



MONETARY POLICY REPORT



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CENTRAL BANK OF PARAGUAY

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Executive Summary*

International and Regional Economy

Since the last IPoM, the global economy has remained resilient in a scenario characterized by a more moderate decrease of inflation rates. The global growth forecast for 2024 has been revised upward from 2.6% to 2.8%, due mainly to the strength of the United States economy. Inflation rates have continued to decrease, although at a slower pace. In this context, the first interest rate cuts in certain economies, especially the United States, have been postponed. On the other hand, increasing geopolitical tensions have generated certain pressures on transport costs and crude oil prices.

In the United States, expectations suggest that interest rates will remain high for a longer period due to the strength shown by the economy and the slower pace of disinflation. The positive dynamics of the economy during 2023 have been supported primarily by domestic expenditure and solid labor market conditions. The first data for 2024 also show a positive performance of the economy, whereby the GDP growth projections have been revised upward from 1.2% to 2.1%. Inflation continued to decelerate in the first months of the year, although it remains above the target. During the first quarter, the Federal Reserve (Fed) kept the target range for federal funds rates unchanged, while authorities reiterated that they would be cautious and make decisions based on data. In this context, long-term bond yields have increased, and the U. S. dollar has strengthened globally in the last few months.

The prospects for the Eurozone and China suggest that growth will remain moderate in 2024. In the Eurozone, interest rates remain high, and economic indicators have continued to show weak performance. Thus, the GDP growth forecast has been revised slightly downward (from 0.6% to 0.5%). Market expectations suggest that the European Central Bank's benchmark interest rates might begin to decrease in June 2024. As regards China, the most recent economic data have been better than expected, with some of the improvement being attributed to the stimulus measures implemented by the government. Notwithstanding, economic growth would remain moderate (4.6%) due to continued weak demand, affected by a deterioration of confidence in the economy and the financial difficulties associated with the real estate crisis.

In Brazil, the 2024 growth forecast has been revised slightly upward, while core inflation has continued to decrease. In the fourth quarter of 2023, GDP grew 2.1% inter-annually, closing the year at 3.0%. A growth rate of 1.7% is foreseen for 2024 (1.6% in the previous IPoM report). Regarding CPI inflation, it has stabilized at the upper limit of the target range, while core inflation has continued with its downward trajectory. The Selic rate has accumulated a reduction of 100 basis points over the course of two meetings this year to stand at 10.75% annually, and the Central Bank of Brazil foresees to maintain a contractive monetary policy to ensure both the convergence of inflation to the target and the anchorage of expectations.

*The Spanish version prevails



In Argentina, monthly inflation has remained at two digits, while a greater economic contraction is anticipated. As a result of the economic adjustment measures that are being implemented by the government, a greater fall in GDP is projected for 2024 (from -1.6% to -2.0%). On the other hand, monthly inflation has decelerated this year, even though it continues to stand at two digits, while the foreign exchange gap has decreased and international reserves show a slight recovery.

Domestic Situation and Monetary Policy

Economic activity has continued to show a positive dynamism in the last few months.

In the fourth quarter of 2023, GDP registered an inter-annual variation of 4.9% (0.8% inter-quarterly), boosted by the positive results of services, manufacturing, livestock production, and the electricity & water sector. On the contrary, growth was attenuated slightly by the construction and agriculture sectors. Likewise, the GDP that excludes agriculture and the bi-national hydroelectric entities registered an increase of 5.8% y-o-y (1.1% inter-quarterly). On the expenditures side, the components that registered a positive incidence were net exports and private consumption, while public consumption and gross fixed capital formation decreased inter-annually. The GDP accumulated a growth rate of 4.7% and GDP without agriculture and the bi-national hydroelectric entities expanded by 2.8% at the close of 2023. According to the Monthly Indicator of Economic Activity (IMAEP), it is expected that economic activity will continue to register positive dynamics during the first quarter of 2024, explained largely by the manufacturing and services sectors.

Since the last IPoM report, total inflation has stabilized below 4%, and market expectations have remained in line with the target.

In the first quarter of 2024, the average inter-annual variations of the IPC and IPCSAE were 3.3% and 3.5%, respectively, lower rates than those registered in the previous quarter. In monthly terms, the IPC registered an average variation of 0.7% (0.3% the IPCSAE), explained mainly by the volatile components (fruits and vegetables) and fuels, which increased in March. In inter-annual terms, core inflation and the underlying X1 inflation were also lower than in the previous quarter, reflecting that inflationary pressures have remained moderate. Inflation expectations in the first quarter continue to be anchored to the 4% target for all the consulted horizons.

During the first quarter of the year, the Monetary Policy Committee (CPM) decided to reduce the MPR by 75 basis points (bps), to stand at 6.00% at the close of this report.

In the international scenario, the resilience of the United States economy stands out while the slight increase of inflation in recent months has been surprising. Given this situation, the Federal Reserve has continued to maintain its referential rates. Regarding the commodities markets, there has been an increase in the international prices of crude oil, due partly to the escalation of geopolitical tensions in the Middle East and between Russia and Ukraine, while the quotes for agricultural commodities have decreased due to favorable supply prospects and the moderation of global demand. Despite the uncertainty in the international sphere, domestic conditions, in terms of inflation and expectations have allowed the Central Bank of Paraguay to continue with the gradual process of monetary policy normalization. In this manner, the Committee decided to decrease the



reference rate by 25 bps at each of the CPM meetings held in January, February, and March 2024.

Projections and Risks

The GDP growth forecast for 2024 remains at 3.8%, although certain internal recompositions have been made (Table A). Adverse weather conditions (drought) affected certain crop yields in the recent period. Thus, expectations for the agricultural sector were revised downward (from 4.2% to 2.0%), explained by a lower estimated production of corn. However, the soybean harvest is proceeding as expected, while an increase in the production of wheat is expected as compared to the previous year. The effects of climate conditions have also led to decreased growth of the Water & Electricity sector (from 4.3% to 3.1%) due to lower generation of electric energy by the bi-national hydroelectric entities, although an upward adjustment in the distribution of electric power partially attenuates that reduction. On the other hand, manufacturing was revised upward, from 3.6% to 4.1%, in line with the positive dynamism observed in various industrial sub-sectors in the last few months. Finally, the Other Services category registered a dynamism that surpassed the level anticipated in the previous revision. This led to an upward adjustment of 0.8 p.p. in the forecast, bringing it to 4.3% for 2024. The favorable performance of services provided to households, financial intermediation, and the Hotel & Tourism sub-sector, among others, are highlighted. With these results, a greater growth rate (0.4 p.p.) of the GDP that excludes both agriculture and the binational entities is expected, reaching 4.0%.

On the expenditure side, lower growth of exports is expected, offset by a greater expansion of private consumption (Table B). The downward revision of exports (from 3.0% to 2.4%) is in line with the lower increases estimated for agriculture and the water & electricity sector. As regards gross fixed capital formation, a 5.0% expansion continues to be forecast, considering the favorable dynamics observed at the beginning of this year. Likewise, private consumption was adjusted slightly upward by 0.2 p.p., to stand at 3.8%. The expected growth of private consumption in 2024 is supported by consumer confidence that stands in the optimism zone, inflation expectations that are aligned to the target, the positive dynamism of loans, and favorable labor market indicators.

The inflation projection for 2024 remains at 4% and is expected to continue at this level over the forecast horizon. No significant imbalances of domestic and external factors relevant to inflation are anticipated for this year. The inflationary results recorded in the first quarter, although higher than expected, were explained primarily by volatile components of the consumer basket, while a reversal of these prices is foreseen in the next few months. Considering that inflation expectations are anchored to the middle-term target and in the absence of new shocks, it is expected that inflation will stand around the 4% target by the end of 2024 (Table C).

The risks derived from the international scenario are similar to those pointed out in the December IPoM report, although some of these risks have intensified in recent months.

The escalation of geopolitical tensions, especially in the Middle East, might continue to affect the prices of crude oil and its derivatives. Changes in shipping routes due to armed conflict continue to represent threats for trade, which could further increase oil prices due



to higher transport costs. Furthermore, the possibility that the OPEC+ might implement additional production cuts in the second half of the year and that demand might be greater than foreseen has created uncertainty in the petroleum market.

Regarding the prices of food commodities, it is noted that certain adverse weather conditions could eventually generate upward risks in international prices. Likewise, the geopolitical instability could cause interruptions in world supply chains, to some extent, and therefore affect food prices. On the other hand, moderate global growth might contribute to either stabilizing or reducing the prices of agricultural and energy commodities, especially in a context of favorable weather conditions, as has happened in the recent past. In this sense, as mentioned in the previous report, a divergence in the evolution of energy and food commodity prices could deteriorate the terms of trade of the countries that export agricultural commodities.

Another risk factor stems from a deeper deceleration in China. Global concerns persist about a weaker-than-expected growth rate due to the fragilities of the Chinese real estate sector and the deterioration of the confidence of economic agents. In this context, it is probable that an even more pronounced reduction of commodity prices will be observed, given the greater moderation of the Chinese economy.

At the local level, the risks for the economy's growth derive primarily from the evolution of climatic conditions. In the last few months, weather conditions changed as compared to the previous IPoM report. The possibility of excessive rainfall due to the El Niño phenomenon has diminished significantly. Instead, deficient soil moisture has been observed, especially in the Northern zone of the Eastern region, which has mainly affected the production of corn. Notwithstanding, the most recent data indicate an improvement of soil moisture levels following the significant rainfall registered since the beginning of April.


Table A. Gross Domestic Product Growth by sectors. Percent.

	2023*	2024(f)	2024(i)
Primary Sector	16.5	2.0	0.2
Agriculture	23.3	1.8	0.1
Livestock	0.5	1.6	0.0
Secondary Sector	3.4	4.0	1.3
Manufacturing	3.1	4.1	0.8
Construction	-7.5	4.7	0.3
Electricity & water	16.0	3.1	0.2
Tertiary Sector	3.6	3.9	1.9
General government	3.4	3.4	0.3
Trade	4.4	3.4	0.4
Other Services	3.4	4.3	1.2
Taxes	3.3	3.7	0.3
GDP at market prices	4.7	3.8	3.8
GDP w/o agriculture and binationals	2.8	4.0	

* Preliminary data (f) Forecast. (i) Incidence

Source: Central Bank of Paraguay

Table B. Economic growth and current account. Percent.

	2023*	2024 (f)
GDP	4,7	3,8
Domestic demand	-1,7	3,9
Gross fixed capital formation	-3,5	5,0
Total consumption	2,9	3,2
Private consumption	2,7	3,8
Public consumption	3,6	0,0
Exports of goods and services	36,7	2,4
Imports of goods and services	14,1	2,8
Current account (% of GDP)	0,3	-0,5

* Preliminary data

(f) Forecast.

Source: Central Bank of Paraguay

Table C. Inflation projection. Percent.

	2023	2024(f)	2025(f)	2026(f)
December CPI inflation (*)	3.7	4.0	4.0	
CPI inflation around 2 years (**)				4.0
December underlying CPI (*)	3.2	4.0	4.0	
Underlying CPI inflation around 2 years (**)				4.0

(f) Forecast includes data as of December 2023.

(*) Corresponds to end-of-period inflation.

(**) Corresponds to the projected inflation for the first quarter of 2026

Source: Central Bank of Paraguay