6. Fiscal consolidation will proceed at a gradual pace

Stronger commitment to deficit reduction in 2017

The primary fiscal deficit (excluding income from the Central Bank and the ANSES social security fund) in 2016 was 4.4% of GDP (taking our estimate of nominal GDP for the year), slightly lower than the 4.8% announced at the beginning of the year. In nominal terms, the deficit reached ARS 359.4 billion, an increase of 53% over the 2015 deficit. There was a significant increase in fiscal revenues of 35.3% YoY, reinforced by the collection of the penalty charged for the fiscal justification in the last quarter of the year, which was, however, surpassed by the increase in primary expenditure of 38.2%. In particular, the December figures reflect an increase in primary spending of 84% YoY driven by transfers to the private sector and to the provinces. The government would have taken advantage of this to cancel pending floating debt, transfer funds to public companies such as CAMMESA and to the province of Buenos Aires (ARS 25 billion), in order to compensate for its small stake in the federal tax Partnership. After paying interest on public debt and income from rent, the total deficit reached 4.7% of GDP, up from 3.9% in 2015 (which does not take in floating debt).

The results of the first and second stages of fiscal justification were favourable, as they declared assets of USD 92 billion. There was a one-time increase in income from the payment of the penalty for justified assets (it amounted to about 1.3% of GDP in December) and also from this year new declared assets will start to be taxed. However, according to the law, some of this income will be used to finance the historical reparation programme for retirees, which will have little impact on the fiscal result for 2017.

In 2016, it was not possible to achieve the fiscal consolidation committed to at the beginning of the year, basically because, due to social and legal pressures, it was not possible to achieve the desired reduction in subsidies to energy sectors. In fact, as a percentage of GDP these subsidies increased slightly from 2.4% to 2.6% as a result of the delay in the rebalancing of tariffs and the payment of arrears. Having exceeded the required procedural steps and with a three-year time-frame for energy tariffs already approved, we expect that, as from 2017, both the reduction of these transfers to the private sector and those made to cover the deficit of public companies can materialize. However, social security expenditures will continue to grow as a result of the Historical Reparation Programme for retirees and the investment in public works as well, with the result that by 2017 primary spending will decline by around 2% of GDP while incomes will fall by 1.7% of GDP due to approved tax cuts (see Figure 6.1).

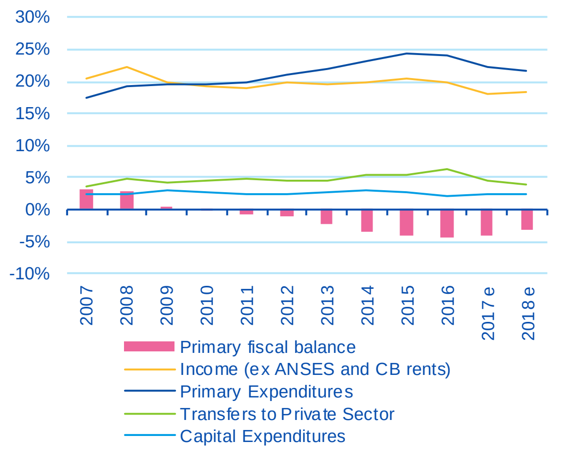
The objective of the new Finance Minister, Nicolás Dujovne, is to meet the national budget targets approved in December 2016, which is achievable and represents a primary deficit of 4.2% of GDP similar to the one we projected considering the above. We maintain our deficit projection path (we estimate a total result after interest of -4.7% and -4.2% of GDP in 2017 and 2018 respectively). The estimate implies a gradual reduction in the primary deficit (-4.2% and -3.2% of GDP in those years) mainly due to lower energy subsidies and transportation, but this does not translate in the same proportion to the total result due to the increase in the interest load on the debt. One of the commitments of the new finance minister is to implement a deeper tax reform that we hope will not lead to a substantial reduction in the fiscal deficit in its transition period.

Although expectations regarding the evolution of fiscal accounts have improved, we only expect a reduction in fiscal vulnerability in the medium term and, therefore, Argentina will continue to depend on debt markets. It is not yet clear that the successful outcome of the justification of assets and changes in the economic cabinet will lead to improvements in the fiscal deficit in the short term, although the new Minister of Finance is committed to the control objective of the budget and the fiscal figures in general and has announced that he will define and monitor quarterly targets for public accounts.

In terms of deficit financing, the 2017 Financial Programme was presented by the Minister of Finance (Table 6.1). Financial needs amount to USD 40 billion in 2017. Debt placements for USD 14 billion are projected in the domestic market, of which USD 733 million were placed on January 26 in Boncer 2021, adjusted for inflation. The government also issued debt onto international markets in January on favourable terms for USD 7 billion and also negotiated a USD 6 billion loan with international banks. With this, the financial needs in dollars for the year would be practically covered, if we suppose that new disbursements refinance the debt maturities of international organisms and, consequently, in an optimistic scenario the rest of emissions could be in the domestic market in pesos as well as dollars. The government has acted securing the necessary funding in an international environment that could become unfavourable for Argentina after the result of the US elections.

Figure 6.1

Fiscal result 2016-17 (% of GDP)



Source: BBVA Research

Figure 6.2

Financial programme

	USD millions	% GDP	1Q17
Financial needs	**40,350**	**7.4**	
Primary deficit	23,000	4.2	
Interest on debt	8,603	1.6	
Maturities of private sector capital	20,247	3.7	
International organisations	2,819	0.5	
Government bonds	17,428	3.2	
Historical reparation law	-3,100	-0.6	
Central Bank	-8,400	-1.5	
Sources of funding	**40,350**	**7.4**	**14,381**
International organisations	3,850	0.7	
Bank repos	6,000	1.1	6,000
Refinancing Letters in USD	4,500	0.8	647
Domestic market	14,000	2.6	734
International market	10,000	1.8	7,000
Public Entities	2,000	0.4	
Average exchange rate (ARS/USD)	17.98	17.98	
GDP (ARS million)	9,750,000	542,269	

Source: Ministry of Finance and BBVA Research

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