



# MONETARY POLICY REPORT



*September 2024*

**CENTRAL BANK OF PARAGUAY**

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[www.bcp.gov.py](http://www.bcp.gov.py)

Asunción - Paraguay





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## Executive Summary\*

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### International and Regional Economy

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**The global economic growth outlook has been revised slightly upward, inflation has continued to fall, monetary conditions have become more flexible, and commodity prices have decreased.** The global growth forecast for 2024 was adjusted from 3.0% to 3.1%, mainly due to better prospects for the United States. Inflation rates in advanced economies have continued to decrease, although the moderation of underlying inflation has been less pronounced. International financial markets registered significant volatility at the beginning of August, but later tended towards normalization. In September, the U.S. Federal Reserve (Fed) began the cycle of federal funds rate cuts, and the European Central Bank (ECB) continued with its monetary easing policy. Energy and agricultural commodity prices fell compared to June levels, due to expectations of moderating global demand and abundant supply, which has offset upward price pressures driven by rising uncertainty around geopolitical conflicts.

**In the United States, labor market indicators have shown less dynamism and inflation has decreased in the last few months, providing the Fed with greater confidence to lower its benchmark interest rates.** Economic activity continued to show solid growth in the second quarter, surpassing expectations and prompting an upwards revision of growth projections from 2.4% to 2.6% for this year, while projections for 2025 remain unchanged. In the last months, the unemployment rate has increased, job creation has moderated, and inflation has decelerated faster than expected, although it remains above the 2% target. In this context, the Fed decided to reduce the target range for federal funds rates by 50 basis points, to stand at 4.75% - 5.00% annually. In international financial markets, the U.S. dollar has weakened and yields on U.S. Treasury bonds across all maturities have decreased since the last IPoM report.

**The economic growth rates of the Eurozone and China were lower than expected in the second quarter.** In the Eurozone, GDP growth remains moderate due to weak private domestic demand, with a growth forecast of 0.7% for this year. Inflation continued to fall gradually, nearing the 2% target, prompting the European Central Bank (ECB) to continue with its monetary easing process. In China, second quarter growth and leading indicators for the third quarter have shown less momentum than expected, leading to a downward adjustment in GDP growth projections from 4.9% to 4.8%, below the 5% target. In this context, the Chinese government has announced new stimulus measures to reactivate the economy.

**In Brazil, economic performance in the second quarter surpassed expectations, while inflation has remained high.** During this period, GDP grew 3.3% inter-annually, above market expectations (2.7%). Thus, the growth forecast for 2024 was revised upward from 2.0% to 2.8%. On the other hand, inflation remains elevated, near the upper limit of the Central Bank of Brazil's (BCB) target range, and inflation expectations for the end of 2024 and 2025 have increased in the recent months, moving further away from the target. In

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\*The Spanish version prevails



this context, in September, the BCB decided to raise the Selic rate by 25 basis points to 10.75%, after keeping it unchanged since June.

**In Argentina, economic activity remained in negative territory, and inflation continued to moderate in line with economic stabilization measures.** In the second quarter of 2024, GDP registered an inter-annual variation of -1.7%, surpassing the anticipated decline (-1.4%). As a result, GDP is projected to end 2024 with a variation of -3.8% (-3.6 in the previous report). On the other hand, monthly inflation continued to decelerate, though at a more gradual pace, standing at around 4.0% in the third quarter. The Central Bank of the Republic of Argentina (BCRA) has kept its monetary policy rate at 40.0% since May. However, the BCRA announced a series of measures to eliminate various sources of currency issuance and reduce the burden of liabilities on its balance sheet. In this context, the foreign exchange gap has decreased since the last report, partly due to the BCRA's interventions in the parallel market, and the accumulation of international reserves has stabilized in recent months.

## Domestic Situation and Monetary Policy

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**Economic activity and domestic demand have continued to show favorable dynamism.** In the second quarter of 2024, GDP expanded 4.8% inter-annually (1.4% inter-quarterly), explained by the positive performance of services, manufacturing, construction, and livestock production. Notwithstanding, the negative results for the generation of electricity attenuated the positive dynamics of economic activity. GDP that excludes agriculture and the bi-national hydroelectric entities registered an increase of 6.9% y-o-y (2.2% inter-quarterly). On the expenditure side, the components with positive incidence were private consumption, gross fixed capital formation (GFCF), and government consumption, while net exports had a negative incidence. By the end of the first semester, GDP increased 4.6% in cumulative terms.

**Since the previous IPoM, total inflation and inflation trend measures have continued to evolve favorably.** In the third quarter, average inter-annual inflation was 4.2%, similar to the average observed in the second quarter. In monthly terms, the average rate decreased from 0.3% to 0.0%, reflecting mainly a reversal of price increases in the volatile components of the IPC basket. Meanwhile, underlying inflation, underlying X1 inflation, and core inflation averaged inter-annual rates of 3.3%, 4.1% and 3.2%, respectively, in the third quarter (3.0%, 4.3%, and 3.1% in the second quarter). Finally, inflation expectations have remained around the 4% target for all the consulted horizons.

**During the third quarter of the year, the Monetary Policy Committee (CPM) decided to maintain the MPR at 6.00%.** The BCP had reduced the MPR from 8.50% in August 2023 to 6.00% in March 2024. During the second and third quarters of 2024, the CPM kept the reference rate unchanged, pointing out that it stands around the neutral range, which is deemed appropriate given the current dynamics of inflation and economic activity. Inflation trend measures, inflation projections, and economic agents' expectations have remained in line with the medium-term target. Likewise, GDP stands near its potential.



## Projections

**In the baseline scenario, the GDP growth forecast for 2024 was revised upward from 3.8% to 4.0% (Table A).** This greater expansion is attributed to better-than-expected results in the trade sector, with its projection increasing from 4.9% to 5.1%. In the same manner, the livestock production sector registered an upward revision (from 1.6% to 5.4%), explained by a higher cattle slaughter rate. In line with the positive performance of economic activity, taxes on products have also shown greater-than-expected growth and was revised upwards from 6.8% to 9.5%. Conversely, the forecast for the water & electricity sector was revised downwards, from -2.8% to -4.0%, due to lower generation of electric energy by the binational entities, affected by the low water flow in the Parana River. As regards the agricultural sector, the expected growth rate remains unchanged from the previous revision (1.8%), though a re-composition has been registered. The lower volume of corn production, compared to the previous estimate, would be offset by higher wheat production. Likewise, the remaining activities (manufacturing, construction, general government, and other services) showed a dynamism according to expectations, whereby their respective estimates have not been modified. Thus, the GDP forecast, when excluding both agriculture and the binational entities, was revised upward from 4.5% to 4.9%.

**On the side of GDP expenditures, domestic demand is expected to show greater-than-anticipated growth (Table B).** Compared to the previous report, private consumption has shown a dynamism that surpassed expectations, leading to an upward adjustment in its growth forecast, from 4.3% to 4.7%. This positive adjustment of 0.4 p.p. is in line with the upward revision of GDP that excludes agriculture and the binational entities, as well as the favorable dynamism observed in imports. The foreseen expansion of gross fixed capital formation was revised upward from 5.0% to 5.8%, due to the favorable performance of investments in machinery and equipment. As regards external demand, the growth of exports was adjusted downwards (from 1.5% to 0.4%), explained by less exports of primary products (corn) and electricity. Meanwhile, the growth forecast for imports was adjusted upward (from 3.1% to 4.1%), mainly explained by greater imports for domestic consumption.

**Inflation projections for 2024 and the forecast horizon remain at 4% (Table C).** As noted in the previous report, no significant imbalances that could divert inflation from its expected trajectory have been observed. On one hand, a continued reversal of price increases in the volatile components of the IPC has been observed, GDP is at levels close to its potential, and the effects of the depreciation of the local currency have been limited. On the other hand, risks stemming from the external scenario have tended to moderate, especially with the decline in food and energy commodity prices. Considering that agents' expectations are aligned with the medium-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 throughout the projection horizon.



## Risk scenarios

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**The risks derived from the international scenario are more balanced.** Geopolitical tensions, especially in the Middle East, continue to be a source of upward risk for inflation due to their potential impact on oil prices. In addition, unfavorable weather conditions in the main producing regions could impact crop yields and heighten the risk of an increase in the international prices of food commodities. At the same time, the risk of a moderation in global growth, stemming from the situation in China, and a deepening of protectionist policies remains a concern. On the other hand, external financial conditions would be more favorable as the Fed's interest rate cut cycle progresses, which could boost global growth and moderate exchange rate pressures on the region's currencies in the next months. However, after the last CPM meeting, U.S. employment and inflation data for September were released, exceeding market expectations and creating some uncertainty regarding the pace of interest rate adjustments by the FED in the coming months.

**At the local level, the risk scenario is mainly tied to the evolution of weather conditions.** The probability of the "La Niña" climatic phenomenon, associated with reduced rainfall, has recently increased. This phenomenon could negatively impact agricultural production in the 2024/2025 crop seasons. However, weather forecasts indicate that the severity of La Niña might be limited. Meanwhile, greater soybean exports have been observed this year compared to previous years, which could imply less dynamism in soy oil production towards the last quarter of 2024. The livestock and meat production sector might perform better-than-expected, given the favorable outlook for the sector.


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

|                                     | 2023*       | 2024(f)    | 2024(i)    |
|-------------------------------------|-------------|------------|------------|
| <b>Primary Sector</b>               | <b>16.5</b> | <b>3.0</b> | <b>0.3</b> |
| Agriculture                         | 23.3        | 1.8        | 0.1        |
| Livestock                           | 0.5         | 5.4        | 0.1        |
| <b>Secondary Sector</b>             | <b>3.4</b>  | <b>2.2</b> | <b>0.7</b> |
| Manufacturing                       | 3.1         | 4.4        | 0.9        |
| Construction                        | -7.5        | 3.0        | 0.2        |
| Electricity & water                 | 16.0        | -4.0       | -0.3       |
| <b>Tertiary Sector</b>              | <b>3.6</b>  | <b>4.5</b> | <b>2.2</b> |
| General government                  | 3.4         | 3.4        | 0.3        |
| Trade                               | 4.4         | 5.1        | 0.6        |
| Other Services                      | 3.4         | 4.6        | 1.3        |
| Taxes                               | <b>3.3</b>  | <b>9.5</b> | <b>0.6</b> |
| <b>GDP at market prices</b>         | <b>4.7</b>  | <b>4.0</b> |            |
| GDP w/o agriculture and binationals | <b>2.8</b>  | <b>4.9</b> |            |

(f) Forecast. (i) Incidence

Source: Central Bank of Paraguay

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

|                                      | 2023 (f)    | 2024 (f)    |
|--------------------------------------|-------------|-------------|
| <b>GDP</b>                           | <b>4.7</b>  | <b>4.0</b>  |
| <b>Domestic demand</b>               | <b>-1.7</b> | <b>5.5</b>  |
| Gross fixed capital formation        | -3.5        | 5.8         |
| Total consumption                    | 2.9         | 4.7         |
| Private consumption                  | 2.7         | 4.7         |
| Public consumption                   | 3.6         | 4.8         |
| <b>Exports of goods and services</b> | <b>36.7</b> | <b>0.4</b>  |
| <b>Imports of goods and services</b> | <b>14.1</b> | <b>4.1</b>  |
| <b>Current account (% of GDP)</b>    | <b>0.2</b>  | <b>-3.2</b> |

(f) Forecast.

Source: Central Bank of Paraguay

**Table C. Inflation projection. Annual change, percent.**

|  | 2023       | 2024(f)    | 2025(f)    | 2026(f)    |
|--|------------|------------|------------|------------|
| December CPI inflation (*)                   | <b>3.7</b> | <b>4.0</b> | <b>4.0</b> |            |
| CPI inflation around 2 years (**)            |            |            |            | <b>4.0</b> |
| December underlying CPI (*)                  | <b>3.2</b> | <b>4.0</b> | <b>4.0</b> |            |
| Underlying CPI inflation around 2 years (**) |            |            |            | <b>4.0</b> |

(f) Forecast includes data as of September 2024.

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

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

Source: Central Bank of Paraguay