

Macro scenario - Paraguay



July 23, 2024

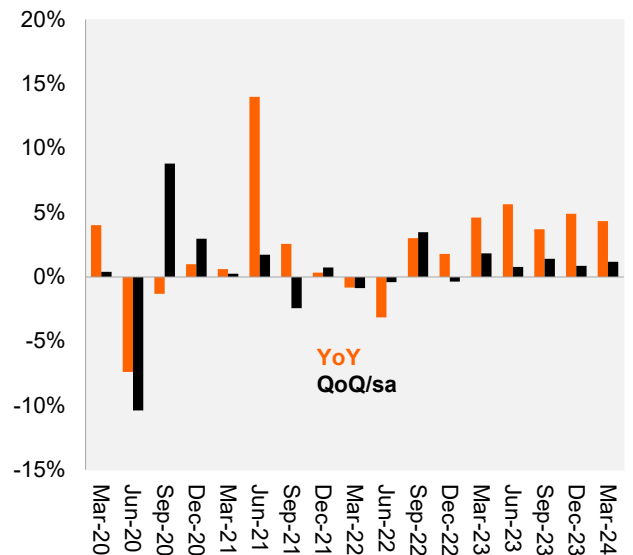
Raising growth

- ▶ We revised our 2024 GDP growth forecast up to 4.0%, from 3.5% in our previous scenario, due to a higher statistical carryover from 1Q24's GDP and a stronger-than-expected start to 2Q24.
- ▶ We now expect inflation to end 2024 at 4.3%, up from 4.0% in our previous scenario, driven by a weaker currency. In fact, we revised our YE24 nominal exchange-rate forecast to 7,600 PYG/USD from 7,500 PYG/USD in our previous scenario.
- ▶ In the context of a better outlook for economic activity and slightly higher inflation, we maintained our terminal rate forecast at 6.00% by YE24.

GDP expanded in 1Q24 and at the beginning of 2Q24

Activity expanded in 1Q24. GDP rose by 4.3% yoy in 1Q24 (IMAEP +3.9% yoy), down from 4.9% in 4Q23. Looking at the breakdown on the supply side, the annual print was influenced by the positive performance in manufacturing (5.5% yoy) and services (+5% yoy), and, to a lesser extent, electricity and water (+0.8% yoy) and agriculture (0.4% yoy). On the other hand, the negative performance of construction (-2.1% yoy) mitigated the favorable economic activity. At the margin, using our seasonally adjusted series, GDP rose by 1.2% quarter over quarter in 1Q24. On the demand side, internal demand increased by 3.2% yoy in 1Q24 (from -0.3% in 4Q23), supported mainly by consumption, rising by 4.7% yoy (from 2.1% 4Q23), while gross fixed capital formation expanded 3.4% yoy (from -0.2% in 4Q23). Finally, exports of goods and services, especially soybean exports, rose by 8.2% due to higher sales of goods, while imports of goods and services increased by 5.1% due to an increase in imports of machinery and equipment, fuels and lubricants and iron products. **Leading indicators point to strong activity for 2Q24.** Using the central bank's seasonally adjusted series, the monthly GDP proxy (IMAEP) expanded in April and May, leading to a 0.7% qoq/sa increase in May (down from 1.7% qoq/sa in 1Q24). On an annual basis, the IMAEP increased by 2.8% yoy in the quarter ending in May (from 6.9% in 1Q24).

GDP

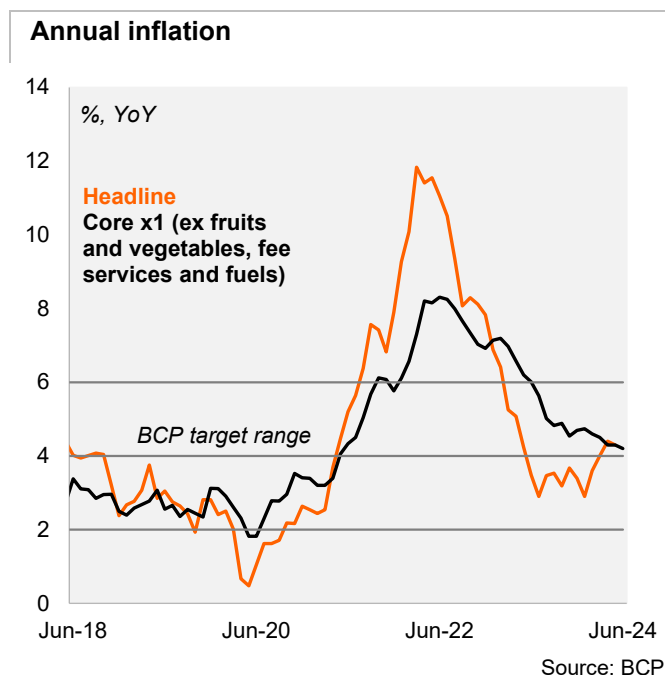


Source: BCP, Itaú

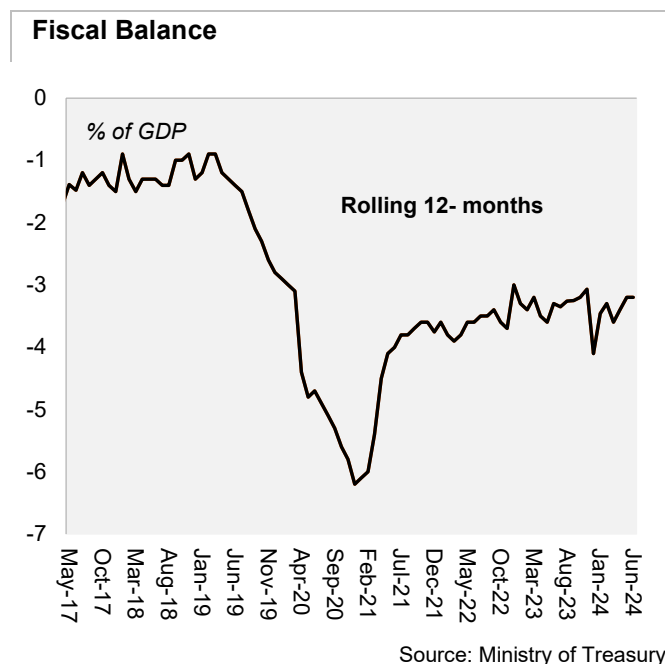
Lower-than-expected inflation in June due to the reversal of volatile prices

CPI fell by 0.4% MoM in June (from -0.3% a year ago), below our forecast (0.1%) and well below the market consensus of 0.4% (according to the BCP survey). Downside pressure came mainly from volatile prices, in particular fruits and vegetables (8.2% MoM; contribution of -0.5 pp) and fuels (-0.1% MoM), which were affected by the reduction of domestic diesel prices. Core CPI x1 (excludes fruits and vegetables, regulated service prices and fuel) stood at 0.1% (from 0.2% a year ago). On an annual basis, headline inflation fell slightly to 4.3% in June (from 4.4% in

May), while core X1 CPI declined to 4.2% from 4.3%. We note headline and core remain within the tolerance band of the BCP’s inflation target (4% +/- 2%).



On the other hand, primary expenditures increased by 6.8% yoy in real terms in 2Q24 (-4.4% yoy in 1Q24), led by the increased in expenditure on goods and services (47.5% in the period).



No rate changes in sight

The central bank’s monetary policy committee decided to maintain the policy rate at 6.00% in June, as widely expected. The committee once again highlighted that the recent rise in inflation is primarily driven by volatile prices in the basket of goods and, therefore, should reverse later this year. Additionally, the BCP highlighted that the risks stemming from the external environment have diminished since the previous monetary policy meeting. While the BCP mentioned that inflation expectations remain around 4.0% across all surveyed horizons, we noted that the statement no longer included the sentence that claimed the monetary policy rate stands around the neutral range. In our view, the level of the policy rate remains contractionary at 2.00% (using expectations for the monetary policy horizon), compared with the BCP’s neutral real-rate range of 0.4%-1.4%.

Fiscal consolidation remains on track

Tax revenues rose materially in 2Q24. The estimated 12-month cumulative fiscal deficit remained at 3.2% of GDP in June, unchanged from May, yet well below the 4.1% of December 2023. This represents a positive development toward fiscal consolidation. Tax revenues rose by 25.4% YoY in real terms in 2Q24 (14.2% yoy in 1Q24), in line with the improvement in economic activity.

Better activity outlook

We revised our 2024 GDP growth forecast upward to 4.0%, from 3.5% in our previous scenario.

A high statistical carryover from 1Q24 (2.7%) and the solid performance of leading indicators in 2Q24 support our call.

We revised our YE24 nominal exchange-rate forecast to 7,600 PYG/USD from 7,500 PYG/USD in our previous scenario, due to a stronger global USD and a weaker BRL. The central bank has intervened in periods of exchange-rate volatility.

We revised our year-end inflation forecast upward to 4.3%, from 4.0% in our previous scenario, despite the downside surprise in June. While a weaker currency led us to revise our call, we still expect a deceleration of monthly inflation in 2H24 (against 1H24).

We maintain our YE24 monetary policy rate forecast at 6.00%. In our view, persistent global economic uncertainty and upside pressure on inflation (amid a slightly weaker currency) will prompt the central bank to leave its policy rate unchanged for the rest of the year.

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Paraguay | Forecasts and Data

	2019	2020	2021	2022	2023	2024F		2025F	
						Current	Previous	Current	Previous
Economic Activity									
Real GDP growth - %	-0.4	-0.8	4.0	0.2	4.7	4.0	3.5	4.0	4.0
Nominal GDP - USD bn	38.8	36.1	40.3	42.1	44.7	47.2	46.9	49.8	50.4
Unemployment Rate - year avg	6.6	7.7	7.5	6.8	5.9	6.0	6.0	6.0	6.0
Inflation									
CPI - %	2.8	2.2	6.8	8.1	3.7	4.3	4.0	4.0	4.0
Interest Rate									
Reference rate - eop - %	4.00	0.75	5.25	8.50	6.75	6.00	6.00	5.50	5.50
Balance of Payments									
PYG / USD - eop	6465	6912	6877	7340	7275	7600	7500	7700	7600
Trade Balance - USD bn	0.5	1.5	1.0	-1.3	1.6	0.9	1.2	0.9	0.9
Current Account - % GDP	-0.6	1.9	-0.9	-7.1	0.7	0.0	0.6	0.1	0.1
Net Foreign Direct Investment - % GDP	1.4	0.4	0.2	1.7	1.0	2.0	2.0	2.0	2.0
International Reserves - USD bn	7.7	9.5	9.9	9.8	10.2	11.0	11.0	11.0	11.0
Public Finances									
NFPS Nominal Balance - % GDP	-2.9	-6.1	-3.6	-3.0	-4.1	-2.6	-2.6	-1.9	-1.9
NFPS Debt - % GDP	22.9	33.8	33.8	35.8	38.2	40.0	40.0	38.1	38.1

Source: FMI, Haver, Bloomberg, BCP, Itaú.

Macro Research – Itaú

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