

El Salvador

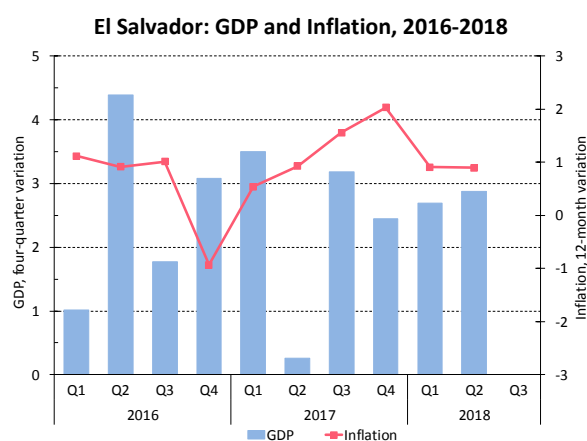
ECLAC estimates that the Salvadoran economy will post real growth of 2.4% in 2018 (slightly above the previous year's 2.3%, fuelled by a combination of domestic factors—such as increased lending to households and enterprises and stepped-up expenditure—and external factors—such as higher remittances and vigorous external demand—. Despite higher oil prices, year-on-year inflation is forecast at 1.6% by the year-end. The non-financial public sector (NFPS), including pension system costs, will post a fiscal deficit of 2.7% of GDP (compared to 2.5% in 2017). The current account deficit on the balance of payments will be 3.2% of GDP (compared to 2.0% in 2017), partly as a result of increased international oil and gas prices.

Fiscal policy pursued containment goals, in keeping with the guidelines set in the Fiscal Responsibility Act. In the first nine months of the year, NFPS income and grants grew at a year-on-year rate of 3.5% in real terms. Tax revenue increased by 6%, owing to a 10.2% increase in value added tax revenues and a 2.5% hike in income tax revenues—driven by the surge in economic activity—as well as additional revenue generated by the tax and customs amnesty, which ended in October. By contrast, non-tax revenue fell by 14%, as a result of the decline in the income of State-owned enterprises.

Total expenditure posted year-on-year growth of 12.3% in real terms between January and September, following a slight (0.3%) decline in the year-earlier period. This was due to a significant (26.2%) rise in capital expenditure (compared to an 11.6% decline in the same period in 2017). Public investment in hydropower projects and in expanding the San Salvador international airport, in particular, contributed to that upturn. Current spending grew by 10.3% in real terms, as a result of a 14.7% increase in interest payments and a 13.5% hike in current transfers. The NFPS tax burden is expected to be equivalent to 18.2% of GDP in 2018.

As of September 2018, total NFPS debt, including the Pension Liabilities Trust Fund, amounted to US\$ 18.002 billion (compared to its end-December 2017 level of US\$ 17.291 billion), or 69.7 % of GDP, a percentage similar to that at the end of 2017. By August 2018, the outstanding balance of Treasury bills—a short-term domestic debt instrument—had increased at a year-on-year rate of 13.8%. The Pension Liabilities Trust Fund proved to be more stable following the pensions reform of 2017 and accounted for 18.7% of GDP in September (up from 18.4% in December 2017). The total debt, including pensions, is forecast at 71.2% of GDP by the end of 2018.

Because the economy is dollarized, the country has no monetary policy as such, and supply and demand determine the interest rate. In the first nine months of 2018, interest rates on 180-day deposits averaged 3.1% in real terms, down from the year-earlier period's 3.6%, while rates on loans for periods of up to one year averaged 5.4% (compared to 5.6% for the same period in 2017). That has stimulated growth in a number of economic sectors.



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

Outstanding loans to the private sector totalled US\$ 13.569 billion in September, representing year-on-year growth of 5.4%. The loan portfolio grew for all economic sectors, including industry, especially the construction industry, up by 15.4% and 25.7%, respectively, commerce (8.8%) and consumption (6.2%)

In August, the President announced an end to diplomatic relations with Taiwan Province of China, and the start of a new era of trade and diplomatic ties with China, which will establish a framework for promoting trade, investment and scientific and technical cooperation. Following that move, China could become the second largest market for Salvadoran exports, after the United States. The government also remitted a bill to the Legislative Assembly on the special economic zone, aimed at boosting the economy in the south-east of El Salvador by attracting investors with tax and other incentives. By joining the Guatemala–Honduras customs union, El Salvador is seeking to boost economic growth, strengthen production chains, and generate employment.

Salvadoran exports grew, in value terms, at a year-on-year rate of 3% between January and September 2018, while volumes fell by 5.9%. In-bond assembly industry exports posted 16% year-on-year growth, largely thanks to textile products (20.3%). The fastest-growing manufactured products included electric wires and cables (81.8%), cotton yarn (51.8%) and clothing (40.1%). The most robust increases in trade were with Mexico (year-on-year growth of 36.3%), followed by the Dominican Republic (up 20.4%), Central American trading partners Honduras (12.5%) and Guatemala (6.9%) and the United States (2.4%).

Good imports grew by 12.3% in value and volume was up by 3.2%; electricity and gas supplies picked up (56.4%), as did in-bond industry products (26.5%). As a result of the higher oil price, reflected in a 22.5% hike in the oil bill, combined with lower coffee prices, by August the terms of trade fell by 7.6%. The trade deficit stood at US\$ 4.202 billion: a year-on-year increase of 24.4%.

In the first six months, the current account deficit on the balance of payments was US\$ 407 million, primarily due to the US\$ 2.706 billion goods trade deficit and a US\$ 414.5 million surplus on the services account. Over the same period, foreign direct investment (FDI) flows totalled US\$ 812 million, 13.1% more than in the prior-year period. Most of the investment was in industry (US\$ 272 million), including clothing, cement and soft drinks. By October remittances posted a 9.1% increase over the prior-year period and totalled US\$ 4.504 billion.

The economy grew by 2.8% in the first half of the year, thanks to a robust construction sector (up 7%), 6.5% growth in mining and quarry output, and 5.2% growth in professional activities. Only the electricity and gas supply segment posted a decline (-1.2%). On the expenditure side, gross fixed capital formation and private consumption (up 5.2% and 4.4%, respectively) are still the main drivers of growth, followed by exports of goods and services (3.2%).

El Salvador: main economic indicators, 2016-2018

	2016	2017	2018 ^a
	Annual growth rate		
Gross domestic product	2.6	2.3	2.4
Per capita gross domestic product	2.2	1.9	2.0
Consumer prices	-0.9	2.0	1.4 ^b
Real average wage ^c	1.0	1.0	1.0 ^d
Money (M1)	3.9	6.5	7.8 ^e
Real effective exchange rate ^f	0.2	3.5	0.1 ^e
Terms of trade	-6.6	5.0	-3.1
	Annual average percentage		
Open urban unemployment rate	6.9	6.8	...
Central government			
Overall balance / GDP	-0.9	-0.1	-0.8
Nominal deposit rate ^g	4.4	4.4	4.2 ^e
Nominal lending rate ^h	6.4	6.5	6.5 ^e
	Millions of dollars		
Exports of goods and services	6 877	7 220	7 590
Imports of goods and services	10 727	11 366	12 445
Current account balance	-500	-501	-808
Capital and financial balance ⁱ	952	809	1 250
Overall balance	453	308	442

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

a/ Estimates.

b/ Figures as of August.

c/ Average wage declared by workers covered by social security.

d/ Interannual variation of the period from January to July.

e/ Figures as of September.

f/ A negative rate indicates an appreciation of the currency in real terms. Refers to the global real effective exchange rate.

g/ Basic deposit rate for up to 180 days.

h/ Basic lending rate for up to one year.

i/ Includes errors and omissions.

Year-on-year inflation to October 2018 was 1.49%, slightly above the 1.43% of the year-earlier period, as a result of the higher prices of accommodation, water and electricity (up 5.6%), which in turn reflect higher prices for oil derivatives and transportation (up 2.9%). Partly offsetting the above was the (1.6%) decline in clothing and footwear prices. Formal employment in July posted an increase of 4,881 jobs over the figure for the same month in 2017: a year-on-year increase of 0.59%, due to the increase in private sector payrolls, as public sector employment remained stable. Wages of contributors to the Salvadoran Social Security Fund posted a 2.1 percent nominal (1% in real terms) increase to July.

For 2019, ECLAC expects the Salvadoran economy to grow by 2.4%, driven by a vigorous domestic market, remittance flows and foreign trade. Inflation is projected at 1.7%. The NFPS deficit—including pensions— is forecast to end the year at 3.7%, owing partly to elimination of the tax on financial transactions and the end of the tax amnesty. The current account deficit will be equivalent to 3.9% of GDP, given the downtrend in coffee prices. Presidential elections are scheduled for February 2019.