Macro scenario - Argentina

April 12, 2024

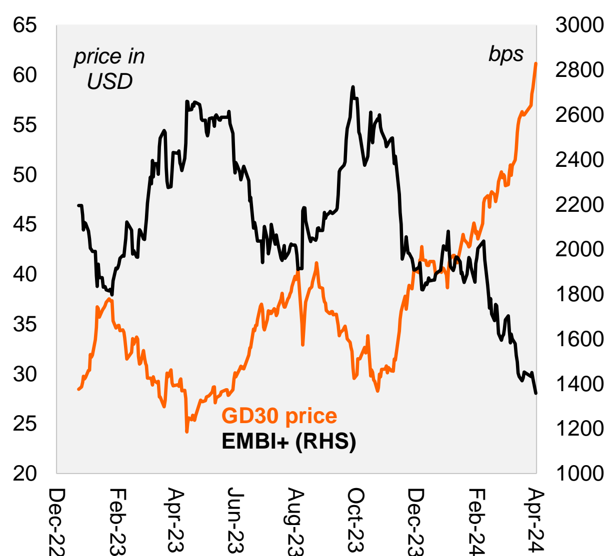
So far, so good, from a macroeconomic perspective

- The stabilization program marches on, yielding a faster-than-expected improvement across nominal data and an unprecedented fiscal consolidation, contributing to a recovery of Argentinean assets. Monthly inflation decelerated, helped by the appreciation of the currency, while the fiscal balance swung positive in the first two months of the year. We now envisage a primary fiscal surplus of 0.5% of GDP in 2024 (from 0% of GDP in our previous scenario).
- We maintain our GDP growth forecast at -3.0%, with downside risks considering the significant decline in real wages and the effects of the swift fiscal consolidation, despite the normalization of the agriculture sector. We still foresee inflation falling to 180% by year-end 2024, with upside risks, down from 211.4% in 2023.
- We revised our nominal exchange rate down to ARS 1,500/USD by YE24 (from ARS 1,695 in our previous scenario), assuming a softer acceleration of the crawling peg policy starting in 2Q24. We reduced our monetary policy rate forecast to 70% by year-end, from 80% previously.
- While from a macroeconomic perspective the program is performing in line or better than expectations, from a political viewpoint the challenges are still dauting, as the effects of “corrective inflation” have yet to peak.

Fiscal discipline reigns supreme

Argentina’s treasury ran another fiscal surplus in February. After running two consecutive monthly fiscal surpluses at the start of the year, we estimate a sharp decline in the 12-month primary deficit, to 0.7% of GDP (from the 2.9% estimated for 2023), while the nominal fiscal balance fell to -2.9% (from -4.7% in December). We note that a large part of the adjustment in the primary expenditures came from a drop in pension payments (-38.2% yoy in real terms in the first two months of the year) and payrolls (-19.5% yoy in the period), both affected by the sharp acceleration of inflation. Although the beginning of the year is promising for fiscal accounts, maintaining steep expenditure contractions during the rest of the year appears challenging in a stagflationary scenario, as we have highlighted in previous notes.

A positive reaction



Source: Bloomberg

Milei maintains popular support

The government’s emergency deregulation decree implemented at the beginning of the year was rejected by the Senate in March, and now heads to the Lower Chamber. We note that to be repealed, the decree needs to be rejected by both chambers of

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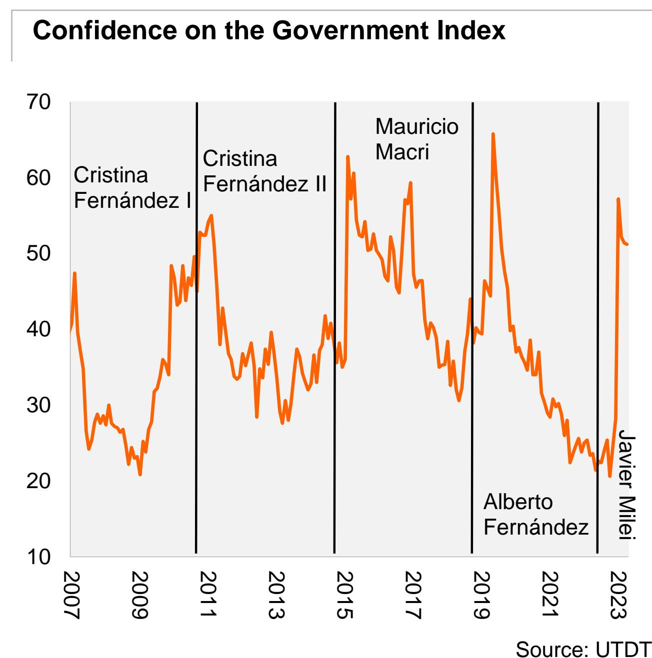
Congress. The decree's rejection in the Senate was a new setback for the government, which followed the decision to withdraw the omnibus bill from Congress in February, also due to the lack of votes. In our view, the government's limited representation in Congress, and the limits of population's tolerance of the adjustment's short-term costs pose significant challenges to the government's agenda. Having said that, confidence in the government remained elevated in March (51%), down only slightly from December (57%).

Confidence on the Government Index

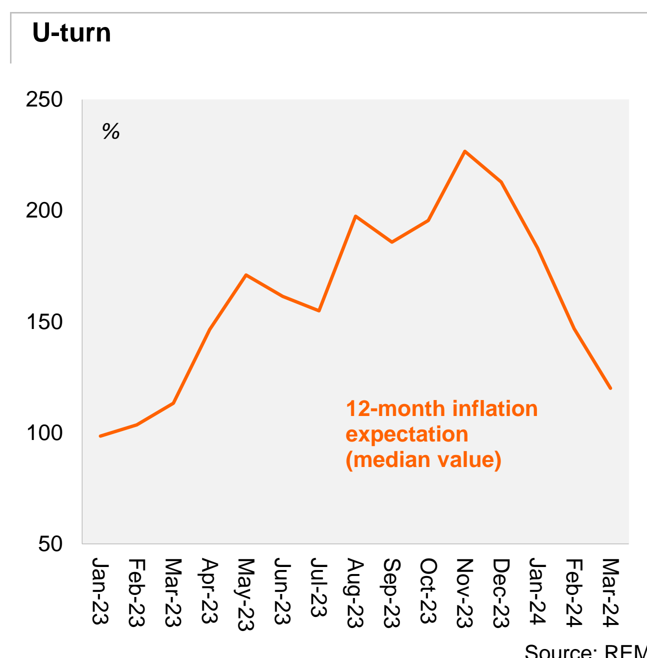


Source: UTDT

Monthly inflation decelerated and expectations recede

Inflation remains high, but deceleration has been sharper than expected. Consumer prices rose by 13.2% MoM in February (from 20.6% in January and 25.5% in December). In our view, the appreciation of the currency and weaker consumption contributed to the improvement at the margin, with monthly inflation projected to fall to one digit in 2Q24. Separately, survey-based one-year-ahead inflation expectations fell to 120.0%, down from a peak of 226.7% in November 2023.

U-turn



Source: REM

Lower rates

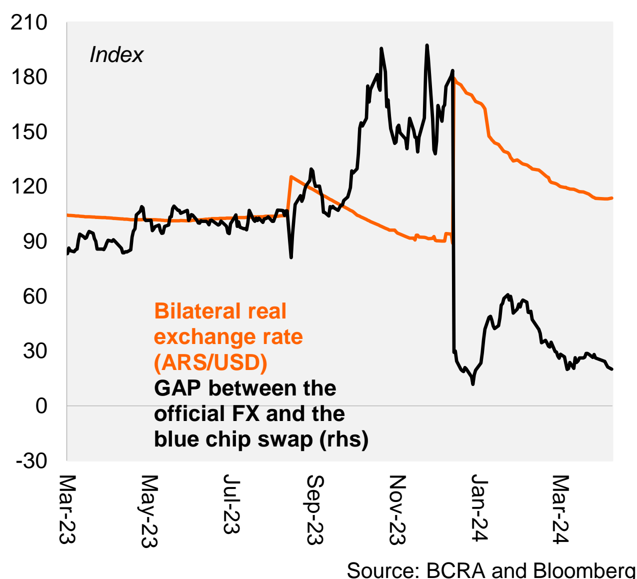
The central bank cut the monetary policy rate to 70%, down from 80% in March. This is the third cut since the new administration took office, reaching a cumulative reduction of 633 bps**.** The decision to lower rates followed the sharp deceleration of monthly inflation. While interest rates are negative in real terms, they are above the pace of depreciation of the official exchange rate (2.0% MoM), favoring carry, amid a sharp contraction of activity. Of course, this seems a brittle situation, as presumably inflation-adjusted currency appreciation cannot go on indefinitely.

The unification of the exchange-rate market gains prominence

The discussion on removing capital controls and unifying the exchange-rate market has moved to the center stage, somewhat earlier than expected. The recovery of international reserves due to the central bank purchases in the exchange-rate market and the stabilization of the gap between the official and the blue-chip swap (below 30% during March) have brought forward the discussion on the next steps of the stabilization program. The authorities have remained cautious on the issues, likely due to the still-challenging macroeconomic backdrop. In fact, to their credit, they are not downplaying the challenges ahead. The build-up of reserves was driven by the new import payment scheme. While importers have full access to the official exchange rate, the transaction must be in

installments, depending on the type of good (the majority in four equal monthly payments), leading to a higher debt with foreign suppliers. In the meantime, the market consensus and the NDF market prices foresee a slightly acceleration of the 2% monthly currency depreciation starting in April. In our view, the effectiveness of efforts to reduce inflation so far and upcoming seasonal export liquidations may lead the central bank to extend the current crawling peg for longer as a mechanism to reduce inflation even faster.

Exchange rate market

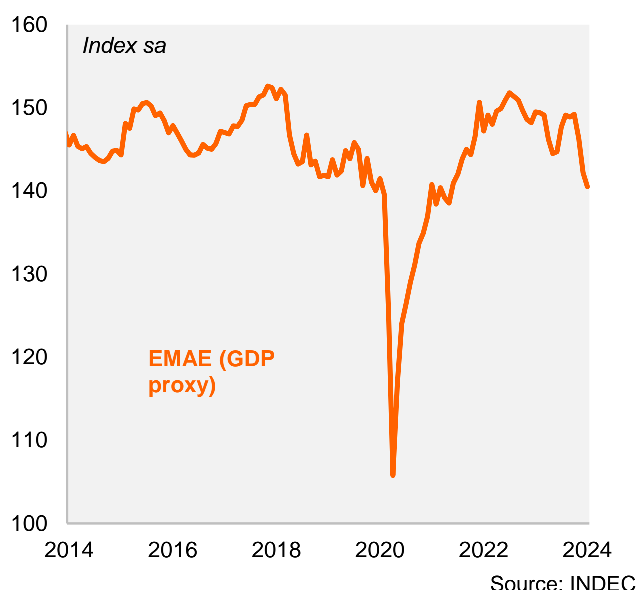


Source: BCRA and Bloomberg

Activity without signs of recovery

Activity contracted sequentially again in January, affected by the collateral effects of the stabilization program. According to the EMAE (official monthly GDP proxy), activity fell by 1.2% mom/sa in January (vs. a drop of 2.8% in December), leading to a contraction of 4.1% qoq/sa in the quarter ended in January (down from -1.8% qoq/sa in 4Q23). On a year-over-year basis, activity declined by 4.3% in January, leading to a 3.2% contraction in the quarter ended in that month (-1.5% yoy in 4Q23).

Activity contracted further



Source: INDEC

Stronger ARS, Lower Rates and Primary Fiscal Surplus

We revised our nominal exchange rate call down to ARS 1,500/USD by YE24 (from ARS 1,695 in our previous scenario), assuming a softer acceleration of the crawling peg policy since 2Q24. We also reduced our monetary-policy-rate forecast to 70% by year-end, from 80%, following recent adjustments by the BCRA and demand for treasury bills. We now envisage a primary fiscal surplus of 0.5% of GDP in 2024 (from 0% of GDP in our previous scenario) due to lower inertia from 2023 and better-than-expected results in the first two months of the year. We maintain our GDP growth forecast for 2024 at -3.0% with downside risks, considering the significant drop in real wages and sharp fiscal consolidation program. We also kept our inflation forecast for December 2024 at 180%, with risks tilted to the upside due to expected tariff adjustments.

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Argentina | Forecasts and Data

	2019	2020	2021	2022	2023F		2024F		2025F	
					Current	Previous	Current	Previous	Current	Previous
Economic Activity										
Real GDP growth - %	-2.0	-9.9	10.7	5.0	-1.6	-	**-3.0**	-3.0	**2.5**	2.5
Nominal GDP - USD bn	444.6	382.8	487.3	632.3	558.4	-	**561.8**	545.0	**554.8**	518.0
Population (millions)	44.9	45.4	45.8	46.2	46.6	-	**47.1**	47.1	**47.5**	47.5
Per Capita GDP - USD	9,894	8,559	10,640	13,679	11,971	-	**11,935**	11,578	**11,681**	10,906
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	-	**180.0**	180.0	**60.0**	60.0
Interest Rate										
Reference rate - eop - %	55.00	38.00	38.00	75.00	100.0	-	**70.0**	80.0	**60.0**	60.0
Balance of Payments										
ARS / USD - eop	59.90	84.15	102.75	177.10	809	-	**1500**	1695	**2350**	2650
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	0.8	1.5	-0.6	-3.6	-	**1.5**	1.5	**1.7**	1.7
Foreign Direct Investment - % GDP	1.5	1.1	1.4	2.6	3.8	-	**1.0**	1.0	**1.0**	1.0
International Reserves - USD bn	44.8	39.3	39.6	44.6	23.1	-	**31.0**	31.0	**35.0**	35.0
Public Finances										
Primary Balance - % GDP (**)	-0.4	-6.5	-3.0	-2.4	-2.7	-	**0.5**	0.0	**1.0**	1.0
Nominal Balance - % GDP (**)	-3.8	-8.5	-4.5	-4.2	-4.4	-	**-1.6**	-2.2	**-1.2**	-1.2
Gross Public Debt - % GDP	93.8	108.7	82.8	87.7	**93.1**	93.1	**97.2**	97.4	**95.8**	97.8
Net Public Debt - % GDP (***)	57.8	66.9	48.1	48.7	**53.5**	53.5	**56.3**	57.2	**56.0**	58.7

(*) 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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