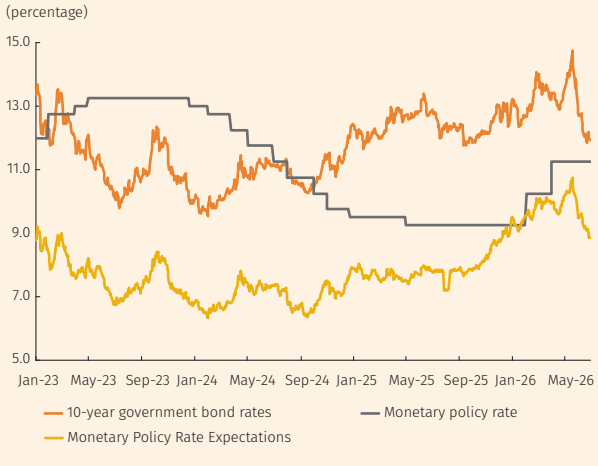
Box 2
Dynamics of the Monetary Policy Interest Rate and the Main Long-Term Interest Rates in the Economy

In Colombia, interest rates play a fundamental role in the economy, access to credit, and the fiscal soundness of the Central Government. The Board of Directors of *Banco de la República* is responsible for determining the monetary policy interest rate (MPR), which corresponds to the economy's overnight reference interest rate and generally guides the performance of other market interest rates.

Other highly relevant interest rates are those paid by the government to access financing through the issuance of bonds. The public debt market, through the trading of these bonds, determines the cost of acquiring debt for the Central Government at different maturities. In these markets, factors such as the level of debt, the soundness of public finances and the risk of default are key to determining the level of interest rates. Participants in these markets include credit institutions, which, in addition to investing in these bonds, can extend loans to the public at different maturities, a function in which reference interest rates, as well as those of alternative investments, play a fundamental role in making credit allocation decisions.

In this context, it is essential to analyze the dynamics of interest rates on public debt instruments together with other market interest rates, rather than in isolation, given that their performance may be related to or affect instruments traded at similar maturities. For example, interest rates on short-term securities tend to be more closely related to the performance of the monetary policy interest rate, while interest rates on long-term bonds may affect mortgage credit interest rates, since, if they are sufficiently high, these two instruments could be seen as substitutes when making investment decisions.

Graph B2.1
Ten-Year Government Bond Interest Rates and Observed and Expected Banco de la República Policy Interest Rates



Source: *Banco de la República.*

Short-Term Interest Rates

In Colombia, the MPR, or benchmark rate, is the main tool used by the Board of Directors of *Banco de la República* to intervene in the money market. Since the intervention rate corresponds to the minimum interest rate *Banco de la República* charges financial institutions for providing liquidity, changes in the level of this rate affect short-term interest rates, and over time, these affect the level of deposit and lending interest rates offered to the public.

Until a few months ago, the performance of the MPR had a certain relationship with the price of public debt bonds (Graph B2.1). However, since 2024, this performance has changed, as other macroeconomic variables have gained relevance in explaining increases in interest rates in this market. For example, between December 2023 and October 2024, both the MPR and the mortgage credit market interest rate showed simultaneous downward trends; whereas between October 2025 and February 2026, an upward trend can be observed in ten-year public debt interest rates and mortgage credit interest

rates, despite stability in the MPR. This phenomenon is mainly explained by: 1) a greater influence of the government's fiscal performance (among other factors), and 2) a higher level of debt in the market.

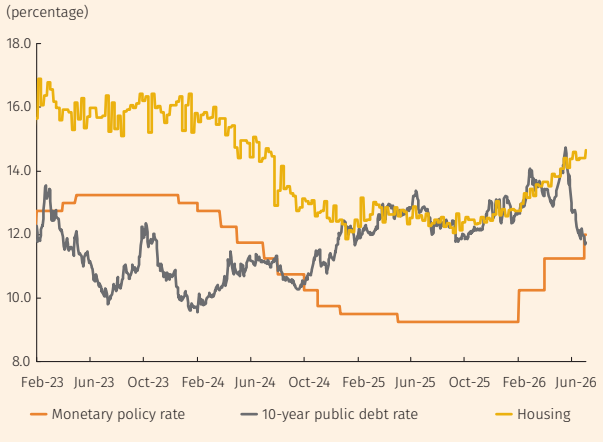
The interest rate at which public debt bonds are traded can be characterized by two main components: first, the interest rate at which investors would be willing to purchase public bonds if there were no risks of default or unforeseen changes in their prices. The second component corresponds to the additional compensation that buyers of public bonds demand for assuming risks related to public debt. The first component is generally associated with the MPR, given its nature as the reference interest rate in the economy. This factor also includes expectations regarding the monetary policy rate and surprises in decisions regarding this rate. The second component corresponds to the additional compensation that buyers demand for assuming risks, which depends on the financial soundness of the government (generally measured through the fiscal deficit), as well as other risk components that affect the ability to pay these bonds. Consequently, if investors perceive a greater deterioration in public finances, they will demand greater compensation for purchasing riskier bonds.

Before 2024, the public debt interest rate in Colombia was determined to a greater extent by the first component; that is, its movements and trend were related to monetary policy decisions. However, since early 2024, an increase has been observed in the contribution of the component associated with compensation for default risks in Colombia, which has caused the public debt interest rate to diverge from the performance of the MPR.

Long-Term Interest Rates

The upward movement in public debt interest rates has important effects on the economy. First, it increases the cost of servicing the Central Government's debt, increasing the future fiscal deficit through higher interest payments. On the other hand, this increase may affect long-term loan interest rates, and consequently, other sectors of the economy. For example, the significant increase in the interest rate on ten-year public debt between early 2024 and May 2026 brough it to levels similar to those of mortgage loans, causing credit institutions to set similar compensation levels for these loans in order to maintain their supply.

Graph B2.2
Nominal Interest Rate



Source: *Banco de la República.*

Thus, it can be seen that, during 2023 and 2024, the mortgage interest rate declined, in line with the performance observed for the MPR during that period and without being influenced by the interest rate on long-term bonds. However, since late 2024, the upward movement in the interest rate on ten-year public debt caused it to exceed the level of the mortgage credit interest rate, which has since closely followed the performance of the former, rather than that of the central bank's benchmark rate (Graph B2.2).

This decoupling of the mortgage credit interest rate from *Banco de la República's* benchmark rate has significant effects on the public seeking to obtain a housing loan, as higher interest rates charged by lenders make credit more expensive for these borrowers to access and could even limit their access to it.

The April 2026 *Monetary Policy Report* included an econometric exercise aimed at explaining the performance of the mortgage credit interest rate through movements in the MPR and the public debt interest rate. This exercise found that, between January 2003 and December

2024, both the MPR and the public debt rate maintained a significant relationship with the interest rate on mortgage[1] loans (Table B2.1).

Table B2.1.
Results of Simple Regressions of the Mortgage Interest Rate on Banco de la República's Policy Interest Rate and the 10-Year Public Debt Interest Rate[a/]

	Regression 1 January 2003 to December 2024	Regression 2 January 2025 to March 2026
Estimate	OLS	OLS
Sample	2003:01 - 2024:12	2025:1 - 2026:03
Banrep's policy interest rate	0.25***	0.04
	(0.03)	(0.26)
10-year public debt rate	0.77***	0.79***
	(0.04)	(0.19)
F-statistic	505.95	13.67
Adjusted R^2	79.34%	64.41%

a/OLS: stands for ordinary least squares, which is the simplest and most widely used method in econometrics for estimating regressions.
F-statistic: the F-statistic helps determine the degree of association between the independent variables and the dependent variable.
Adjusted R2: indicates the percentage of the variation in the mortgage interest rate explained by the model.
Source: *Banco de la República.*

In contrast, when evaluating the same relationship between January 2025 and March 2026, the MPR shows no significant effects, while the ten-year public interest rate does, and the estimated coefficient is practically the same as that observed in the first period. The regression result for the second period analyzed is consistent with the decoupling between the mortgage credit interest rate and the benchmark rate described above.

Conclusions

Since the end of 2024, a breakdown in the relationship between the monetary policy rate and the interest rate in the public debt market has been observed in Colombia, in contrast to the performance observed in previous years. This breakdown is mainly explained by endogenous macroeconomic phenomena that affect the risk premium demanded by agents when purchasing public debt bonds, mainly due to the increase in the fiscal deficit since late 2024 and the rise in inflation during 2026.

In addition, the higher cost of public debt has led to increases in interest rates in other markets, such as mortgage credit market, in contrast to the effect of the monetary policy rate on these markets before late 2024. With respect to mortgage credits, financial agents have increased the cost of access to credit to make investment in this sector more competitive compared to public debt bonds issued by the National Government, negatively affecting the public's ability to access housing through debt.

1 See: https://repositorio.banrep.gov.co/server/api/core/bitstreams/c5501263-167a-427a-b0e0-4f635b92c4e1/content

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