Macro scenario - Argentina

July 12, 2024

Reforms lay the groundwork for a post-stabilization recovery

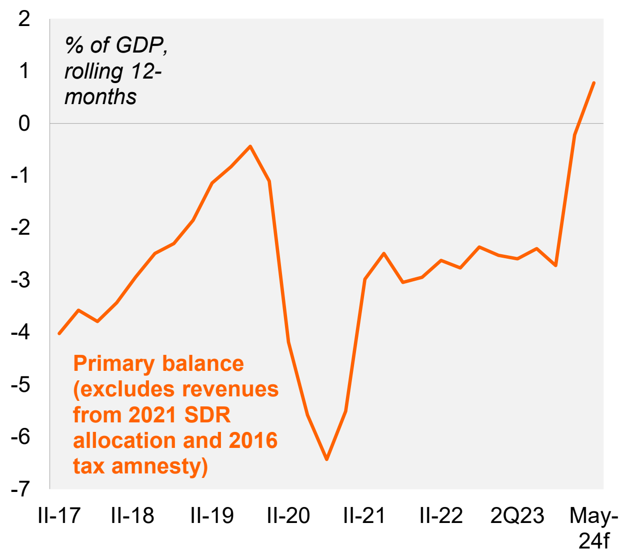
- The approval of the "Bases" bill and the fiscal package should be a turning point in the administration's efforts to stabilize and deregulate the economy, foster investment, and gradually improve the fiscal accounts. The approval of the fiscal package led us to raise our primary fiscal surplus projection for 2024 to 1.0% of GDP, from 0.5% in our previous scenario.
- Following sequential contractions in economic activity over the past two quarters, the economy fell again in April, and uncertainty persists regarding the removal of capital controls, leading us to revise our GDP growth forecast to -3.5%, from -3.0%, materializing downside risks we had flagged earlier. We still envisage an improvement in economic activity later this year, driven by the normalization of the agricultural sector.
- We revised our nominal exchange rate forecast to ARS 1,027/USD for YE24 (from ARS 1,150/USD previously) assuming that the central bank will maintain the current crawling peg policy through December 2024. We reduced our inflation forecast to 130% for YE24 (from 140%), reflecting a stronger ARS and weaker activity.

Habemus Law

The approval of the Bases bill and the fiscal package should be a turning point for the ambitious stabilization plan and deregulation program proposed by President Milei (see our report for more details here). While it is watered down from its original version, the approved Bases bill includes the so-called delegated powers to the government, the reorganization of the public administration, privatizations, changes that favor investment towards Argentina, and labor reform, among others. In a separate bill, a similarly diluted fiscal package was approved, which is projected to raise tax revenues by roughly 0.5% of GDP per year. The approval of the fiscal package appears to be key to the proposed fiscal consolidation path and the IMF targets, consistent with a primary surplus of 1.7% of GDP in 2024 (from a deficit of 2.7% in 2023).

Fiscal surpluses continued in May. Argentina's Treasury ran another fiscal surplus in May, reaching a primary balance of 1.0% of GDP during the first five months of the year, while the nominal balance stood at 0.4% of GDP. Based on these figures, we estimate a consolidated nominal deficit of around 1.5% of GDP year to date (including net interest payments from the central bank), narrowing from 4.3% in the same period of 2023.

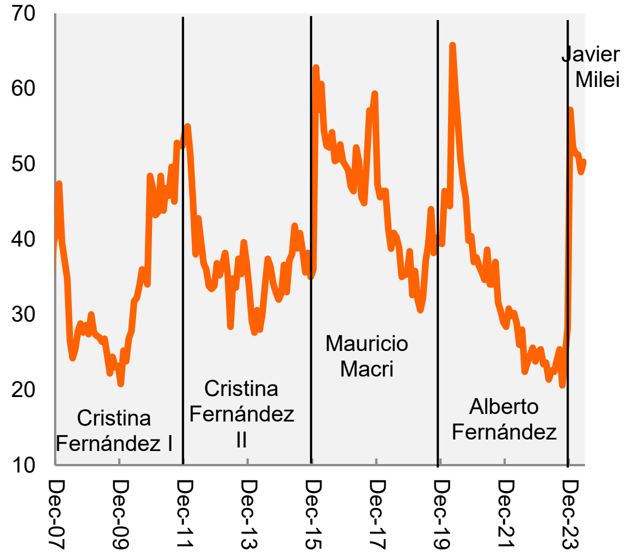
Primary fiscal surplus



Source: Ministry of Economy, Itaú

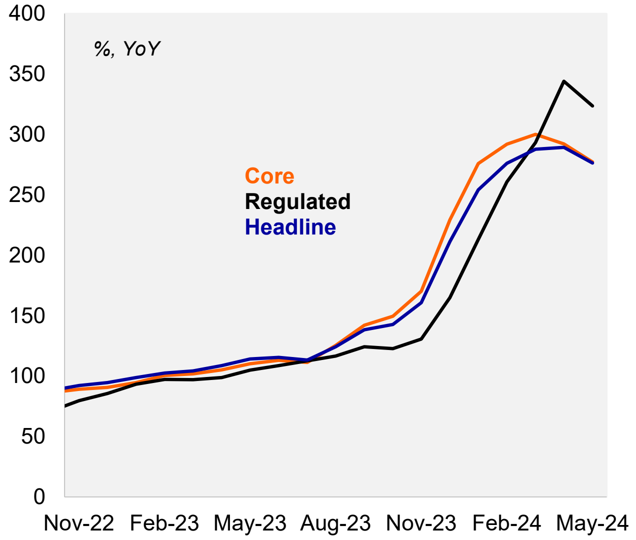
Confidence in the administration remains strong. Confidence in the government, according to the monthly survey conducted by Universidad Torcuato Di Tella, fell slightly in June to 49.2% from 50.3% in May. The index, closely watched by market participants as a proxy for the population's willingness to tolerate the macro adjustment as well as the administration's ability to implement its stabilization program, is 14.0% below its peak in December, when the government took office, but at a still decent level.

Confidence on the Government Index



Source: UTDT

Falling inflation



Source: INDEC

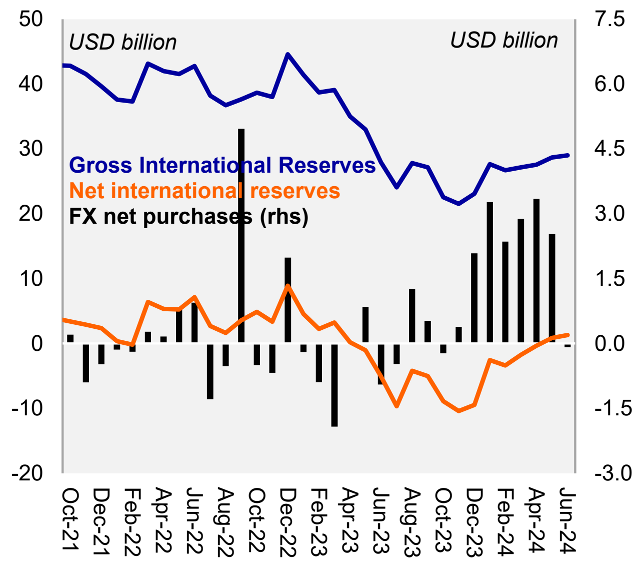
Annual inflation over the hump

Consumer prices rose by 4.2% mom in May (from 8.8% in April), marking the lowest reading since January 2022, driven by the appreciation of the ARS and weak activity. The 12-month inflation reading fell to 276.4% in May, from a peak of 289.4% in April. The Eco Go price tracker estimates inflation of 5.6% mom for June, up from May due to adjustments in electricity tariffs. In our view, the significant real appreciation of the currency and weaker consumption, contributed to the slowdown in monthly inflation. Meanwhile, inflation expectations continue to fall, with analysts surveyed by the central bank expecting 69% inflation over the next 12 months (down from 88% in the previous survey).

Net international Reserves return to positive ground

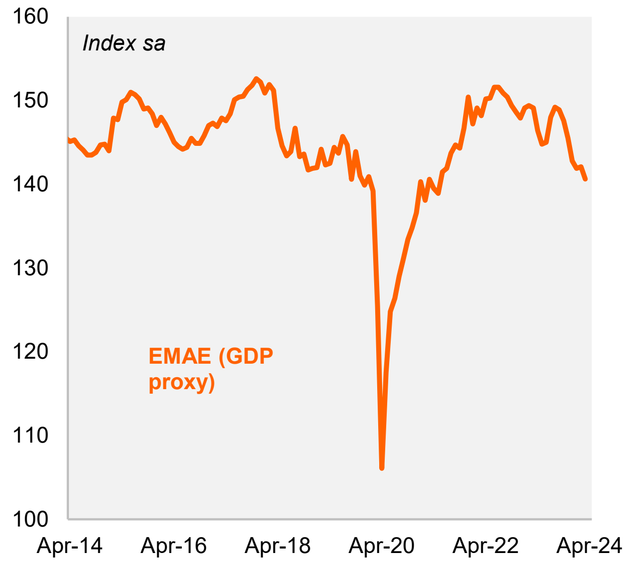
Following the IMF's disbursement of USD 800 million (after meeting all quantitative targets for 1Q24), net reserves returned to positive ground. Net international reserves ended June at around USD 1.3 billion, compared with a negative balance of USD 10.4 billion before the new administration took office. The central bank has purchased USD 17.0 billion year-to-date, despite a recent deceleration of export liquidations amid an appreciation of the official exchange rate. Meanwhile, the central bank continues with its crawling peg policy of a depreciation pace of 2.0% mom. In our view, the expected rebound in economic activity should lead to higher imports in the coming months (leading to greater demand for foreign currency), while multiple exchange rates (such as the so-called USD-blend) work against reserve accumulation in 2H24, given that the central bank can purchase 80% of exports.

International reserves



Source: BCRA

Waiting to rebound



Source: INDEC

Monetary framework: Stage 2

After the elimination of monetary financing of the fiscal deficit, the government advances in the elimination of monetary issuance of interest payments on remunerated liabilities. Thus, the government has decided to replace central bank interest-bearing liabilities with Treasury debt. However, the central bank will continue to manage monetary policy. According to the officials, the monetary autonomy of the BCRA should be restored, since the interest rate will not have an endogenous peso-creating effect on the economy. At the end of June, the stock of central bank remunerated liabilities reached the equivalent of USD 17 billion.

Activity recovery still to come

Activity contracted at the start of 1Q24. GDP fell in 1Q24 by 5.1% yoy, reflecting the fallout of the stabilization program. On a sequential basis, GDP contracted by 2.6% qoq/sa, following a contraction of 2.5% in 4Q23. Thus, the statistical carryover for 2024 stood at -3.9%. In 1Q24, real wages fell by 21.1%, while at the same time the employment rate fell slightly, from 45% in 1Q23 to 44.3% in 1Q24. As a result, we estimate that the real wage bill fell by 21.7% yoy in 1Q24. In that context, the EMAE (official monthly GDP proxy), activity fell by 0.1% mom/sa in April, leading to a drop of 1.6% qoq/sa in the quarter ended in that month. On a year-over-year basis, activity declined by 1.7% in April and contracting by 4.3% in the quarter ended in that month.

Following the saga in congress, all eyes move to the expected recovery of activity

Activity continues to contract sharply at the start of 2Q24. Following the sequential contractions over the past two quarters, which continued in April, we are projecting an improvement later this year, led by the normalization of the agricultural sector. However, we lowered our GDP growth forecast to -3.5%, from -3.0% in our previous scenario. The timing of the removal of capital controls remains uncertain. We revised our nominal exchange rate forecast to ARS 1,027/USD for YE24 (from ARS 1,150/USD before), assuming that the central bank will maintain the current crawling peg policy through year-end. A stronger ARS and weaker activity led us to lower our inflation forecast to 130% for YE24 (from 140%). Our forecast for the policy rate stands at 30% (from 40% currently). Following the approval of the fiscal package in congress we have improved our primary fiscal surplus to 1.0% of GDP in 2024, from 0.5% in our previous scenario.

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Argentina | Forecasts and Data

	2019	2020	2021	2022	2023F	2024F		2025F	
						Current	Previous	Current	Previous
Economic Activity									
Real GDP growth - %	-2.0	-9.9	10.4	5.3	-1.6	**-3.5**	-3.0	**3.5**	2.5
Nominal GDP - USD bn	452.0	385.3	487.3	630.6	597.6	**649.7**	639.9	**778.2**	702.5
Population (millions)	44.9	45.4	45.8	46.2	46.6	**47.1**	47.1	**47.5**	47.5
Per Capita GDP - USD	10,057	8,490	10,640	13,643	13	**14**	13,595	**16**	14,790
Unemployment Rate - year avg	9.8	11.6	8.8	6.8	6.1	**8.5**	8.5	**8.0**	8.0
Inflation									
CPI - % (*)	53.8	36.1	50.9	94.8	211.4	**130.0**	140.0	**50.0**	50.0
Interest Rate									
Reference rate - eop - %	55.00	38.00	38.00	75.00	100.0	**30.0**	30.0	**30.0**	30.0
Balance of Payments									
ARS / USD - eop	59.90	84.15	102.75	177.10	809	**1027**	1150	**1500**	1700
Trade Balance - USD bn	16.0	12.5	14.8	6.9	-6.9	**15.0**	15.0	**15.0**	15.0
Current Account - % GDP	-0.9	0.9	1.4	-0.7	-3.4	**1.5**	1.5	**1.7**	1.7
Foreign Direct Investment - % GDP	1.5	1.1	1.4	2.4	3.8	**1.0**	1.0	**2.0**	1.0
International Reserves - USD bn	44.8	39.3	39.6	44.6	23.1	**28.0**	31.0	**35.0**	35.0
Public Finances									
Primary Balance - % GDP (**)	-0.4	-6.5	-3.0	-2.4	-2.7	**1.0**	0.5	**1.0**	1.0
Nominal Balance - % GDP (**)	-3.8	-8.5	-4.5	-4.2	-4.4	**-1.1**	-1.6	**-1.2**	-1.2
Gross Public Debt - % GDP	93.8	108.7	82.8	87.7	163.3	**83.2**	169.5	**81.4**	166.4
Net Public Debt - % GDP (***)	57.8	66.9	48.1	48.7	92.6	**45.8**	96.6	**45.3**	95.3

(*) National CPI since 2017.
(**) Excludes central bank transfer of profits from 201
(***) Excludes central bank and social security holding.
Sources: Central Bank, INDEC and Itaú

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