists even in present day. Around 1863, the region became known as the United States of Colombia, before adopting its present name, Republic of Colombia, in 1886. The divisions between the two parties were so great, that nine constitutions were adopted post-independence, with each party drafting a new constitution upon assuming power.

The roles of church and state became the basis of the conflict between the two opposing parties, with the Conservatives favoring a strong central government and powerful role for the Roman Catholic Church, and the Liberals supporting a weaker central government and strong regional rule. To this day, these political parties are some of the oldest political parties in existence in the Americas.

But continued hostilities between the two parties led to a civil war known as The War of a Thousand Days, which lasted from 1899-1902 and claimed 100,000 lives. Not long after the debacle, Panama was the last country to break away from the confederation in 1903.

With the nation enjoying only a few short decades of political stability, a clash between Conservative and Liberal parties once again resurfaced in 1948 with the assassination of a Liberal Party leader. The warfare between the parties lasted through the greater part of the 1950s in a period known as "La Violencia" (The Violence) that claimed about 300,000 lives. Following this bloodshed, the parties adopted a short truce in 1957, forming a coalition government that lasted until 1974.

<b>Colombia and the World</b>	
Nominal GDP	\$ 243,765 million
GDP Rank	35/191
Per Capita GNI	\$4,620
Per Capita GNI Rank	104/210
Population Rank	29/223
Geographical Area Rank	26/249
Global Competitiveness Rank	69/133
Economic Freedom Index Rank	58/179
Human Development Index Rank	77/182
Major Industries	Textiles and clothing, petrochemicals, leather products, processed food and beverages, iron and steel products

But out of the ashes of Violencia, a new menace surfaced- the Revolutionary Armed Forces of Columbia or FARC- a group of militant communist insurgents. During 1974 to 1982, various ruling parties tried their best to put an end to the nagging insurgency issue, with limited success. The ravaged period paved the way for the emergence of the powerful drug cartels, with FARC embracing drug trafficking as a lucrative business.

By the 1990s, violence reached its peak, resulting from the frequent conflicts between security forces and the resurgent militant groups led by FARC. President Andres Pastrana and the guerrillas attempted to forge peace treaty during the period from 1999-2002, but the effort failed. Pastrana also tried to implement a U.S.-led initiative to stem the narcotic trade and armed conflict. But Colombia could not raise the \$4 billion needed to launch the plan due to the after-effects of the nation's economic crisis of 1997-98. The country's efforts to enlist the support of the European Union and some other countries came to no avail.

Alvaro Uribe, who became the president in 2002, succeeded in reining in the militants through stepped-up military force. The domestic security situation began to improve after 2002 when his new government began to control domestic violence, setting the stage for economic revival and prosperity. With this, cocaine production has been reduced to half of what it was in 2001, but drug money continues to fund guerrillas and other criminal gangs. The improvement in domestic security has helped improve Colombia's trade relations.

## **Forging its own Identity**

The fifth-largest country in Latin America in terms of geographic area, Colombia is the third-largest by population, and the second after Brazil in biodiversity. The country also boasts of the highest percentage of working women than any other country on the continent. People of mixed European and Amerindian ancestry, known as Mestizo, comprise the majority of the population (58%), while whites, mainly of Spanish origin, constitute 20%. A small minority of pure indigenous Amerindians make up only 2% of the country's population. Spanish is the official language and is spoken by the overwhelming majority of Colombians.

Many facets of the Colombian culture, such as faith in Roman Catholicism and bull fights, can be traced to the country's Spanish legacy. The cuisine of the country not only mirrors its European past, but also blends influences from Africa and the Mestizos.

But after attaining independence from Spain, many Colombian politicians, intellectuals, and the elite turned to France for inspiration, so much so that Colombia's civil code, adapted in 1887, is based on Napoleonic Code. French architect Gaston Lelarge is credited with designing many of



Bull rings such as these and the faith in Roman Catholicism are legacies from Columbia's prolonged Spanish occupation.

the landmark buildings in Bogota. Because of its close ties with the United States, North American culture holds sway over Colombia, from shopping malls to tract housing mimicking U.S. suburbs. Colombians are also big fans of Hollywood films, pop music, and American haute couture. The country's music is a fusion of the African rhythms of the Caribbean, Cuban salsa, and Spanish-influenced Andean music. The small Colombian town of Barranquilla prides itself as the hometown of international pop singer Shakira, who

has funded many schools to educate the underprivileged children of Columbia.

Culturally active, the country is home to a living legend, the Nobel Prize-winning novelist and journalist Gabriel Garcia Marquez, whose works mix myths, dreams, and reality to create what is known in literary genre as magical realism. Columbia also gave the world Fernando Botero, probably the greatest Latin American living visual artist. Colombia's cities are dotted by bookshops and the country is the biggest exporter of books in the region.

## Industry and Agriculture

Bogota, Medellin, Cali, and Barranquilla are the four major industrial production centers in Colombia. The country boasts of a variety of industries such as metalworking, chemicals and petrochemicals, paper and paper products, and processed foods and beverages, as well as textiles, leather and clothing. In addition, Colombia also produces cement, iron and steel, and construction products.

Columbia's diverse climate and topography is suited for growing a wide variety of crops. The country's hot climate areas are conducive for the cultivation of rice, cotton, tobacco, cassava, cocoa, sugar cane, coconuts, plantains, bananas, and beef cattle. Temperate regions are known for growing coffee and certain flowers, apart from corn and other vegetables, and fruits such as pineapples, citrus, pears, and tomatoes. Potatoes, and other select climate-specific vegetables, as

well as wheat, barley, flowers, dairy cattle and poultry, flourish in cool climatic conditions. Most of the regions are known for forest produce, with tropical hardwoods thriving in hot regions, and pine and eucalyptus favoring colder climes. This creates the perfect environment for the bird population, with Columbia offering the richest variety of avifauna on earth. The country is also the world's second-biggest exporter of cut flowers.

## **Nature's Bounty**

Colombia is naturally blessed with minerals and energy resources, with the country sitting on the most abundant coal reserves in Latin America. El Cerrejon, situated in Colombia's Guajira Peninsula, is the world's largest open pit coal mine, contributing 65% of the country's total production. In addition to its significant coal reserves, the country also is rich in oil. However, the country does not refine enough oil to cater to domestic demand. Therefore, some refined products, especially gasoline, are imported.

Columbia is a producer of ferronickel, and precious metals such as gold, silver, and platinum. The country also is the major source of another precious commodity, emeralds, comprising over 80% of the world's emerald gem production. Colombian emeralds are highly sought after because they are typically extracted using large pick machines and shovels, rather than by explosives, which tend to create imperfections in the stone.

On the energy front, the country ranks only second to Brazil in hydroelectric potential. But Colombia's immense hydroelectric prospects were affected by a prolonged drought in 1992, which forced the government to introduce power cuts across the country in the mid-90s. The government has decided to build or upgrade 10 thermoelectric power plants to make up for the shortfall in power generation caused by the drought. It also plans to construct a natural gas pipeline system by the middle of the next decade to transport gas to the country's major cities.

## **From Coffee Republic to Coca Country**

For nearly a century, Colombia's economy and democracy revolved around a single crop – coffee. The country ranks as the second largest coffee exporter in the world, accounting for more than half of Columbia's total exports. The success of the coffee industry helped the emergence of a new rural middle class, creating a third of rural jobs, and even helped launch an international brand Café de Colombia.

Toward the beginning of 2001, though, the arrival of low-cost producers such as Vietnam and better-equipped Brazilian growers created a glut in the world coffee market, bringing down the price of the commodity. Poor marketing by the federation of coffee growers accelerated the downslide of the industry. The decline in coffee production in the country led to a chain reaction of sorts, giving rise to unemployment in coffee-growing regions and begetting violence. It is thought that the collapse of the coffee economy and cotton crop might have pushed farmers into the lucrative, but illegal cultivation of cocoa, the key ingredient for cocaine.



Mention Colombia and you can almost smell coffee! The country is one of the world's biggest producers of coffee and the agricultural crop remains a mainstay of the economy.

Today, Colombia is the biggest supplier of refined cocaine in the world and a huge base for heroin. The increased demand for drugs, especially in the U.S. and Europe, fueled coca growing in the country during the 1990s. The majority of the cocaine that enters the U.S. market is produced, processed, or transshipped in Colombia. Despite the government crackdowns, Colombian drug cartels have held a vice-like grip on the processing of cocaine, and controlling the drug's global distribution networks and markets. The country's efforts to contain the spread of narcotics include aerial spraying of herbicide and manual eradication of plants, apart from keeping tabs on the cultivation of coca, opium, poppy, and cannabis. The Colombian government has made it a top priority to eradicate all illicit crops, keep track of drug shipments, and adopt financial controls to prevent money laundering. However, corruption and intimidation by traffickers are hampering the government's drug-control efforts. To tackle the drug menace, the U.S. joined hands with the Colombian government in 2000 under 'Plan Colombia', a \$7.5 billion program that also aimed at strengthening the Colombian economy.

### **Slowed Down by Recession**

Despite the various political conflicts, Colombia is a free-market economy, which clocked an average growth rate of 5% from 1945-1995, and keeping close trade and investment relations with the United States, its biggest trading partner. President Cesar Gaviria launched economic liberalization or "apertura," in 1990, opening the floodgates to the global economy. This was followed by measures such as the reduction of tariffs, deregulation of finances, privatization of government-owned enterprises, and liberalization of foreign exchange rate. Most of the sectors were opened up for foreign investment, although the farm segment remained protected.

Until 1997, the country's economy remained fairly stable. The opening up of the economy helped the country clock commendable growth rates in the five years which followed the liberalization. The Samper administration (1994-1998) focused on social welfare schemes aimed at uplifting Colombia's lower income population. However, the reforms had the undesirable effect of increasing government spending, which led to a ballooning fiscal deficit and public sector debt. To finance the debt, interest rates had to be raised. The government also decided to maintain an overvalued peso, in line with its predecessor's policy. Adding to this, the drug business fueled lawlessness, which contributed to the derailing of the nation's economy.

By 1998, GDP growth crawled to 0.6 %, plunging the country into its first recession since the Great Depression. As a result, the economy contracted by 4.5%, with unemployment hovering at over 20%. President Andres Pastrana, who assumed office on August 7, 1998, inherited an economy in crisis, plagued by domestic violence and global economic turbulence. The country's economic ambitions were further jolted when it lost its investment grade rating on its sovereign debt in 1999.

The government responded by devaluing the peso and followed up with the decision to let the currency float. Colombia also received a \$2.7 billion loan from the International Monetary Fund by making a commitment toward budget discipline and structural reforms.

The year 2000 was marked by a rebound in the economy as foreign trade improved, thanks to a competitive exchange rate and increasing petroleum prices. During the period from 2002 to



Over 70% of the flowers in the United States are imported from Colombia.

2007, the country witnessed rapid economic growth, helped by an improved domestic security situation, rising oil prices, and market reforms initiated by President Uribe. Private businesses flourished, while the government issued licenses to expand several ports. In 2007, Columbia clocked an impressive 8.2% growth rate, one of the largest expansions in Latin America. The administration also decided to invest up to \$50 billion in the mining and oil sector over the next decade. The investment climate improved, reflected in \$10 billion foreign direct investment in 2008. The reforms in the oil and gas sector and the export-led growth were the main catalysts for the increase in FDI inflows.

However, the global financial crisis and weak demand in Colombia's export markets resulted in the economy contracting slightly toward the end of 2008, though it has recovered steadily in 2009. Understandably, Colombia's coffee exports declined to 8.1 million 60-kg sacks of coffee in 2009, down

from 11.1 million sacks in 2008.

The Uribe administration has been proactive in tackling the crisis, getting rid of capital controls, providing for emergency credit lines, and promoting investment initiatives, such as the launching of free trade zones. The government has also called upon exporters to diversify their customer base beyond the United States and Venezuela.

Buoyed by improved GDP growth in the first quarter of 2010, the central bank has commented that it now expects the economy to grow at the rate of 2.5% this year, helped by the turnaround in demand for its commodity exports. Moreover, inflation remains under control, and the country's industrial production and retail sales have risen in recent months. With inflation expected to slow down, the apex bank was prompted to reduce interest rates to 3% recently. According to central bank estimates, inflation is seen to remain at 3.28% in 2010 and 3.58% in 2011.

### **Strained Ties with Venezuela**

The relationship between the outgoing Colombian President Uribe and his Venezuelan counterpart Hugo Chavez hit a new low in 2009 when the two countries disagreed over Colombia's move to make its bases more accessible to U.S. troops. Chavez sees a bigger U.S. conspiracy in Colombia's move. Though a full-blown conflict is unlikely, Venezuela insists that a rapprochement is possible only after Uribe leaves, and Colombia in turn is accusing Chavez of interfering with the country's election process. Adding fuel to the fire, one of the presidential contenders, Juan Manuel Santos, has openly said he cannot get along well with the Venezuelan leader. If the issue goes unresolved, Colombia would stand to lose as Venezuela is its second biggest trading partner after the United States.

### **Roadblocks Ahead**

The new government which gets elected in the June 2010 polls will have its hands full. In 2002, Colombia was on the brink of becoming a failed state. Now, the restoration of the country's investment grade rating will have to be given top priority by the incoming government. Despite Uribe's best efforts, urban violence resurfaced in 2009, marked by murders in Medellín, the country's second biggest city. More worrying is the fact that thousands of former paramilitaries have returned to arms, and there are signs of a regrouping of FARC. Although UN figures show a 50% drop in cocaine production since 2001, drug money is still used to fund the guerrillas and other criminal gangs, posing challenges for security forces. Adding to this, the army has been accused of murdering up to 1,800 civilians, branding them as militants. The next government will need to consolidate Uribe's achievement while reforming his policies to tackle new threats.

The alarming unemployment rate, which stands at 11.8%, also needs to be urgently addressed to prevent the country's youth from joining the dark underworld of drug gangs and armed groups.

Higher payroll taxes deter employers from adding new jobs. Regarding the country's tax system, President Uribe has been accused of doling out tax breaks to favored companies, something which the president defends as necessary to foster investment.

While the Colombian economy may be recovering moderately after the recession, a comparison with some of its Latin American peers subdues the comforting statistics. While Brazil is recovering sharply, Colombia is estimated to grow only modestly in 2010 and 2011. The problem is complicated by the country's dismal export scene. Even as Brazil, Chile, and Peru benefit from China's huge demand for commodities, Colombian exporters find the going tough, as the United States, its biggest market, is yet to recover fully from the recession. What's more, Colombia's other trade partners, Venezuela and Ecuador, have slapped trade sanctions, impeding flow of trade.

But Álvaro Uribe, the two-term president, who assumed office in 2002, has made significant strides toward improving Colombia on all fronts. He has made Colombia less violent. Armed with U.S. aid and a new wealth tax, he has expanded the security forces by half. Better security in turn has helped to boost economic growth. During Uribe's reign, Colombia emerged as one of Latin America's top oil producers, a major coal exporter, and a growing player in gold investment, thanks to a stable government, improved



The financial district in downtown Bogotá, Colombia. The economy has recovered steadily from the recession. The central bank now expects the economy to grow at the rate of 2.5% in 2010.

security situation, and business-friendly environment. The mining sector in Columbia is also making headway, with global majors such as AngloGold Ashanti expressing interest in exploring for gold in the country. Encouragingly, the presidential favorite Juan Manuel Santos, who served as finance minister in the late 90s, is credited with restoring the country's finances after the global financial crisis. And if the trends continue, the stage looks set for Colombia to continue on its path of restoration to play an even bigger role in the Latin American region in the years to come. 🌐

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