



MONETARY POLICY REPORT



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CENTRAL BANK OF PARAGUAY

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Asunción · Paraguay





Executive Summary*

International and Regional Economy

Since the last IPoM, the global growth prospects for 2024 have improved, despite restrictive monetary policies and geopolitical tensions. The global economic growth forecast for 2024 has been revised upward from 2.8% to 3.0%, due mainly to better prospects for the United States, the Eurozone, and China. Inflation rates have continued to decrease, although less sharply. The United States' Federal Reserve (Fed) has shown great caution about when it will begin to cut federal funds interest rates, while the European Central Bank (ECB) lowered its interest rates in June. Favorable crude oil supply prospects, together with a certain moderation of geopolitical tensions in the second quarter, among other factors, have led to less pressure on petroleum prices. Meanwhile, the prices of agricultural commodities have increased due to more adverse weather conditions in the main producing regions.

In the United States, the GDP growth projections have been revised upward and inflation has stabilized above the target. Economic activity showed positive dynamics in the first half of the year, driven by the strength of domestic demand and solid labor market conditions. In this scenario, a growth rate of 2.3% is foreseen for 2024, above the rate projected in March (2.1%). On the other hand, inflation has continued to diminish, although at a slower pace. The Fed kept the target range for federal funds rates unchanged at its last meetings, and the market expects that the first interest rate cut will materialize in the second semester. In this context, long-term bond yields have increased slightly, and the U.S. dollar has strengthened globally during the second quarter.

Economic performance in the Eurozone and China was more positive than expected in the first quarter. In the Eurozone, economic indicators have shown some signs of recovery, leading to an upward adjustment of the GDP growth forecast (from 0.5% to 0.7%). The ECB reduced its referential interest rates in June and expects to keep such rates at restrictive levels for as long as necessary to ensure the convergence of inflation to the target. As regards China, the growth prospects have improved, from 4.6% to 4.9%, in line with better-than-expected results in the first quarter, and the foreseen impact of the stimulus measures announced by the government.

In Brazil, better-than-expected data in the first quarter contributed to the upward revision of the 2024 growth forecast, while inflation has continued to decrease. In the first quarter of 2024, GDP expanded 2.5% inter-annually, above the expected level (2.2%), and the growth rate projection for 2024 was adjusted upward from 1.7% to 2.0%. CPI inflation has shown a downward trajectory, although it remains above the target. In this context, the Central Bank of Brazil (BCB) reduced the Selic rate to 10.50% annually at the May meeting and kept the rate unchanged in June. Looking forward, the BCB 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 continued to decelerate, while a greater economic contraction is foreseen. As a result of the economic stabilization program, a greater fall in GDP is projected for 2024 (from -2.0% to -3.6). On the other hand, monthly inflation has decelerated to one-digit figures since April, while the foreign exchange gap has increased slightly and international reserves have continued to show a recovery.

Domestic Situation and Monetary Policy

At the domestic level, economic activity and domestic demand have shown a favorable performance. In the first quarter of 2024, GDP registered an inter-annual variation of 4.3% (1.2% inter-quarterly), explained by the positive dynamics of services, manufacturing, livestock production, the electricity & water sector, and, to a lesser degree, by agriculture. The negative incidence of the construction sector slightly attenuated the positive performance of aggregate activity. The GDP that excludes agriculture and the bi-national hydroelectric entities registered an increase of 5.6% y-o-y (1.2% inter-quarterly). On the expenditures side, a rebound of domestic demand has been observed, highlighting the impact of consumption (private and public), gross fixed capital formation, and net exports. According to the Monthly Indicator of Economic Activity (IMAEP), it is expected that GDP will continue to register positive dynamics in the second quarter of 2024, mainly driven by the services and manufacturing sectors.

Inflation trend measures have evolved favorably, and expectations have remained in line with the target. Total average inflation showed a rebound, standing at 4.2% in the second quarter (3.3% in the first quarter), mainly due to the volatile components of the IPC basket, particularly increased prices of vegetables. Meanwhile, underlying inflation, underlying X1 inflation, and core inflation averaged inter-annual rates of 3.0%, 4.3%, and 3.1% in the second quarter, similar to the rates observed in the first quarter (2.8%, 4.6%, and 3.3%, respectively). Finally, inflation expectations have remained around the 4% target for all the consulted horizons.

During the second quarter of the year, the Monetary Policy Committee (CPM) decided to maintain the MPR at 6.00% annually. The BCP initiated the reduction of its benchmark interest rate starting in August 2023, and accumulated a decrease of 250 basis points by February 2024. Starting at its March meeting, the Committee considered that maintaining the interest rate at 6.00% was the most prudent decision, considering that in the international scenario, the first interest rate cut by the Federal Reserve had been postponed to the second semester of the year, while uncertainty persisted about the evolution of the prices of crude oil, due to geopolitical tensions. In addition, the CPM pointed out that the current MPR stands around the neutral range, a monetary policy stance that is considered consistent with economic activity performance and inflation.

Projections and Risks

The GDP growth forecast for 2024 remains at 3.8%, while a greater expansion of the GDP that excludes agriculture and the bi-national hydroelectric entities is foreseen (Table A). In recent months, reduced water flow of the Parana River significantly affected the generation of electric energy by the bi-national entities, leading to a downward revision of the growth of the water & electricity sector (from 3.1% to -2.8%). On the other hand, the performance of the



agricultural sector stood in line with the level expected in the previous IPoM, whereby the growth estimate remained unchanged (1.8%). When excluding both agriculture and the binational entities, the GDP showed a dynamism that surpassed the level anticipated in the previous report, and the projection was revised upward from 4.0% to 4.5%. This revision was largely explained by the greater growth estimated for the tertiary sector, from 3.9% to 4.5%. In particular, trade was revised upward from 3.4% to 4.9%, driven by stronger growth of the commercial margin of imports and manufacturing. The “other services” category would also show greater expansion (from 4.3% to 4.6%), explained by the favorable performance of financial intermediation, services provided to households, and business services. As regards other secondary sector activities, most of the sub-sectors of the manufacturing industry reported better than expected results, compared to the estimates in the previous revision, while the construction sector is projected to show less growth in the year. Finally, consistent with the positive dynamism shown by economic activity, taxes on products showed a better-than-expected performance compared to the estimate in the previous revision, whereby a growth rate of 6.8% is expected in 2024 (3.7% in the previous revision).

On the side of GDP expenditures, greater growth of domestic demand is expected (Table B).

As compared to the previous report, the dynamism of private consumption stood above the expected level, leading to an upward adjustment of growth (from 3.8% to 4.3%). This positive revision (0.5 p.p.) is in line with the favorable performance of both economic activity (greater than expected growth of the GDP that excludes agriculture and the bi-national entities) and the labor market. While less growth is expected for construction, the foreseen expansion of gross fixed capital formation remained unchanged (5.0%), due to the favorable performance of investments in machinery and equipment. As regards external demand, the growth of exports was adjusted downward (from 2.4% to 1.5%), consistent with less production of electricity by the bi-national entities, while the growth of imports was adjusted upward (from 2.8% to 3.1%), explained by greater imports of consumer, intermediate, and capital goods.

The inflation projections for 2024 and the forecast horizon remain at 4% (Table C). As pointed out in the previous IPoM report, no significant unbalances of domestic and external factors that could have an impact on domestic inflation are expected. This is despite higher inflation rates during the first months of the year, explained largely by the high incidence of volatile components of the consumer basket. However, these prices have shown a certain reversal in June, and it is expected that this behavior will continue in the upcoming months. Meanwhile, uncertainty factors associated with the evolution of the price of crude oil have moderated in recent months. Considering that agents’ expectations are anchored to the middle-term target and in the absence of new shocks, it is expected that inflation will stand at the 4% target by the end of 2024 and over the projection horizon.

The risks derived from the international scenario are similar to those pointed out in the March IPoM report. Geopolitical tensions remain latent, whereby an escalation of conflicts, especially in the Middle East, could generate disruptions in global supply chains and affect oil prices. Regarding food commodities, certain adverse weather conditions could eventually generate upward risks in international prices, as was observed recently during part of the second quarter. Conversely, a moderation of global growth could generate a smaller boost for external demand, which might be due to a greater than expected slowdown of China’s economic growth. In this context, the prices of agricultural and energy commodities might remain stable or even decrease. In this situation, a divergence in the evolution of energy and



agricultural commodities prices could deteriorate the terms of trade for countries that export food products.

At the local level, the evolution of weather conditions constitutes the most relevant risk factor. Since the previous report, while the amount of rainfall has allowed adequate soil moisture levels, the possibility of adverse weather conditions that could eventually affect winter crop yields remains latent. For the second semester of the year, the most recent forecasts mention the probability that rainfall will be below the historical average. Notwithstanding, at the end of this report, expectations for corn and wheat production remain positive. At the same time, downward risks persist in the generation of electrical power by the bi-national entities, due to the impact of weather factors on the Parana River’s water flow.

Table A. Gross Domestic Product Growth by sectors. Annual change, percent.

	2023(f)	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	2,5	0,8
Manufacturing	3,1	4,4	0,9
Construction	-7,5	3,0	0,2
Electricity & water	16,0	-2,8	-0,2
Tertiary Sector	3,6	4,5	2,2
General government	3,4	3,4	0,3
Trade	4,4	4,9	0,5
Other Services	3,4	4,6	1,3
Taxes	3,3	6,8	0,5
GDP at market prices	4,7	3,8	3,8
GDP w/o agriculture and binationals	2,8	4,5	

(f) Forecast. (i) Incidence
 Source: Central Bank of Paraguay

Table B. Economic growth and current account. Annual change, percent.

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

(f) Forecast.
 Source: Central Bank of Paraguay



Table C. Inflation projection. Annual change, 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 June 2024.

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

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

Source: Central Bank of Paraguay