THE WEEK

AT A GLANCE

ECONVIEWS

ECONOMÍA Y FINANZAS

March 18th 2024

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Editorial: The First 100 Days: Test Passed With Merit

The first 100 days of Milei's government have already passed. An experiment for the Argentine political system. As has already been demonstrated in this short time, politics is precisely the weakest link in Milei's management. The main figures in the government have no experience in the public sector and the establishment also has to get used to a new form of communication and politics that Milei imposes.

In the economy things are much better, although the challenges ahead are not minor. The Central Bank has already purchased 10 billion dollars since December 13. It is true that imports are restricted and there may have been some progress in exports, but it is not an achievement to ignore. Now the Central Bank has negative reserves of 3 billion dollars, so it could go positive in April or perhaps May. Thumbs up on this matter.

In the fiscal area, there was an unmistakable signal of austerity. Once again, we look cautiously at the good data for January and February because part of this is payment deferrals. Furthermore, the part consumed by inflation has to be reduced by pure mathematics: if inflation is lower, the opportunity to reduce liabilities decreases. We believe that it will be difficult to reach a primary surplus of 2 points of GDP, but that a primary balance is possible. And even more so, we believe that the market will buy Argentina if that result is reached. If that happens, our scenario is a country risk of around 800 basis points.

The structural reform agenda is ambitious, but essential. We already saw that the battle will not be easy. The justice system has already blocked part of the labor reforms. But it will be very important that in the coming months we begin to see deregulations and simplifications. Many of them will not have a macroeconomic impact, but they will have a sectoral or regional impact. For example, the release of commercial flights with Brazil that was announced this week is a step forward for the sector. There are thousands of items to simplify at all levels.

The challenges are many. Regarding macroeconomics, we highlight two. In the very short term, it will be necessary to seek an exchange rate policy that avoids excessive strengthening of the peso. The Argentine economy is still weak to support a strong peso and public opinion may not have patience if the solution is a discrete jump at some point in the second quarter when the recovery of activity has yet to begin or has just begun. The exchange architecture will have to take into account the removal of exchange restrictions, at least as we know it now.

In the medium term, some stabilization plan has to appear. The fiscal policy can be very good, but that will lead to a very slow decline in inflation. A kind of "regime change" is needed. We believe that around the end of the year may be the time.

Social issues and public opinion are also important challenges. The recession exacerbated the poverty problem Milei inherited. It will be important for the economy to bottom out in the coming weeks. We believe this will be the case, but it may fail. Public opinion seems to accept the decline in activity quite well, but there are no guarantees that support will continue until the recovery is more noticeable.

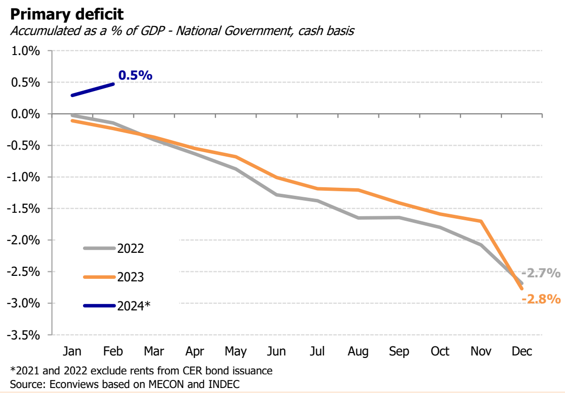
In short, the first 100 days show many more successes than failures. Even more so being a government without management experience. Now the easy fiscal and exchange gains are coming to an end, so the economic team will have to roll up its sleeves. If the government reaches an agreement with the governors and a reasonably achievable May Pact, although not perfect, that may be the signal to increase the probability that many projects will be unblocked. The interest of potential investors is real. There were more visits in these 100 days than in the previous 3 years. And no one expects perfection. A dignified negotiation can be the key to a new Argentina.

LAST WEEK IN REVIEW

The fiscal result for February was a surplus. The primary balance was ARS 1,232,525 million, while the financial balance was ARS 338,112 million. It is the second consecutive month with a positive result.

Total revenues fell 6.3% year-on-year in real terms, but this was offset by a **larger drop in primary spending, of 36.4%.**

The **accumulated primary result for 2024** is ARS 3,243,270 million, **0.5% of the estimated GDP.**



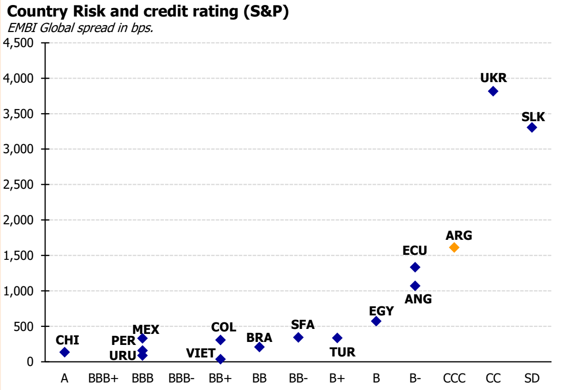
Primary deficit
Accumulated as a % of GDP - National Government, cash basis

*2021 and 2022 exclude rents from CER bond issuance
Source: Econviews based on MECON and INDEC

S&P Global Ratings raised Argentina's rating to "CCC" (Stable Outlook) from CCC-. The previous day the rating agency had taken the long-term debt to Selective default, a technicality that is used for only one day each time there is a debt swap.

The agency argues that CCC's rating "reflects the Government's modestly better liquidity position."

The country risk fell to 1.604 last Friday.

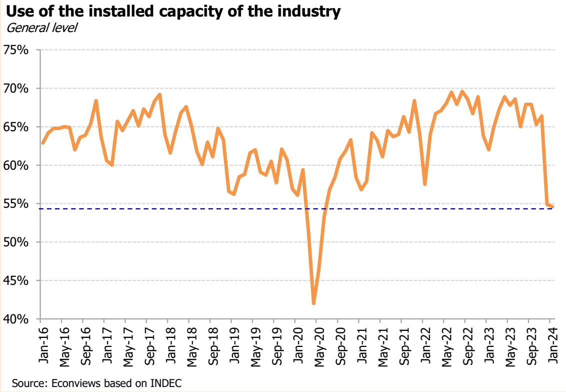


Country Risk and credit rating (S&P)
EMBI Global spread in bps.

In January, the utilization of the industry's installed capacity was 54.6%, vs. 62% in January 2023 (-7 p.p.). **This percentage represents the lowest level of use since the indicator was created**, excluding the most critical months of the pandemic (March to June 2020).

Petroleum refining (83.5%) and basic metal industries (76.3%) are well above the average. Both industries also had a reduction compared to the previous year, when their levels reached 84.1% and 81.7%.

The segment with the **greatest contraction** was **Chemical Substances and Products** (-15 p.p. compared to January 2023).



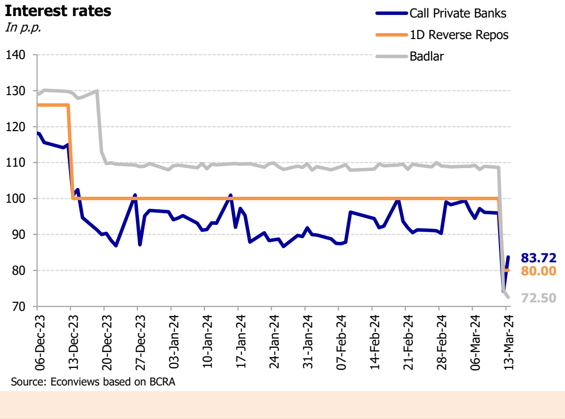
Use of the installed capacity of the industry
General level

Source: Econviews based on INDEC

Last Monday, **the BCRA ordered a reduction in the monetary policy rate from 100% to 80% nominal annual rate.** The effective value of the annual rate was 122.4% (vs. 171.5% previously) or 6.79% monthly (vs. 8.55% previously).

The elimination of the minimum time deposits rate was also established. Until now, banks were required to guarantee a minimum rate of 110%. The Badlar remained between 70-75% the following days.

According to the BCRA, this decision was based on the **slowdown in inflation, monetary contraction** in real terms, the **accumulation of reserves** and the **stability of parallel dollars.**



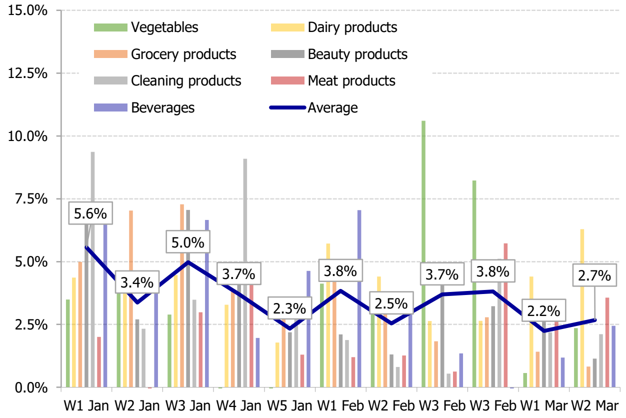
Interest rates
In p.p.

Source: Econviews based on BCRA

WEEKLY INFLATION

Inflation rate - high frequency data

Weekly price variation in major supermarkets in Great Buenos Aires



Note: The variations are based on the average price per week, from Friday to Thursday.
Source: Econviews based on own estimates

NEXT WEEK'S HIGHLIGHTS

✓ On **Tuesday 19**, INDEC publishes its **construction cost index and wholesale price indices** corresponding to February.

✓ On **Tuesday 19**, INDEC will also announce the **Argentine trade exchange** for February.

✓ On **Wednesday 20**, the **rates and socioeconomic indicators of the INDEC labor market** corresponding to the fourth quarter of 2023 will be published.

✓ On **Thursday 21**, the results of the January INDEC **surveys of supermarkets, wholesalers and shopping malls** will be announced.

✓ On **Friday 22**, the results of the **hotel occupancy survey** carried out by INDEC in the month of January will be published.

Market dashboard

Weekly, monthly and yearly variations

	Last data	w/w	m/m	y/y	
Official exchange rate ARS/USD	850.8	0.5%	1.9%	320.1%	↑
MEP	1026.8	2.1%	-6.2%	168.9%	↑
Blue Chip Swap	1065.6	1.7%	-7.7%	170.4%	↑
Parallel	1005.0	3.1%	-4.7%	168.0%	↑
Official exchange rate BRL/USD	5.0	0.3%	0.5%	-5.5%	↑
CB reserves (USD million)	28,203	-18	+1,562	-9,580	↓
Policy rate (Leliq)	80.0%	-20.00 p.p.	-20.00 p.p.	+5.00 p.p	↓
Badlar rate (private banks)	72.5%	-36.44 p.p.	-37.13 p.p.	+1.94 p.p	↓
Private Deposits (trillion ARS)	41.5	-1.2%	5.3%	134.7%	↓
Private Loans (trillion ARS)	17.9	-3.3%	5.0%	140.9%	↓
Merval (in ARS)	1,066	6.4%	-2.5%	408.2%	↑
Merval (in USD)	1,001	4.6%	5.6%	88.0%	↑
Country Risk (spread in %)	1,604	-4.9%	-12.8%	-32.9%	↓
Soybean (USD/tn)	440.3	2.4%	3.1%	-19.5%	↑
Corn (USD/tn)	171.9	2.5%	4.5%	-30.3%	↑
Wheat (USD/tn)	194.2	0.3%	-6.8%	-24.8%	↑
Oil - Brent (USD/barrel)	86.4	0.6%	-0.6%	19.6%	↑
Oil - WTI (USD/barrel)	81.9	3.8%	4.4%	21.6%	↑
LNG (USD/MMBTU)	8.6	0.0%	-9.5%	-36.3%	=
Gold (USD/oz.)	2,156.8	-1.0%	7.6%	12.4%	↓

Note: arrow depends on weekly variation

Stoplight for Economic Activity

Seasonally adjusted variations

		m/m	q/q	LD vs previous Q	
Industrial production	*Jan-24*	-1.3%	-6.7%	-7.0%	🔴
Automobile production	*Feb-24*	-4.7%	-12.6%	-7.2%	🔴
Steel production	*Feb-24*	-5.0%	-5.5%	6.5%	🟢
Poultry production	*Jan-24*	4.2%	-2.4%	0.4%	🟡
Dairy production	*Jan-24*	-4.3%	-5.9%	-6.4%	🔴
Beef production	*Feb-24*	-0.2%	-4.1%	2.8%	🟢
Real Estate transactions (CABA)	*Jan-24*	-3.8%	-12.7%	-11.8%	🔴
Flour Production	*Jan-24*	1.5%	-0.8%	-3.4%	🔴
Oil production	*Jan-24*	2.3%	4.9%	4.0%	🟢
Gas production	*Jan-24*	-9.8%	-8.6%	-10.6%	🔴
Cement production	*Feb-24*	-5.8%	-12.3%	-7.7%	🔴
Construction activity	*Jan-24*	-10.2%	-11.6%	-16.6%	🔴
Gas sales	*Jan-24*	-0.1%	-4.8%	-5.0%	🔴
Motorcycle licenses	*Feb-24*	2.9%	-8.3%	-7.5%	🔴
Use of electricity	*Jan-24*	0.6%	-3.3%	-1.4%	🔴
Subway rides (CABA)	*Dec-23*	-8.0%	-17.5%	-12.2%	🔴
Imports CIF	*Jan-24*	-1.7%	-10.9%	-7.2%	🔴
Exports FOB	*Jan-24*	9.4%	2.8%	12.5%	🟢
Loans in ARS to private sector	*Feb-24*	-1.1%	-26.1%	-16.5%	🔴
VAT-DGI Revenues	*Feb-24*	7.2%	-10.8%	-0.7%	🔴
Formal private jobs (SIPA)	*Nov-23*	-0.7%	0.3%	-0.5%	🟡
Formal private jobs (EIL)	*Dec-23*	-0.4%	-0.1%	-0.5%	🟡
Consumer confidence	*Feb-24*	1.2%	-18.1%	-12.0%	🔴
Government confidence	*Feb-24*	-1.5%	119.7%	12.1%	🟢

Note: stoplight color depends on last month vs previous quarter variation

Is Monetary Policy Tight or Loose?

- *The monetary base is falling in real terms and that suggests a restrictive policy.*
- *At the same time, the BCRA has already lowered the interest rate twice, a sign that goes in the opposite direction.*
- *We think that the real interest rate has to be positive in a scenario where exchange market restrictions are lifted.*

From the discursive point of view, Milei always emphasized the importance of having a strict monetary policy, limiting the growth of the monetary base, and not financing the Treasury with money issuance to control inflation. **But does this imply a contractionary monetary policy?** The answer is not entirely obvious since there are some contractionary biases, but there are also others that look expansionary.

If we look at the monetary base, we could quickly answer that we are under a restrictive policy. So far in Santiago Bausili's administration, the monetary base has grown 6.9% in nominal terms, which means that it has practically remained constant. Adjusting for the accumulated inflation in this period, the fall in real terms exceeds 37% (see graph 1).

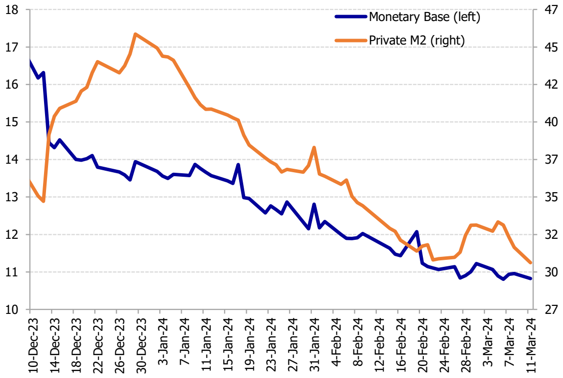
Aiming to maintain the monetary base constant, the Central Bank uses reverse Repos and the Bopreal as absorption tools, while the Treasury also sterilizes pesos through debt buybacks, depositing the pesos in the BCRA (see graph 2). However, it must be considered that the Bopreal aid will disappear when the last series is finished being tendered. It is also not obvious that the Treasury will continue to have financial surpluses to buy back debt.

These three instruments serve to neutralize the money issuance that is being generated by the purchase of dollars in the market, the payment of interest on Repos, the repayment of Lediv, and the intervention of the Central Bank in the secondary market (whether direct or indirect). In any case, Repos' interests are almost automatically sterilized with new Repos, so in practice, it is not a monetary base growth factor.

This is not the first time that a monetary policy where the amount of money is controlled has been carried out. In 2018, when Guido Sandleris took the presidency of the Central Bank, he established a target of zero growth of the monetary base, with exceptions for June and December when the seasonality of demand is higher. Taking the initial period from October 2018 to June 2019, the objective was exceeded. At the same time, inflation showed some decline. Taking the three-month moving average of monthly inflation, when this policy started it was 5.3% and at the end, it was 3.1%. Year-on-year inflation continued to rise until May 2019 and from then on it began to decline. **That is**

Graph 1. Monetary Base & Private M2

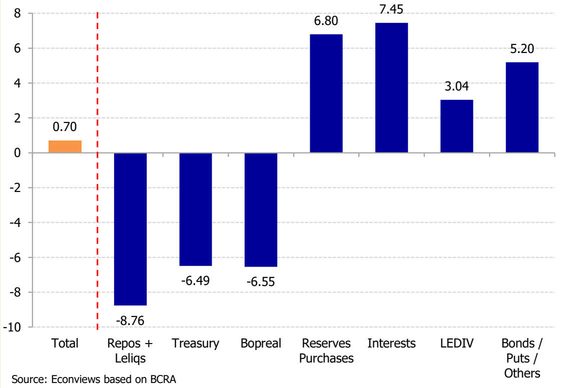
In trillion ARS of Mar-24



Source: Econviews based on BCRA

Graph 2. Monetary Base - Factors of Variation

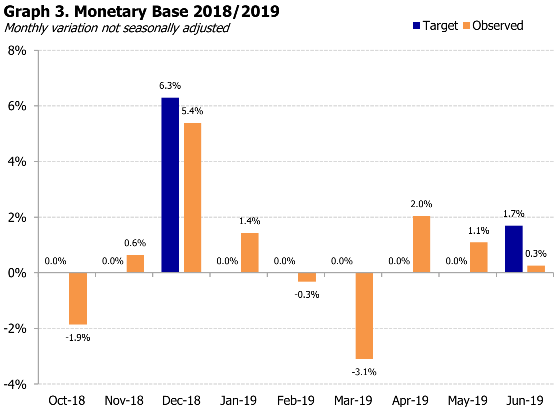
In trillion ARS - Accumulated from Dec-11 up to Mar-11



Source: Econviews based on BCRA

Graph 3. Monetary Base 2018/2019

Monthly variation not seasonally adjusted



Source: Econviews based on BCRA

to say, there was some improvement, although it took time and was not very significant.

An important difference between both “zero emissions” is that in the Sandleris period, real interest rates were high and positive, while current rates remain well below inflation.

Indeed, if we look at current interest rates, we could say that monetary policy is expansionary. In this sense, one of the first measures of the new authorities of the BCRA was to lower the monetary policy rate from 133% to 100%, something that it did again on Monday of last week when it took it to 80%, which is equivalent to a 122.4% effective rate (see graph 4). In other words, this is a period of negative real rates.

It is not clear what the purpose of the latest reduction was. One option is that the idea is to continue reducing the BCRA's liabilities in real terms, and given that inflation is falling, they are accompanying this decline with lower interest rates.

We estimate that between the fourth quarter of last year and the first one of this year, the stock of interest-bearing liabilities fell from 9.3 to 8.3% of GDP (see graph 5). In the four months from December 2023 to March 2024, the reduction in real terms reaches 22%. Now that inflation is lower compared to the peaks of previous months, a lower rate is needed to be able to continue reducing this debt. **In line with this fact, another thing that may have influenced the lowering of rates is that less will have to be issued to pay the interest on remunerated liabilities and that makes the snowball grow more slowly.**

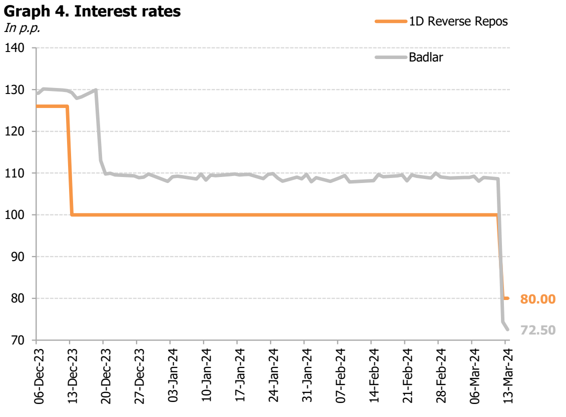
Another argument is that the reduction in the interest rate is justified because markets like Rofex “priced” a reduction in rates, so what the Central Bank did is simply validate that reduction. **This reasoning has a problem, and that is that central banks are the ones that, through their decisions, determine the time structure of interest rates and not the other way around.** The market determines rates based on what it expects the BCRA will do with the exchange rate and the monetary policy rate.

This is not the only hypothesis. Making peso investments less attractive can generate a rise in parallel exchange rates. It is much more difficult to know if this is what the government sought, but we do know that a higher BCS makes the blend through which exports are settled more competitive. What we think is that, if the objective was to increase the Blue-Chip Swap, it could have been achieved by making the exchange market restrictions more flexible, for example, by increasing the daily limit to buy BCS, or allowing operations to be carried out in this way without losing access to the MULC.

Other possibilities are that efforts are being made to encourage consumption through a lower cost of financing or also to limit the carry trade of exporters.

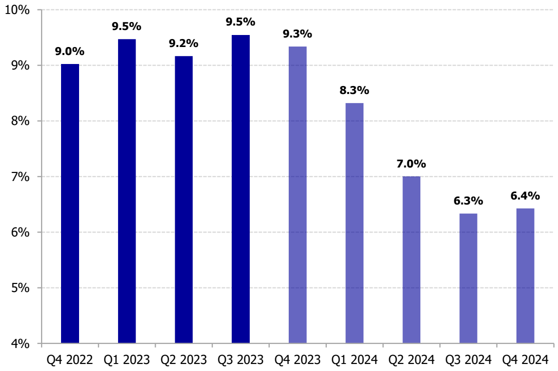
As we see, there is no single explanation. What we do believe is that this scheme of financial repression with such negative interest rates cannot be maintained when exchange market restrictions are lifted. At that moment the

Graph 4. Interest rates
In p.p.



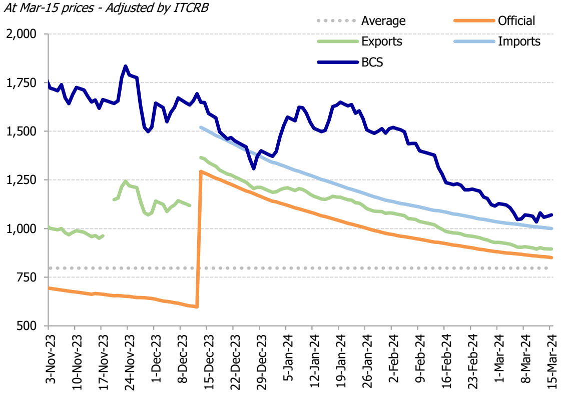
Source: Econviews based on BCRA

Graph 5. Stock of BCRA's interest bearing liabilities
Average - As % of quarterly GDP



Source: Econviews based on BCRA & own estimates

Graph 6. Exchange rate at constant prices
At Mar-15 prices - Adjusted by ITCRB



Source: Econviews based on BCRA

interest rate will have to be higher than inflation and thus encourage the demand for pesos. The IMF was always in favor of maintaining positive real rates and in the last review it made it very clear. **This is one more reason to think that monetary policy should follow this path in the future.**

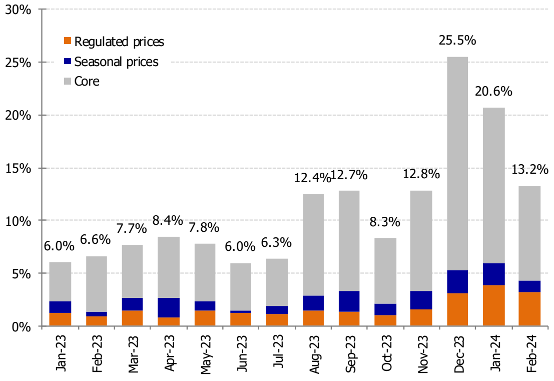
Inflation Is Slowing Down, Mostly in Goods Due to the FX Peg

- *February's CPI print came in at 13.2% monthly and 276.2% year-on-year; the price of services (+17.6%) is increasing much faster than goods (+11.9%).*
- *The dynamics of goods inflation is positive: the diffusion and frequency of increases is falling, although in the second week of March they accelerated slightly.*
- *The adjustment in regulated prices is going ahead in public transportation, gasoline and healthcare, while education, telecommunications or gas are still lagging the general CPI.*

February's inflation came in at 13.2%. In the last twelve months, the Consumer Price Index increased 276.2%. The government celebrated the figure for being below the 15% estimate from private consulting firms and Javier Milei himself, who demonstrated his ability to manage expectations. It was the second consecutive month of slowdown, and the core CPI was slightly lower, 12.3%. On the negative side, we are back at November 2023's print and lost 11 points of purchasing power along the way. It must also be said that the government is stepping on the real exchange rate to try to keep inflation in check.

Beyond the number, the drivers of inflation are not the same as in November (see table 1). The December devaluation's pass-through to prices has been largely absorbed. Between December 15 and January 15, the wholesale price of imported goods rose only 5.1% (February's print comes out on Monday). With adjustments in public services, private healthcare and telecommunications (coming up next is education) and a weak recovery in wages, **now inflation in services (+17.6%) is running ahead of inflation in goods (+11.9%)**. In addition to the variation, the dynamics of goods' inflation has other two positive highlights.

Graph 1. Monthly inflation
Contribution of each category



Source: Econviews based on INDEC

Chart 1. Inflation in November 2023 and February 2024
Monthly variation by category

	Nov-23	Feb-24
General CPI	**12.8%**	**13.2%**
Goods	13.8%	11.9%
Services	10.2%	17.6%
Food and non-alcoholic drinks	15.7%	11.9%
Alcohol and tobacco	11.8%	17.7%
Apparel	10.0%	7.2%
Housing and utilities	7.1%	20.2%
Home equipment	12.4%	10.3%
Healthcare	15.9%	13.6%
Transport	10.4%	21.6%
Communication	15.2%	24.7%
Recreation and culture	13.2%	8.6%
Education	8.3%	9.9%
Restaurants and hotels	12.0%	11.2%

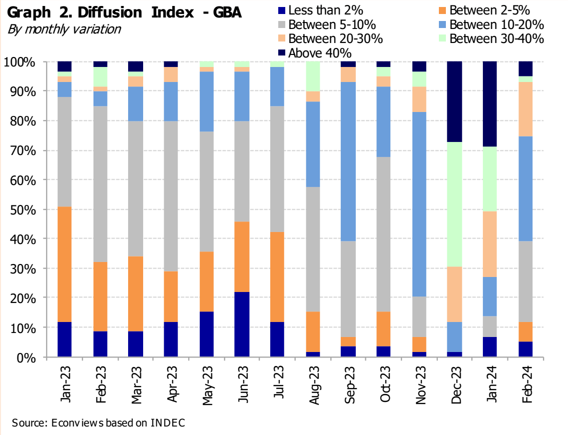
Source: Econviews based on INDEC

Price increases are less widespread. Of a basket of 59 basic products in GBA, in November almost two-thirds (63%) rose between 10 and 20% monthly. In February, only a third (36%) increased at that rate. Another third was below that, with single-digit variations (mostly meats), and another third above that. The increases of more than 30% seen in December and January were diluted (except in fruits and vegetables).

The frequency of price increases also decreased. Our online survey of more than 300 products in GBA supermarkets shows that on average, the price of each product changed only once in February. In January it had been closer to 2. In November and December it ranged between 2 and 3, and some goods adjusted their price up to 8 times in a single month. There is no direct correlation, but the frequency and percentage of increases usually go hand in hand. For now, the first half of March shows a rate of increases similar to that of February.

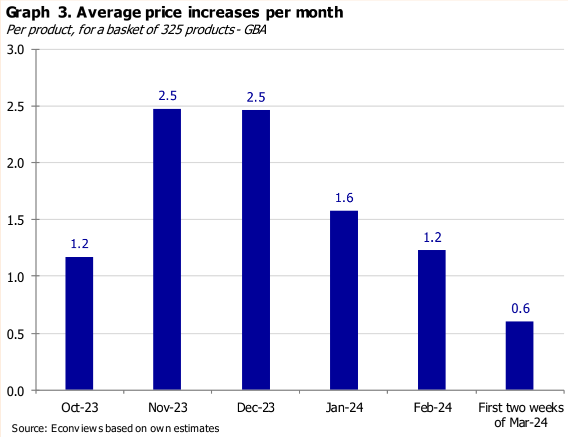
It is true that the inflation measured by Econviews through websites accelerated slightly this week. It was 2.2% between March 1 and 7 and rose to 2.7% between March 8 and 14. But it is still below February's 3.5% average. This slowdown in goods inflation is a product of a practically fixed exchange rate, at a 2% monthly crawling peg. With expectations anchored on exchange rate matters, there is no reason for goods inflation to spike up much. That is why we think the government's heterodox attempts at reducing inflation are ill-guided. Promotions and discounts affect only a tiny portion of the CPI. In the end, meeting with supermarkets to coordinate prices can improve the index (very slightly), but not inflation. Opening up food imports is desirable in itself, but affects the price level, not its variation. Ideally, this policy should be applied to most imports.

The battle in the coming months is inflation in services. In Buenos Aires, gasoline and public transportation have already corrected to a level close to the end of 2019. The lag in private healthcare prices has been reduced considerably in the last three months. On the other hand, education is still getting cheaper in real terms. Today the government announced it wants to postpone the increases in transportation and gas prices in Buenos Aires. After the first 100 days and the "honeymoon", fiscal consolidation begins to enter in conflict with the need to show faster results in terms of inflation.



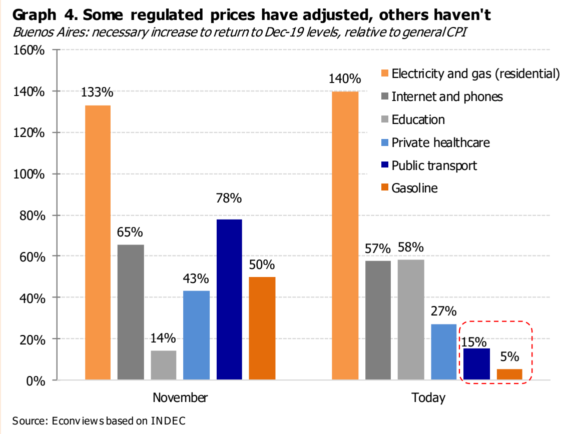
Graph 2. Diffusion Index - GBA
By monthly variation

Source: Econviews based on INDEC



Graph 3. Average price increases per month
Per product, for a basket of 325 products - GBA

Source: Econviews based on own estimates



Graph 4. Some regulated prices have adjusted, others haven't
Buenos Aires: necessary increase to return to Dec-19 levels, relative to general CPI

Source: Econviews based on INDEC