BBVA Research

# Argentina Economic Outlook

June 2023

Creating Opportunities

# Key points. Global

**Recent developments**

A combination of easing supply shocks (due to lower commodity prices and normalized supply bottlenecks) and resilient demand (thanks to tight labor markets and lingering post-covid reopening effects) has continued to support growth. While, in general, headline inflation has peaked, core inflation has yet to decline more significantly. In this context, the central bank's focus on inflation has been reaffirmed, which has contributed to the creation of tensions in US regional banks.

**Growth outlook**

2023 growth will be higher than previously forecasted, mostly due to positive incoming data, but 2024 growth will be weaker than anticipated, thanks to the lagged impact of tighter monetary and credit conditions. Global growth will slow from 3.4% in 2022 to 2.9% (+0.2pp higher than the previous forecast) in 2023 and 2.9% (-0.3pp) in 2024.

**Inflation and rates outlook**

Central banks will keep rates at restrictive levels for some time, probably for longer than markets are expecting. Liquidity withdrawal programs, credit tightening boosted by the US banking turmoil and, eventually, less expansive fiscal policies will also favor a gradual easing of demand and prices. Still, some second round effects will contribute to keep inflation above the targets for a long period. Against this backdrop, the main risk is that high inflation and tight monetary conditions triggers a sharp recession or new financial instability episodes.

# Key points. Argentina

**Political outlook**

Most of the provinces separated their local elections from the national elections. The first results showed triumphs for local parties and a lower turnout than in the 2019 elections. The ruling coalition has lost votes in comparison with 2019, Juntos por el Cambio improved its results and, thus far, La Libertad Avanza has had a poor performance.

**Economic activity**

Although 1Q23 registered a slight growth, successive drought-related soybean crop cuts and weak economic activity lead us to lower our GDP forecast from -2.5% to -3.5% for 2023. For 2024, we project another drop (-2.0%) due to the adjustment that will be caused by the correction of macroeconomic imbalances.

**External sector**

The lower supply of agricultural products due to the drought resulted in a strong fall of exports, which are only partially offset by an improvement in the energy balance. This will leave a narrow trade balance of USD 1.8 billion by 2023. The Balance of Payments current account will worsen from -0.6% to -2.4% of GDP in 2023, but with prospects for improvement for 2024.

**Fiscal sector**

The retraction of fiscal revenues and the insufficient reduction in public spending entailed a deterioration of the primary fiscal result in comparison with 2022, which we estimate will end 2023 at -2.6% of GDP (higher than the target agreed with the IMF). By 2024 we expect a fiscal adjustment to -0.9% of GDP.

# Key points. Argentina

**Inflation**

Inflation significantly accelerated during the year, towards a higher and more volatile regime. With a monthly average of 7.7% up to November and an acceleration in December, we expect inflation to reach 145% in 2023. We project inflation in 2024 to be 120%, as a result of the expected exchange rate adjustment and corrections of utility prices that will probably be implemented.

**Monetary sector**

Monetary issuance accelerated as a result of the fiscal deterioration, exacerbating exchange rate and inflationary pressures. To face the rising inflation, the Central Bank increased the monetary policy rate to 97% per annum (8% per month). However, it is insufficient to impose a clear anti-inflationary stance. We expect further hikes during the year, and a significant increase in the interest rate by end-2023 or early-2024.

**Foreign exchange market**

The severe drought added considerable stress to the foreign exchange market. The situation is fragile and net international reserves are in negative territory, but we expect that the Government will do whatever it takes to avoid a devaluation jump in the official FX rate before the elections. However, we do forecast it occurring by December, which would take the parity to 400 ARS/USD by Dec-23 (monthly average) and to 944 ARS/USD in Dec-24.

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# Global Economic Outlook June 2023

Creating Opportunities

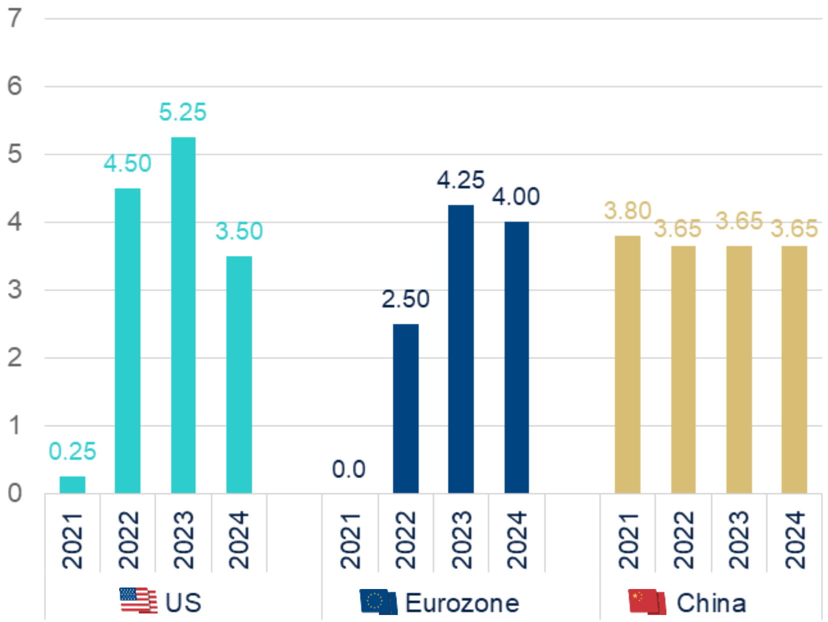
# Reinforced prospects for growth and inflation easing despite recent resilience: credit tightening amid banking stress likely to add to monetary tightening

## BBVA RESEARCH BASELINE SCENARIO

| High-for-long interest rates | Growth slowdown | Gradual disinflation | Financial volatility |
|---|---|---|---|
| Restrictive monetary stance, also on credit tightening and liquidity withdrawal; cautious policy reversal from 1Q24 (or later). | Labor markets and demand will eventually ease, driving growth down despite supply normalization. | Contained commodity prices and limited second round effects, but inflation above targets for some time. | Relatively high volatility and limited flows to riskier assets; US banks stress, with no contagion to large banks or abroad. |

# Central banks will remain focused on inflation despite banking stress: after reaching restrictive levels, rates will likely remain unchanged for a long period

**MONETARY POLICY INTEREST RATES (*)**
(%, END OF PERIOD)



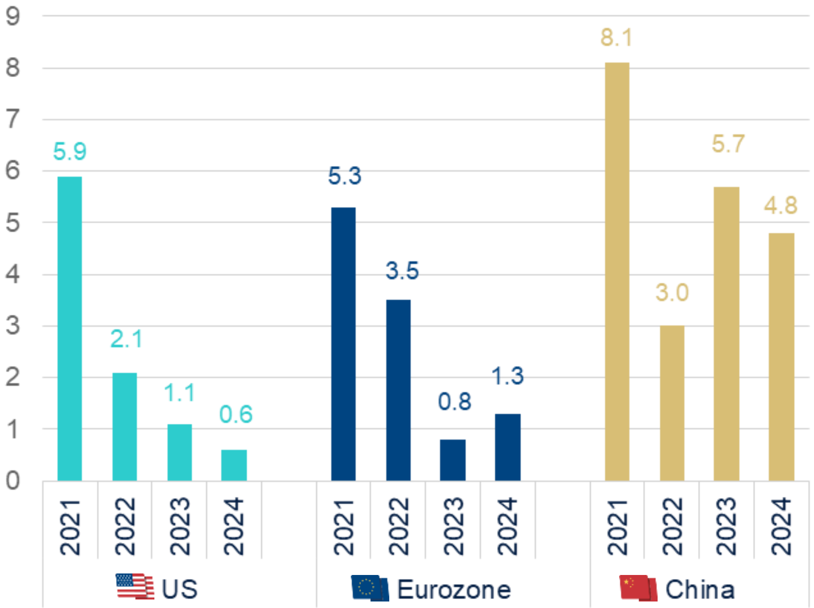

(*) In the case of the Eurozone, interest rates on refinancing operations.
Source: BBVA Research based on Bloomberg data.

- Central banks are likely to use policy rates to fight inflation and liquidity tools to address bank stress; financial dominance is not expected, but is a risk.
- The rate hiking cycle is presumably over in the US (but one more hike is possible) and closer to its end in the EZ, where at least two more hikes are likely.
- Easing cycles are not likely before 1Q24 in the US and 4Q24 in the EZ.
- Still, Fed and ECB will maintain quantitative tightening programs in place, with a gradual and predictable liquidity withdrawal pace.
- Credit tightening and, eventually, fiscal policy are likely to help monetary policy to reign in on inflation.

# GDP forecasts: up in 2023 on robust demand and easing supply shocks, but down in 2024 on the lagged impact of tighter monetary and credit conditions

## GDP: ANNUAL GROWTH IN REAL TERMS (*)

(%)



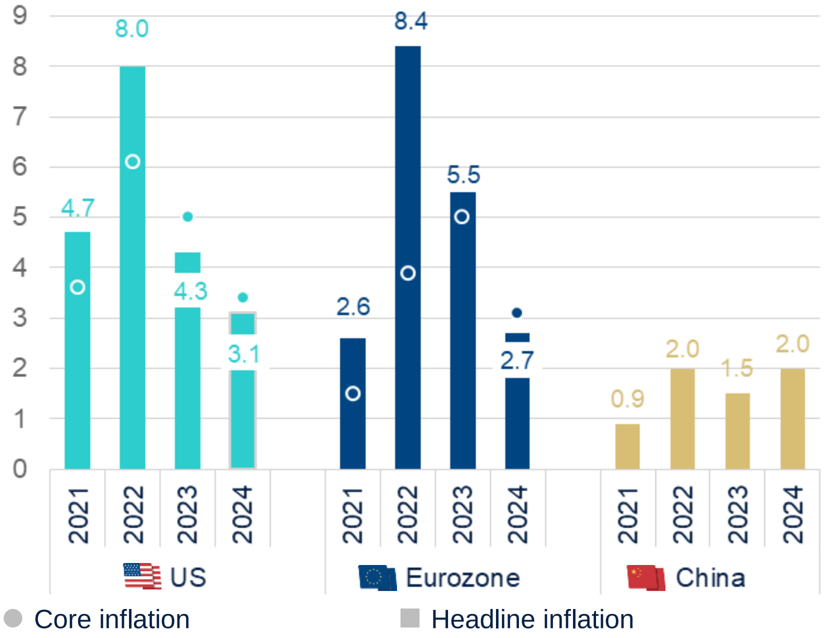

(*) Previous forecasts: 0.8% in 2023 and 1.8% in 2024 in the US, 0.6% in 2023 and 1.6% in 2024 in the Eurozone, 5.2% en 2023 and 5.0% in 2024 in China.
Source: BBVA Research.

- 2023 upward revisions (US: 0.3pp, EZ: 0.2pp, CHN: 0.5pp) on supportive incoming data reflecting strong private consumption (mainly in the US and China) and lower energy prices (mainly in the EZ).
- 2024 downward revisions (US: -1.2pp, EZ: -0.3pp, CHN: -0.2pp) on effects of tighter monetary policy and less supportive credit conditions, to which the recent banking stress is likely to contribute.
- Vanishing reopening effects, easing fiscal support and financial volatility are also likely to hit growth.
- Global growth to slow from 3.4% in 2022 to 2.9% (+0.2pp) in 2023 and 2.9% (-0.3pp) in 2024.

# Inflation will continue to ease, but will be more persistent than previously expected; it will be over the targets for long in the US and EZ

## INFLATION:CPI

(Y/Y %, PERIOD AVERAGE)

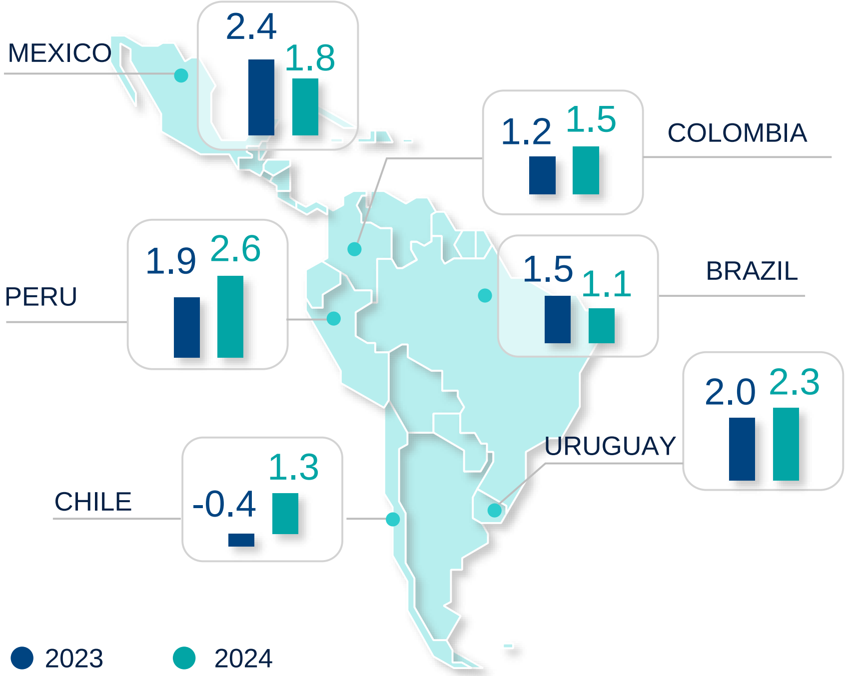



Source: BBVA Research.

- Supply improvement (lower commodity prices, bottleneck normalization) and monetary tightening will pave the way for a further decline in inflation: headline inflation has peaked; core inflation is set to soon ease more significantly.
- Still, the dynamism of private consumption amid tight labor markets will favor (contained) increases in wages and profit margins, slowing inflation's downward trend.
- In China, price pressures remain under control despite the post-covid recovery due to favorable commodity prices, supply recovery and private sector "balance sheet recession".

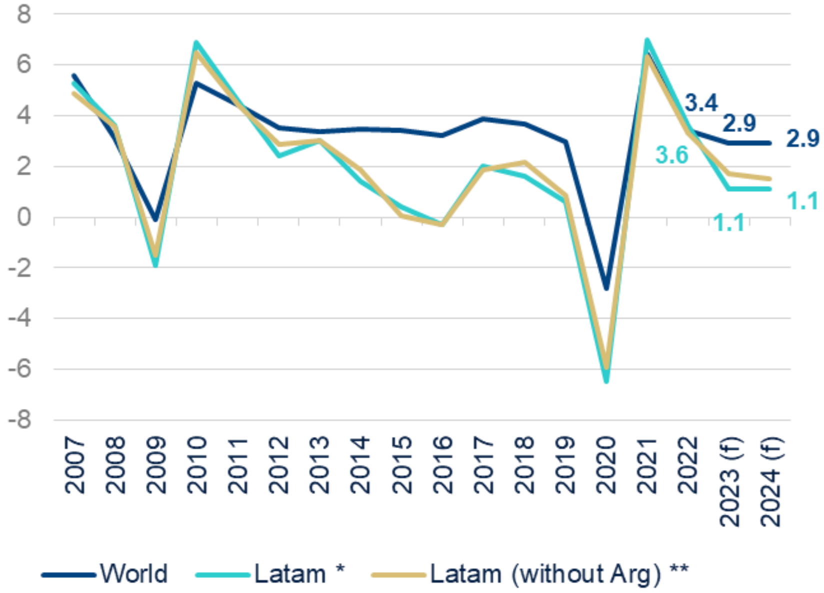
# Latam will experience a significant growth moderation in 2023, greater than the world average, and will maintain a weak performance in 2024

## GDP GROWTH
(ANNUAL CHANGE, %)




Source: BBVA Reseach.

## WORLD AND LATAM GDP
(ANNUAL CHANGE %)




(f): BBVA Research projections.
(*): Includes Argentina, Brazil, Chile, Colombia, Mexico, Paraguay, Peru y Uruguay.
(**): Includes Brazil, Chile, Colombia, Mexico, Paraguay, Peru and Uruguay.

# In an uncertain context, the risk that high inflation and tight monetary conditions triggers a recession or financial instability has increased lately

## MAIN RISKS

**PERSISTENT INFLATION AND TIGHT MONETARY POLICY:**

- strong demand
- tight labor markets
- China recovery
- higher commodity prices
- wage-price spirals
- not fully anchored expectations

→

**FINANCIAL INSTABILITY**
(contagion from US banking stress, vulnerabilities in real estate and leverage markets, non-banking sector, etc.)

**GLOBAL RECESSION**

## MAIN UNCERTAINTIES

**GEOPOLITICAL TENSIONS**

**US-CHINA RIVALRY (DEGLOBALIZATION, ETC)**

**ENERGY TRANSITION AND CLIMATE CHANGE**

**SOCIAL TENSIONS AND POPULISM**

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03

# Argentina
# Economic Outlook
# June 2023

Creating Opportunities

# The electoral calendar was set in motion in the provinces, with the National ruling coalition loosing support in comparison with 2019

## ELECTORAL CALENDAR
(DISTRICTS WITH CONFIRMED DATES)

**April** — Neuquén / Río Negro ✓

**May** — La Pampa / Misiones, Jujuy / Salta / La Rioja, Tierra del Fuego ✓

**June** — San Luis / Tucumán; Córdoba / Formosa; National: Candidates announcement

**July** — San Juan / Chubut

**August** — National: PASO*; Santa Cruz

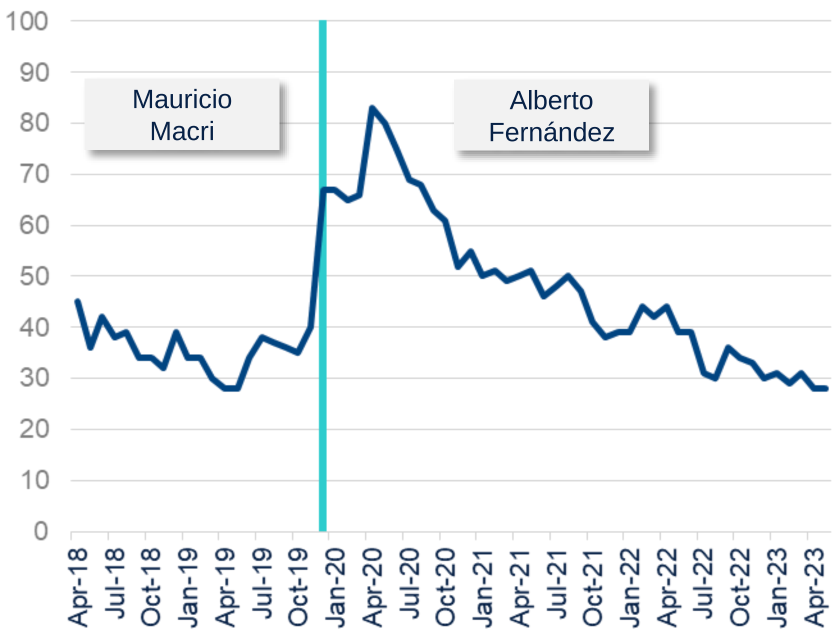
**September** — Santa Fe / Chaco / Mendoza

**October** — National: First round; City of BA / Buenos Aires Prov.; Catamarca / Entre Ríos

**November** — National: Ballotage

* PASO: primary, open, simultaneous and compulsory elections.

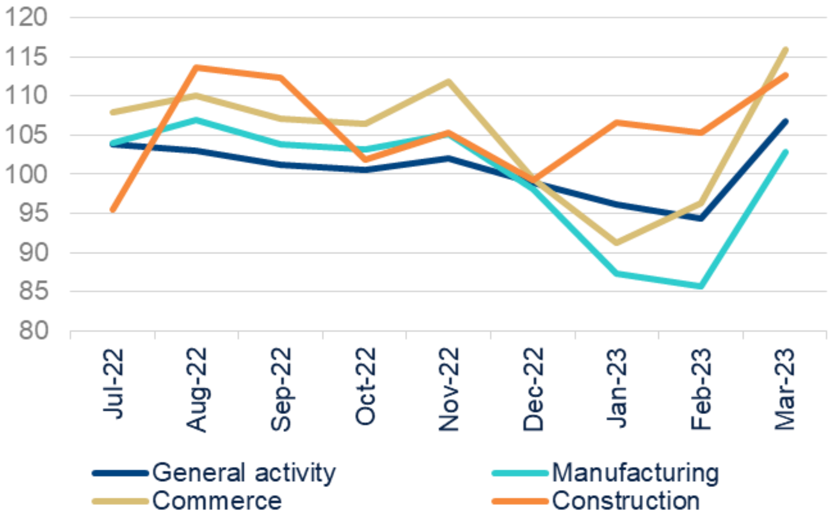
## PRESIDENTIAL APPROVAL RATE
(0 = TOTAL DISAPPROVAL; 100 = FULL APPROVAL)




Source: BBVA Research and Poliarquía Consultores.

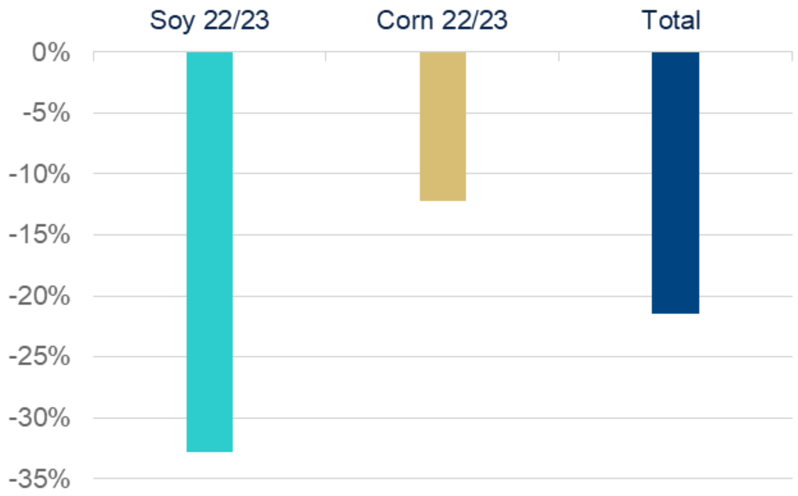
# In 1Q23, activity rebounded in comparison with the previous quarter, but the intense drought has dampened the outlook for the following months...

## ECONOMIC ACTIVITY
(BASELINE DEC'21 = 100; SA)




Source: BBVA Research and INDEC.

## HARVEST: SOYBEAN AND CORN
(% CHANGE VS. PREVIOUS SEASON)

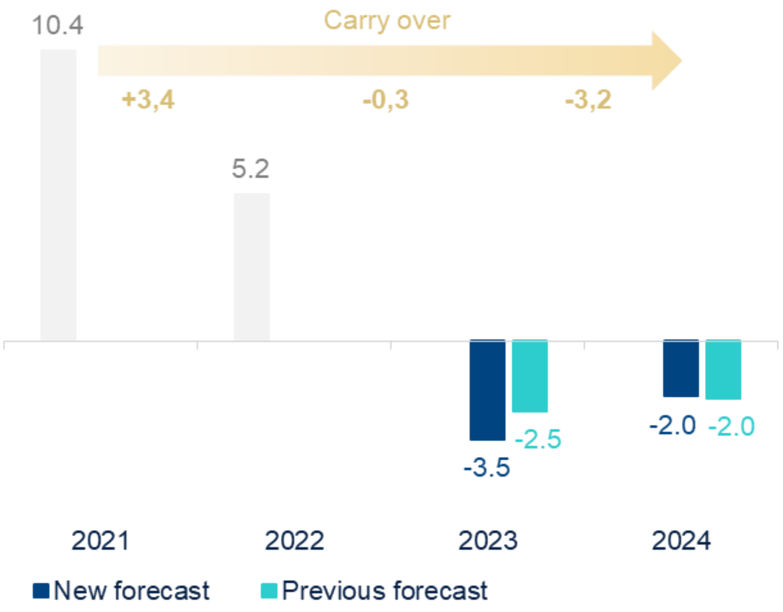



Source: BBVA Research and Buenos Aires Grain Exchange.

The harvest is progressing worse than the already negative forecasts, with a damaging impact on exports, GDP and fiscal revenues. Delayed rains would complicate wheat planting (harvesting takes place toward the end of the year). In addition, accelerating inflation will imply a significant drop in real income and activity will contract even more in 2023.

# ...so, we project a recession from 2Q23 onwards, which leads us to cut our GDP estimate to -3.5% y/y

## GDP FORECAST
(% CHG Y/Y)

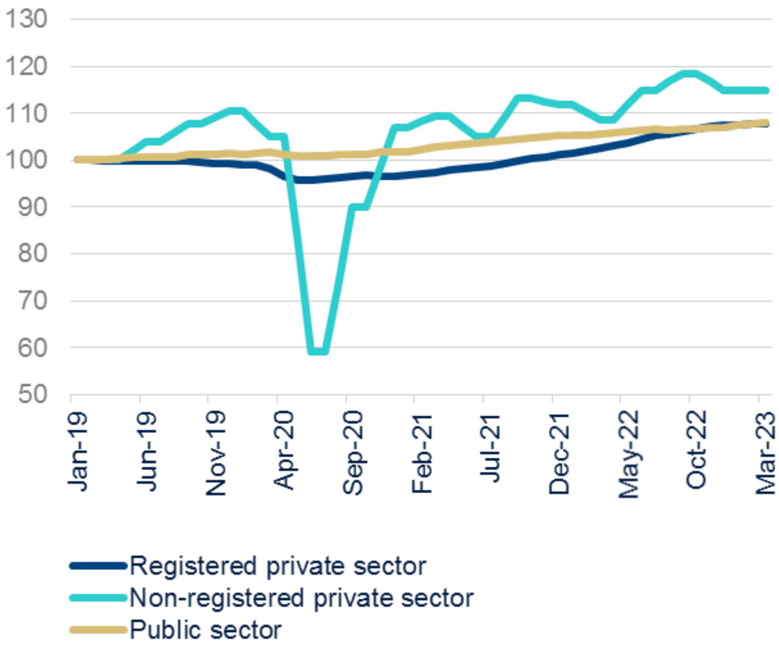



Source: BBVA Research and INDEC.

- The severity of the drought, high inflationary pressure and tighter exchange rate restrictions will exacerbate the unfavorable prospects for private consumption, investment and the external sector in 2023.
- This context would determine a fall in GDP of 3.5% for this year.
- The macroeconomic adjustments expected for the coming year anticipate that there will probably be a new economic downturn, concentrated in the first half of 2024.

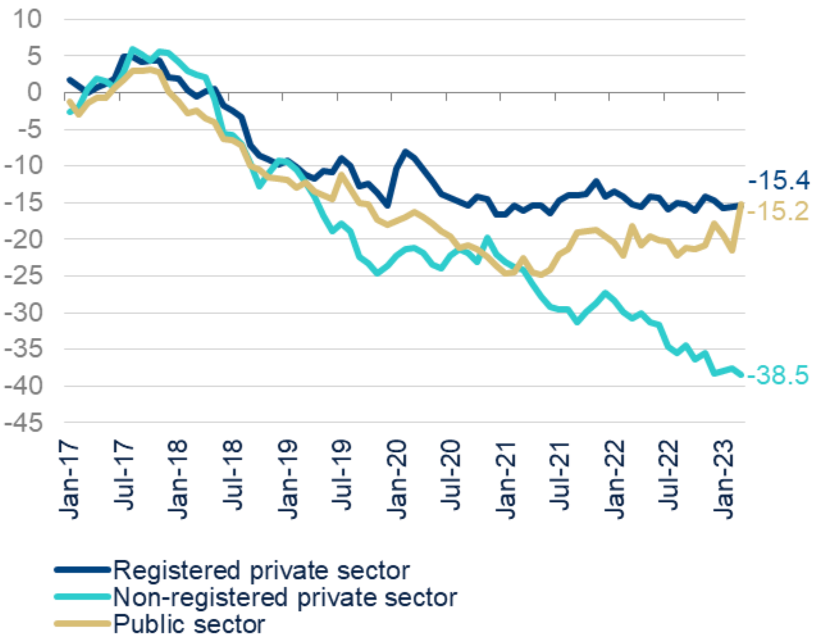
# The income of informal workers is being eroded by inflation, while registered wage earners are managing to maintain real income levels

## EMPLOYMENT BY SECTOR
(BASELINE JAN'19 = 100)




Source: BBVA Research Ministry of Economy and INDEC.

## REAL WAGES BY SECTOR
(CUMULATIVE % CHANGE SINCE JANUARY 2017)

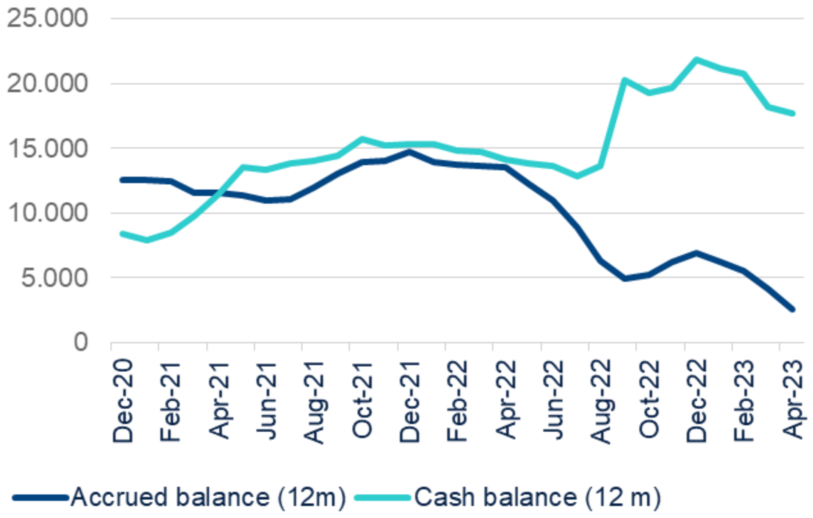



Source: BBVA Research and INDEC.

# Exports to be hit hard by the drought in 2023, while imports will decrease mainly due to the fall of global energy prices

## ACCRUED TRADE BALANCE VS. CASH

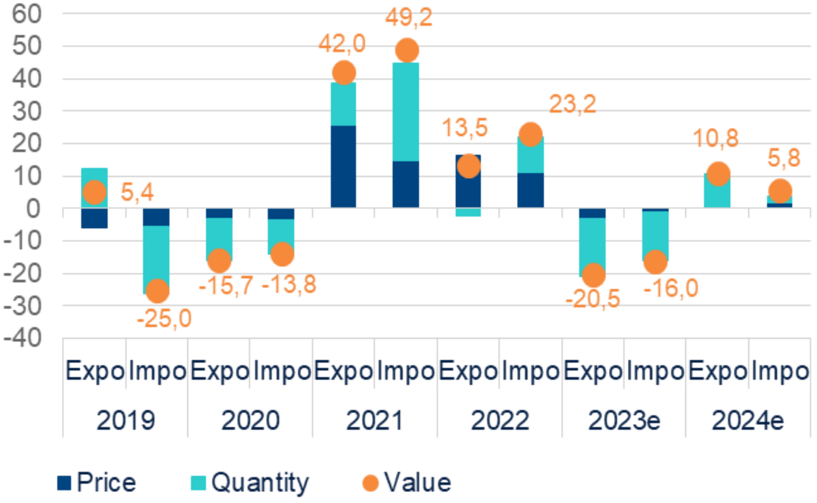
(MILLIONS OF USD, 12-MONTH MOVING SUM)




Source: BBVA Research BCRA and INDEC.

## EXPORTS AND IMPORTS

(VAR % YOY)

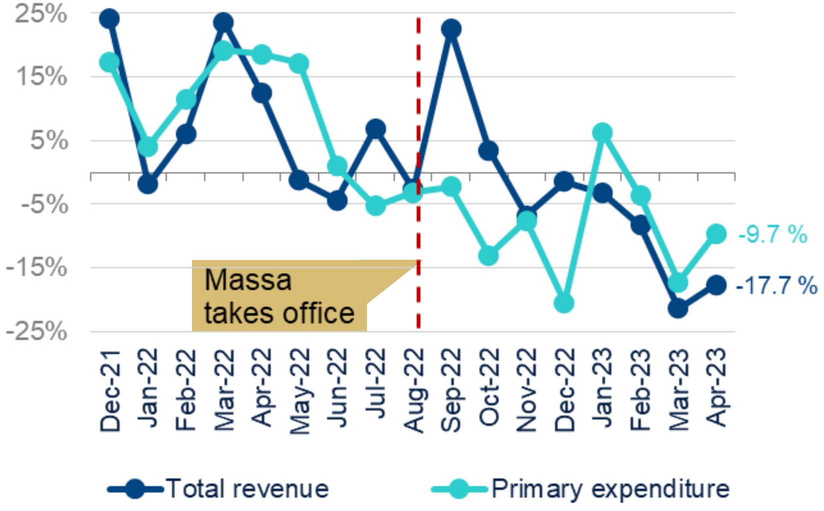



Source: BBVA Research and INDEC.

This year exports will fall to USD 70.3 bn (USD -18 bn) while imports will stand at USD 68.5 bn (USD -13.0 bn). The decrease of dollar inflows due to the drought forced the Government to impose harder import restrictions, which is leading to an increase in importers' commercial debt. Year to date, this debt has increased by USD 3.85 bn, (2022 = USD 12.8 bn).

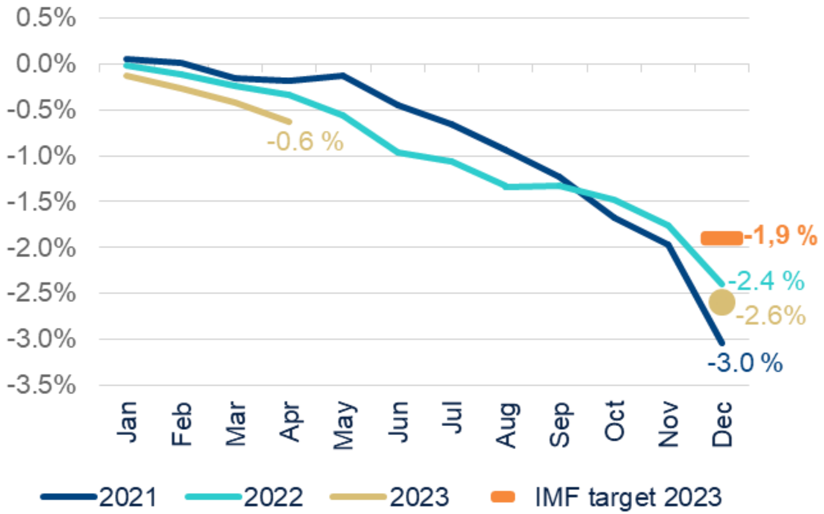
# The fiscal deficit is widening in 2023, with public expenditure decelerating at a slower pace than the fall in fiscal revenues...

## FISCAL REVENUES AND PRIMARY EXPENDITURE
(% CHANGE Y/Y, IN REAL TERMS)




Source: Ministry of Economy and BBVA Research.

## FISCAL RESULT
(% GDP, YEAR ACCUM.)

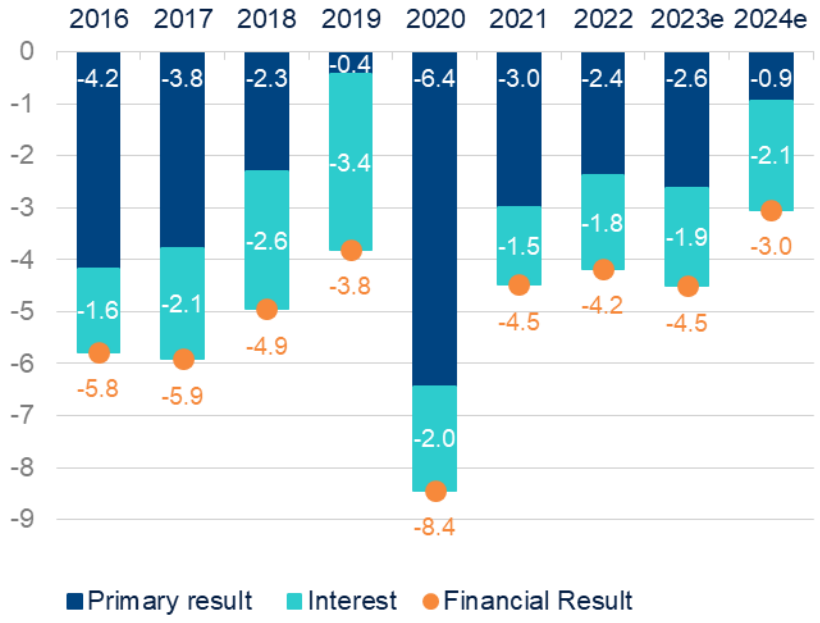



Source: Ministry of Economy and BBVA Research.

The advance of export duties in order to meet the 2022 target (soybean dollar I and II) and the delicate situation left by the drought prevent fiscal revenue recomposing itself this year, making it very challenging to meet the 2023 fiscal target agreed with the IMF (1.9% of GDP; BBVAe: 2.6% of GDP). The Government is cutting energy subsidies, but it is not enough to offset lower revenues.

# …we therefore forecast a primary fiscal deficit at 2.6% of GDP by 2023 and continue to expect a correction to 0.9% in 2024

**FISCAL RESULT**
(% GDP)

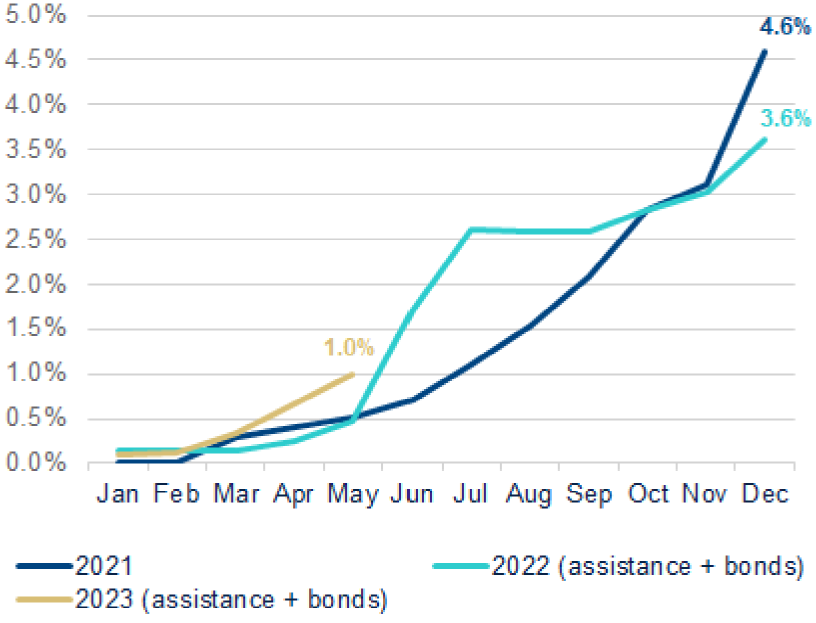



Source: Ministry of Economy and BBVA Research.

- The fiscal correction for 2024 will be a priority to be able to continue with the IMF program and reduce the country's sovereign risk.
- More favorable weather conditions for the agricultural sector will make it possible to reverse the sharp drop in foreign trade tax revenues next year.
- High inflation will help to cut public spending in real terms. The reduction in economic subsidies - currently equivalent to 2% of GDP - will represent the core of the fiscal adjustment next year.

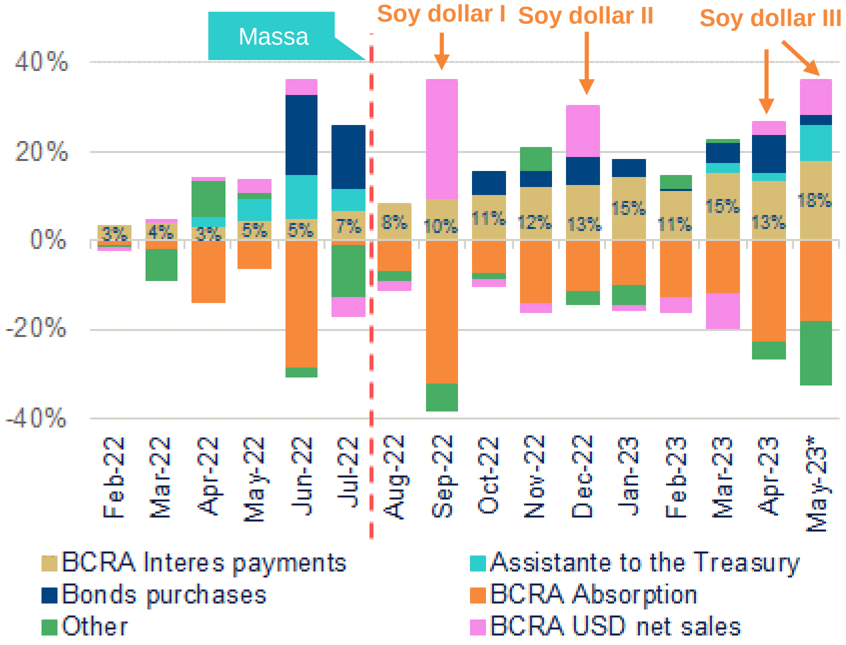
# The deterioration of the fiscal accounts at the start of 2023 translates into greater needs for monetary issuance by the BCRA....

## MONEY ISSUED TO FINANCE FISCAL NEEDS AND BOND PURCHASES (% GDP)




Source: BBVA Research and BCRA.

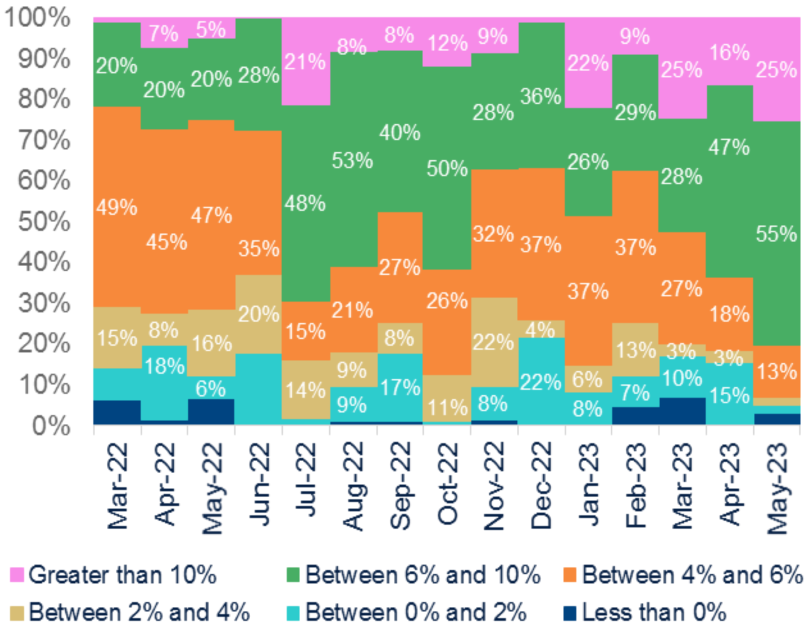
## MONETARY BASE: EXPANSIONARY FACTORS (% OF THE PREVIOUS MONTH'S MONETARY BASE)




Source: BBVA Research and BCRA.

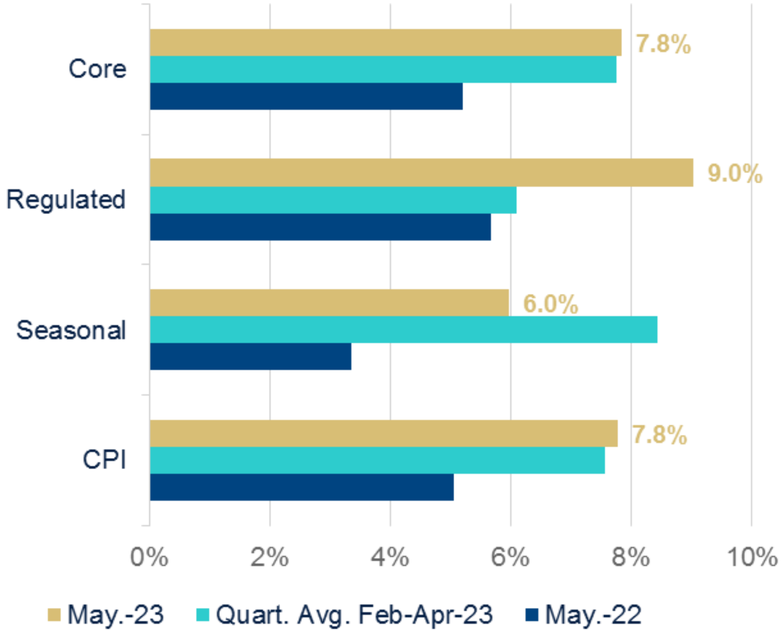
# … boosting exchange rate and inflationary pressures, which have already pushed inflation to a higher, more volatile and un-anchored level...

## MONTHLY CHANGE OF ITEMS WITHIN THE CPI
(AS % OF CPI-BA BASKET, ACCORDING TO M/M % CHANGE)




Source: BBVA Research and Department of Statistics of the City of Buenos Aires.

## MONTHLY INFLATION
(CHG. % M/M)

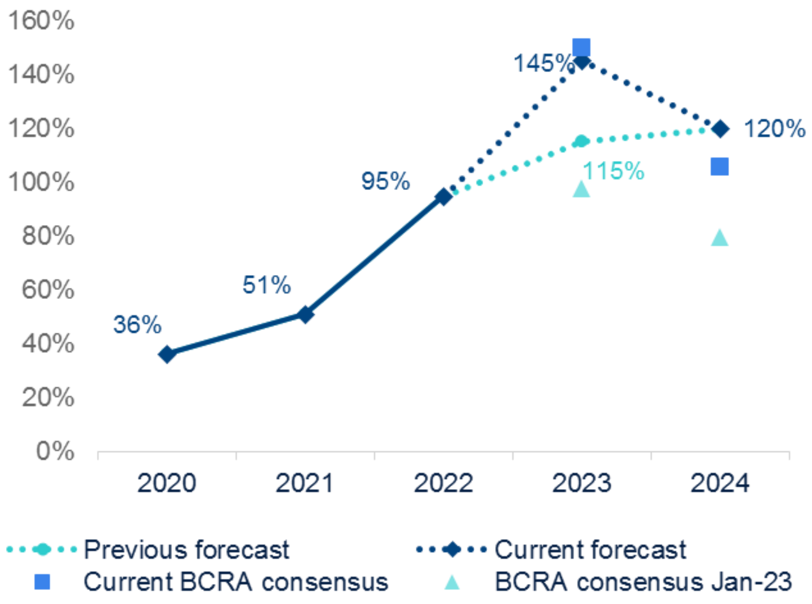



Source: BBVA Research and INDEC.

# …therefore, we raised the annual inflation forecast for 2023 to 145% (from 115%)

## OBSERVED AND EXPECTED INFLATION BY BBVA AND THE ANALYSTS' CONSENSUS

(CHG. % Y/Y)

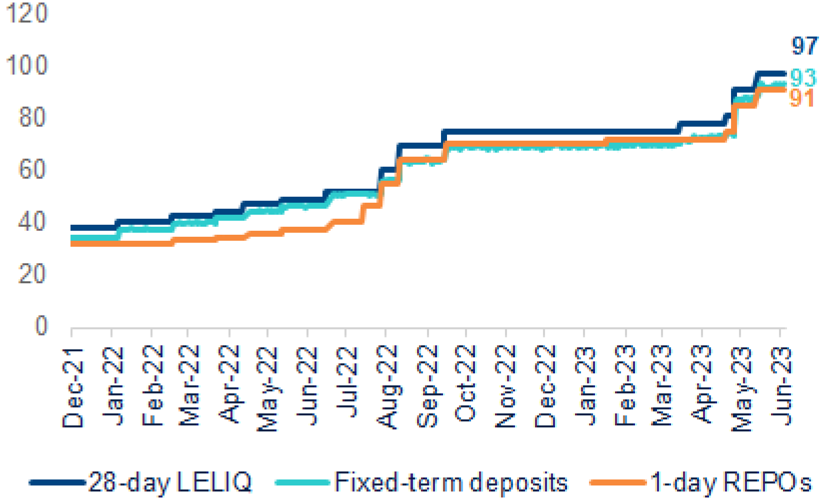



Source: BBVA Research and BCRA.

- The de-anchoring of expectations and the absence of a stabilization plan for the remainder of the current government's term ensure an inflation floor of 7.5% m/m for the rest of the year.
- We are facing a new quantitative and qualitative change in the high inflation scenario. Monthly inflation averages 7.3% in 2023 and we find no reason to believe that it may come down.
- The government will only aim to apply palliative measures to avoid further acceleration until the elections.
- We are revising upward our forecast to 145% by 2023, although any disruptive event in any month this year may push it higher.

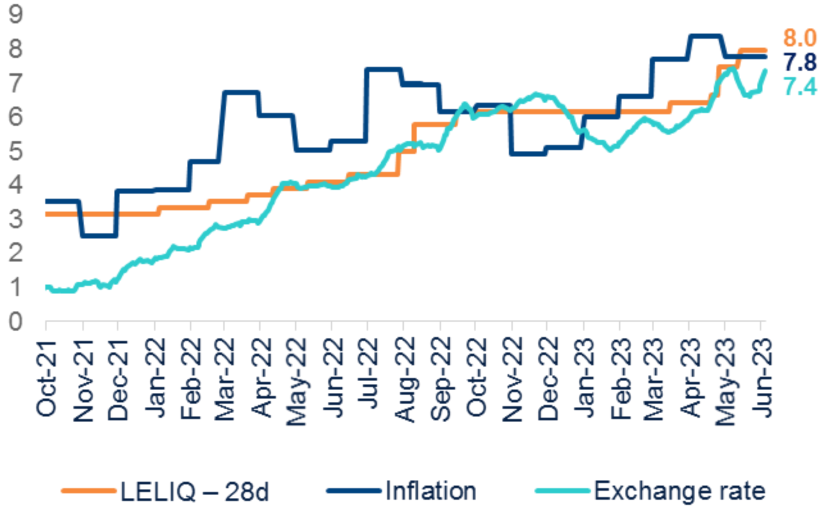
# The BCRA raised the reference interest rate to 97%, bringing it in line with expected inflation, but it will not have a substantial effect on prices...

## INTEREST RATES
(% ANR)




Source: BBVA Research and BCRA.

## MONTHLY INTEREST RATES, INFLATION AND EXCHANGE RATE VARIATION (FX: DAILY CHG ON A MONTHLY BASIS, AVG 7-DAY MOVING AVERAGE)

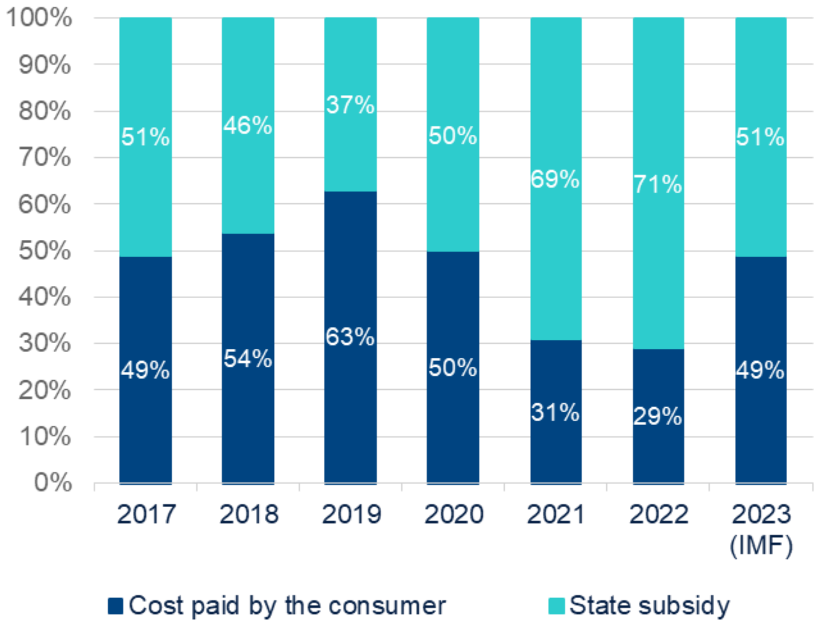



Source: BBVA Research and BCRA.

Rising interest rates underpin the attractiveness of peso deposits, but are barely in line with inflation expectations for the coming months. We do not anticipate a substantial impact on prices and expect further increases to around 100% as we approach the elections, with more pronounced hikes in Dec-23 to 120%.

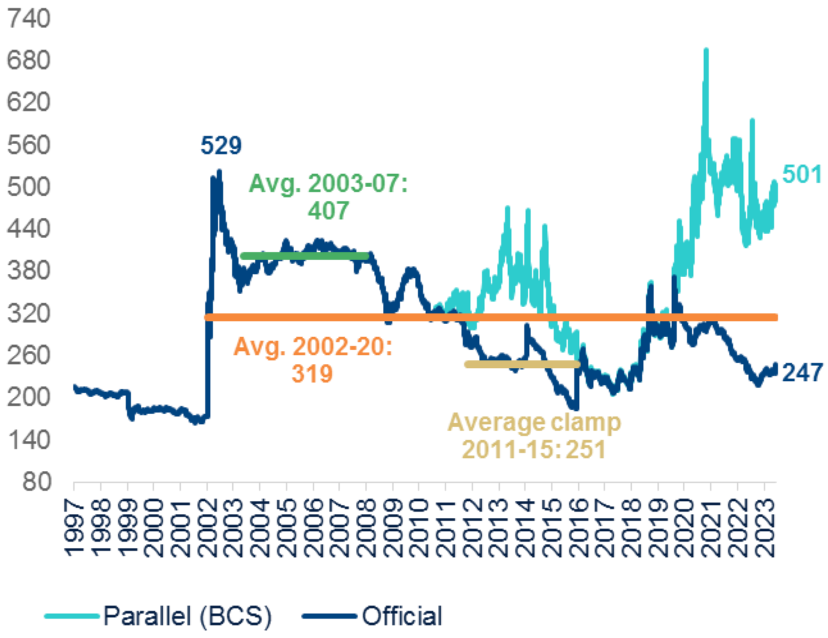
# …and continues with the (exhausted) instruments to fight inflation: utility prices and FX peg, which have already had little effect at a very high cost

## COVERAGE OF THE COST OF ELECTRIC ENERGY
(%)




Source: BBVA Research and FMI.

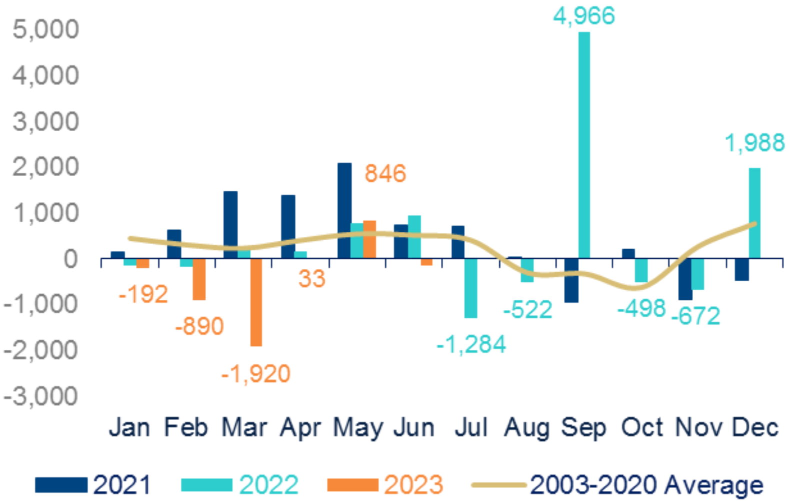
## OFFICIAL REAL EXCHANGE RATE AND PARALLEL EXCHANGE RATE (BLUE CHIP SWAP)
(PESOS PER DOLLAR, CONSTANTE PRICES OF 14/JUN/23)




Source: BBVA Research and BCRA.

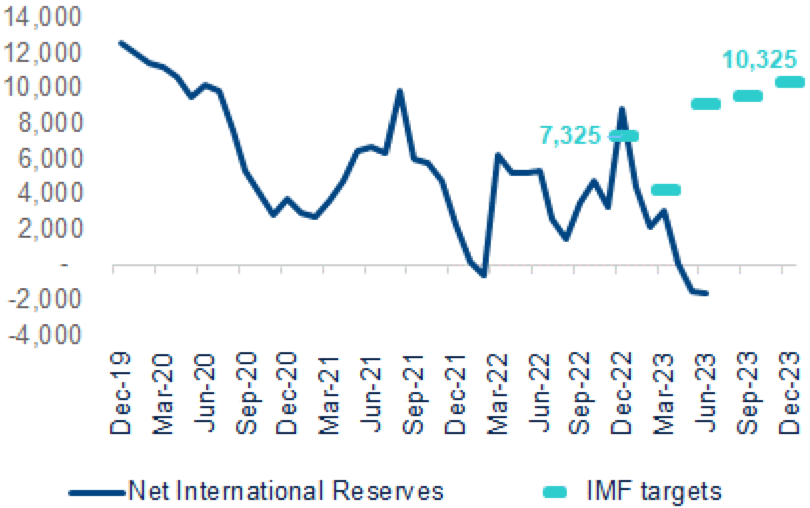
# The substantial exchange rate imbalance deepened in 1Q23, leading the BCRA to sell a record level of international reserves

## BCRA's NET FX SALES ON THE OFFICIAL EXCHANGE MARKET (USD MILLION)




Source: BCRA, IMF and BBVA Research.

## NET INTERNATIONAL RESERVES (USD MILLION)



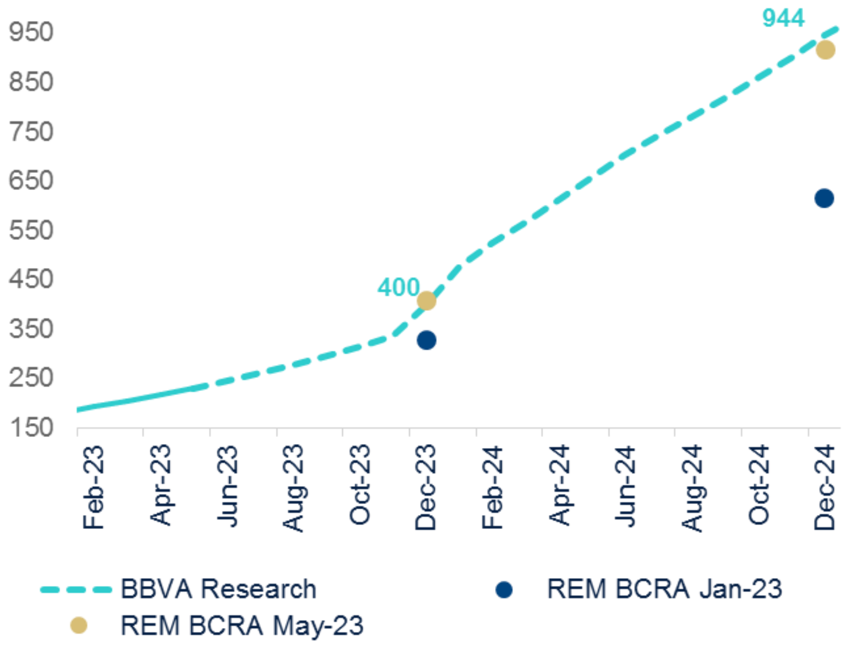

Source: BCRA, IMF and BBVA Research.

Year-to-date, the BCRA sold more than USD 2 billion to avoid a devaluation jump, depleting its international reserves.

The IMF agreed to relax the reserves target for this year by USD 1.8 billion. However, we expect further reductions in the future as the target remains impossible to meet.

# Given the observed acceleration of inflation and the vulnerable situation of the foreign exchange market, we have raised our exchange rate forecast for 2023

**OFFICIAL EXCHANGE RATE AND FORECASTS**
(ARS/USD, MONTHLY AVERAGE)

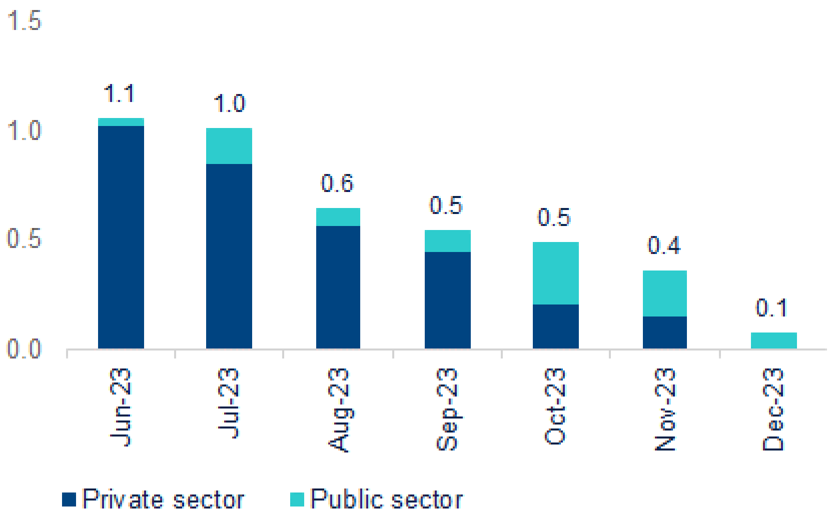



Source: BBVA Research and BCRA.

- The government will maintain its stance on avoiding an exchange rate jump at all costs until the elections, through a deepening of FX restrictions and the implementation of multiple exchange rates for different sectors.
- The administration that takes office at the end of the year will have no margin to maintain this position, so we estimate that an exchange rate correction will take place by the end of the year.
- The exchange rate would grow more than inflation in 2024 to gain competitiveness and reach an equilibrium in the official exchange market.
- Given the electoral calendar, there is a risk of exchange rate instability in the months leading up to the general election.

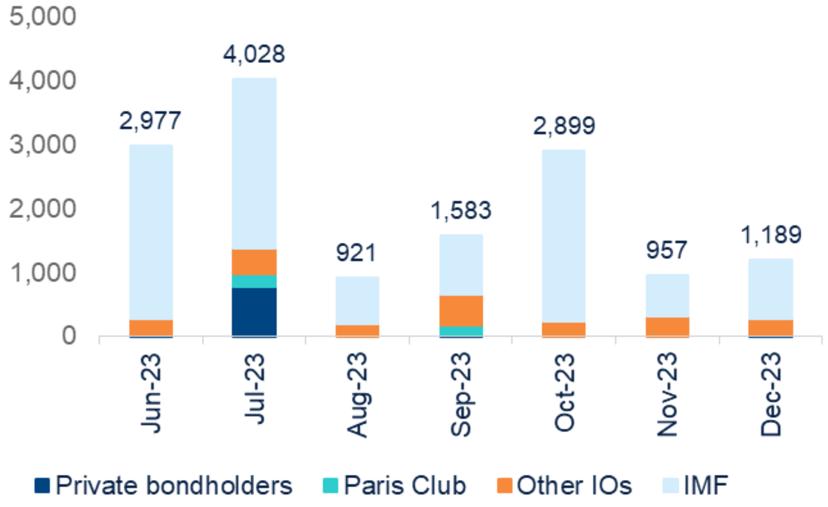
# The government managed to clear the bulk of the 2023 debt obligations in pesos, eliminating one of the main risk factors for the year

## PUBLIC DEBT MATURITIES IN PESOS, BY CREDITOR
(TRILLIONS OF PESOS)




Source: Ministry of Economy and BBVA Research.

## PUBLIC DEBT MATURITIES IN USD, BY CREDITOR
(USD MILLION)




Source: Ministry of Economy and BBVA Research.

With the recent voluntary peso debt swap, the government largely cleared the 2023 payment schedule and reduced *roll-over risks.* The stressed front now is that of foreign currency, as payments to private bondholders (in July), Club the Paris and to the IMF have yet to be made (while international reserves stand at a very low level).

# Macroeconomic Forecasts

| | 2020 | 2021 | 2022 | 2023f | 2024f |
|---|---|---|---|---|---|
| Gross Domestic Product (% YoY) | -9.9 | 10.4 | 5.2 | -3.5 | -2.0 |
| Inflation (% YoY eop) | 36.1 | 50.9 | 94.8 | 145.0 | 120.0 |
| Exchange Rate (vs USD, December avg.) | 82.6 | 101.9 | 172.9 | 400.0 | 944.0 |
| Monetary Policy Rate (% eop) | 37.1 | 36.7 | 75.0 | 120.0 | 65.0 |
| Private Consumption (% YoY) | -13.7 | 10.0 | 9.4 | -2.7 | -4.9 |
| Public Consumption (% YoY) | -1.9 | 7.1 | 1.8 | -4.0 | -7.1 |
| Private Investment (% YoY) | -13.0 | 33.4 | 10.9 | -17.0 | 4.6 |
| Primary Fiscal Balance (% GDP) | -6.4 | -3.0 | -2.4 | -2.6 | -0.9 |
| Current Account Balance (% GDP) | 0.8 | 1.4 | -0.6 | -2.4 | -1.7 |

Source: INDEC, BCRA and BBVA Research.

# Disclaimer

BBVA Research

# Argentina Economic Outlook

June 2023

Creating Opportunities