

EL SALVADOR

1. General trends

El Salvador's economy grew by 2.5% in 2015, up from the previous year's 1.4% growth and at a higher rate than the average for the most recent five-year period. Economic performance was driven mainly by domestic demand. Private consumption was strengthened by improved real wages, as well as by additional inflows to households from family remittances and an increase in personal loans. Year-on-year inflation stood at 1.0% in December, up from 0.5% in 2014. As a result of the drop in the oil bill, the current account deficit shrank to 3.6% of GDP (from a deficit of 5.2% in 2014), the lowest ratio since 2010. In the public finance domain, the fiscal deficit of the non-financial public sector (NFPS), including pensions, narrowed from 3.6% to 3.3% of GDP. On the employment front, the number of formal jobs registered with the Salvadoran Social Security Institute (ISSS) grew, on average, by 1.6% (compared with 2.4% in 2014).

Following the priorities set out by the National Council on Citizen Security and Coexistence, through the Plan for a Safe El Salvador, the legislative assembly approved two special new taxes at the end of 2015 to finance its initiatives. The revenue will go toward specific programmes designed to stem the wave of gang-related violence, as well as to prevent crime in general.

The Economic Commission for Latin America and the Caribbean (ECLAC) forecasts economic growth of 2.4% in 2016, subject to the performance of domestic demand and the progress of new investment projects. El Salvador's Central Reserve Bank (CRB) anticipates higher inflation for 2016 to finish the year at around 1.4%, as the statistical effect of lower imported raw materials prices wears off. The Bank expects the current account deficit to continue to narrow, to around 3.0%. Meanwhile, the Ministry of Finance estimates the fiscal deficit will edge up to 3.5% of GDP. On the employment front, continued new formal job creation is expected as a result of increased domestic economic activity.

2. Economic policy

In 2015, macroeconomic policy continued to focus on generating a growth-enabling economic climate and breaking the low-growth trend of recent years. Despite significant pressure on debt from pension payments, public policy struck a balance between meeting expenditure and investment needs and maintaining public finance sustainability.

(a) Fiscal policy

Fiscal policy had an expansionary thrust in 2015. The narrowing of the NFPS fiscal deficit from 3.6% to 3.3% of GDP was driven in part by a rise in the primary surplus (from 0.7% in 2014 to 1.1% in 2015). The costs of pensions represented 1.9% of GDP, while the upturn in the overall balance of the public finances reflected a slight rise in total NFPS revenue, rather than a reduction in expenditures.

Total NFPS income in 2015 was up by 4.7% in real terms, to reach the equivalent of 20% of GDP. Real tax revenues rose by 4.7%, fuelled by income tax contributions and value added tax (VAT) receipts, resulting in a tax burden slightly up in year-on-year terms, to 15.2% of GDP. On the expenditure

side, total spending climbed 3.0% in real terms as current expenditures and capital spending expanded by 2.8% and 3.9%, respectively, as a result of increased public investment. Total expenditure came to 21.4% of GDP. Current transfers continued the downward trend seen over the past three years, with a year-on-year decline of 2.4% in real terms.

In late October 2015, the legislative assembly approved the law requiring large taxpayers to make a special contribution to the citizen security plan. The central pillar of the plan's financing is a special 5% tax on firms that earn net profits of US\$ 500,000 or more. A special levy of 5% on the acquisition or use of telecommunication services by corporate and private consumers was also approved for the same purpose. The two new taxes will remain in effect for five years, during which time the government expects annual revenues of US\$ 140 million (equivalent to 0.5% GDP).

As has been the case in recent years, the government financed the deficit with short-term local debt placements through the issue of treasury bills (LETES), whose balance just topped US\$ 772 million in December 2015 (equivalent to 3.0% GDP). Total NFPS debt closed 2015 at US\$ 12.028 billion, equivalent to 46.3% of GDP, while debt, including pensions, climbed to US\$ 15.507 billion, an increase of 6.3% over the 2014 figure. In GDP terms, total NFPS debt, including pensions, was 59.6%, up 1.6 GDP points from 2014. This factor raises concerns in relation to debt sustainability.

Real tax revenue increased by 2.6% in the first four months of 2016. With respect to the year-earlier period, current revenue was up by 2.9% and total expenditures, by 2.1% in real terms. Current expenditures contracted (1.1%) while capital spending jumped (28.2%). Total NFPS debt was 58.4% of GDP, slightly below the total for December 2015 in GDP terms.

(b) Monetary policy

The central bank lacks monetary autonomy since the economy has been dollarized since 2001 and international capital moves freely into and out of El Salvador. Thus, in the short term, interest rates are determined by the supply and demand between financial intermediaries operating in the country. In 2015, liquidity conditions remained stable.

In 2015, the average nominal interest rate paid on 180-day deposits was 4.24%, up from 3.78% the previous year. For the same period, the nominal rate charged on loans of up to one year increased 17 basis points to stand at 6.17%. Total deposits in the financial system expanded, fuelled by private sector deposits, which registered 6.5% growth year-on-year in December 2015. Private sector lending to both households and businesses rallied strongly in the second half of the year to yield a growth rate of 4.7% overall for 2015.

Net international reserves were up slightly (0.3%) at the end of 2015, at US\$ 2.670 billion, equivalent to almost three months of imports and approximately 24.8% of M2.

The financial sector outlook in April 2016 indicated greater credit demand on the part of economic agents. The total lending portfolio of other credit institutions until April showed annual growth of 5.3%. The interest rate on 180-day deposits was 4.37%, a slight rise over the 4.30% registered in May 2015. Short-term corporate financing costs, measured by interest rates on loans of up to one year, stood at 6.41%, compared to 6.08% 12 months earlier. Net international reserves totalled US\$ 2.840 billion in May 2016, an increase of 6.4% over the total in December 2015.

(c) Other policies

The law on financial inclusion was enacted by the legislative assembly in August 2015, with a view to expanding formal financial services through the use of electronic money and opening simplified accounts. Subsequently, in March 2016, the Superintendency of the Financial System and the Office of the Attorney General of the Republic signed agreements to strengthen their efforts to combat money laundering and the financing of terrorism, by allowing confidential information to be shared between the two institutions. The law on online signatures came into effect in April, granting legal equivalence to signatures on online transactions and laying the groundwork for regulating providers of these services.

In the trade policy domain, negotiations began on a partial scope agreement with the Plurinational State of Bolivia, with which the products most exported at present are manufactured goods. Moreover, El Salvador will resume free trade negotiations with Ecuador and, together with other Central American countries, has entered into negotiations on a free trade agreement with the Republic of Korea.

3. The main variables

(a) The external sector

The Salvadoran export sector showed growth of 4.0% at the end of 2015, as a result of an increase of 13.9% in traditional exports, 8.6% in the maquila sector and 2.1% in non-traditional exports. The fastest-growing sectors were agriculture and manufacturing, in particular of clothing and textiles, chemical and medical products, food, beverages and paper and paperboard products. The main traditional export product was coffee, which bounced back from the effects of the coffee leaf rust outbreak in recent years to grow by 34.9%, thanks to larger volumes. Sugar exports to China in 2015 were significant, after El Salvador withdrew the reservation it had lodged with the World Trade Organization (WTO) against China over high tariffs. By volume, 98,700 tons of sugar were exported to China in 2015 (12.3% of total sugar exports). The recovery in the maquila sector, after a decline of 11.6% in 2014, reflected economic growth in the United States, the main export destination for El Salvador's maquila products (92.7% of the total). In fact, the United States remains the main destination for all Salvadoran exports (more than 46% of the total), followed by Honduras and Guatemala. In 2015, exports increased to Taiwan Province of China and the introduction of China as a trading partner boosted exports in other key products as well as sugar.

Imported goods fell by 0.9% from the previous year —mainly due to falling prices since volumes were up by 11.8%— with a year-on-year decline of 1.7% in consumer goods. The oil bill dropped by US\$ 394 million as a result of lower international oil prices. Capital goods imports rose by 12.4% over the previous year, demonstrating growing confidence in the business sector to boost its production capacity. Thanks to lower international prices for raw materials, the terms of trade were up by 13.1%. As a result, the goods trade deficit narrowed by 5.9% year-on-year, to the equivalent of 19.1% of GDP.

Remittance flows grew by 3.0% in nominal terms in 2015 to stand at US\$ 4.280 billion, equivalent to 16.6% of GDP. Family remittances were impacted favourably by the United States' economy, above all by increased employment in industries important to Salvadoran workers, such as construction, private services and hotels and restaurants. Foreign direct investment (FDI) flows totalled US\$ 429 million in 2015, 37.8% higher than the total for 2014. These flows go mainly to the manufacturing, financial and insurance services and communications sectors.

In the first four months of 2016, exports registered a cumulative decline of 3.6% (down 16.1% in volume and up 14.9% in unit value) and imports shrank by 6.2% (despite year-on-year growth of 8.9% in

volume terms). El Salvador received US\$ 1.842 billion in family remittances in the first five months of 2016, representing growth of 6.8% compared to the prior-year period.

(b) Economic activity

Growth in 2015 was driven by a positive performance across all sectors of the economy. This upturn was led by the manufacturing industry, which expanded 3.4% on the back of demand for Salvadoran goods from the United States, and by commerce, which was up by 2.8%, thanks in part to a rise in private consumption propelled by higher disposable income. The transport, storage and communications sector expanded at a rate of 3.3% year-on-year. Over the course of 2015, GDP gathered speed quarter-on-quarter, with an increase from 2.2% to 2.3% in the first and second quarters to a stronger 2.7% and 2.6% in the final quarters of the year.

On the spending side, growth was driven by household consumption, which contributed 1.6 points of GDP growth, and government consumption, which gathered pace over the year and accounted for 0.4 GDP points. Investment added 1.3 points to GDP in 2015, unlike in 2014, when its contribution was negative by 1.2 percentage points. The performance of investment reflected the increase in gross fixed capital formation by both the public and private sectors (up 8.0% in total in year-on-year terms), primarily in the category of machinery and equipment (up 18.3%), in response to improved expectations for the economy overall and for the execution of infrastructure projects in particular. The net export contribution was negative, at -0.9 percentage points.

In the first quarter of 2016, the economic activity index (IVAE) showed an upturn of 1.1% as measured by its trend-cycle series (more robust than the -0.2% for the year earlier period), driven mainly by the transport, electricity, gas and water and manufacturing industries, as well as government services. Meanwhile, construction, community, social and personal services, and mining and quarrying registered slightly weaker economic activity over the first few months of this year.

(c) Prices, wages and employment

Interannual inflation to December reached 1.0%, higher than the 0.5% registered in 2014. Over the first 10 months of 2015, yearly inflation remained negative, owing largely to lower prices for fuels and other primary materials. However, this trend changed in the last two months of the year thanks to moderate growth in some areas such as water supply, following subsidy revisions by the National Water and Sewerage Administration (ANDA). Prices for food and non-alcoholic beverages rose slightly, by 1.4%, over the year. Owing to the decline in international prices of oil and its derivatives, prices in the transport sector were down by 6.8% at the end of the year. Long-term inflation, measured by the core inflation index, remained low throughout the year and in December 2015 registered annual growth that was negative by 0.1%.

On the employment front, ISSS records reveal a slower pace of formal job creation, with the average number of ISSS contributors rising by 1.6% year-on-year in 2015, versus 2.4% for 2014. The largest gains in job numbers were reported in manufacturing, financial institutions, insurance and real estate and the construction industry. The agriculture and the transport, storage and communications sectors registered slight decreases in ISSS contributors. In February 2016, the Government of El Salvador launched an employment programme called *Jóvenes con Todo*, a platform aimed at the unemployed aged between 15 and 29. The initiative will include a training component with skills-building aimed at facilitating access to the labour market, with a view to increasing productivity by promoting enterprise.

Starting in January 2015, minimum monthly wages in several branches of activity were as follows: US\$ 118.20 for agricultural workers, US\$ 251.70 in commerce and services, US\$ 246.60 in manufacturing and US\$ 210.90 in the maquila textile and apparel sector. These rates reflect the final tranche of the increases approved in June 2013, when the national minimum wage council (CNSM) authorized an increase of 12% in the minimum wage (applicable in three phases of 4% each). In the first quarter of 2016, CNSM began its three-yearly tripartite process to negotiate an agreement on a new minimum wage increase under article 159 of the Labour Code.

In the first five months of 2016, inflation remained low due to the effects of lower prices for electricity and oil derivatives. Year-on-year inflation to May stood at 0.7%, with the strongest upward pressure coming from accommodation, water, electricity and others (12%), alcoholic beverages, tobacco and others (3.8%), and education (1.7%). The largest single driver of year-on-year inflation was the rise in the price of drinking water. Core inflation remained negative, at -0.1%.

Table 1
EL SALVADOR: MAIN ECONOMIC INDICATORS

	2007	2008	2009	2010	2011	2012	2013	2014	2015 a/
	Annual growth rates b/								
Gross domestic product	3.8	1.3	-3.1	1.4	2.2	1.9	1.8	1.4	2.5
Per capita gross domestic product	3.4	0.9	-3.5	1.0	1.8	1.5	1.4	1.0	2.0
Gross domestic product, by sector									
Agriculture, livestock, hunting, forestry and fishing	8.5	3.0	-2.9	3.1	-2.5	3.5	-0.4	1.3	0.8
Mining and quarrying	-1.9	-6.8	-15.4	-11.4	13.7	2.8	1.3	-1.6	2.3
Manufacturing	2.5	2.3	-3.0	1.9	2.7	1.3	3.1	1.6	3.4
Electricity, gas and water	2.7	2.3	-1.0	-0.6	0.4	0.8	1.0	2.3	0.3
Construction	-6.9	-7.3	-2.8	-5.0	8.9	0.3	-0.1	-10.7	1.5
Wholesale and retail commerce, restaurants and hotels	4.3	1.0	-5.4	1.5	2.3	2.6	1.5	2.4	2.8
Transport, storage and communications	4.8	-0.8	-5.9	-0.2	4.6	1.6	1.8	0.9	3.3
Financial institutions, insurance, real estate and business services	3.0	0.9	-1.3	1.9	1.8	0.2	2.3	2.1	1.6
Community, social and personal services	3.8	2.0	1.3	1.8	3.4	2.5	3.1	2.7	1.9
Gross domestic product, by type of expenditure									
Final consumption expenditure	5.9	1.7	-9.2	2.2	2.5	2.4	1.0	1.6	2.0
Government consumption	0.4	-0.4	5.8	2.2	3.9	2.5	3.7	-0.4	4.7
Private consumption	6.3	1.8	-10.3	2.2	2.4	2.4	0.7	1.8	1.7
Gross capital formation	2.8	-5.4	-19.2	2.4	13.8	-1.4	9.3	-6.4	8.0
Exports (goods and services)	7.1	6.9	-16.0	11.6	9.3	-7.3	4.8	-0.9	2.4
Imports (goods and services)	8.8	3.3	-24.8	10.4	10.8	-4.6	4.5	-2.2	3.2
Investment and saving c/	Percentajes of GDP								
Gross capital formation	16.3	15.2	13.4	13.3	14.4	14.1	15.0	13.6	14.0
National saving	10.3	8.1	11.9	10.8	9.6	8.8	8.4	8.4	10.4
External saving	6.1	7.1	1.5	2.5	4.8	5.4	6.5	5.2	3.6
Balance of payments	Millions of dollars								
Current account balance	-1,217	-1,532	-312	-533	-1,112	-1,280	-1,586	-1,307	-920
Goods balance	-4,740	-5,113	-3,506	-4,022	-4,772	-4,927	-5,295	-5,208	-4,940
Exports, f.o.b.	2,794	3,276	2,924	3,473	4,243	4,235	4,334	4,256	4,381
Imports, f.o.b.	8,855	9,699	7,414	8,595	10,202	9,162	9,629	9,463	9,321
Services trade balance	234	224	308	398	449	532	618	741	786
Income balance	-456	-389	-556	-538	-618	-891	-992	-1,074	-1,137
Net current transfers	3,746	3,747	3,442	3,629	3,830	4,007	4,083	4,234	4,372
Capital and financial balance d/	1,496	1,866	736	235	698	1,930	1,259	1,274	1,033
Net foreign direct investment	1,455	824	366	-226	218	484	176	311	429
Other capital movements	40	1,042	371	461	479	1,447	1,083	963	604
Overall balance	279	333	424	-297	-414	651	-327	-33	113
Variation in reserve assets e/	0	0	0	0	0	-651	327	33	-113

Table 1 (concluded)

	2007	2008	2009	2010	2011	2012	2013	2014	2015 a/
Other external-sector indicators									
Real effective exchange rate (index: 2005=100) f/	100.9	101.7	99.6	101.2	102.4	103.1	104.1	105.3	105.3
Terms of trade for goods (index: 2010=100)	104.0	94.1	105.9	100.0	97.5	98.0	96.3	99.6	111.3
Net resource transfer (millions of dollars)	1,039	1,477	-36	-303	79	1,039	267	200	-104
Total gross external debt (millions of dollars)	9,349	9,994	9,882	9,698	10,670	12,521	13,238	14,885	15,482
Employment									
	Average annual rates								
Labour force participation rate g/	62.1	62.7	62.8	62.5	62.7	63.2	63.6	63.6	62.8
Open unemployment rate h/	5.8	5.5	7.1	6.8	6.6	6.2	5.6	6.7	...
Visible underemployment rate h/	5.3	6.3	7.7	7.0	3.4	5.8	5.8	6.7	...
Prices									
	Annual percentages								
Variation in consumer prices (December-December)	4.9	5.5	-0.2	2.1	5.1	0.8	0.8	0.5	1.0
Variation in industrial producer prices (December-December)	13.9	-6.0	4.9	6.2	7.0	2.4	-0.2	-5.8	-6.0
Variation in average real wage	-2.4	-3.1	3.5	1.1	-2.9	0.2	0.5	0.7	7.9
Nominal deposit rate i/	4.7	4.2	4.5	2.9	1.8	2.5	3.4	3.8	4.2
Nominal lending rate j/	7.8	7.9	9.3	7.6	6.0	5.6	5.7	6.0	6.2
Central government									
	Percentajes of GDP								
Total revenue	14.8	15.1	13.8	15.0	15.4	15.8	16.3	15.8	16.0
Tax revenue	13.6	13.5	12.6	13.5	13.8	14.4	15.4	15.1	15.2
Total expenditure	15.0	15.8	17.6	17.7	17.6	17.5	18.1	17.4	17.1
Current expenditure	12.4	13.0	14.7	14.5	14.6	14.2	15.0	14.6	14.5
Interest	2.5	2.4	2.5	2.3	2.2	2.2	2.4	2.4	2.4
Capital expenditure	2.6	2.8	2.9	3.2	3.1	3.3	3.0	2.8	2.6
Primary balance	2.3	1.8	-1.2	-0.4	-0.1	0.5	0.6	0.8	1.3
Overall balance	-0.2	-0.6	-3.7	-2.7	-2.3	-1.7	-1.8	-1.6	-1.1
Central government public debt									
Domestic	10.7	11.6	14.9	14.3	14.8	15.5	14.5	11.9	13.7
External	24.2	22.8	27.6	28.3	26.9	30.2	29.5	32.4	31.0
Money and credit									
	Percentages of GDP, end-of-year stocks								
Domestic credit	55.0	54.5	56.2	56.8	56.7	57.2	62.2	64.2	68.1
To the public sector	17.0	18.2	21.0	24.3	26.5	26.0	29.3	29.6	32.9
To the private sector	43.6	43.0	42.4	40.9	39.8	40.2	42.5	44.1	44.9
Others	-5.6	-6.7	-7.2	-8.4	-9.5	-9.0	-9.6	-9.5	-9.7
Monetary base									
Money (M1)	9.6	9.1	11.2	12.3	12.0	11.7	11.9	11.7	12.6
M2	52.9	49.1	52.0	50.3	45.5	44.7	44.6	43.5	44.9

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 1990 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. New measurements have been used since 2007; the data are not comparable with the previous series.

h/ Urban total.

i/ Basic rate for deposits of up to 180 days.

j/ Basic lending rate for up to one year.

Table 2
EL SALVADOR: MAIN QUARTERLY INDICATORS

	2014				2015				2016	
	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/	1.9	1.6	1.0	1.2	2.2	2.3	2.7	2.6	2.5	...
Gross international reserves (millions of dollars)	2,941	2,937	2,927	2,939	2,939	2,911	2,913	2,813	3,115	3,177 c/
Real effective exchange rate (index: 2005=100) d/	104.9	106.3	105.3	104.8	104.6	105.0	105.4	103.8	103.6	105.0 c/
Consumer prices (12-month percentage variation)	0.4	1.1	1.7	0.5	-0.8	-0.8	-2.3	1.0	1.1	0.7 c/
Wholesale prices (12-month percentage variation)	-1.4	0.9	4.0	3.8	3.1	0.8	-1.3	-0.1	-2.6	-2.2 c/
Nominal interest rates (average annualized percentages)										
Deposit rate e/	3.5	3.7	3.8	4.1	4.2	4.3	4.2	4.3	4.3	4.4 c/
Lending rate g/	6.0	5.9	6.1	6.0	6.0	6.1	6.3	6.3	6.2	6.3 c/
Sovereign bond spread, Embi Global (basis points to end of period) h/	420	376	383	414	459	443	610	634	667	671
International bond issues (millions of dollars)	-	-	800	-	-	300	-	-	-	-
Domestic credit (variation from same quarter of preceding year)	10.8	12.0	9.2	6.2	6.8	5.6	6.7	9.9	8.9	8.5 c/
Non-performing loans as a percentage of total credit	2.4	2.5	2.6	2.5	2.4	2.4	2.5	2.4	2.4	2.3

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 1990 prices.

c/ Figures as of May.

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

e/ Basic rate for deposits of up to 180 days.

f/ Basic lending rate for up to one year.

g/ Measured by J.P.Morgan.