

# Macro scenario - Paraguay



April 19, 2024

## Time for a pause?

- ▶ In light of our call for the Federal Reserve to begin the easing cycle towards the end of the year, combined with rising oil prices, the central bank is likely to adopt a more cautious approach. Consequently, we revised our terminal monetary policy rate call up slightly to 5.75%, from our previous estimate of 5.50%, in line with similar adjustments elsewhere in the region.
- ▶ We still envisage inflation at 4.0% by year-end 2024, in spite of volatile inflation in 1Q24. Higher inflationary risks from oil spot prices, amid elevated geopolitical uncertainty, could lead to an upward adjustment to our inflation forecast.
- ▶ Our 2024 GDP growth projection remains at 3.5%. However, recent leading indicators suggest robust growth in 1Q24, introducing upside risks to our forecast.

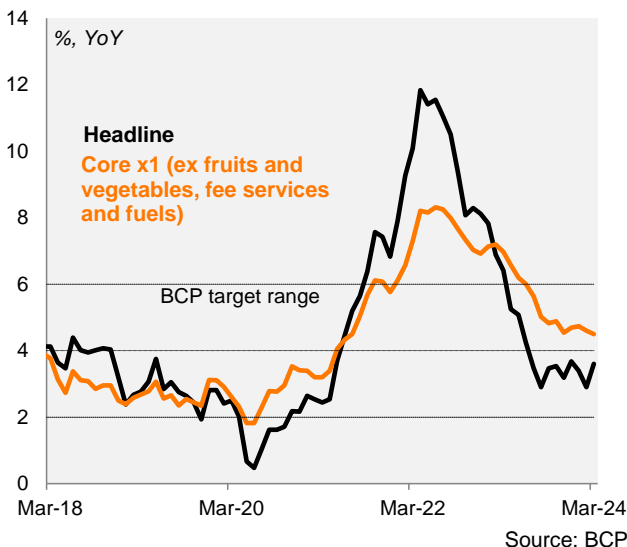
## Volatile inflation in 1Q24

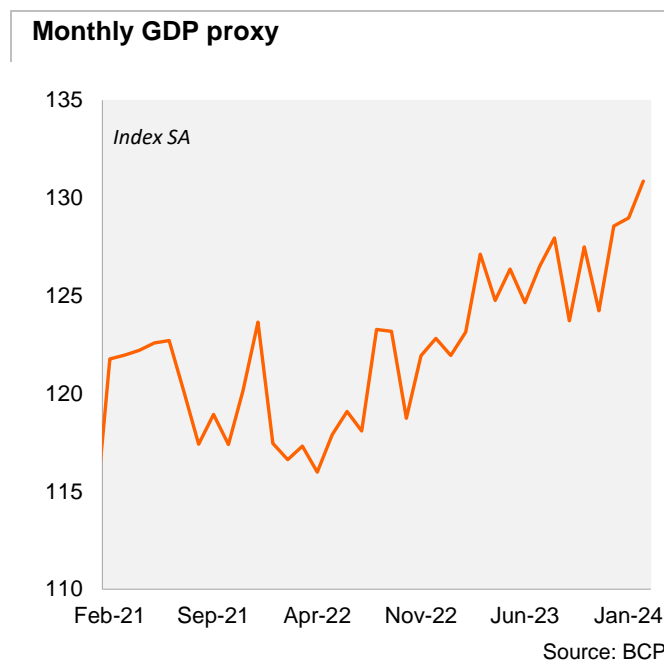
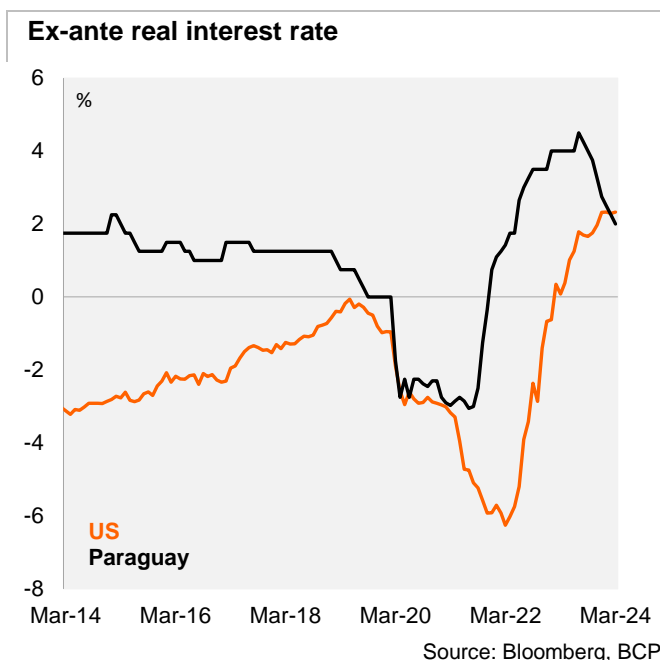
**CPI surprised to the upside in March, rising by 1.1% mom (from 0.4% a year ago).** The upside pressure mainly stemmed from an increase in fuel prices (5.7% mom), amid higher spot oil prices. Core CPI X1 (which excludes fruits and vegetables, regulated services and fuel) was 0.4% (from 0.5% a year ago). On an annual basis, headline inflation rebounded to 3.6% in March (up from 2.9% in February), while core CPI X1 was 4.5% (down slightly from 4.6% in the previous month). Despite the upside surprise, both headline and core annual inflation remain inside the central bank's target range of 2%-6%.

## BCP maintains an easing bias, but external headwinds emerge

**The board of the Central Bank of Paraguay (BCP) unanimously cut the policy rate by 25 bps to 6.00% in March, repeating the pace for the third consecutive monthly meeting.** The decision was in line with our call and market expectations as per the BCP survey. This brought the BCP's easing cycle to a cumulative 250 bps in cuts since August 2023. The BCP highlighted that domestic inflation and expectations provide room to continue gradually moving toward monetary normalization. In our view, the level of the policy rate remains contractionary, with the real ex-ante policy rate following the decision at 2.00% (using expectations for the monetary policy horizon), compared with the BCP's neutral real-rate range of 0.4%-1.4%. However, we noted that the level of the ex-ante real interest rate is similar to the U.S., using inflation expectations for the next twelve months that are posing headwinds to additional sizable cuts.

### Annual inflation





### Activity gains momentum

**Activity rose sequentially in February for the third consecutive month.** Using the central bank’s seasonally adjusted series, the monthly GDP proxy (IMAEP) expanded by 1.5% mom/sa in February, bringing growth to a solid 3.4% qoq/sa (up from +0.6% qoq/saar in 4Q23). On an annual basis, the IMAEP increased by 5.5% in the quarter ending in February (from 4.1% in 4Q23). The monthly GDP proxy excluding agriculture and utilities increased by 3.3% qoq/sa and 5.8% yoy in the quarter ending in February. According to the statement, all sectors expanded in February, with the exception the energy sector.

### Fiscal balance improved in 1Q24

**The estimated 12-month cumulative fiscal deficit narrowed to 3.6% of GDP in March, down from a peak of 4.1% in December 2023.** This represents a positive development toward fiscal consolidation. Tax revenues rose by 14.2% YoY in real terms in 1Q24 (-3.4% yoy in 4Q23), in line with the strong activity and likely helped by lower expenditures abroad due to the appreciation of the parallel exchange rate in Argentina. On the other hand, primary expenditures fell by 4.4% yoy in real terms in 1Q24, led by lower capital expenditures (+18.4% in 4Q23 after the regularization of debts with the construction and pharmaceutical sectors).

### We now expect a pause in the easing cycle

**In our view, several factors play in favor of a pause in the easing cycle.** A new delay in the beginning of the Fed’s easing cycle, higher oil spot prices and volatile domestic inflation in 1Q24 should lead the central bank to pause its easing cycle in the April 22 monetary policy meeting. We revised our terminal monetary policy rate up to 5.75%, from 5.50% in our previous scenario, in line with our adjustments for the rest of the countries in the region.

**We still maintain our year-end inflation forecast of 4.0%, in spite of an upside surprise in March.** We noted that monthly inflation was volatile in 1Q24, and higher oil prices, amid elevated geopolitical uncertainty, pose upside risks to our year-end inflation forecast.

**We still project 3.5% GDP growth this year, but now with risks tilted to the upside.** Leading indicators such as monthly GDP proxy and tax collection point to strong growth in 1Q24, supporting our upside bias.

**Andrés Pérez M.**  
**Diego Ciongo**

## Paraguay | Forecasts and Data

	2018	2019	2020	2021	2022	2023	2024F		2025F	
							Current	Previous	Current	Previous
<b>Economic Activity</b>										
Real GDP growth - %	3.2	-0.4	-0.8	4.0	0.2	4.7	<b>3.5</b>	3.5	<b>4.0</b>	4.0
Nominal GDP - USD bn	40.7	38.8	36.1	40.3	42.1	44.7	<b>47.7</b>	47.6	<b>50.8</b>	50.7
Unemployment Rate - year avg	6.2	6.6	7.7	7.5	6.8	5.9	<b>6.0</b>	6.0	<b>6.0</b>	6.0
<b>Inflation</b>										
CPI - %	3.2	2.8	2.2	6.8	8.1	3.7	<b>4.0</b>	4.0	<b>4.0</b>	4.0
<b>Interest Rate</b>										
Reference rate - eop - %	5.25	4.00	0.75	5.25	8.50	6.75	<b>5.75</b>	5.50	<b>5.50</b>	5.50
<b>Balance of Payments</b>										
PYG / USD - eop	5964	6465	6912	6877	7340	7275	<b>7400</b>	7400	<b>7500</b>	7500
Trade Balance - USD bn	0.8	0.5	1.5	1.0	-1.3	1.6	<b>1.2</b>	1.2	<b>0.9</b>	0.9
Current Account - % GDP	-0.2	-0.6	1.9	-0.9	-7.1	0.7	<b>0.6</b>	0.6	<b>0.1</b>	0.1
Net Foreign Direct Investment - % GD	0.6	1.4	0.4	0.2	1.7	1.0	<b>2.0</b>	2.0	<b>2.0</b>	2.0
International Reserves - USD bn	8.0	7.7	9.5	9.9	9.8	10.2	<b>11.0</b>	11.0	<b>11.0</b>	11.0
<b>Public Finances</b>										
NFPS Nominal Balance - % GDP	-1.3	-2.9	-6.1	-3.6	-3.0	-4.1	<b>-2.6</b>	-2.6	<b>-1.9</b>	-1.9
NFPS Debt - % GDP	19.8	22.9	33.8	33.8	35.8	38.2	<b>40.0</b>	40.0	<b>38.1</b>	38.1

Source: FMI, Haver, Bloomberg, BCP,

## Macro Research – Itaú

## Mario Mesquita – Chief Economist

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