El Salvador

The Salvadoran economy grew by 3.8% in 2006, to record the largest increase in per capita GDP (2.1%) of the last nine years. Growth was driven by reconstruction work following the damage caused by hurricane Stan and the eruption of the Ilamatepec volcano in 2005, supported by better performances in the agriculture and services sectors. Public and private investment grew on a sustained basis. The large flow of family remittances (18% of GDP) helped to fuel private consumption and ease the impact of rising international oil prices on the current account, which posted a deficit of 4.6% of GDP. The fiscal deficit of the non-financial public sector (NFPS) was 2.9% of GDP, and inflation averaged 3.9%.

Economic growth of 4% is forecast for 2007, with improvements expected in the agriculture, services and construction sectors, thanks to the execution of funds from the Millennium Challenge Account (US$ 461 million in five years). In addition, inflation is expected to be between 3% and 4%, thanks mainly to the stability of international oil prices. The main economic policy goal is to maintain fiscal discipline. Over the next three years, the Government of El Salvador plans to promote other key areas for the country's development in order to make the most of the commercial facilities provided under the Dominican Republic-Central America-United States Free Trade Agreement (CAFTA-DR), which entered into force in 2006. As a first step, to promote competitiveness and productivity, measures will be taken to attract new investments and improve the business climate; and secondly, the Government will support manufacturing industry through a productive development fund created in October 2006.

The tax burden amounted to 13.4% of GDP in 2006, following the tax reform that made it possible to obtain additional revenue, involving changes in the tax code, the pensions law, the law on banks and the income tax law, supported by more widespread supervision of taxpayers by the Internal Revenue Service and customs. This has made it possible to provide support to over 26,000 extremely poor families from 32 municipalities in the framework of the Solidarity Network programme. Current expenditure grew mainly as a result of public consumption, an increase in net interest payments and pension payments. Subsidies totalling US$ 19 million were provided to transport (eliminated in mid-2006), the consumption of electric energy (US$ 37 million) and liquefied gas (US$ 72 million). These measures, compounded by reconstruction expenses, generated an NFPS deficit of 2.9% of GDP, similar to the 2005 figure. For 2007, the government is expecting fiscal accounts to improve, thanks mainly to the creation in September 2006 of a trust fund to manage the pension system debt, payments of which are expected to shrink from 1.9% to 0.2% of GDP between 2006 and 2007.

The external public debt amounted to US$ 5.577 billion as of September 2006. This reflects bond issues totalling US$ 656.3 million: US$ 617.6 million on international markets and US$ 38.7 million on the domestic market. The domestic public debt, meanwhile, amounted to US$ 2.647 billion. Consequently, the total public debt edged downwards to 44.8% of GDP (0.7% less than in the same period in 2005).

Nominal interest rates rose in 2006, following the rise in international rates. Real interest rates on 180-day deposits increased from -1.2% in 2005 to 0.7% in 2006, while rates on loans with maturities of up to one year rose from 2.1% to 3.8% in the same period. Nonetheless, the stronger economic performance elicited an expansion of bank credit to both the private and public sectors. At year-end the Central Reserve Bank was holding net international reserves of US$ 2.146 billion equivalent to just 4.7 months of goods and services imports, slightly less than 12 months earlier.

The favourable prices for certain agricultural products boosted sector performance in 2006 for the second year running. Reconstruction works (started following the natural disasters that occurred in October 2005), in conjunction with increased demand for housing, fuelled growth in the construction sector (5.4%). There were better performances in the tourism, mining, electricity, financial, and transport and communications sectors, and also in manufacturing industry, which grew by 2.5% in 2006, compared with 1.4% in 2005. Public investment was up by 3.5%, and private investment by 5.6%. All of this contributed to GDP growth of 3.8%.

Annual inflation averaged 3.9%, slightly less than the 2005 figure, thanks to the stabilization of oil prices and a reduction in the cost of gasoline, transport, and food products in the last few months of 2006. On the wages front, there was a 10% increase in the minimum wage paid to workers in the manufacturing, commerce and services sectors, and a 4% rise for maquila workers. In January 2006, public-sector employees received their first pay hike since 1998 (ranging from 3% to 10%). Nonetheless, despite economic growth, the open unemployment rate rose as a result of job losses in the maquila sector.

Despite stronger prices for several agricultural products, including coffee and sugar, the export sector grew by just 4.7% —only slightly above the 2005 figure. Exports of non-traditional goods expanded by 23.2%, while traditional exports grew by 17%, having increased by 40% in the previous year. Maquila production continued to decline (10.5%) in 2006.

Imports were more buoyant and expanded by 12%, with foreign purchases of consumer goods, intermediate goods and capital goods growing by 21%, 18% and 11%, in that order, compared with their 2005 levels. In contrast, maquila imports declined by 10%. The oil bill is estimated to have reached a level of US$ 1.1 billion in 2006, up by US$ 200 million on the 2005 figure.

Table 1
EL SALVADOR: MAIN ECONOMIC INDICATORS

	2004	2005	2006 [a]
	Annual growth rates		
Gross domestic product	1.8	2.8	3.8
Consumer prices	5.4	4.3	3.9 [b]
Average real wage	-1.4	-4.5	-0.5
Money (M1)	8.5	9.3	14.4 [c]
Real effective exchange rate [d]	0.2	1.4	0.5 [c]
Terms of trade	-1.0	0.0	-1.9
	Annual average percentages		
Urban unemployment rate	6.5	7.3	5.7 [e]
Central government overall balance/GDP	-1.1	-1.0	-0.4
Nominal deposit rate	3.3	3.4	4.3 [f]
Nominal lending rate	6.3	6.9	7.5 [f]
	Millions of dollars		
Exports of goods and services	4 412	4 573	4 832
Imports of goods and services	7 151	7 652	8 463
Current account	-632	-786	-832
Capital and financial account	579	728	961
Overall balance	-53	-59	129

Source: Economic Commission for Latin America and the Caribbean (ECLAC), on the basis of official figures.
[a] Preliminary estimates.
[b] Twelve-month variation to November 2006.
[c] Year-on-year average variation, January to October.
[d] A negative rate indicates an appreciation of the currency in real terms.
[e] Estimate based on data from January to September.
[f] Average from January to October, annualized.

As a result, the current account deficit of the balance of payments represented 4.5% of GDP, similar to the previous year's figure.

The net flow of foreign direct investment was down by 23% on the previous year's figure at US$ 397 million. In contrast, tourism promotion linked to the National Tourism Plan 2014, generated income in excess of US$ 700 million. The economy once again received a considerable boost from additional family remittances (18% more than in 2005) sent home to mitigate the consequences of natural disasters. These foreign exchange inflows (US$ 3.339 billion) supported private consumption and financed 94% of the merchandise trade deficit (18.3% of GDP).