

Macro scenario - Paraguay

October 6, 2020



The decline in GDP this year likely to be lower than anticipated

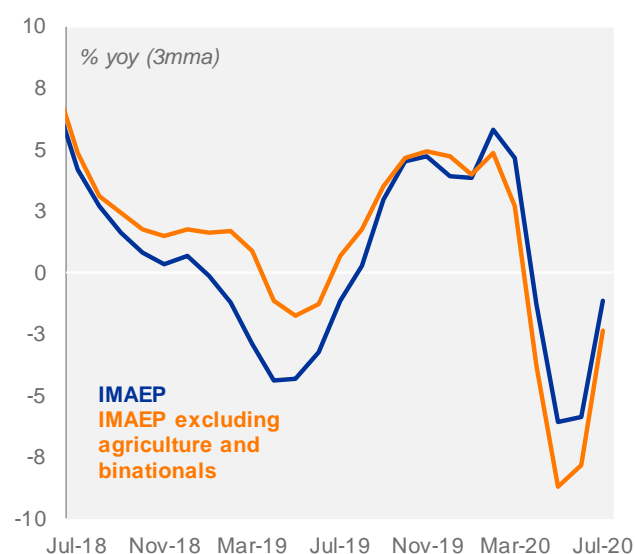
- ▶ GDP fell less than expected in 2Q20, as the revision of agricultural output accentuated the positive base effect. We have revised our GDP growth forecast for this year up, to -2.0% from -3.5% previously.
- ▶ The COVID-19 contagion stabilized in September, and the government has decided to abandon the quarantine phase and move to a new normal known as “the coronavirus way of life.” The authorities are determining the protocols for the opening of border trade before mid-October.

Agricultural sector moderates fall in GDP

The GDP fell less than expected in 2Q20, and the 1Q20 figures were revised upward due to higher agricultural production. GDP fell 6.5% yoy in 2Q20, compared with our estimate of -7.1%. On a sequential basis, production fell 8.6% qoq/sa in 2Q20 after upwardly revised growth estimates in 1Q20 (to 4.4% yoy and 0% qoq/sa). Domestic demand fell 5.2% yoy, driven by a 7.5% year-over-year drop in private consumption due to lower spending on services (in particular recreation), education and non-durable goods. On the supply side, the strong contraction in the energy, services and manufacturing sectors due to social distancing measures was partially offset by an increase in agriculture and construction due to the base effect of the drought that affected the soybean harvest last year and heavy rains that interrupted construction work in 2Q19. Leading indicators like the official monthly activity index (IMAEP) anticipate that the recovery is underway. The index was up 2.3% qoq/sa in July and up 2.9% qoq/sa, excluding agriculture and binational companies. Thus, we have revised our GDP growth forecast for this year upward, to -2.0% from -3.5% previously. A drought and the increase in COVID-19 cases continue to be the main risks going forward.

Inflation moderated in September. Consumer prices rose 0.3% mom in September, after increasing 0.5% in the previous two months. Thus, annual inflation remained at 1.6%, remaining below the lower limit of the BCP target range (4% ± 2%). Food prices rose 0.7% mom, led by fruits and meat, due to lower local supply as international markets normalize. The prices of durable goods increased due to the depreciation of the guaraní against the dollar, while the price of cement also showed an increase. We maintain our inflation estimate of 1.5% for 2020 and an exchange rate of 6,900 guaraníes to the dollar.

Recovery is underway



Source: BCP

Monetary policy unchanged. The BCP maintained the reference rate at 0.75% for the third consecutive month in September. The committee highlighted better dynamics in activity led by construction, industry and a lower annual drop in services. It is worth noting the change in tone regarding activity, given that in the previous meeting the BCP had warned of downside risks. Regarding prices, the committee reiterated that the different inflation measures remain at low levels, while expectations are still anchored to the target. We do not expect changes in the monetary policy rate for the remainder of the year.

The fiscal deficit continued to rise in August despite the recovery in revenues. The fiscal deficit accumulated in twelve months reached 5.1% of GDP in August, from 4.9% in July. Tax revenue rose 4.1% yoy in real terms in the quarter ended in August (-27.4% in 2Q20), with a gradual recovery in revenues after the

tightest months of quarantine. On the other hand, primary expenditures expanded 6.2% yoy in the quarter ended in August, from 22.7% yoy in 2Q20, led by higher social spending. We expect a fiscal deficit of 7.0% of GDP this year.

Weak imports improved the trade balance. Exports fell 7.6% yoy in the quarter ended in August due to the sharp drop in re-exports associated with the closure of borders. However, the fall in imports was significantly greater (-18% yoy in the quarter to August) due to the lower economic activity in comparison with 2019. Thus, the accumulated trade balance reached USD 700 million in August, up from USD 500 million in July. We expect a trade surplus of USD 500 million and a current account deficit of 1.1% of GDP by 2020, both with upside risk.

the government decided to abandon the quarantine phase and move to the new normal known as the “coronavirus way of living.” The authorities are defining the protocols for the opening of border trade before mid-October.

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The “coronavirus way of life”

The number of daily infections per million inhabitants stabilized at around 100 cases at the end of September, while the mortality rate stood at 2.6 cases using the same measurement. Since October

Forecast: Paraguay

	2014	2015	2016	2017	2018	2019	2020F	2021F
Economic Activity								
Real GDP growth - %	4.9	3.1	4.3	5.0	3.4	0.0	-2.0	3.8
Nominal GDP - USD bn	40.3	35.5	36.0	39.0	40.4	38.1	35.4	36.4
Population (millions)	6.7	6.8	6.9	7.0	7.1	7.2	7.3	7.4
Per Capita GDP - USD	6,006	5,371	5,303	5,667	5,650	5,333	5,251	5,691
Unemployment Rate - year avg	8.0	6.5	7.7	6.1	6.2	6.6	7.5	7.0
Inflation								
CPI - %	4.2	3.1	3.9	4.5	3.2	2.8	1.5	3.0
Interest Rate								
Reference rate - eop - %	6.75	5.75	5.50	5.25	5.25	4.00	0.75	2.00
Balance of Payments								
PYG / USD - eop	4,636	5,782	5,738	5,588	5,964	6,465	6,900	7,000
Trade Balance - USD bn	1.0	0.8	2.2	1.9	0.8	0.4	0.5	0.4
Current Account - % GDP	-0.1	-0.4	3.6	3.1	-0.2	-1.0	-1.1	-1.5
Foreign Direct Investment - % GDP	1.0	0.9	1.2	1.3	1.2	1.3	1.0	1.0
International Reserves - USD bn	6.9	6.2	7.1	8.1	7.9	8.0	8.0	8.0
Public Finances								
NFPS Nominal Balance - % GDP	-0.9	-1.3	-1.1	-1.2	-1.3	-2.8	-7.0	-4.0
NFPS Debt - % GDP	13.4	15.4	17.5	18.4	19.9	23.2	32.5	34.4

Source: FMI, Haver, Bloomberg, BCP, Itaú

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