

PARAGUAY

1. General trends

In 2012 Paraguay's GDP contracted by 1.2%, which equates to a 2.9% drop in per capita GDP. This setback was mainly the result of the sharp downturn in agriculture—the largest sector in the Paraguayan economy—in the wake of the severe drought that hit the country in late 2011 and early 2012. The countercyclical fiscal and monetary policies implemented during the year prevented an even greater contraction of the economy by boosting economic activity in the non-agricultural sector. The livestock sector posted solid growth in 2012, despite the negative impact of an outbreak of foot-and-mouth disease (detected in late 2011) on the country's meat exports. The fiscal impulse was reflected in a significant increase in government spending that caused a fiscal deficit equivalent to 1.7% of GDP, the first public account deficit since 2003. The year-on-year inflation rate was 4.0% at year-end, the lowest figure since 2009, reflecting the economic downturn and falling demand in 2012. In the external sector, the current account surplus narrowed from 1.1% of GDP in 2011 to 0.4% in 2012, mainly owing to the fall in volumes of agricultural exports during the year. Economic activity is expected to rally in 2013, primarily in the agricultural sector, resulting in estimated growth of 12.5%. The year-on-year inflation rate was 1.7% at June 2013, but for 2013 overall is likely to be pushed higher by the economic upturn and growing domestic demand. The fiscal balance is projected to improve in 2013 owing to the gradual withdrawal of the countercyclical policies implemented in 2012, and to a significant boost to public revenues from the revival of the economy and the introduction of the new personal income tax law. On the external front, strong export growth expected in 2013, driven by the agricultural and livestock sectors, will widen the current account surplus.

After President Lugo was impeached in June 2012 and the hitherto Vice President, Federico Franco, was sworn in, presidential elections were held in April 2013. The new President elect, Horacio Cartes, will take office on 15 August 2013.

2. Economic policy

(a) Fiscal policy

The slowdown in economic activity in 2012, caused by the decline in the agricultural sector, prompted the government to implement an expansionary fiscal policy, with a strong rise in public spending. Total central government expenditure was up by 24.2% in 2012, taking it to 20.1% of GDP, with hefty increases in both current and capital spending (24.5% and 23.4% respectively). Much of the jump in current expenditure went on improving the wages of public employees, which rose by 30% on average.

Public revenue collections grew by 8.7% over the previous year, largely due to a 23.0% rise in non-tax income. Amid lacklustre economic activity, tax receipts posted a moderate increase (of 5.0%), with the take from value added tax (VAT) up by a modest 4.3%. With agricultural exports down, taxes on foreign trade slipped by 3.6%. However, the impact of the agricultural downturn on public funds was limited by the sector's relatively small share of the government tax take.

The substantial growth of central government expenditure in 2012, far outpacing total revenue growth, led to a fiscal deficit equivalent to 1.7% of GDP. The primary balance also showed a deficit, of 1.5% of GDP. This was the first public account deficit since 2003.

On the legislative front, the personal income tax bill was approved and entered into force on 1 August 2012, having been shelved for the past four years. Before the bill was passed, Paraguay was the only country in Latin America without personal income tax. However, the law will not greatly increase public revenue in the short term because it will apply to only a limited number of taxpayers during the first few years. The law will also have an indirect impact on VAT receipts, since it encourages the formalization of certain transactions. The tax burden in Paraguay remains among the lowest in the region, despite increasing slightly to 12.3% in 2012.

Projections for 2013 indicate significantly faster growth in tax revenues than in 2012, owing to the recovery in economic activity and, probably, an upturn in agricultural exports. On the public spending side, the fiscal stimulus applied in 2012 will likely be gradually withdrawn, followed by a period of fiscal consolidation, thus reducing the fiscal deficit in comparison to 2012. According to 2013 national budget estimates, public revenue will see a 16.7% increase (compared with 8.7% in 2012) while expenditure will rise by 14.2% (24.2% in 2012), resulting in a deficit of 1.3% of GDP (lower than the 1.7% posted in 2012). These figures include a projected rise of 46.4% in capital expenditure, reflecting a shift in public spending towards investment, particularly on infrastructure.

The authorities expect this capital expenditure to be financed mainly by the proceeds of sovereign bonds issued in January 2013. This was the country's first international sovereign bond issue since 2000 and amounted to a total of US\$ 500 million. The transaction swelled Paraguay's external public debt by 17.2% between December 2012 and May 2013, to 8.0% of GDP. This nonetheless represents a relatively low level of debt compared with the rest of the region, and with Paraguay's own historical debt levels.

(b) Monetary policy

Given the economic contraction and low inflationary pressures in 2012, the Executive Committee for Open Market Operations and Reserves (CEOMA) of the Central Bank of Paraguay adopted an expansionary monetary policy stance. The weighted average interest rate on monetary regulation instruments thus fell from 6.6% in January 2012 to 5.5% in August, where it remained for the rest of the year. The balance of monetary regulation instruments dropped by 10.7% on average over the year.

Interest rates fluctuated in line with the rates on monetary regulation instruments. Real lending rates in foreign currency decreased from 11.3% to 10.1% between January and December 2012. The expansionary trend in bank credit to the private sector continued, but at a slower rate: from 28.2% in 2011 to 21.0% in 2012.

Monetary policy is expected to be tighter in 2013 than in the previous year, as the economy picks up and the monetary stimulus applied in 2012 is reduced. The weighted average interest rate on monetary regulation instruments rose from 5.6% in December 2012 to 5.8% in April 2013. In the same month, total bank lending to the private sector posted year-on-year growth of 11.3%, down from the 23.2% posted in April 2012.

(c) Exchange-rate policy

The nominal exchange rate of the guaraní against the dollar showed 3.4% year-on-year appreciation in late 2012, albeit following a relatively volatile course over the year. While the value of the guaraní remained more or less stable in the first quarter, it depreciated sharply during the second and third quarters, mainly owing to the widening of the country's current account deficit during this period. A change in trend from the fourth quarter onward culminated in a moderate year-on-year appreciation against the dollar in December. This trend accelerated during the early part of 2013, with the guaraní posting 4.3% year-on-year appreciation against the dollar in May. Contributing factors included the disbursements made to pay off the public debt, and large foreign-exchange inflows, received in exchange for energy transfers from the Itaipú and Yacyretá binational entities.

In terms of the real effective exchange rate, at December 2012 the guaraní showed appreciation against the dollar (by 6.1%), the euro (6.0%), the Argentine peso (8.2%) and the Brazilian real (12.3%). This trend carried over into the first few months of 2013, with the Paraguayan currency appreciating against these currencies by 3.7%, 0.5%, 9.4% and 2.0% respectively.

To mitigate the fluctuations of the guaraní against the dollar, in 2012 the central bank made net sales on the foreign exchange market totalling US\$ 697 million. Net international reserves stood at US\$ 4.994 billion (equivalent to 19.5% of GDP) in December, with little variation over the year. In the first few months of 2013, the central bank accumulated net purchases of US\$ 16.2 million, with net international reserves increasing substantially to US\$ 5.93 billion. This was attributable mainly to a surge in public-sector deposits in foreign currencies in the central bank resulting from January's sovereign bond issue.

(d) Other policies

In September 2012, a law was approved creating the National Public Investment and Development Fund (FONACIDE) and the Fund for Excellence in Education and Research.¹ The law requires the government to earmark over 80% of the revenue received from hydroelectric energy sales to Brazil, via the Itaipú dam, to investments in infrastructure and education. This revenue amounted to around US\$ 550 million in 2012. The new law reflects the shift in public expenditure to close the investment gaps that still exist in the country, particularly in infrastructure and education.

3. The main variables**(a) The external sector**

Goods and services exports accounted for US\$ 12.681 billion in 2012, a year-on-year decrease of 5.3%. This was the result of the decline in agricultural exports, especially soybeans (the country's main export product), following the drought that affected agricultural production in late 2011 and early 2012. Soybean exports were down by 31% in value and 38% in volume. In the livestock sector, and in spite of the animal health emergency arising from the outbreak of foot-and-mouth disease in late 2011, which led to the suspension of Paraguay's "FMD-free with vaccination" status, meat exports were up 6% in 2012. This is explained by the redirection of these exports to new international markets over the course of the year. Exports of the surplus energy produced at the Itaipú and Yacyretá hydroelectric plants edged down

¹ Law 4758/2012.

(by 2%) in 2012. Differing patterns were observed in Paraguay's exports to MERCOSUR countries (Argentina, Brazil and Uruguay), the country's main trade partners, which together account for around 50% of total exports. While the value of exports to Brazil and Uruguay climbed significantly, by 14% and 18%, respectively, exports to Argentina declined by 13%, largely owing to the trade barriers introduced by this country during 2012.

The value of goods and services imports decreased to US\$ 11.985 billion, a fall of 5.2% with respect to 2012. The value of consumer goods and capital goods imports declined by 7% and 17%, respectively, while imports of intermediate goods were up 5%. Within the intermediate goods category, imports of fuel and lubricants stood out with a 12% surge over 2012. The combined value of imports from Argentina, Brazil and Uruguay fell by 8%, in line with the downturn in the country's trade flows in 2012. Imports from China were down 13%.

The current account posted a surplus equivalent to 0.4% in 2012, smaller than the surplus recorded in 2011 (which was equivalent to 1.1% of GDP). As a result, the balance of payments went from a surplus of US\$ 784 million in 2011 to a deficit of US\$ 610 million in 2012. Already substantial capital inflows, mostly in the form of foreign direct investment, jumped by 27% in 2012 and helped reduce the balance-of-payments deficit. The balance of the external public debt remained at 8.8% of GDP in 2012. This reflected the fact that although capital and interest payments exceeded the disbursements received —by around US\$ 50 million— the effect was somewhat offset by the fall in GDP in 2012.

Paraguay's exports are expected to stage a strong recovery in 2013 on the back of an upturn in the agricultural sector and the reopening of the main meat export markets, especially Chile. Imports are projected to be up, as well, as the economy picks up in 2013. At May 2013, the value of goods exports posted a year-on-year increase of 39%. Year-on-year imports grew by 13% over the same period.

(b) Economic growth

Paraguay's GDP shrank by 1.2% in 2012. On the supply side, the deterioration was due to the contraction of its key sector —agriculture— owing to adverse weather conditions that caused a 28% fall in agricultural production in 2012. However, thanks to moderate growth (5%) in the non-agricultural sector, the drop in GDP was relatively slight considering the outright contraction in agriculture and its importance within the Paraguayan economy. The livestock sector recovered from the blow of the foot-and-mouth outbreak to deliver growth of 6%.

On the expenditure side, a marked increase (21%) in public consumption sustained domestic demand in 2012, which supported the growth of the non-agricultural sector. Lower household income and poorer consumer expectations led to the stagnation of private consumption, which edged up a meagre 1%, contributing to a modest upturn (of 3%) in total consumption. Gross fixed capital formation declined by 7.5%. The drop in exports of agricultural products was reflected in a 5.3% reduction in total exports. With falling private consumption keeping domestic demand sluggish, imports fell by 5.2% compared to the previous year.

A significant upturn in the economy is expected in 2013, driven by the recovery of the agricultural sector as a result of better weather conditions, and by the growth of the livestock sector. The projected growth rate is therefore around 12.5%.

(c) Inflation, wages and employment

The annual inflation rate was 4.0%, below the midpoint of the target range set by the central bank (5%, plus or minus 2.5 percentage points). Lower inflation in 2012 was the result of weak economic performance and falling prices for livestock-sector products, due to restrictions on meat exports to certain markets following the outbreak of foot-and-mouth disease. Year-on-year core inflation, which is calculated excluding the most volatile items in the basket (fruits and vegetables), stood at 3.9%. Year-on-year X1 core inflation, which excludes not only fruits and vegetables but also regulated services and fuels, was 4.0%. In May 2013, the year-on-year inflation rate was 1.7%. Low inflation over the year to date reflects falling food and energy prices.

The wage and salary index had increased by 4.4% at December 2012. The financial intermediation sector posted the highest growth (10.8%) while construction and the manufacturing industry had the lowest, at 1.7% and 2.2% respectively. Both figures are significantly below the inflation rate (4.0%) for the same period. The legal minimum wage has remained at 1,658,232 guaraníes since 2011, representing an annual average real reduction of 1.3% in 2012 compared to April 2011, and of 1.6% in the first five months of 2013.

According to the findings of Paraguay's continuous employment survey, the open unemployment rate was 8.1% in 2012, higher than the 7.1% recorded in 2011. The open unemployment rate during this period was 6.7% for men and 9.9% for women.

Table 1
PARAGUAY: MAIN ECONOMIC INDICATORS

	2004	2005	2006	2007	2008	2009	2010	2011	2012 a/
	Annual growth rates b/								
Gross domestic product	4.1	2.1	4.8	5.4	6.4	-4.0	13.1	4.3	-1.2
Per capita gross domestic product	2.1	0.2	2.9	3.5	4.5	-5.6	11.2	2.6	-2.8
Gross domestic product, by sector									
Agriculture, livestock, hunting, forestry and fishing	3.9	-0.1	3.6	14.3	9.2	-17.3	34.2	3.7	-20.1
Mining and quarrying	2.7	7.8	-2.2	3.5	5.0	3.0	3.2	5.3	1.5
Manufacturing	3.3	2.7	2.5	-1.2	2.0	-0.8	6.3	-1.6	4.6
Electricity, gas and water	3.6	2.8	8.5	5.9	3.5	4.8	5.1	8.7	7.0
Construction	2.1	4.5	-3.5	7.2	11.0	2.0	13.0	1.5	1.5
Wholesale and retail commerce, restaurants and hotels	5.1	2.4	5.5	5.1	4.2	-3.2	10.7	3.2	-2.1
Transport, storage and communications	9.6	7.2	10.7	10.7	5.2	-3.2	6.6	9.1	7.8
Financial institutions, insurance, real estate and business services	2.1	4.0	4.0	3.8	7.9	7.5	7.2	8.6	6.9
Community, social and personal services	2.7	5.9	4.3	3.0	3.9	11.5	9.1	6.2	15.9
Gross domestic product, by type of expenditure									
Final consumption expenditure	5.2	3.1	2.9	5.3	7.1	-0.5	13.5	8.2	3.1
Government consumption	6.0	11.5	4.0	3.0	3.5	13.7	12.0	5.3	21.0
Private consumption	5.2	2.2	2.8	5.5	7.5	-2.0	13.7	8.6	1.0
Gross capital formation	1.9	-12.2	8.2	4.8	20.6	-12.5	22.7	10.8	-7.5
Exports (goods and services)	8.3	11.2	3.8	9.3	2.0	-9.3	19.7	2.8	-7.0
Imports (goods and services)	9.9	8.1	2.0	9.7	7.0	-8.5	24.8	10.4	-3.5
Investment and saving c/	Percentajes of GDP								
Gross capital formation	16.6	17.0	17.1	15.8	16.4	13.8	16.2	16.2	15.0
National saving	18.4	17.2	18.3	17.1	14.7	14.2	13.0	17.3	15.4
External saving	-1.8	-0.2	-1.2	-1.3	1.7	-0.4	3.3	-1.1	-0.4
Balance of payments	Millions of dollars								
Current account balance	143	16	128	177	-319	68	-654	294	97
Goods balance	-244	-462	-621	-533	-1 064	-1 043	-1 397	897	845
Exports, f.o.b.	2 861	3 352	4 401	5 652	7 798	5 867	8 520	12 634	11 962
Imports, f.o.b.	3 105	3 814	5 022	6 185	8 862	6 910	9 916	11 737	11 117
Services trade balance	327	313	414	499	558	894	719	-150	-149
Income balance	-134	-58	-92	-162	-227	-302	-533	-1 167	-1 358
Net current transfers	194	224	426	373	414	519	557	714	759
Capital and financial balance d/	128	144	255	558	713	849	973	490	-707
Net foreign direct investment	32	47	167	178	272	194	340	215	273
Other capital movements	96	97	89	380	442	655	633	275	-979
Overall balance	271	160	383	735	395	916	319	784	-610
Variation in reserve assets e/	-179	-146	-387	-727	-394	-915	-319	-784	-10
Other financing	-92	-14	4	5	0	0	0	0	620
Other external-sector indicators									
Real effective exchange rate (index: 2005=100) f/	92.3	100.0	88.5	81.6	72.9	80.4	77.9	69.8	70.6
Terms of trade for goods (index: 2005=100)	107.1	100.0	98.1	102.7	110.2	107.8	107.8	110.3	111.4
Net resource transfer (millions of dollars)	-98	72	168	400	486	546	439	-676	-1 445
Total gross external debt (millions of dollars)	2 901	2 700	2 739	2 868	3 256	3 167	3 719	3 823	3 770
Employment	Average annual rates								
Labour force participation rate g/	63.4	61.8	59.4	60.8	61.7	62.9	60.5	60.7	...
Open unemployment rate h/	10.0	7.6	8.9	7.2	7.4	8.2	7.0	6.5	8.1
Visible underemployment rate i/	8.3	7.5	5.6	5.8	6.6	8.2	5.7	6.3	5.4

Table 1 (concluded)

	2004	2005	2006	2007	2008	2009	2010	2011	2012 a/
Prices	Annual percentages								
Variation in consumer prices (December-December)	2.8	9.9	12.5	6.0	7.5	1.9	7.2	4.9	4.0
Variation in nominal exchange rate (annual average)	-7.6	3.3	-8.7	-10.8	-13.5	14.3	-4.4	-11.7	5.4
Variation in average real wage	1.7	1.1	0.6	2.4	-0.8	4.6	0.6	2.8	0.7
Nominal deposit rate j/	5.7	6.1	9.8	5.9	6.2	3.4	2.0	4.7	5.4
Nominal lending rate k/	21.0	15.5	15.7	12.8	13.5	14.6	12.5	15.3	14.7
Central government	Percentajes of GDP								
Total revenue	15.9	15.7	16.0	15.6	15.8	17.5	17.1	17.4	18.4
Tax revenue	11.2	11.1	11.4	11.2	11.8	12.9	13.2	13.4	13.8
Total expenditure	14.6	15.0	15.5	14.8	13.5	17.5	15.9	16.7	20.1
Current expenditure	11.2	11.5	11.9	11.5	11.1	13.4	12.5	12.8	15.5
Interest	1.0	1.0	0.9	0.7	0.6	0.5	0.4	0.3	0.2
Capital expenditure	3.5	3.5	3.7	3.3	2.5	4.1	3.4	3.9	4.7
Primary balance	2.4	1.7	1.3	1.6	2.8	0.6	1.6	1.0	-1.5
Overall balance	1.4	0.7	0.4	0.9	2.3	0.1	1.2	0.7	-1.7
Central government public debt	35.1	29.4	22.6	16.5	14.5	14.4	13.9	11.7	10.9
Domestic	5.8	5.1	4.2	3.7	3.3	3.3	2.8	2.6	2.5
External	29.3	24.3	18.4	12.8	11.2	11.0	11.0	9.1	8.4
Money and credit	Percentages of GDP, end-of-year stocks								
To the private sector l/	11.7	11.8	11.6	14.4	18.4	22.9	27.2	29.6	32.3
Monetary base	8.5	7.9	8.0	9.3	9.4	12.8	10.8	10.7	12.1
Money (M1)	24.4	23.6	23.4	26.6	28.5	35.5	36.2	35.8	38.9
M2	13.1	13.6	14.2	17.1	17.5	23.0	22.1	22.7	24.7
Foreign-currency deposits	11.3	10.0	9.2	9.5	11.1	12.6	14.0	13.1	14.2

Source: Economic Commission for Latin America and the Caribbean (ECLAC), on the basis of official figures.

a/ Preliminary figures.

b/ Based on figures in local currency at constant 1994 prices.

c/ Based on values calculated in national currency and expressed in current dollars.

d/ Includes errors and omissions.

e/ A minus sign (-) indicates an increase in reserve assets.

f/ Annual average, weighted by the value of goods exports and imports.

g/ Nationwide total.

h/ Asunción and urban areas of the Departamento Central. Up to 2009, urban total.

i/ Urban total. New measurements have been used since 2010; the data are not comparable with the previous series.

j/ Weighted average of effective interest rates on time deposits.

k/ Commercial lending rate, local currency.

l/ Refers to the credit extended to the banking sector by the central bank.

Table 2
PARAGUAY: MAIN QUARTERLY INDICATORS

	2011				2012				2013	
	Q.1	Q.2	Q.3	Q.4	Q.1	Q.2	Q.3	Q.4	Q.1	Q.2 a/
Gross domestic product (variation from same quarter of preceding year) b/	6.9	4.9	3.3	2.6	-3.0	-2.3	1.4	-0.9	14.8	...
Goods exports, f.o.b. (millions of dollars)	1 709	2 129	2 244	1 684	1 633	1 974	1 923	1 754	2 233	918 c/
Goods imports, c.i.f. (millions of dollars)	2 698	3 103	3 344	3 223	2 630	2 770	3 024	3 131	2 943	2 134 d/
Gross international reserves (millions of dollars)	4 377	4 907	4 881	4 984	4 804	4 800	4 838	4 994	5 793	5 930 d/
Real effective exchange rate (index: 2005=100) e/	73.8	67.8	66.4	71.1	72.6	69.8	69.8	70.2	64.9	65.7 d/
Consumer prices (12-month percentage variation)	10.3	8.8	9.4	4.9	3.3	3.9	2.8	4.0	1.2	0.9 d/
Average nominal exchange rate (guaraníes per dollar)	4 515	4 028	3 943	4 309	4 451	4 409	4 436	4 406	4 085	4 226
Nominal interest rates (annualized percentages)										
Deposit rate f/	2.2	6.1	5.5	5.0	6.3	4.9	5.0	4.7	4.4	5.7 d/
Lending rate g/	14.3	16.0	15.9	15.0	14.6	14.4	14.7	15.4	15.4	15.5 d/
Interbank rate	6.0	8.1	8.2	7.7	6.2	6.1	5.4	5.0	5.5	4.9 d/
Monetary policy rates	6.3	8.9	8.6	8.0	6.5	6.3	5.7	5.5	5.5	5.5
International bond issues (millions of dollars)	100	-	-	-	-	-	-	500	500	- d/
Domestic credit (variation from same quarter of preceding year)	38.1	29.9	23.4	23.7	23.0	23.5	22.1	16.0	11.0	11.8 d/
Non-performing loans as a percentage of total credit	1.5	1.6	1.8	1.7	2.0	2.2	2.3	2.1	2.3	2.3 c/

Source: Economic Commission for Latin America and the Caribbean (ECLAC), on the basis of official figures.

a/ Preliminary figures.

b/ Based on figures in local currency at constant 1994 prices.

c/ Figures as of April.

d/ Figures as of May.

e/ Quarterly average, weighted by the value of goods exports and imports.

f/ Weighted average of effective interest rates on time deposits.

g/ Commercial lending rate, local currency.