

# Colombia: Recent Weakness in Government Finances Needs Urgent Attention

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The recently released 2025 Medium-Term Fiscal Framework signals an emerging weakness in Colombia’s central government finances. The deficit target has been revised upward to 7.1% of GDP, compared to the earlier projection of 5.1% of GDP. In addition, the fiscal rule has been temporarily suspended starting in 2025 for the next three years, reflecting the need for greater fiscal flexibility amid ongoing challenges such as declining tax revenue and a rigid expenditure structure.

Further, the ongoing legislative gridlock and a rise in security challenges have added another layer of uncertainty on the political front. Together, these factors have made the policy landscape more difficult to navigate.

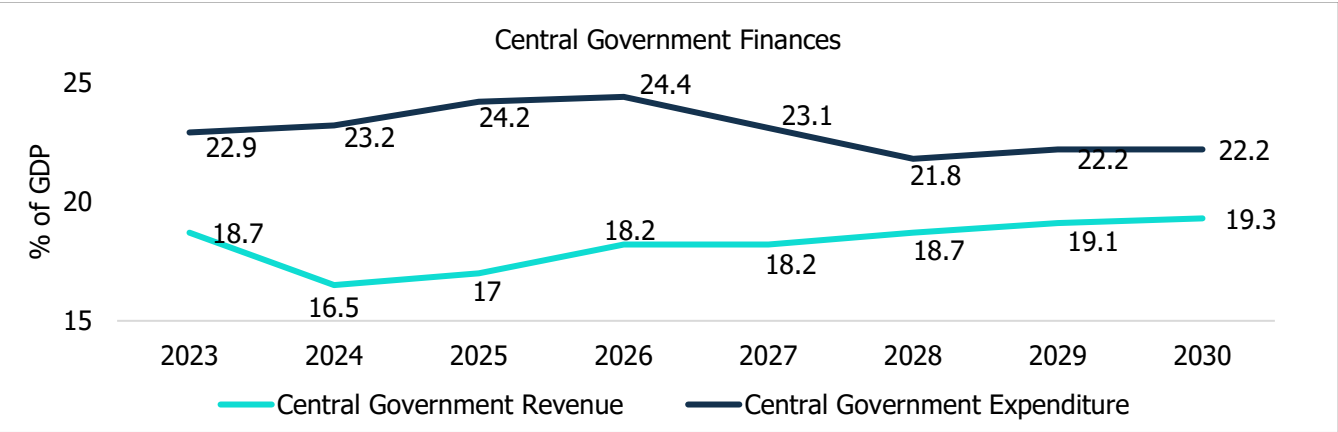
CareEdge Global believes that attention is needed to address the current fiscal weakness and security challenges. However, leading up to the 2026 general elections, the window for meaningful fiscal reform remains narrow over the next few weeks. Thus, any credible plan and its implementation by the government to address fiscal imbalances has become a key element to monitor in the months ahead.

## Recent Deterioration in Central Government Finances Likely to Persist

The current deterioration of Colombia’s fiscal position is driven by a combination of various factors, both on the revenue front and expenditure patterns.

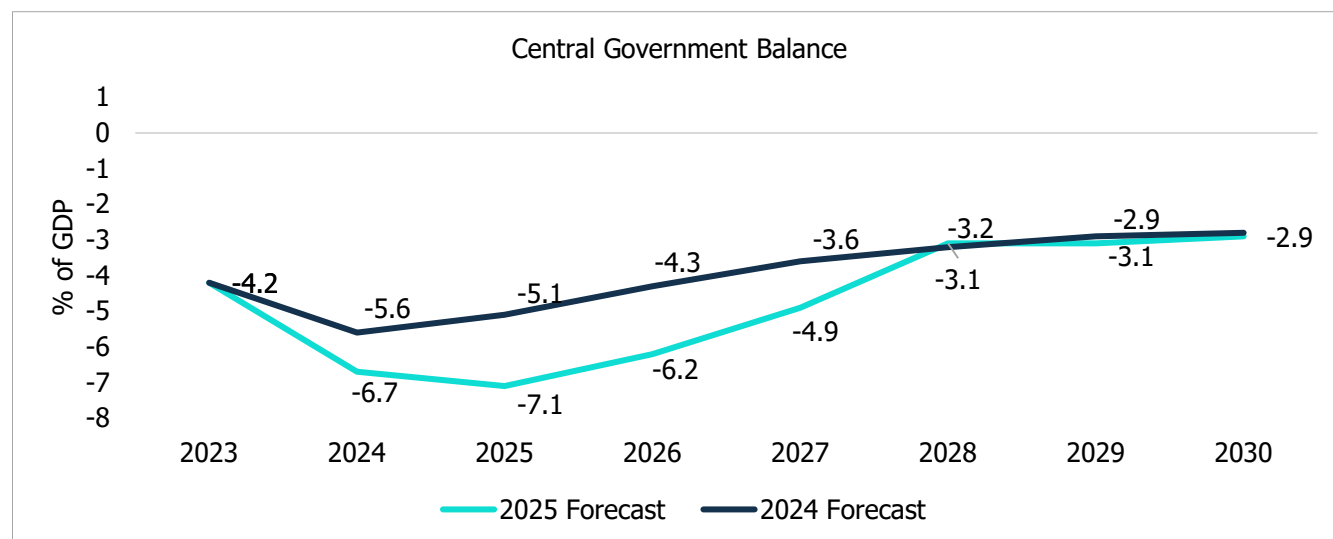
**Recent Revenue Weakness:** The revenues of the central government declined from 18.7% of GDP in 2023 to 16.5% in 2024, primarily due to a sharp fall in tax collections. While a modest recovery to 17.0% of GDP is projected for 2025, due to a slight improvement in tax revenues, it remains below earlier expectations. Throughout 2026-30, central government revenue is expected to average 18.7% of GDP, indicating only a slight improvement.

**Expenditure Pressure:** On the spending side, expenditure rose to 23.2% of GDP in 2024 (up from 22.9% in 2023) and is forecast to increase further to 24.2% in 2025, driven by rising interest payments projected to be at 4.7% of GDP in 2025 and inflexible primary expenditures tied to pension, healthcare and security. Central government expenditure is forecasted to peak at 24.4% of GDP in 2026 before gradually declining to 22.2% by 2030.



Source: MFMP 2025, Ministry of Finance

**Widening Deficit:** The fiscal deficit for 2025 is now projected at 7.1% of GDP, which is significantly above the original target of 5.1%. The recent data release has also worsened the deficit forecasts for 2026 and 2027, now estimated at -6.2% and -4.9% respectively, reflecting continued fiscal weakness.



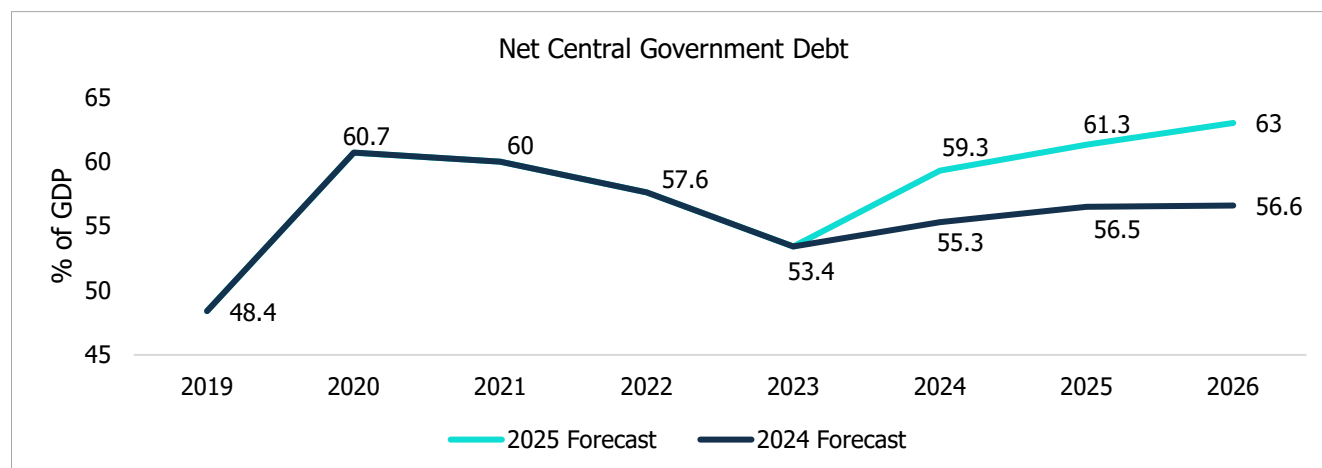
Source: MFMP 2025, Ministry of Finance

As per the forecast, the deficit is likely to be higher over the next 3 years and will only return to the earlier expectations starting in 2028.

### Fiscal Rule Pause Enables Spending, May Raise Debt

To accommodate the widening deficit, the government has invoked the escape clause of the fiscal rule, allowing for its suspension for up to three years starting in 2025. The government's claim justifies the current activation, as 86.4% of public spending is inflexible, linked to pension obligations, health insurance, and the operations essential for sectors such as public forces, posing a risk to macroeconomic stability.

As a result, the central government debt levels are now projected to increase at a level higher than what was expected a year ago. Suspension of the fiscal rule for the next three years could also result in the debt rising to a higher level. If this continues unchecked, the debt may potentially reach closer to 70% by the end of this decade. A level that can challenge long-term debt sustainability, especially in the absence of credible consolidation measures.



Source: MFMP 2025, Ministry of Finance

### Continued Legislative and Security Challenges

President Gustavo Petro has faced continued legislative gridlock throughout his term. Despite early momentum, his administration has struggled to pass key reforms in health, labour, and pensions, reflecting the country's political fragmentation.

In addition, recent violence has intensified security concerns in Colombia, with clashes between armed groups displacing thousands of people in the Catatumbo region, a series of bombings in southwest Colombia, and an attempted assassination of a presidential candidate. These events are fueling political tension ahead of the 2026 elections and complicating the country's fiscal agenda.

With elections scheduled for May 2026, Colombia is entering a crucial political phase. As the country enters campaign mode, the political space for enacting meaningful fiscal reforms appears to have narrowed considerably.

### Limited window available for potential reforms

To address growing fiscal challenges, the Colombian government has proposed a reform strategy:

1. In 2025, A tax reform aimed at expanding indirect taxes, including special levies on coal and oil, as well as broadening the VAT base and introducing new taxes on pesticides, noise pollution, vaping products, and more.
2. In 2026, A review of laws mandating national expenditures and further tax reforms targeting personal income taxation.

However, in the lead-up to the 2026 election, the likelihood of passing new fiscal reforms before the election is slim. The government's reliance on the fiscal rule's escape clause to accommodate rising deficits has raised concerns among investors, who worry that without a credible medium-term consolidation plan, Colombia's debt trajectory could become unsustainable.

Although this report focuses on the developments in central government finances, we would like to analyse the Colombian finances from the point of view of the general government to better understand the overall economic

impact of current issues. Please note that CareEdge Global assesses debt at the general government level as part of our sovereign rating assessment.

### **In Summary**

Colombia's recent deterioration in fiscal outlook is due to revenue underperformance, mounting expenditures, and intensifying political and security pressures. The government's suspension of the fiscal rule and a limited reform window ahead of the 2026 elections underscore the fragile environment. Without a credible implementation path to consolidation, risks to debt sustainability and macroeconomic stability have intensified.

The road ahead is crucial. Without timely corrective measures, the deterioration in Colombia's fiscal metrics could place pressure on its sovereign credit profile. Key areas to monitor will include the government's ability to outline and implement a credible fiscal consolidation plan, the evolving political landscape ahead of the 2026 general elections, and efforts to ensure security and the rule of law across the country.

The next few years will test the resilience of Colombia's institutional framework and the resolve of its policymakers. CareEdge Global will closely track fiscal performance in FY2025, with special attention to revenue recovery, spending discipline, and debt dynamics. Additionally, sustained progress on economic diversification and structural reforms will be crucial to strengthening long-term macroeconomic stability and restoring investor confidence.

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