MAY
2023

MONTHLY ECONOMIC
SITUATION REPORT

Office of the Chief Economist

The monthly economic situation report presents an ad hoc analysis of the macroeconomic performance of the world in general and Central America in particular, with information available as of June 12, 2023. The document elaboration was led by Armando E. Navarrete, Chief Economist. The review was conducted by Pablo Flores, Principal Economist. The research and writing were carried out by Miguel Ángel Medina Fonseca (Economist), Leily Mendoza (Economist), Fanny Vargas (Country Economist), Rodrigo Méndez (Country Economist) and Clara Rivera (Junior Economist).

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OPINION

The world economy growth remains stable amidst an environment with tighter financial conditions. Inflation continues to slow at the international level, while monetary authorities show signs stopping policy rates increases. However, unemployment rates remain at low levels, still signaling a robust performance in advanced economies.

Central American economies growth shows sign of moderation. Inflationary pressures continue, although they show signs of deceleration, in line with the trend of price movements at the international level. In this context, some countries have already begun to lower their policy rates to alleviate local financial conditions. However, less favorable external conditions are beginning to affect the performance of international trade, with exports and imports contracting in some countries in the first months of the year.

Onward, governments must continue prioritizing macroeconomic stability, through timely monetary and fiscal policy actions. Additionally, it is important to implement macroprudential policies to reduce the negative effects of international interest rate hikes. Likewise, they must continue to maintain a healthy business climate to ensure the attraction of foreign investment that broadens the possibilities of growth.

Armando E. Navarrete
Chief Economist

MONTHLY ECONOMIC SITUATION REPORT

I. US and Eurozone economies slow and total inflation continues to decelerate

1. The US reported a mixed evolution of the economic indicators. Latest quarterly GDP estimates a slower growth, while the total unemployment rate rose. The Federal Reserve's persistent implementation of a restrictive monetary policy, and the decreased impact of international commodity prices, has played a significant role in reinforcing the ongoing downward trend in inflation.

i. Real gross domestic product increased 1.3% in the first quarter of 2023 (1.1% in the advance estimate). This growth can be attributed to several factors, including heightened consumer spending, increased exports, amplified spending by the federal administration as well as state and local administrations. Furthermore, non-residential fixed investments exhibited a positive trend, albeit partially counterbalanced by declines in private inventories and residential fixed investment. Additionally, imports increased, subtracting in the calculation of GDP.[1]

ii. Weekly economic index[2] rose 1.0% in the week ending June 3 (1.4% as of December 31, 2022). The 13-week moving average also increased 1.0%.[3]

iii. GDPNow model estimated an increase in real GDP of 2.2% for the second quarter of 2023 (June 8), which is a deceleration from the average of the May estimates (2.5%). This result was above the 1.3% growth of the first quarter of 2023. The slowdown was due to the release of first quarter GDP statistics, manufacturing purchasing managers' index, construction spending, employment, auto sales, international trade, wholesale trade, among others.[4,5]

iv. The total unemployment rate increased to 3.7% in May 2023 (3.4% previous month).[6,7] Unemployment among Latinos fell to 4.0% (4.4% in April). Meanwhile, total non-agricultural employment generated 339,000 jobs (294,000 the previous month); while the average hourly earnings have increased by 4.3% over the past 12 months.

v. Initial claims for unemployment benefits reached 261,000 in the week ending June 3, up 28,000 from the previous week.[8] The average number of requests for the last month increased by 0.1% compared to the previous month and was 18.9% higher than January 2023.

[1] Bureau of Economic Analysis. Gross Domestic Product (Second Estimate), First Quarter 2023. May 25, 2023.
[2] The Weekly Economic Index (WEI) is constructed using data available on a daily or weekly basis for 10 indicators of real economic activity related to the consumer, labor market, and production.
[3] Federal Reserve Bank of New York. Weekly Economic Index (WEI). June 8, 2023.
[4] GDPNow is not an official Atlanta Fed forecast. It is an estimate of seasonally adjusted real GDP growth based on the economic data available for the current quarter (nowcast).
[5] Federal Reserve Bank of Atlanta. GDP Now. Estimate for 2023: Q2. June 8, 2023.
[6] United States Bureau of Labor Statistics. Employment situation summary. June 2, 2023.
[7] It has remained in a tight range between 3.4%-3.7% since March 2022.
[8] United States Department of Labor. Unemployment insurance weekly claims, Seasonally Adjusted Data. June 8, 2023.

2. Total inflation in the US reached the lowest level in more than two years. This behavior was influenced by the drop in fuel prices and the deceleration in the prices of food and transportation services.

i. Year-on-year inflation was 4.0% in May 2023 (4.9% the previous month), the lowest rate since March 2021. The groups that registered the highest year-on-year increases were transportation services (10.2%), shelter (8.0%), food (6.7%) and electricity (5.9%), while energy commodities fell -20.4%. For its part, the total index minus food and energy grew 5.3% (5.5% in the previous month), the lowest in the last year and a half.[9]

ii. Fed increased the range of the monetary policy rate to 5.00%-5.25% in May, a 25bps increase. This decision took into consideration that inflation continues to be high, and furthermore, the growth of economic activity was moderate in the first quarter of the year, employment has shown a solid increase in recent months, and the unemployment rate has fallen. Additionally, Fed communicated that the US banking system is strong and resilient, and that tightening credit conditions for households and businesses could impact economic activity, hiring, and inflation. The Committee will continue to reduce its holdings of Treasury securities, agency debt and agency mortgage-backed securities (quantitative tightening). Lastly, they reaffirmed their commitment to achieving the long-term inflation goal of 2.0%.[10]

3. Quarterly GDP and unemployment slightly decreased in the Euro Zone. GDP reduced -0.1% in the first quarter of 2023 compared to the previous quarter and increased 1.0% compared to the same quarter of 2022;[11] retail trade volume was unchanged in April from the prior month[12] and production in construction fell -2.4% in March compared to the previous month.[13] Besides, unemployment rate was 6.5% in April, lower than March (6.6%) and April 2022 (6.7%).[14]

4. Consumer prices in the Euro Zone resumed the path of deceleration. Estimated annual Inflation rate for May was 6.1%, lower than April (7.0%) and May 2022 (8.1%). Total price index variation that excludes energy, food, alcohol and tobacco fell to 5.3% in May, after reaching a record high in March (5.7%). Food, alcohol and tobacco prices presented the highest year-over-year rate with 12.5% (15.5% in March), non-energy industrial goods increased 5.8% (6.6% in March) and services 5.0% (5.1% in March). For their part, energy prices decreased -1.7% (-0.9% in March), after experiencing a rate of 39.1% in May of last year.[15] European Central Bank has projected average annual inflation of 2.1% for 2025, slightly above the target, and expected that annual inflation rates will converge to 2.0% until the second half of 2025[16].

5. European Central Bank maintained its restrictive monetary policy. As a result of the high inflationary pressures, the Board decided to raise the interest rate of the main financing operations, the marginal credit facility and the deposit facility by 25 basis points to 3.75%, 4.00% and 3.25%, respectively, with effect from May 10.[17]

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[9] US Bureau of Labor Statistics. Economic news release: Consumer Price Index Summary. June 13, 2023.
[10] Board of Governors of the Federal Reserve System. Federal Reserve issues FOMC statement. May 3, 2023.
[11] Eurostat. GDP down by 0.1% and employment up by 0.6% in the euro area. 8 June 2023.
[12] Eurostat. April 2023 compared with March 2023. Volume of retail trade unchanged in the euro area and up by 0.1% in the EU. 6 June 2023.
[13] Eurostat. March 2023 compared with February 2023. Production in construction down by 2.4% in the euro area and by 1.9% in the EU. 22 May 2023
[14] Eurostat. April 2023. Euro area unemployment at 6.5%. June 1, 2023.
[15] Eurostat. Flash estimate - May 2023. Euro area annual inflation down to 6.1%. June 1, 2023.
[16] European Central Bank. Speech The fight against inflation. Christine Lagarde. June 1, 2023.
[17] European Central Bank. Press Release Monetary Policy Decisions. 4 May 2023.

6. Most of CABEI's non-regional partner countries present a slowdown in inflation levels. Spain, Colombia, Mexico, the Republic of Korea and the Republic of China (Taiwan) reduced their annual inflation in May by -0.90 pp, -0.46 pp, -0.41 pp, -0.40 pp y -0.33 pp compared to the previous month, reaching rates of 3.20%, 12.36%, 5.84%, 3.30% and 2.02%, respectively. In May, two central banks increased their monetary policy rates: Argentina from 91.00% to 97.00% and Colombia from 13.00% to 13.25%.

7. Production indices and unemployment rates present mixed results in CABEI's non-regional partner countries. The industrial production index fell in April in the Republic of China (Taiwan), the Republic of Korea and Spain, the former presenting a decrease of -23.5%. Moreover, the greatest variation in the unemployment rate in the same month was registered by Colombia, with a monthly increase of 0.7 pp to reach 10.7%.

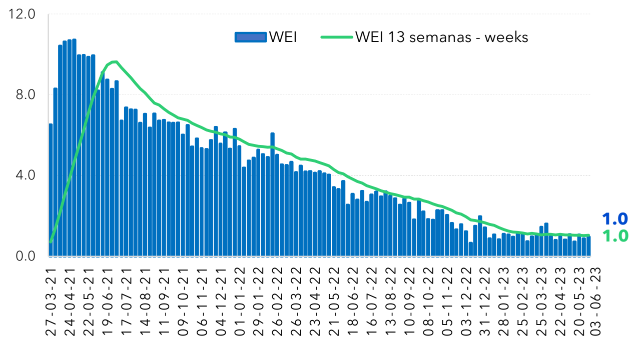
8. The FAO Food Price Index resumed its downward trend in May, after falling for 12 consecutive months in March and rebounding slightly in April. Index fell -2.6% compared to April and -22.1% compared to the all-time high of March 2022. May decline was due to significant falls in price indices of vegetable oils (-8.7%), cereals (-4.8%) and dairy products (-3.2%), which were partly offset by increases in sugar (5.5%) and meat (1.0%) indices. Vegetable oils index reflected the decline in world prices for palm, soybean, rapeseed and sunflower oils due to abundant global supply and lower demand. The sugar index experienced the fourth consecutive monthly increase and the highest level since October 2011, due to concerns about the decrease in sugar availability worldwide because of the *El Niño* phenomenon and lower production forecasts in the 2022/23 harvest.[18]

9. Most of the prices of the main commodities in the Central American region registered a monthly decrease. Products that showed reductions in May compared to the previous month were WTI oil (-9.9%), palm oil (-7.1%), Arabica coffee (-4.1%), beef (-3.2%), bananas (-2.5%) and gold (-0.4%); besides, sugar (3.0%) reported an increase. Likewise, palm oil (-45.6%) and WTI oil (-34.7%) registered the most significant price decreases compared to the same month of the previous year, while sugar (17.0%) and bananas (10.4%) the largest year-over-year increases.[19]

[18]Food and Agriculture Organization of the United Nations. FAO Food Price Index. June 2, 2023.
[19]*The World Bank. Commodity Price Data. Updated June 02, 2023.*

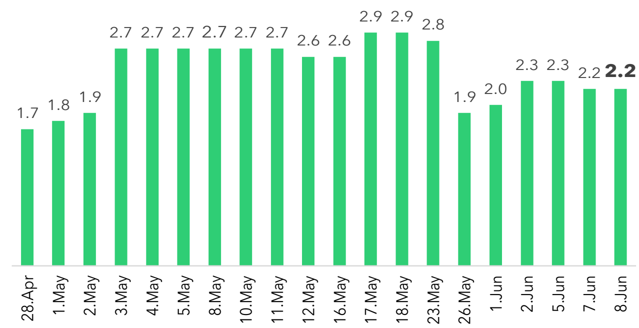
Panel 1 Selected US Macroeconomic Indicators

Graph 1. Weekly economic activity
(year-over-year percent change)



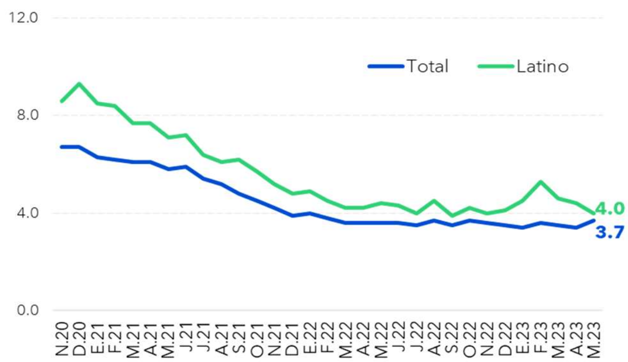
Stable around 1.0% so far this year

Graph 2. Second quarter 2023 real GDP estimate
(seasonally adjusted annualized rate, percent)



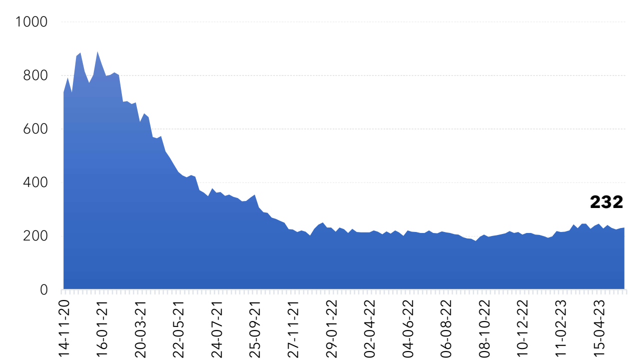
GDPNOW model estimated lower GDP growth

Graph 3. Unemployment rate (percent)



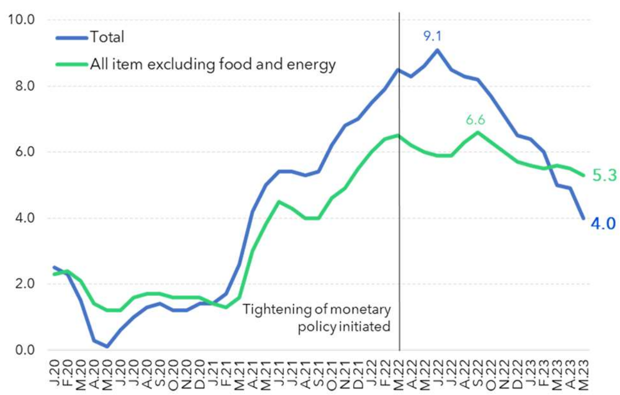
Total unemployment rose, Latino unemployment fell

Graph 4. Initial subsidy claims (thousands)



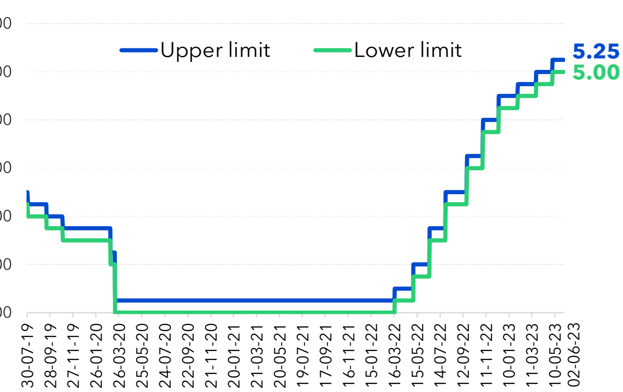
Applications increased in the last month

Graph 5. Inflation (year-over-year percent change)



Lowest total inflation since March 2021

Graph 6. Federal funds interest (percent)

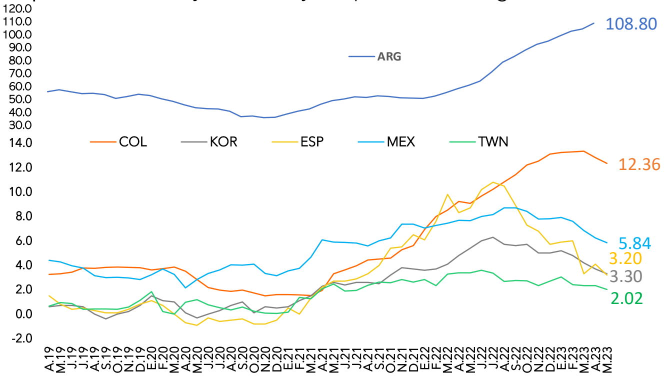


FED raised rate by 25 bp in May 2023

Source: Office of the Chief Economist with information from the Federal Reserve Bank of New York. Federal Reserve Bank of Atlanta. Federal Reserve Bank of St.Louis. Bureau of Labor Statistics. Board of Governors of the Federal Reserve System. United States Department of Labor.

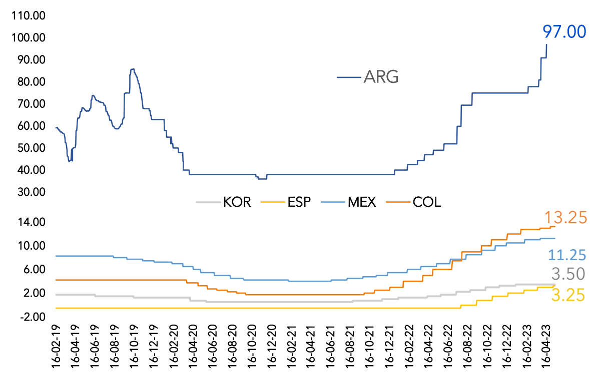
Panel 2 Selected macroeconomic indicators of non-regional CABEI member countries and commodity prices

Graph 7. Inflation (year-over-year percent change)



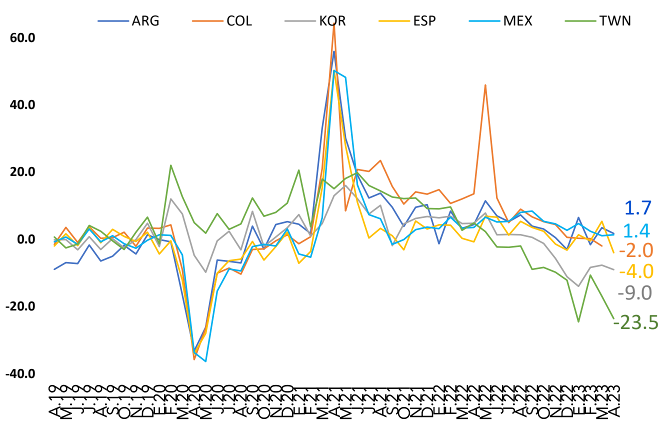
Inflationary pressures reduced in most countries

Graph 8. Monetary Policy Rate (percent)



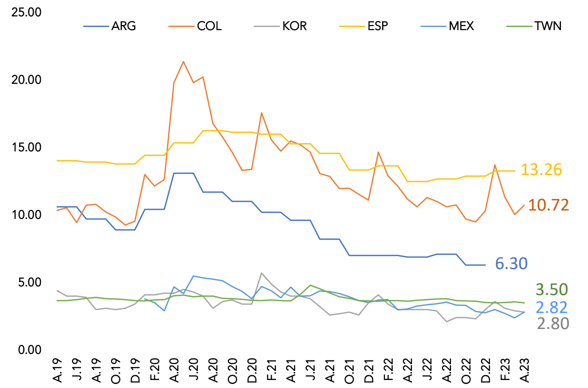
Tighter monetary policy efforts continue

Graph 9. Industrial production index (year- over-year percent change)



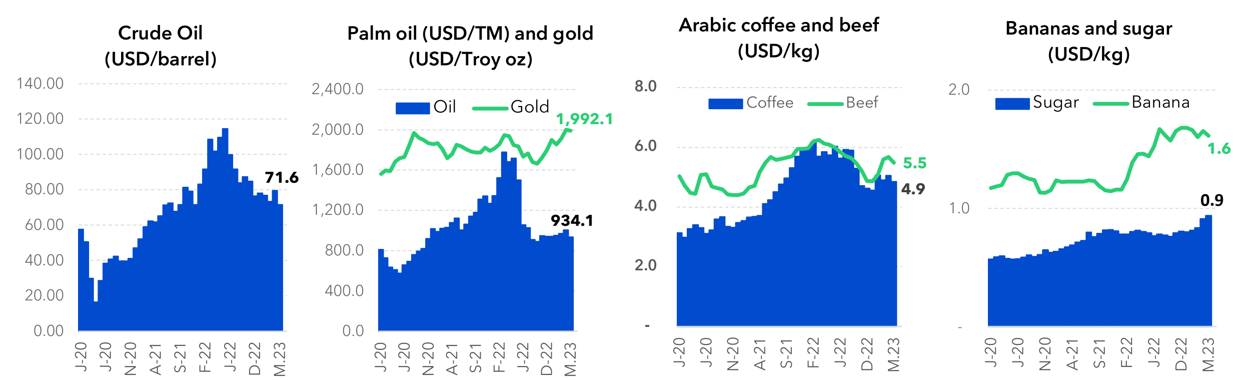
Industrial production with mixed results

Graph 10. Unemployment rate (percent)



Unemployment with heterogeneous results

Graph 11. International prices of main commodities in the Central American region as of May 2023



Monthly prices decreased in most commodities

Source: Office of the Chief Economist with information from the statistics institutes, central banks of the extra-regional partner countries and the World Bank.

II. Central American region grows at a slower pace

10. Economic activity maintains stable growth rates. Regional average growth reached 2.9% in March, it is still outperforming 2019 rate (2.3%). Production was driven by an increase in more than half of the activities, highlighting transportation, commerce, and accommodation and food service activities.

11. Labor market robust performance continues. Formal employment level increased in all countries for which information is available.[20] During April year on year variation for the Dominican Republic was 4.8%, and Nicaragua 0.4%, while in March the increase in Guatemala was 5.3% and for El Salvador 2.6%. Guatemala and the Dominican Republic are the ones that grew the most comparted to their February 202 level, with 17.2% and 8.9%, respectively.

12. Inflation registers a downward trend in all countries. The combined effects of a more restrictive monetary policy, the slowdown in international prices and a decrease in other inflationary pressures have caused inflation to begin to moderate in all countries.

13. Restrictive monetary policy is kept throughout the region. Banco de Guatemala increased its policy rate by 25 basis points to 5.0%. Nicaragua's Central Bank kept its rate at 7.00%, meanwhile for Honduras it has remained constant at 3.00% since November 2020. Costa Rica's authorities lowered its rate by 100 basis points to 7.50% and Dominican Republic Central Bank also made the decision to set its rate at 8.00%, 50 basis points lower than its previous level.

14. Central government cumulative financial balances present mixed results. All countries closed 2022 with growth in public revenues, a trend that seems to continue in 2023: in April, Guatemala's revenues grew 9.3% and Costa Rica 4.6%, while El Salvador's income contracted by -3.2% in March. Likewise, expenses grew moderately in Costa Rica (2.5%) and Nicaragua (9.8%) in April, while they increased more significantly in Guatemala (20.3%) and the Dominican Republic (35.0% in February); however, they contracted in El Salvador (-3.9%) during March. Thus, a slight improvement is observed in the fiscal position in relation to the previous month and year for El Salvador and Honduras, and a deterioration in Guatemala and the Dominican Republic[21].

15. Foreign trade slows down compared to the previous year. The year-on-year variation of accumulated growth in exports ranged from -5.6% in Honduras to 17.8% in Panama.[22] Likewise, there is a variation in imports from -8.1% in Nicaragua to 40.4% in Panama.

16. Accumulated remittances grow at a slower rate. All countries exhibit positive year on year variations, but growth rates tend to decrease. Income for remittances amounted to USD 5,984.8 million in Guatemala and USD 1,394.6 million in Nicaragua in April; while in March USD 2,487.7 million accumulated in the Dominican Republic, USD 2,119.7 million in Honduras and USD 1,912.7 million in El Salvador.

[20] Measured by the number of contributors to social security.
[21] The exceptions were the Dominican Republic, Guatemala and Nicaragua, where the higher increase in spending compared to revenues drove an increase in the deficit in the former, a shift from surplus to deficit in Guatemala and a lower surplus in Nicaragua.
[22] To monitor the situation of exports and imports, the variations of the nominal values are estimated, since the values at constant prices are only calculated to compile the Gross Domestic Product (GDP) in the national accounts.

17. The exchange rate registered a higher level in most of the countries. The interannual variation exhibited an appreciation for Costa Rica (-19.6%) and the Dominican Republic (-1.2%) in May, while the rest of the currencies exhibited a slight depreciation. The month-on-month variation registered a slight appreciation in the Dominican Republic (-0.2%) and a slight depreciation in Costa Rica (0.5%) and Nicaragua (0.1%). The interest rate differential resulting from increases in the US monetary policy rate may explain part of the dynamics of this variable. The effect in Costa Rica and the Dominican Republic has been less influenced by the important increases in their policy rates. Additionally, the flow of remittances can be a factor that decreases the variability in the exchange rate in countries like Guatemala and Honduras.

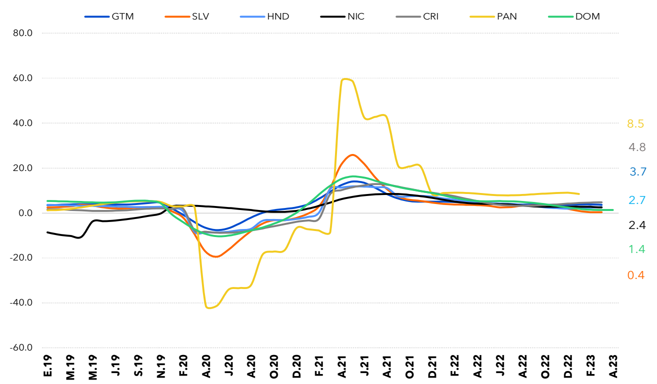
18. Net international reserves (NIR) contracted. The greater trade deficit, generated by an increase in imports greater than that of exports, coupled with the slowdown in remittances, determined the year-on-year contraction of the NIR in most countries except the in the Dominican Republic (13.6% in May), Costa Rica (59.9% in April) and Nicaragua (13.6% in April). Likewise, the increase in the FED rate rises the probability of capital outflows or a reduction in its flow to the region, which could be affecting its accumulation. Most countries have enough reserves to cover at least three months of their imports, in line with the minimum threshold defined by the IMF.[23]

19. Fitch affirms Nicaragua's sovereign rating at 'B-' and revises outlook to positive. The outlooks' revision from table to positive reflects the Nicaraguan economy's resilience to political tensions and resulting economic sanctions, relatively low debt burden and adequate external liquidity bolstered by increased remittances, guided by a prudent policy mix that has strengthened fiscal and external buffers. Nevertheless, sanctions pose downside risks for growth prospects and constrain the sovereign's external financing options.

[23] Panama and El Salvador are the exception with 2.6 and 1.9 months, respectively.

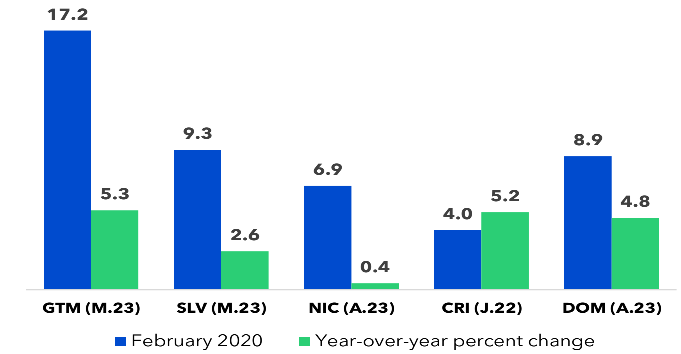
Panel 3. Central America: Selected Macroeconomic Indicators

Graph 12. IMAE (year-over-year percent change)



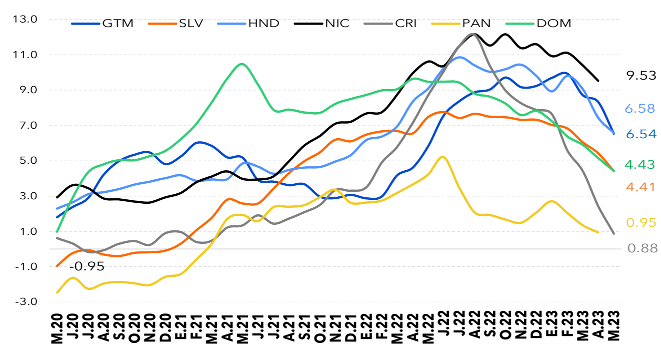
Activity converges to pre-pandemic rates

Graph 13. Formal employment (variation, percentage)



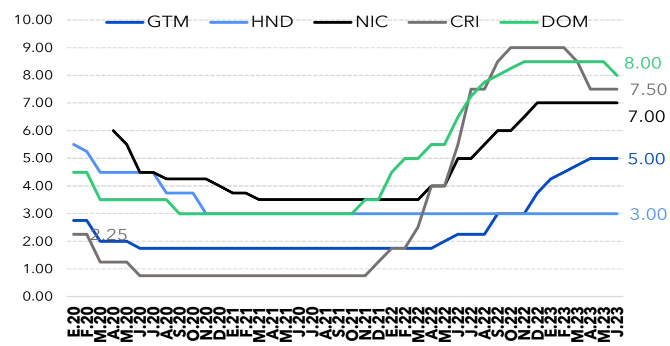
Dynamics have led to robust employment growth

Graph 14. Inflation (year-over-year percent change)



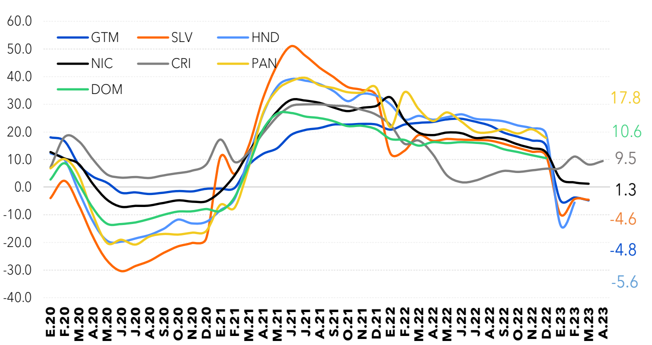
External pressures continue to affect inflation, but it is beginning to decline

Graph 15. Monetary Policy Rate (percent)



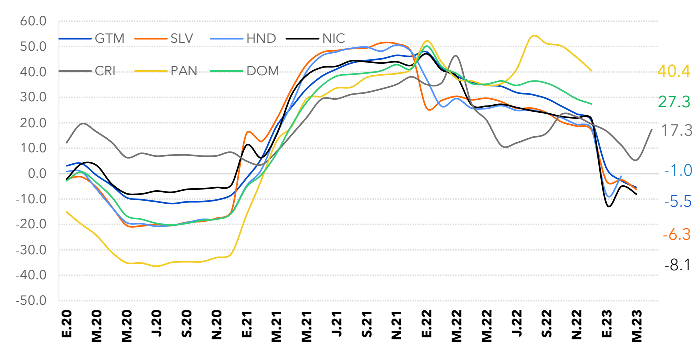
Tight monetary policy to counter inflation

Graph 16. Accumulated exports
(year-over-year percent change)



Exports show signs of slowdown and in some cases drop compared to the previous year

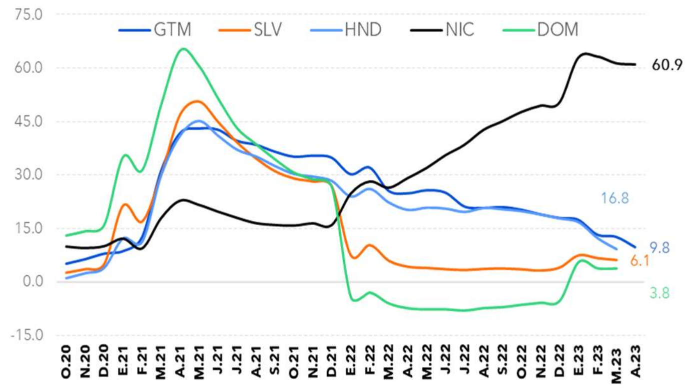
Graph 17. Accumulated imports
(year-over-year percent change)



Imports show a downward trend, although to a lesser extent than exports

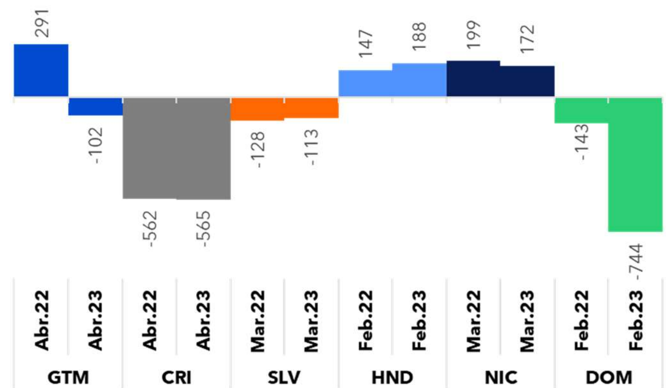
Source: Office of the Chief Economist with information from the SECMCA as of June 2.

Graph 18. Accumulated remittances received
(year-over-year percent change)



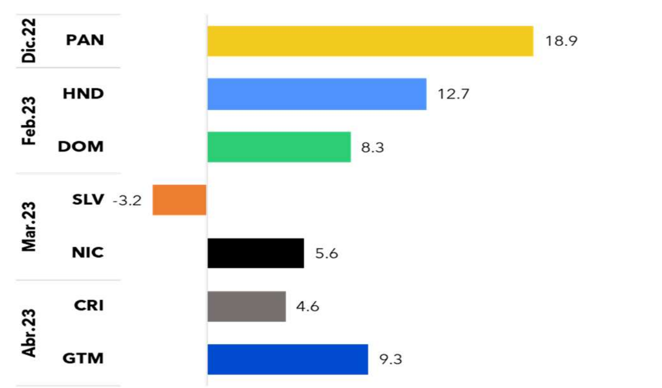
Accumulated family remittances continue to grow at more moderate rates

Graph 19. Central government: accumulated financial balance (USD millions)

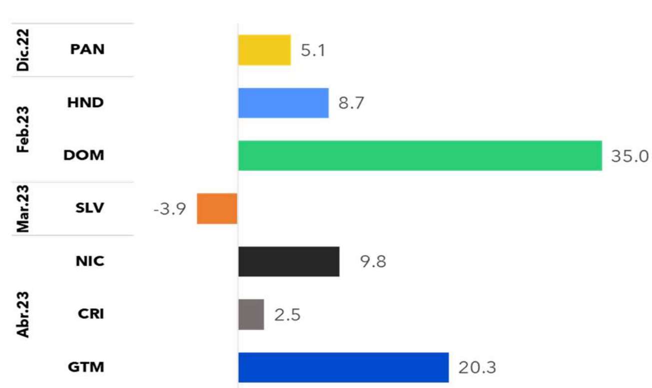


Mixed developments in the fiscal balance

Graph 20. Central government: total accumulated revenue *(year-over-year percent change)*

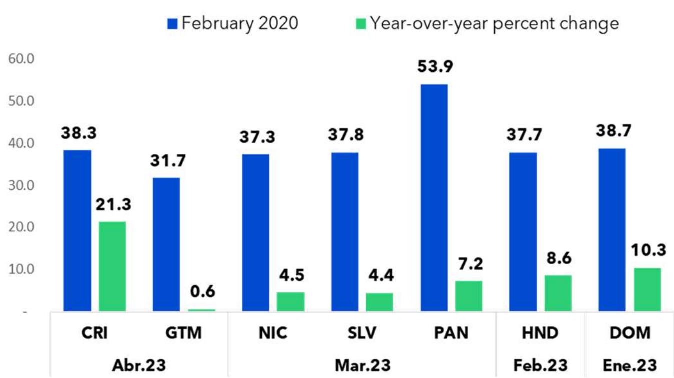


Graph 21. Central government: total accumulated expenditures (*year-over-year percent change*)



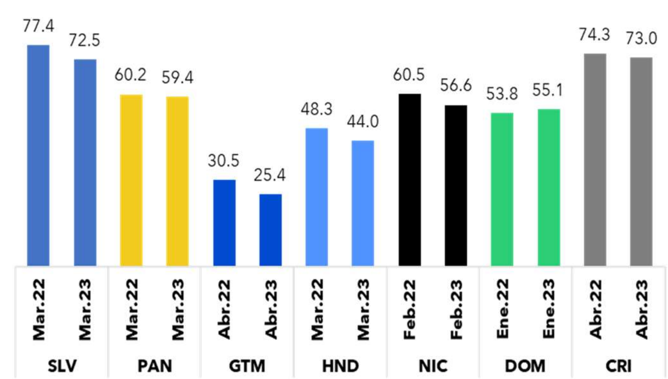
Revenues grow more than public expenses for som countries, favoring some improvement in the fiscal balance; other show large increases in expenditure

Graph 22. Central government: total debt (*year-over-year percent change*)



Public debt growth continues to moderate

Graph 23. Total public debt
(as a percentage of GDP)



Decreased due to lower deficits and GDP growth

Source: Office of the Chief Economist with information from the SECMCA as of June 12.

Annex 1. Long-term sovereign debt rating in foreign currency

Moody's Countries	Rating as of March 2020		Previous rating		Rating as of June 12, 2023	
	Rating	Outlook	Rating	Outlook	Rating	Outlook
Belize	Caa2	Stable	Caa3	Stable	Caa2	Stable
Guatemala	Ba1	Stable	Ba1	Stable	Ba1	Stable
El Salvador	B3	Stable	Caa3	Negative	Caa3	Stable
Honduras	B1	Stable	---	---	B1	Stable
Nicaragua	B3	Stable	---	---	B3	Stable
Costa Rica	B2	Stable	B2	Negative	B2	Stable
Panama	Baa1	Stable	Baa2	Stable	Baa2	Negative
Dominican Republic	Ba3	Stable	---	---	Ba3	Stable
Colombia	Baa2	Stable	Baa2	Negative	Baa2	Stable
Republic of China (Taiwan)	Aa3	Stable	Aa3	Positive	Aa3	Stable
Argentina	Caa2	En revisión	Ca	Negative	Ca	Stable
Mexico	A3	Negative	Baa1	Negative	Baa2	Stable

Standard & Poor's Countries	Rating as of March 2020		Previous rating		Rating as of June 12, 2023	
	Rating	Outlook	Rating	Outlook	Rating	Outlook
Belize	B-	Stable	SD	n.a.	B-	Stable
Guatemala	BB-	Stable	BB-	Positive	BB	Stable
El Salvador	B-	Stable	CCC+	Negative	CCC+	Stable
Honduras	BB-	Stable	---	---	BB-	Negative
Nicaragua	B-	Stable	B-	Stable	B	Stable
Costa Rica	B+	Negative	B	Stable	B+	Stable
Panama	BBB+	Stable	BBB	Stable	BBB	Negative
Dominican Republic	BB-	Stable	BB-	Stable	BB	Stable
Colombia	BBB-	Stable	BBB-	Negative	BB+	Stable
Republic of China (Taiwan)	AA-	Stable	AAu	Positive	AA+u	Stable
Argentina	CCC-	Negative	CCC+	Negative	CCC-	Negative
Mexico	BBB+	Negative	BBB	Negative	BBB	Stable

Fitch Ratings Countries	Rating as of March 2020		Previous rating		Rating as of June 12, 2023	
	Rating	Outlook	Rating	Outlook	Rating	Outlook
Belize	---	---	---	---	---	---
Guatemala	BB	Negative	BB-	Positive	BB	Stable
El Salvador	B-	Stable	CC	---	CCC+	---
Honduras	---	---	---	---	---	---
Nicaragua	B-	Stable	B-	Negative	B-	Positive
Costa Rica	B+	Negative	B	Stable	BB-	Stable
Panama	BBB	Negative	BBB-	Negative	BBB-	Stable
Dominican Republic	BB-	Stable	BB-	Stable	BB-	Stable
Colombia	BBB	Negative	BB+	Stable	BB+	Stable
Republic of China (Taiwan)	AA-	Stable	AA	Stable	AAu	Stable
Argentina	CC	n.a.	CCC-	n.a.	C	n.a.
Mexico	BBB	Stable	BBB	Stable	BBB-	Stable

Source: Office of the Chief Economist with information from Bloomberg.

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