1. Monetary Policy: Assessment and Outlook

Because of a more persistent-than-expected inflation at international level, the central banks of advanced countries have deepened their contractionary monetary policy, resulting in a lower GDP growth than anticipated for the first quarter of the year. Instead, in developing economies, where inflation has tended to subside more quickly, central banks have interrupted their interest rate rises. The lesser momentum of the global economic activity led to a decrease in the prices of food and energy, thus contributing on the one hand to a deceleration of inflation but simultaneously impacting adversely on the growth perspectives of commodity exporting countries on the other. Towards the future, the risks that may affect the world context continue to lie in a lesser momentum of the economic activity. The still high underlying inflation might give rise to new increases of the policy interest rates, which might result in the re-emergence of financial turbulences similar to the ones observed in the banking system of the United States during the first quarter of the year or related to episodes of unsustainable corporate or sovereign debts.

In Argentina, the economic activity grew 0.7% seasonally-adjusted (s.a.) during the first the quarter of 2023, despite the fact that the farming sector activity contracted for the second consecutive quarter. The main reasons behind this performance of GDP were the expansion of the Mining Activity led by the unconventional exploitation in Vaca Muerta and the recovery of the manufacturing industry. The temporary impact of the drought on GDP was stronger during the second quarter of the year, even though it is estimated that the activity of the remaining sectors (non-agricultural GDP) would continue to go up. Data corresponding to April were in line with the expectations and showed a 36.8% year-on-year (y.o.y.) drop in the agricultural activity and a 2.7% y.o.y. growth in the rest of the sectors (without taxes). Over the rest of the year, the domestic economy would be favored by the rebound of the farming sector and the boost of the mining sector, in a context that might show a higher financial volatility associated with the electoral process ahead.

In this context, the inflation rate was on the rise once again in the second quarter of the year, posting a monthly average of 7.4% (+0.6 p.p. against the first quarter) and an expansion of 115.6% in the aggregate of the last 12 months up to June. The highest inflation rate increase occurred during the last week of April, within a context of rising financial volatility due to the exchange rate uncertainty and the impact of the drought on foreign currency settlement and on public finance. As a result, the Federal Government and the BCRA adopted a series of measures intended to reduce financial volatility, which contributed to contain price acceleration. Consequently, the monthly inflation rate of June stood at 6%, down 2.4 percentage points (p.p.) against the maximum figure of April, within a context of moderation in the price of fresh food. It is estimated that, in the next few months, the monthly rates of core inflation (excluding meat) will gradually go down. In turn, the typical volatility of seasonal prices —which tend to accelerate in September and October— and the price of meat will have an impact on headline inflation. The pace of increase of nominal wages, in the context of the collective bargaining agreements recently arranged by the main trade unions, and the preservation of corporate profitability margins explain in part the inflation inertia, which will continue standing at high levels for the rest of the year.

Against this backdrop, the BCRA accelerated the pace of increase of the monetary policy interest rate in order to underpin positive yields in real terms on investments in domestic currency and consequently reduce to a minimum the impact of financial volatility on the evolution of the foreign exchange market and on inflation expectations. Thus, the Board of Directors of the BCRA decided, as from mid-April, to raise the interest rate on the 28-day LELIQs for a total of 19 p.p., to a nominal annual percentage rate (APR) of 97% (effective APR of

154.9%). At the same time, it has also raised the minimum guaranteed interest rates on time deposits and has three-folded the maximum amount of the deposits on which such rate apply (taking it to ARS30 million) in the case of natural persons, which are remunerated at an interest rate equivalent to the monetary policy rate.

Simultaneously, the BCRA continued gauging monetary liquidity and adjusting it to the macroeconomic context. In particular, all the Monetary Base change factors, resulting from private and public sectors' transactions, have made a positive contribution from March to June. They include the purchase and sale of foreign currency and open market operations tending to contain an excessive price volatility of the National Treasury's debt instruments and public sector transactions. Regarding the latter, there was an increase in Temporary Advances in a context of a deteriorated tax collection due to the negative impact of the drought on the economic activity and to the change of profile in the collection of export duties related to the soybean sector, despite the continuity of the government spending consolidation process. Likewise, the payment made to the International Monetary Fund (IMF) upon the scheduled maturity arranged in the 2018 Stand By Agreement also impacted amidst a context of a delay in the disbursements corresponding to the 5th Review of the Extended Fund Facility (EFF) Arrangement. Even though this financing operation of external payments via Temporary Advances had a neutral monetary effect, the net increase of liquidity during this quarter amid a context of lesser momentum in the demand for the Monetary Base required the use of sterilization instruments. Thus, remunerated liabilities expanded 0.7 p.p. in terms of GDP, while the Monetary Base contracted at an average monthly rate of 4.4% in the second quarter, posting a drop of around 30% in the aggregate of the last twelve months up to June.

Regarding the foreign exchange market, the Central Bank of Argentina has continued adjusting the crawl rate within the current managed float system to a level consistent with the inflation pace. Thus, the multilateral real exchange rate went up at a monthly average of 0.1% during the second quarter, in a period in which the foreign currency flow was severely impacted by the drought. Likewise, for the purpose of increasing the supply of foreign currency via the creation of stimulus measures for exports, the "Export Increase Program" was implemented for the settlement of foreign currency resulting from soybean exports and its byproducts effective until May 31, which was extended in turn to Regional Economies until August 31. Thus, transactions in foreign currency were settled for an amount of USD5.4 billion under this program until late June. On the other hand, it is worth mentioning that the BCRA has renewed the swap agreement for CNY130 billion for a three-year term and started the process to request an increase in the amount of use for another CNY35 billion. In addition, several regulatory amendments were introduced to favor an efficient allocation of foreign currency.

The consequences of the drought, whose record-high impact was unpredictable just a few months ago, have changed the 2023 macroeconomic context on which the targets of the Extended Fund Facility Arrangement had been outlined. It must be taken into account that complying with such targets, even in the absence of a shock of these characteristics, required a sizable effort in terms of the monetary and fiscal policies. The technical discussions about re-gauging the program in this new context have extended the term of the 5th Review of the EFF. This delay resulted in a mismatch in the schedule of payments and disbursements agreed with this multilateral credit agency. After the net payments equivalent to USD6.92 billion made to the IMF by the end of June, the BCRA's international reserves were standing at USD27.93 billion as of June 30, posting a drop of USD11.13 billion in the second quarter.

In the next few months, within the context of a more complex international scenario and a record-high drought that impacted adversely on the domestic economy, the BCRA will continue defining its policies in a dynamic and flexible manner, complying with the guidelines announced for the current year in terms of its monetary, exchange, financial and credit policies. Regarding interest rates, the BCRA will keep on gauging the monetary policy rate and paying special attention to the past and prospective evolution of headline inflation, the economic activity level and the performance of the foreign exchange market, seeking to provide positive yields in real terms in order to consolidate exchange and financial stability. In this respect, the monetary authority will continue intervening in the secondary market of National Treasury' instruments so as to prevent an excessive volatility that might endanger the domestic capital market's development and stability. In terms of the foreign exchange market, the measures to be adopted by the BCRA will continue to be focused on preserving adequate levels of external competitiveness and on favoring the accumulation of international reserves on the basis of a prudent management of the regulations in force. Lastly, the financial strategy will continue to boost credit intermediation, especially in terms of productive development by means of the "Credit Line for Productive Investment (LFIP)".