

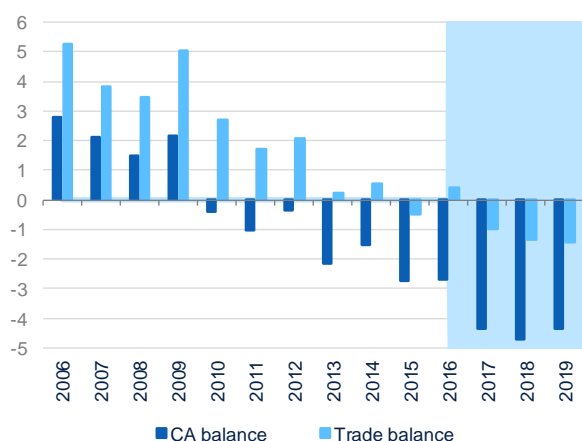
7. The external deficit will continue to widen without becoming unsustainable

The trade deficit continued to burgeon in 2017, with a balance of -USD1,443 million in the first eight months of the year, a trend that will become more pronounced in 2018 up to deficit of USD8,800 million against a background of higher economic growth and slight fall in the terms of trade (Figure 7.1). In turn, the higher deficit in real services, due to the impact on tourism of the real appreciation of the peso, and in net interest burden, due to the rise in external debt, will keep the current account deficit above 4% until 2020.

Against the current global backdrop of low interest rates and low aversion to risk, Argentina should not face serious problems in financing this imbalance with external savings. The weight of external debt on GDP will increase from the low current level of 35% to 37% at the end of 2018, without showing an explosive trend, provided foreign direct investment (FDI) grows to similar levels as in other countries in the region. Meanwhile, reforms have to be made to make exports more competitive (reducing logistics and tax costs and improving labour productivity) in order to be able to sustain higher imports of capital goods to ensure sustained growth in investment.

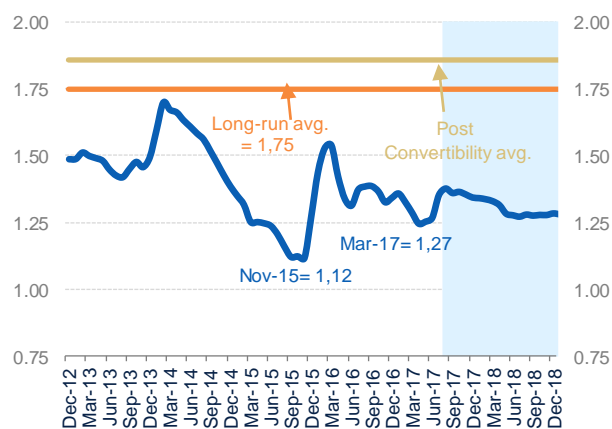
Capital inflows to Argentina, until now concentrated in short-term financial investments, will allow a sustained increase in reserves despite the fall in trade flows. Against this backdrop, and not counting volatility spikes associated with the electoral cycle or external shocks, this inflow of hard currency will continue to put pressure on the real appreciation of the peso (Figure 7.2).

Figure 7.1 Trade balance and current account (% of GDP)



Source: INDEC and BBVA Research

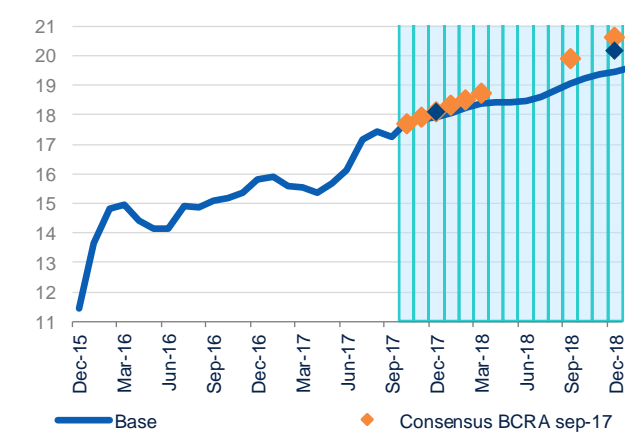
Figure 7.2 Real multilateral exchange rate (2001: 12=1)



Source: Indec, Central Bank of Argentina, Haver and BBVA Research

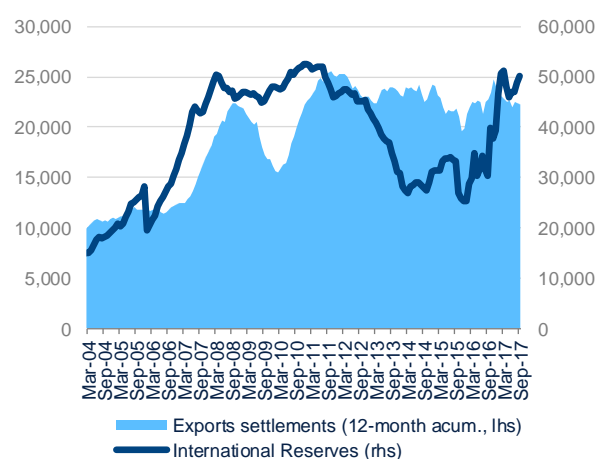
This real appreciation, will eventually reduce net inflows into Argentina, putting upside pressure on the nominal exchange rate which will partially offset it. We have made a slight upward revision of our depreciation forecasts for 2017 and 2018, but have kept them below expected inflation throughout the forecast horizon, and below analysts' consensus (Figure 7.3). The Central Bank has shown that it does not have a specific exchange rate target, but rather that (1) it has sought to build up reserves to make its balance sheet more solid and increase the capacity to react to internal and external shocks, and (2) it only intervenes on occasions when the exchange rate is either below or above certain thresholds which are considered to be dangerous for its target of cutting inflation or for financial stability. Furthermore, the dollar's weakness at global level will help to moderate Argentina's appreciation against its major trade partners, as shown in the evolution in the multilateral real exchange rate index.

Figure 7.3 Peso/dollar exchange rate: Research and consensus forecasts (ARS/USD)



Source: BCRA, Latinfocus and BBVA Research

Figure 7.4 Central Bank of Argentina international reserves and settlements of the agro-exporter complex (UDS MN)



Source: BBVA Research based on INDEC and Central Bank data

DISCLAIMER

This document, prepared by BBVA Research Department, is informative in nature and contains data, opinions or estimates as at the date of its publication. These derive from the department's own research or are based on sources believed to be reliable, and have not been independently verified by BBVA. BBVA therefore makes no guarantee, express or implied, as to the document's accuracy, completeness or correctness.

Any estimates contained in this document have been made in accordance with generally accepted methods and are to be taken as such, i.e. as forecasts or projections. The historical evolution of economic variables (positive or negative) is no guarantee that they will evolve in the same way in the future.

The contents of this document are subject to change without prior notice for reasons of, for example, economic context or market fluctuations. BBVA does not give any undertaking to update any of the content or communicate such changes.

BBVA assumes no responsibility for any loss, direct or indirect, that may result from the use of this document or its contents.

Neither this document nor its contents constitute an offer, invitation or solicitation to acquire, divest or obtain any interest in assets or financial instruments, nor can they form the basis of any contract, commitment or decision of any kind.

In particular as regards investment in financial assets that may be related to the economic variables referred to in this document, readers should note that in no case should investment decisions be made based on the contents of this document; and that any persons or entities which may potentially offer them investment products are legally obliged to provide all the information they need to take these decisions.

The contents of this document are protected by intellectual property law. It is expressly prohibited to reproduce, process, distribute, publicly disseminate, make available, take extracts, reuse, forward or use the document in any way and by any means or process, except where it is legally permitted or expressly authorised by BBVA.

This report has been produced by the Argentina Unit

Head Economist Argentina

Gloria Sorensen
gsorensen@bbva.com

Marcos Dal Bianco
marcos.dalbiano@bbva.com

Juan Manuel Manias
juan.manias@bbva.com

María Celeste González
celeste.gonzalez@bbva.com

Andrea Savignone
asavignone@bbva.com

Adriana Haring
aharing@bbva.com

Jorge Lamela
jorge.lamela@bbva.com

BBVA Research

Group Chief Economist

Jorge Sicilia Serrano

Macroeconomic Analysis

Rafael Doménech
r.domenech@bbva.com

Global Economic Situations

Miguel Jiménez
mjimenezg@bbva.com

Global Financial Markets

Sonsoles Castillo
s.castillo@bbva.com

Long term Global Modelling and Analysis

J. Julián Cubero
juan.cubero@bbva.com

Innovation and Processes

Oscar de las Peñas
oscar.delaspenas@bbva.com

Financial Systems And Regulation

Santiago Fernández de Lis
sfernandezdelis@bbva.com

International Coordination

Olga Cerqueira
olga.gouveia@bbva.com

Digital Regulation

Álvaro Martín
alvaro.martin@bbva.com

Regulation

María Abascal
maria.abascal@bbva.com

Financial Systems

Ana Rubio
arubiog@bbva.com

Financial Inclusion

David Tuesta
david.tuesta@bbva.com

Spain and Portugal

Miguel Cardoso
miguel.cardoso@bbva.com

United States

Nathaniel Karp
Nathaniel.Karp@bbva.com

Mexico

Carlos Serrano
carlos.serranoh@bbva.com

Middle East, Asia and Geopolitical

Álvaro Ortiz
Alvaro.ortiz@bbva.com

Turkey

Álvaro Ortiz
alvaro.ortiz@bbva.com

Asia

Le Xia
le.xia@bbva.com

South America

Juan Manuel Ruiz
juan.ruiz@bbva.com

Argentina

Gloria Sorensen
gsorensen@bbva.com

Chile

Jorge Selaive
jselaive@bbva.com

Colombia

Juana Téllez
juana.tellez@bbva.com

Peru

Hugo Perea
hperea@bbva.com

Venezuela

Julio Pineda
juliocesar.pineda@bbva.com

CONTACT DETAILS: BBVA Research – BBVA Banco Francés: Reconquista 199, 1st floor. C1003ABC - Buenos Aires (Argentina).

Tel.: (+54) 11 4346 4000 / Fax: (+54) 11 4346 4416 - bbvaresearch@bbva.com www.bbvaresearch.com