BBVA Research

Argentina Economic Outlook

1Q21

January 2021

Creating Opportunities

Key points

Global GDP will expand by around 5.3% in 2021 and 4.1% in 2022 after contracting by approximately 2.6% in 2020. In the short term, growth will be affected by the more negative evolution of the pandemic in many countries. Uncertainty will remain high despite forecasts for "normalization" and there are both upward and downward risks to growth forecasts.

Argentina is experiencing a second wave of infections caused by increased population mobility, as a result of the weather conditions and the holiday period, so far without putting the health system under pressure. The vaccination process has begun, albeit slowly.

We reduce the contraction of GDP in 2020 to 11% due to slightly better than expected 3Q20 data, leaving more of a carry-over for 2021, enabling us to improve our forecast for this year to 6%.

Owing to the high degree of informality in the labor market and the lack of dynamism shown by the economy, we are expecting a slow reduction in unemployment which will reach 11% in 2021.

The primary fiscal deficit was 6.5% of GDP in 2020, a lower value than expected. The Ministry of Economy showed greater fiscal responsibility in 4Q20. We anticipate new tax reforms within the framework of any future program agreed with the IMF, which would increase tax pressure.

Key points

Inflation in 2020 was 36.1% Y/Y and slowed down compared to 2019 due to the recession, the freezing of regulated prices and the containment of the exchange rate. We maintain our baseline scenario of inflation at 50% for 2021, in view of the fact that the economy will have to process the large amount of money issued in 2020 in the framework of monetary policy that we expect to be lax, together with corrections (even if partial) of tariffs and with no room to lag the exchange rate.

As long as the gap between the official and parallel FX rates does not rise sharply, better commodity prices increase the likelihood that the government can reach the elections without a sharp exchange rate correction, at the expense of more exchange rate regulations and weak economic activity.

We cut the trade surplus forecast, so we are expecting a current account balance of 1.1% of GDP for 2020, from 2.1%, and 0.5% for 2021, from 1.6%.

Any macroeconomic program agreed with the IMF should include sound fiscal consolidation in order to make it very probable that the debt is sustainable. This somewhat reduces the chances of launching the new program before the legislative elections, so we would only expect announcements of partial progress until then.

01

Global Economic Outlook

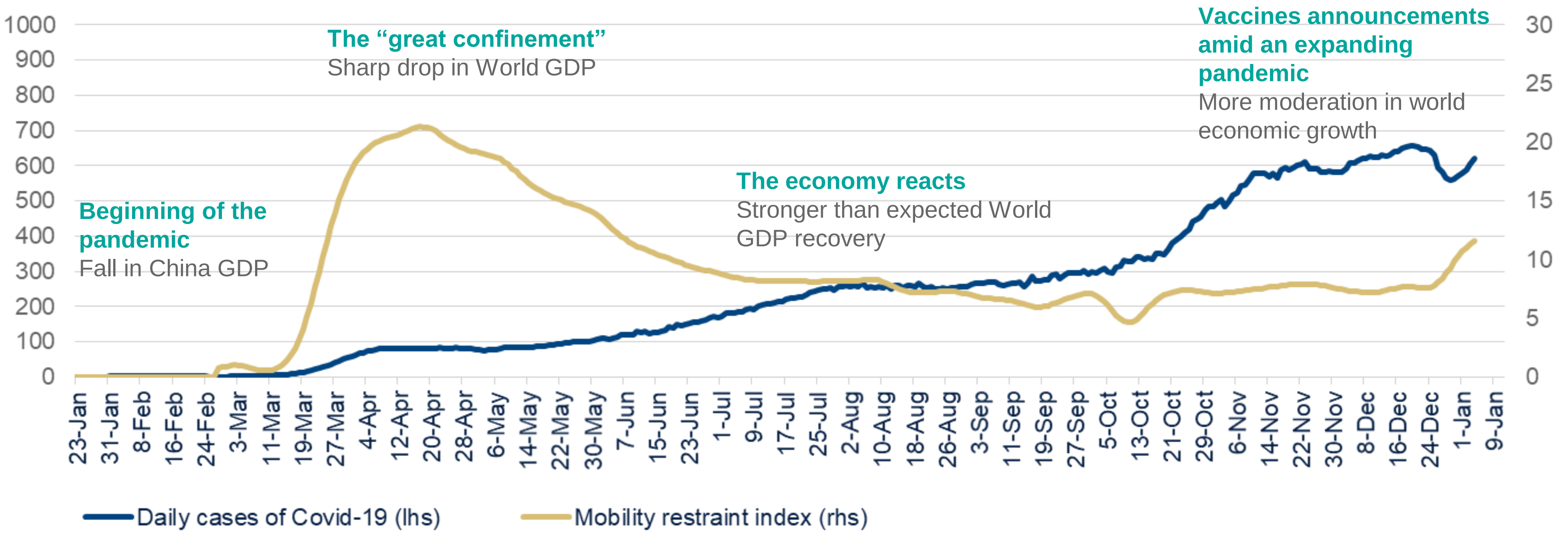
1Q21

Creating Opportunities

Covid-19 vaccines are a key development after a year marked by the expansion of the pandemic, lockdowns and an economic crisis

WORLD DAILY CASES OF COVID-19 AND GLOBAL MOBILITY RESTRAINT INDEX (*)

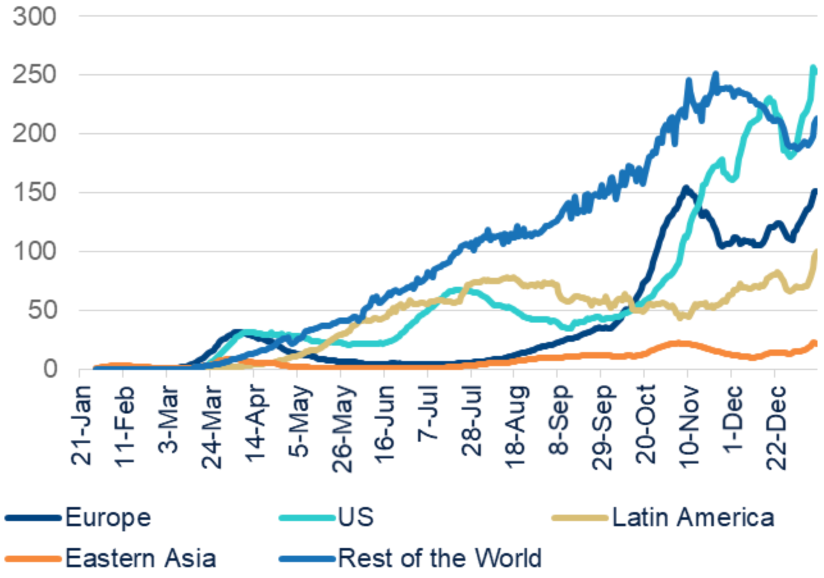
(DAILY CASES:THOUSANDS OF PEOPLE, 7-DAY MOVING AVERAGE; INDEX: HIGHER VALUES INDICATE LOWER MOBILITY)



*: The mobility restraint index reflects changes with respect to the period of reference (January 3 to February 6 2020). It is the simple average of all countries within Google Mobility Reports.
BBVA Research based on data from John Hopkins University and Google.

Infections have surged in the last months, particularly in the US and Europe; the new strains of the virus pose a threat

DAILY CASES OF COVID-19 (*)
(THOUSANDS OF PEOPLE, 7-DAY MOVING AVERAGE)



- In the US, Europe and Latam contagions have increased again in the last few weeks.
- Eastern Asia is experiencing outbreaks, but the situation remains under control.
- Rising uncertainty on the evolution of the pandemic due to the new strains of the virus.
- Mobility has decreased again, particularly in recent weeks and in Europe, but less than in the first wave.

(*): Europe: Germany, Spain, France, Italy, Portugal, United Kingdom, and Turkey. Latin America: Argentina, Brazil, Chile, Colombia, Mexico, Peru and Uruguay. Eastern Asia: China, South Korea, Japan and Singapur.
Source: BBVA Research based on data from John Hopkins University.

Covid-19 vaccine inoculation process has already started in some of the main world economies, in line with expectations

EU

Population covered by the vaccine purchase contracts already signed
(not all approved yet)

Inoculation started at a low pace with the BioNTech/Pfizer vaccine.

US

Population covered by the vaccine purchase contracts already signed
(not all approved yet)

Inoculation started with the BioNTech/Pfizer and Moderna vaccines.

CHINA

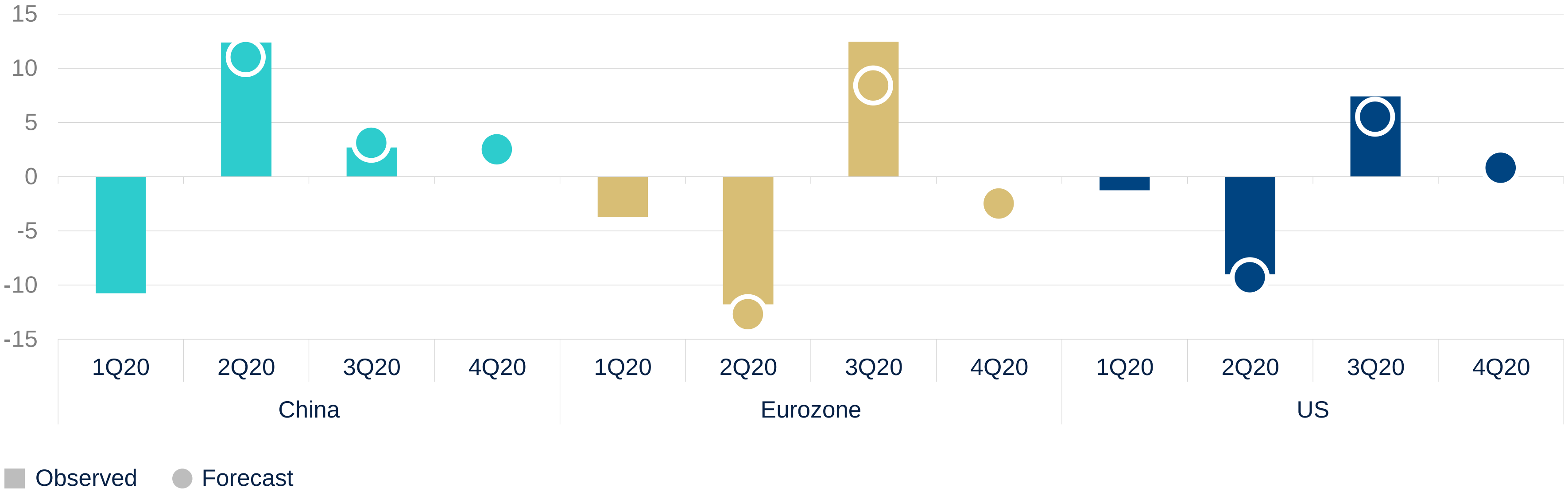
Inoculation started with the Sinopharm vaccine.

OTHER REGIONS

Heterogeneity across countries.
Ongoing vaccination in Israel, United Kingdom, Russia, Argentina, Chile, Mexico etc.

Economic growth has picked up significantly more than expected in the third quarter, but has moderated in the fourth due to the increase in infections

GDP: OBSERVED AND FORECASTED
(Q/Q %)



Source: BBVA Research based on own data and Haver.

A large-scale distribution of vaccines will pave the way for economic recovery, which will be gradual and heterogeneous across countries

MAIN ASSUMPTIONS BEHIND FORECASTS, UNDER A HIGHLY UNCERTAIN ENVIRONMENT

COVID-19

Massive distribution of vaccines in the main economies in 1H21 and afterwards in the others.

Return to “normality” in 2022

Economic Policy

Stimuli will be maintained, or even amplified, at least until the recovery consolidates.

Financial Markets

Volatility and risk aversion will remain relatively low, in 2021-22.

Economic growth will slow down more than expected in the short-term, due to rising contagions, but it will invigorate from mid-year on

	US	Eurozone	China	World
2019	2.2	1.3	6.1	2.9
2020	▲ -3.6	▲ -7.3	► 2.2	▲ -2.6
2021	▼ 3.6	▼ 4.1	► 7.5	▼ 5.3
2022	2.4	4.4	5.5	4.1

▲ Upward forecast revision
► Unchanged forecast
▼ Downward forecast revision

Source: BBVA Research.

Uncertainty will remain high, despite improved perspectives

Epidemiological uncertainty

- Virus strains and new waves of contagions.
- Vaccines: distribution pace, effectiveness, social rejection.
- Herd immunity.
- “New normalcy” and social preferences.

Financial uncertainty

- Deterioration of corporate, public and banking sector balance sheets (NPL, bankruptcy, debt, restructurings).
- Financial tensions.
- Portfolio flows to emerging markets.

Economic uncertainty

- Stimuli effectiveness.
- Savings evolution.
- Significant disruptions in sectors and value chains.
- Inflation and oil prices.
- Lagged recovery in emerging economies.
- Size of the impact of the pandemic on potential GDP.

Geopolitical uncertainty

- China – US rivalry.
- Social unrest.
- Protectionism.

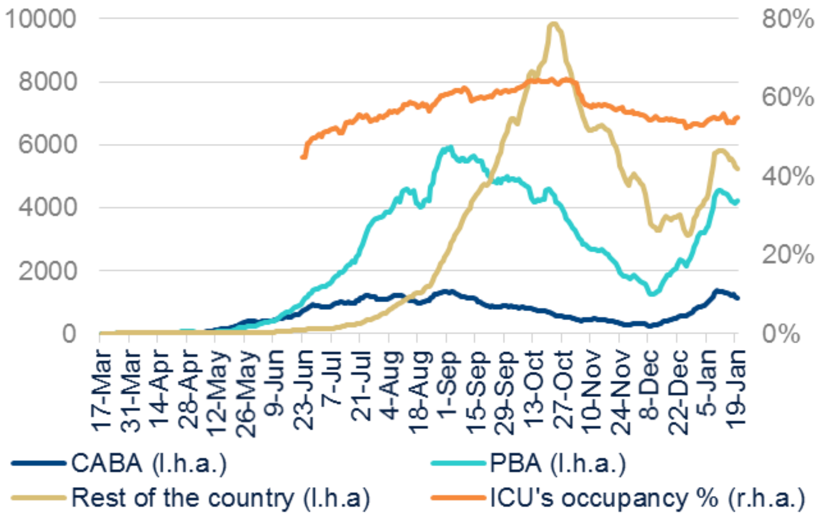
BBVA Research

02

Argentina Economic Outlook 1Q21

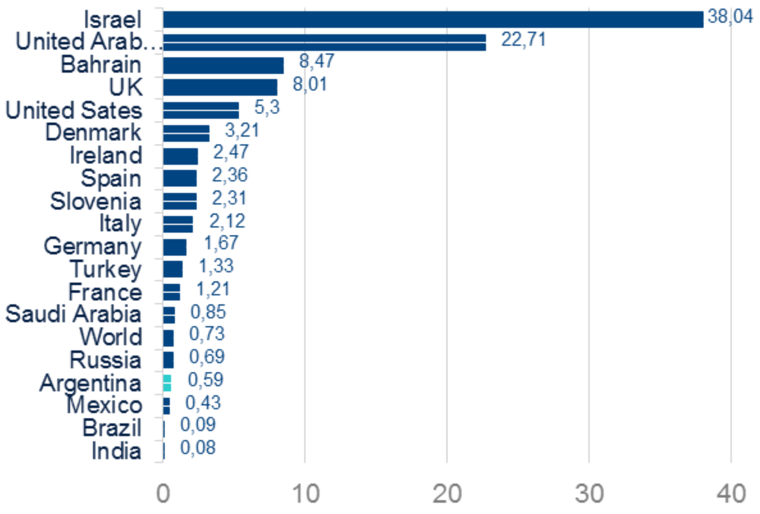
COVID infections are picking up in Argentina just as the vaccination plan is being launched

EVOLUTION OF INFECTIONS BY JURISDICTION
(7D AVERAGE)



Source: BBVA Research and the Argentine Ministry of Health.

VACCINES PER MILLION INHABITANTS (1 dose)



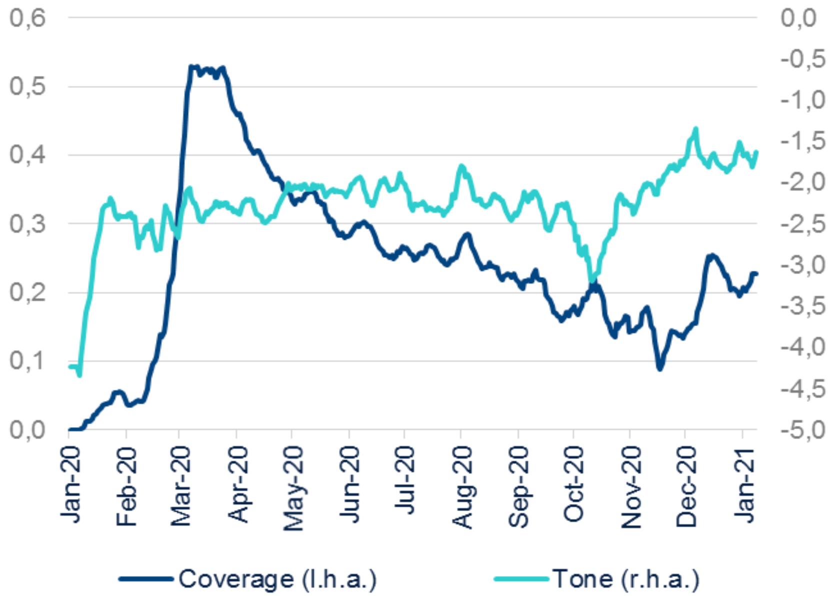
Source: BBVA Research and Our World in Data.

The government granted greater autonomy to the provinces to determine the rigidity of the lockdown measures in each jurisdiction

In Dec-20, the rollout of the Sputnik V vaccine began, although slowly. The government has also secured a contract to purchase the Oxford vaccine and access to the Covax program.

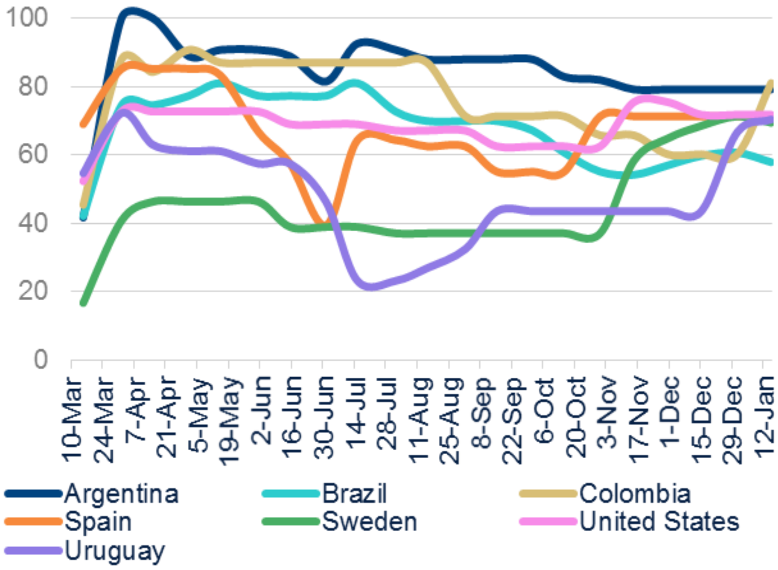
Slight improvement in the tone of the news on the pandemic and a marginal relaxation of the rigidity of the health measures

COVERAGE AND TONE OF NEWS ARTICLES THAT MENTION ARGENTINA AND COVID-19
(7-DAY MOVING AVERAGE)



Source: BBVA Research & GDELT. Using media data (GDELT), we construct a media coverage indicator that could be interpreted as a measure of the popularity of the "Covid-19" + "Argentina" topic, while the tone captures the positive or negative connotations of the news items that mention "COVID-19" + "Argentina."

LOCKDOWN RIGIDITY INDEX
(LEVELS FROM 0 TO 100)

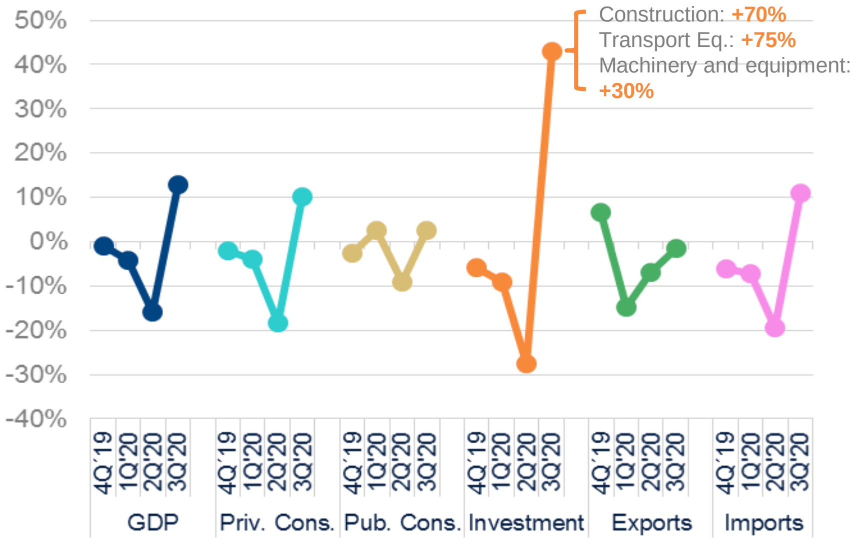


Source: BBVA Research and Oxford University. The Oxford Stringency Index is an indicator that measures the toughness of the lockdown in different countries at each moment based on the measures they are taking to deal with the pandemic.

Activity was better than expected in 3Q (with many one-off contributions)

GDP BY COMPONENT

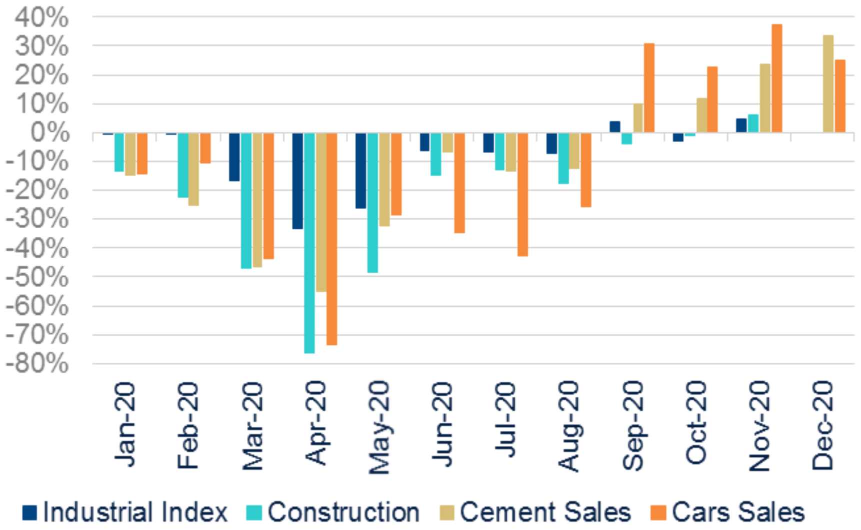
(% CHANGE, Q/Q; SERIES WITHOUT SEASONALITY)



Source: BBVA Research and INDEC.

SELECTED INDUSTRY INDICATORS

(% CHANGE, Y/Y)

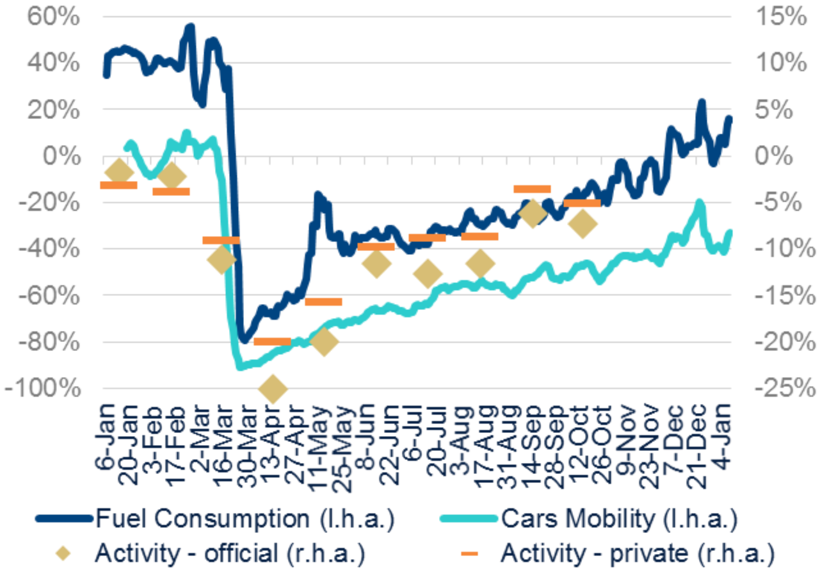


Source: BBVA Research, INDEC, AFCP and ACARA.

After the economic collapse of 2Q20, investment was triggered by private construction works and by the purchase of motor vehicles and agricultural machinery. This can be explained by savings strategies given devaluation expectations.

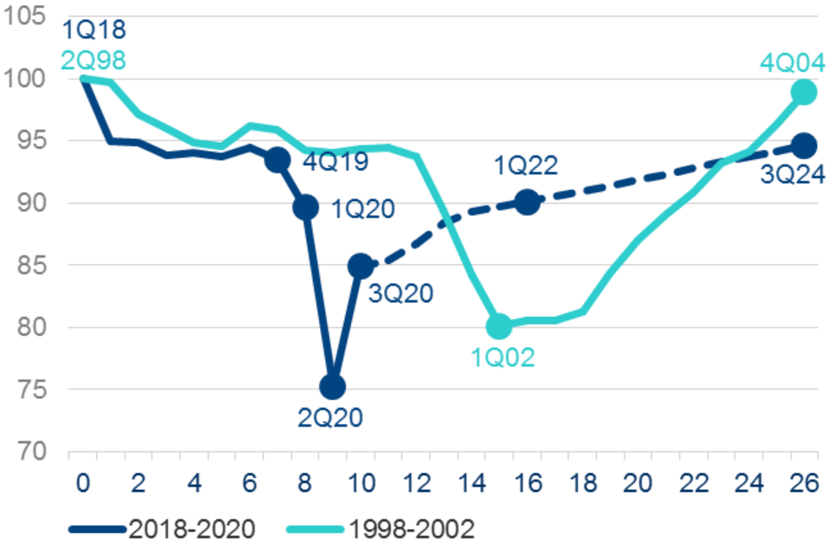
Durable goods purchases and the resumption of activities spur the recovery in activity in 2H20 but it has a slow pace going forward

FUEL CONSUMPTION AND ACTIVITY
(CONSUMPTION: % CHANGE Y/Y IN CURRENT ARS; ACTIVITY INDICATORS: % CHANGE Y/Y ORIGINAL SERIES)



Source: BBVA Research, INDEC, OJF & Associates and Apple.

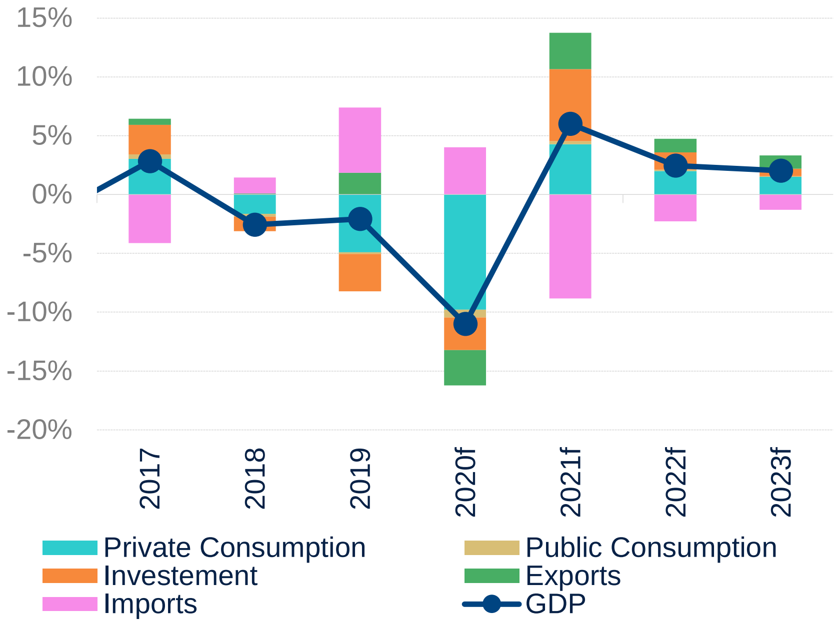
1998–2002 CRISIS AND 2018–2020 CRISIS
(QUARTERS SINCE THE BEGINNING OF THE RECESSION; SERIES WITHOUT SEASONALITY; BASE 100 = QUARTER BEFORE THE FALL)



Source: BBVA Research and INDEC.

We adjust the fall in GDP in 2020 to 11%, expecting a 6% recovery in 2021

CONTRIBUTION TO ECONOMIC GROWTH
(CONTRIBUTION BY GDP COMPONENT)



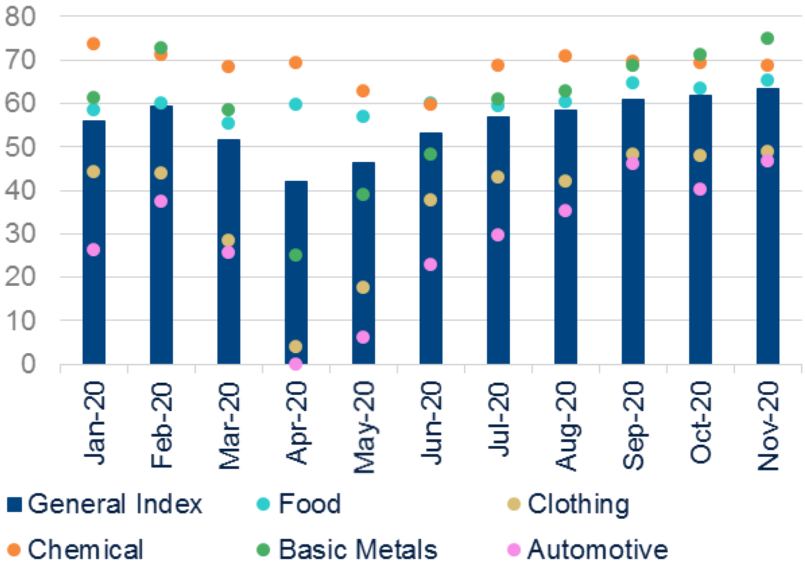
(f): forecast.
Source: BBVA Research.

- The economy as a whole will have little dynamism this year: we expect average growth of 1.5% Q/Q in 2021.
- Consumption will be lackluster owing to household indebtedness, loss of real wages and high unemployment.
- Investment will be hit by high inflation and much uncertainty.
- Exports will perform weakly while imports grow rapidly, both influenced, in different directions, by the exchange rate gap.
- Unemployment will fall and employment will grow but with lower quality jobs.

We estimate that unemployment will reach 11% in 2021 as a result of weak labor demand and offset by the temporary depression of labor supply

UTILIZATION OF INDUSTRIAL CAPACITY

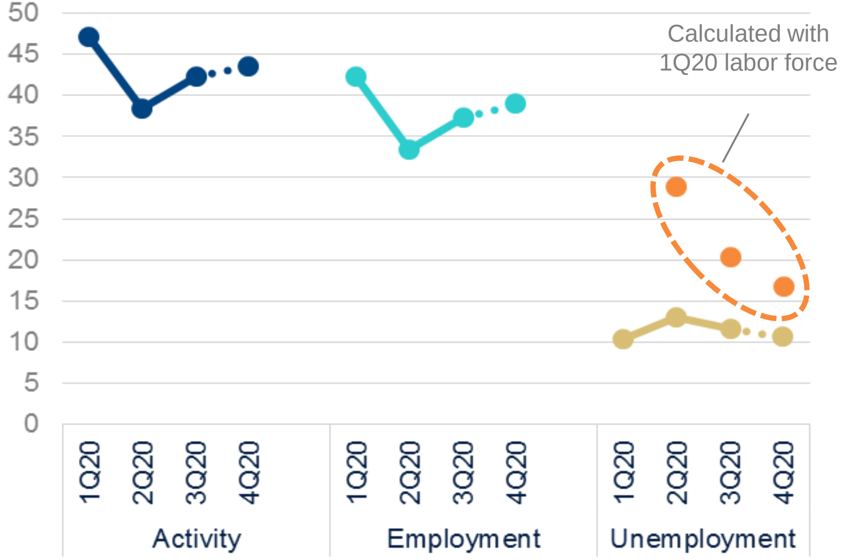
(%)



Source: BBVA Research and INDEC.

LABOR MARKET: MAIN INDICATORS

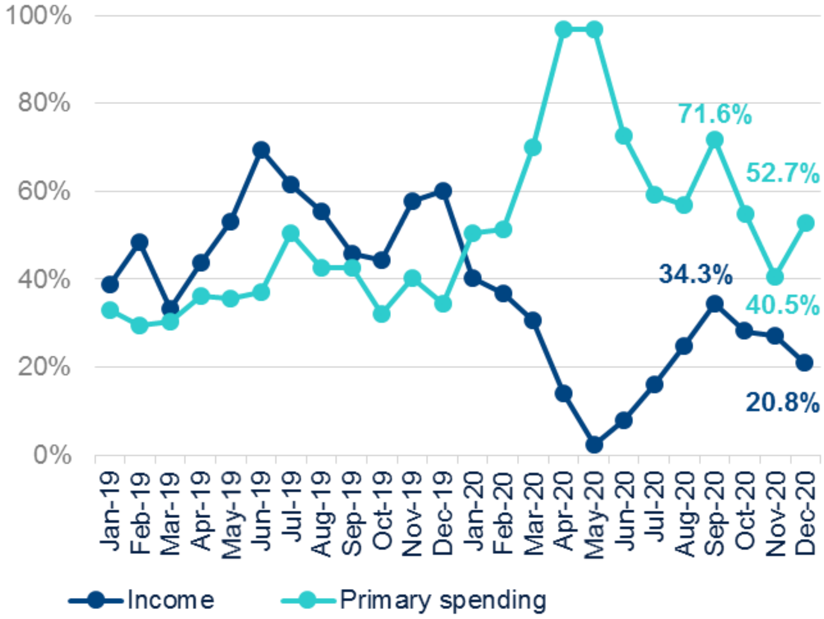
(%)



Source: BBVA Research and INDEC.

The Government ends 2020 with an incipient fiscal responsibility

TOTAL INCOME AND PRIMARY EXPENDITURE
% CHANGE, Y/Y

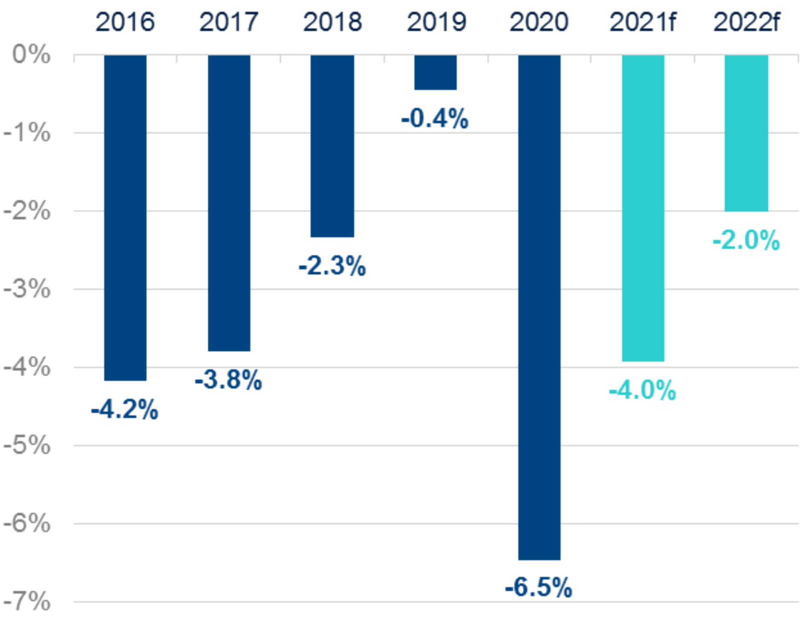


Source: BBVA Research and Treasury.

- After increasing by almost 90% Y/Y in 2Q20, the government managed to moderate the increase in public spending and reduce imbalances.
- The first thing it did was to restrict the costs associated with COVID.
- The lukewarm recovery of activity from 3Q20 made it possible to restore income somewhat, after the minimal growth in May.
- Thus, the year 2020 concluded with a lower deficit than previously forecast, although it turned out to be the highest in recent years that, in view of the inability to go to the debt markets, had to be financed entirely by the Central Bank.

The fiscal balance will improve in 2021, but this is not without its challenges

PRIMARY FISCAL BALANCE
AS A % OF GDP



Source: BBVA Research and Treasury.

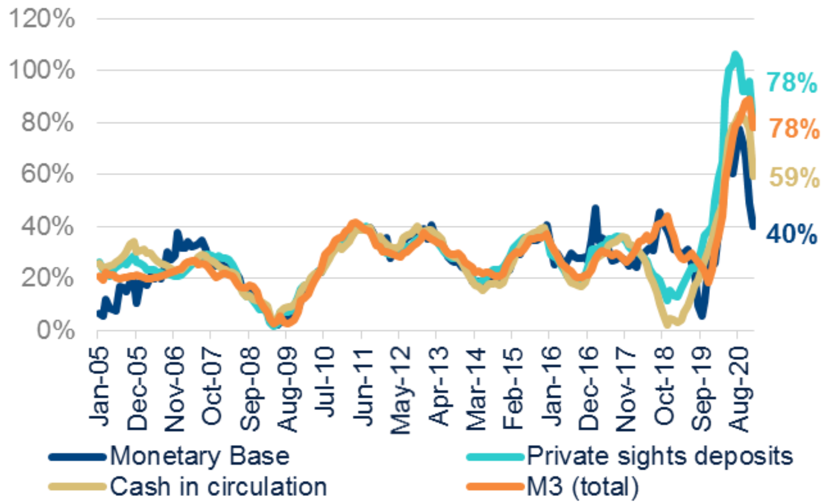
- Government revenues will improve in 2021 due to a recovery in the level of activity and increased retentions due to high soybean prices.
- Our forecast of a deficit of 4% of GDP assumes that the outbreak of COVID-19 is controlled during the year and that an agreement is reached with the IMF.
- The fiscal balance in 2022 adopts a path of fiscal consolidation until it finds its equilibrium in 2024, a path that could emerge from the agreement with the IMF.

The large-scale fiscal financing with the issuing of money during 2020 could give rise to inflationary pressures for this year

MONEY ISSUED TO ASSIST THE TREASURY
(% GDP, ACCUMULATED AT 12 MONTHS)

Source: Central Bank of Argentina and BBVA Research..

MONETARY AGGREGATES
(% CHANGE, Y/Y)

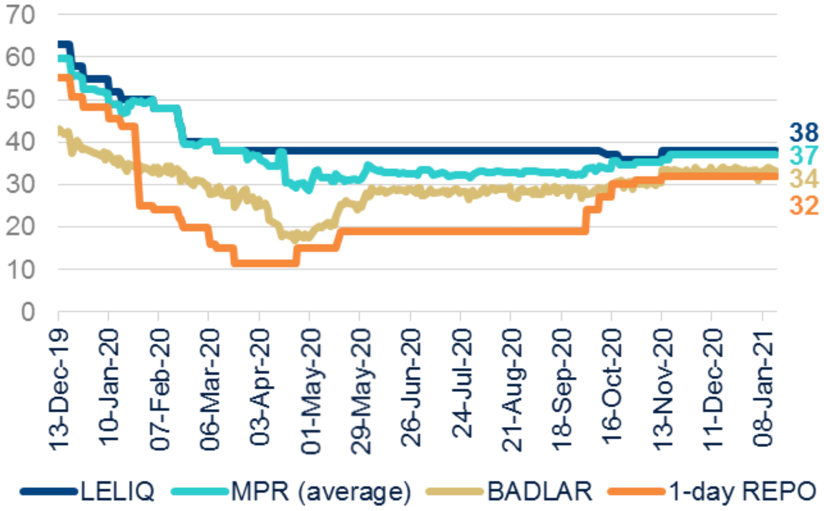


Source: Central Bank of Argentina and BBVA Research.

During 2020, the CB had to issue an equivalent of 116% of the monetary base at Dec-19 to assist the treasury. Broader monetary aggregates grew 78% Y/Y. This increase is one of the main drivers behind the inflationary pressures we are forecasting for 2021.

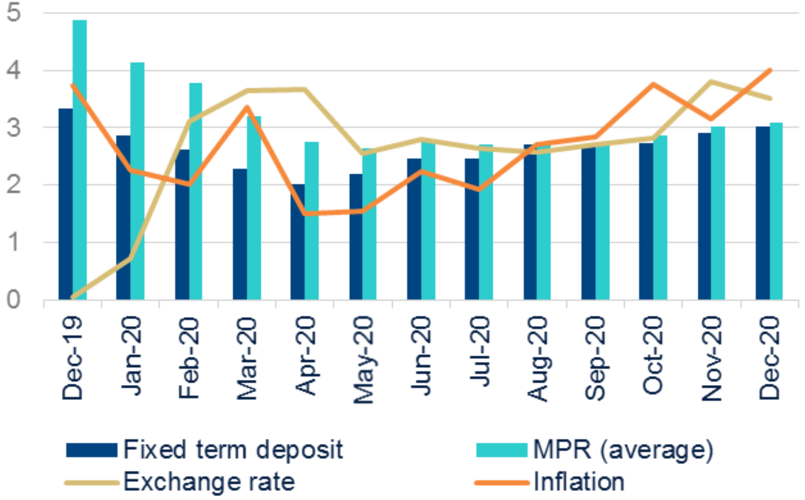
Interest rates are increasingly lagging behind inflation and devaluation...

MONETARY POLICY INTEREST RATES AND BADLAR RATE (% ANR)



Source: Central Bank of Argentina and BBVA Research.

INTEREST RATES, EXCHANGE RATE AND INFLATION (MONTHLY RATES IN %, EXCHANGE RATE: % CHANGE, M/M)

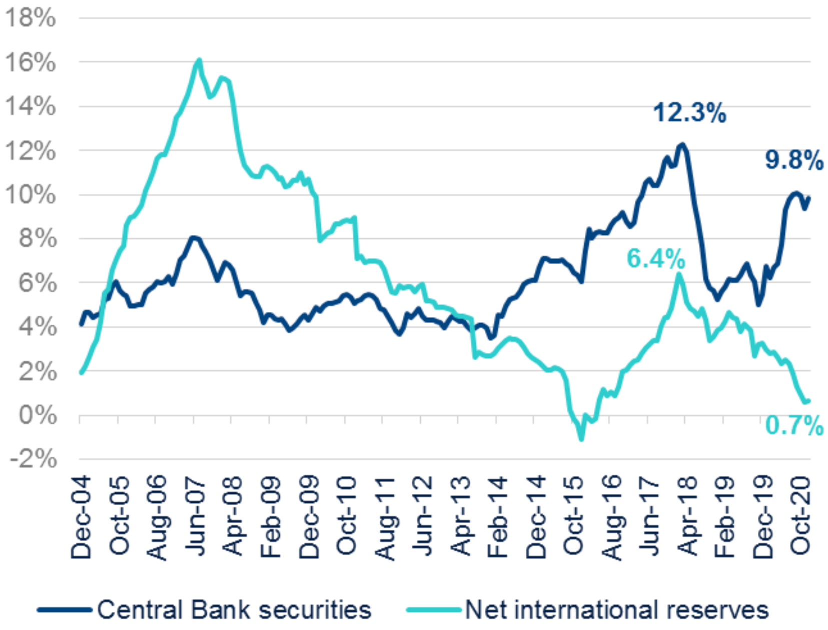


Source: Central Bank of Argentina and BBVA Research.

The CB is reluctant to raise interest rates, as it is trying to contain the quasi-fiscal deficit and maintain the expansionary bias of its monetary policy. However, we believe that continued inflationary and currency pressures in the coming months will drive interest rate increases by the monetary authority.

… but the vulnerability of the CB balance sheet limits the room for maneuver in monetary policy

CENTRAL BANK INTEREST-BEARING LIABILITIES AND NET INTERNATIONAL RESERVES (% GDP)

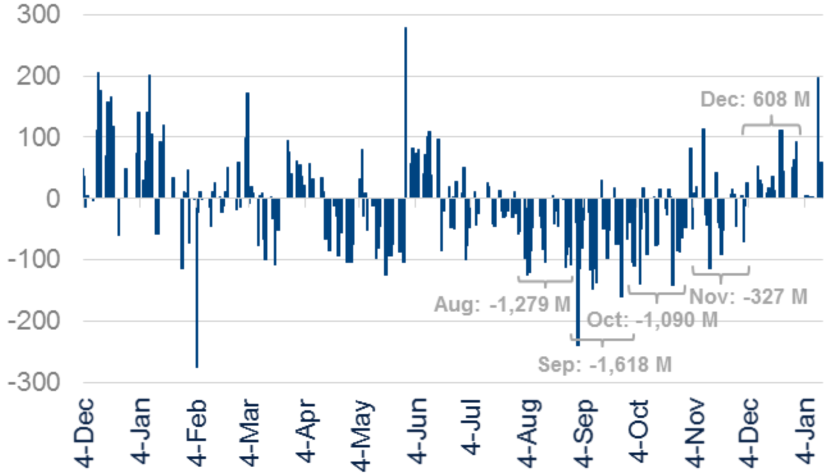


Source: Central Bank of Argentina and BBVA Research.

- The CB's high stock of interest-bearing liabilities (liquidity bills and repos) reduces its room to correct the monetary imbalance.
- Since September, the treasury has made efforts to reduce the need for monetary assistance, which has allowed the upward curve of interest-bearing liabilities to be curbed.
- Even so, in 2021, the CB has limited scope to maintain its sterilization policy and/or to increase interest rates without fueling a rise in the quasi-fiscal deficit.

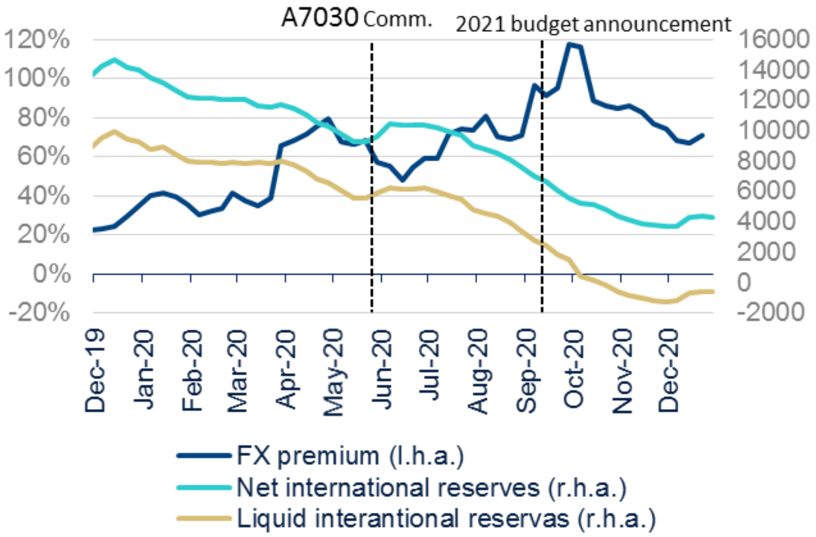
Following increased FX rate controls and helped by seasonal factors, the CB began buying back reserves in December

CENTRAL BANK EXCHANGE RATE INTERVENTIONS
(USD MILLIONS DAILY)



Source: Central Bank of Argentina and BBVA Research.

INTERNATIONAL RESERVES AND EXCHANGE RATE GAP (RESERVES IN USD MILLIONS; EXCHANGE RATE GAP VS LCR IN % WITH RESPECT TO THE OFFICIAL EXCHANGE RATE)



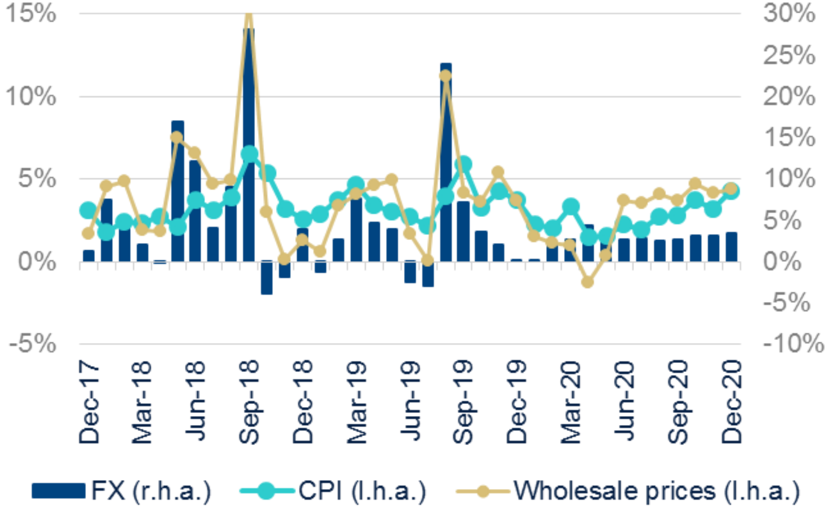
Source: Central Bank of Argentina and BBVA Research.

With the gap contained and better commodity prices, there is more chance that the government can reach the elections without currency disruptions…

…but the exchange rate gap remains high and disruptive for economic activity and the level of reserves remains very low.

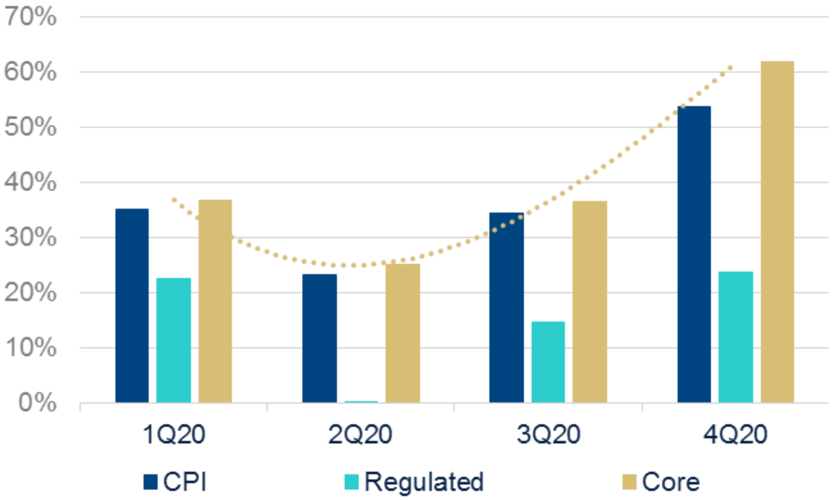
In parallel with increased mobility, all prices accelerated in 2H20

CPI, WPI AND EXCHANGE RATE
(USD MILLIONS DAILY)



Source: Central Bank, INDEC and BBVA Research.

INFLATION, BY COMPONENT
(ANNUALIZED AVERAGE MONTHLY INFLATION)

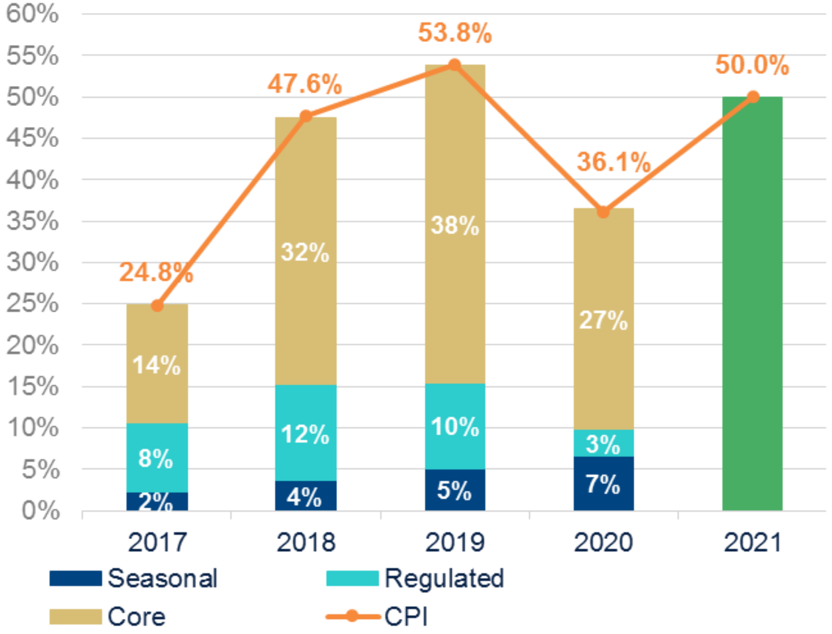


Source: Central Bank of Argentina and BBVA Research..

Wholesale price inflation (WPI) predicts consumer price increases (CPI) between the first and the sixth month afterward. This phenomenon is consistent with our forecast for an increase in inflation in 2021 given the scenario of the relaxing of social distancing measures and higher rates of average annual depreciation.

We maintain our scenario of inflation accelerating to 50% in 2021

INFLATION, BY COMPONENT
(ANNUALIZED AVERAGE MONTHLY INFLATION)

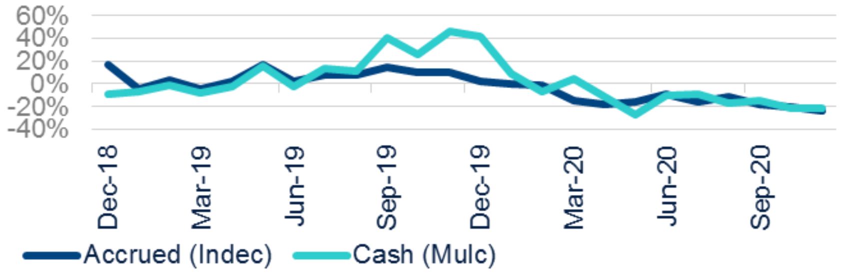


Source: INDEC and BBVA Research.

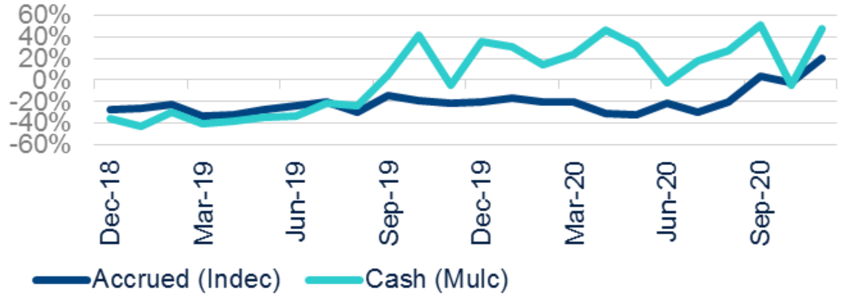
- In 2020 inflation was 36.1%, contained by the effects of the lockdown and transitional instruments.
- We maintain our baseline scenario of 50% inflation for 2021 (+13.5 pp Y/Y) which incorporates the large monetary imbalance, a weak monetary policy attitude and corrections of the exchange rate and tariff lags accumulated in the year of COVID-19.
- The balance of risks has a marked upward bias.

The persistence of a high FX exchange rate gap ends up eroding the trade surplus

EXPORTS: % CHANGE Y/Y



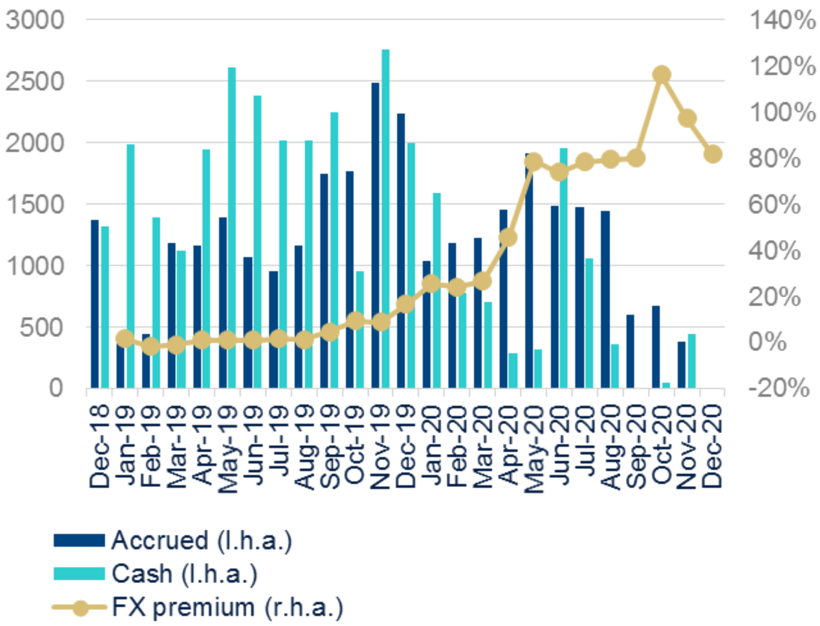
IMPORTS: % CHANGE Y/Y



Source: BBVA Research, Indec and Central Bank o of Argentina.

TRADE BALANCE AND EXCHANGE RATE GAP

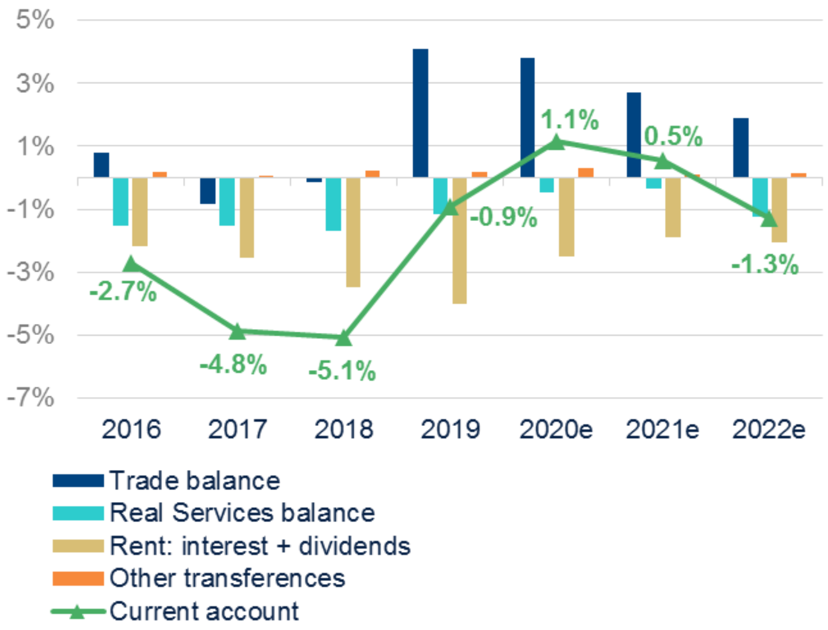
(IN MILL. USD AND %)



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

The reduced contribution from trade led to the downward revision of the current account surplus

CURRENT ACCOUNT AND ITS COMPONENTS
(% of GDP)



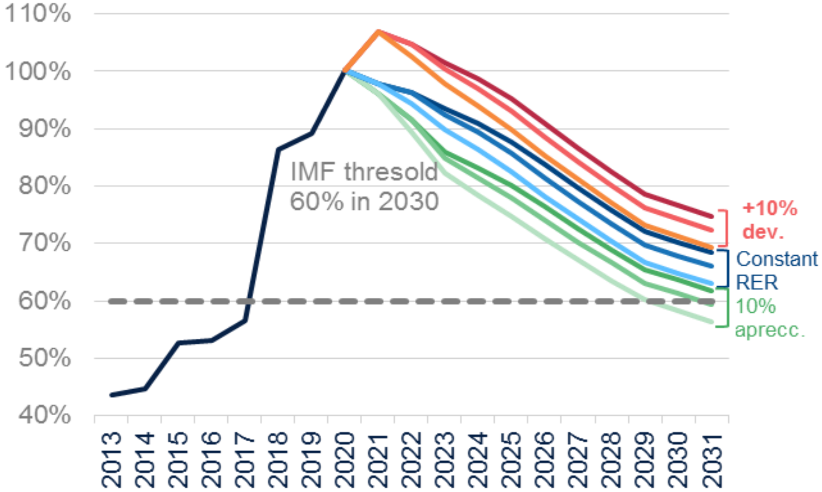
Source: BBVA Research, Indec.

- We adjust GDP to 1.1% for 2020 (formerly 2.1%) and to 0.5% for 2021 (formerly 1.6%) due to the erosion of the trade surplus.
- The rise in commodity prices is an upward bias to our revision.
- As long as the borders remain closed, the deficit in the real services account (dominated by tourism) will remain controlled.

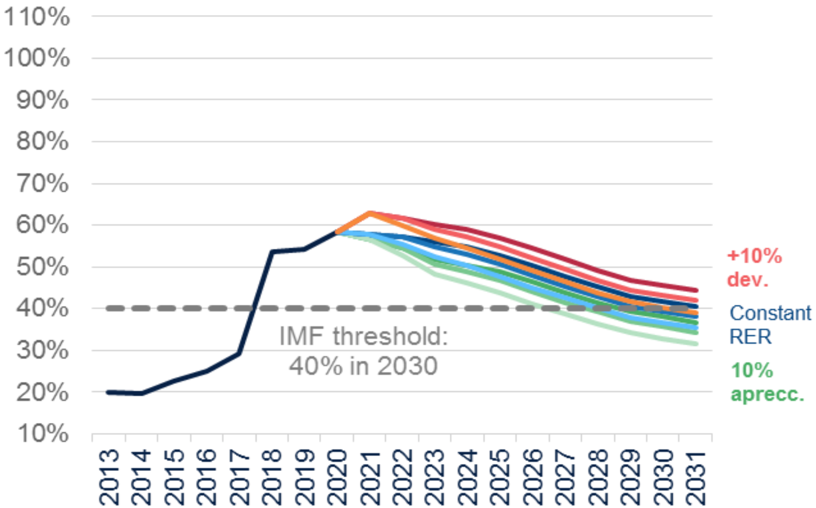
Negotiations with the IMF: there is still a long way to go…

THE TRAJECTORY OF ARGENTINE PUBLIC DEBT IN DIFFERENT MACROECONOMIC SCENARIOS
(% GDP)

TOTAL DEBT



DEBT TO PRIVATE AND MULTILATERAL CREDITORS



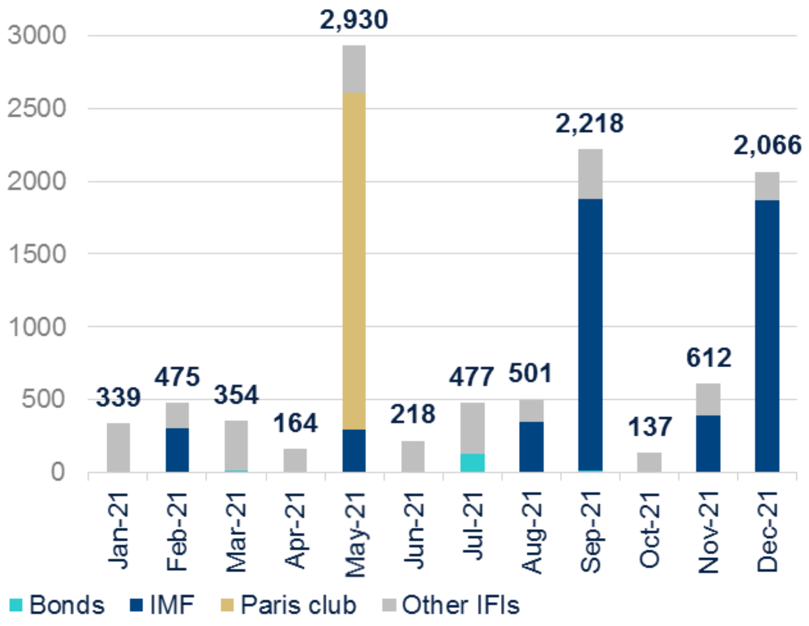
Dark lines: Fiscal eq. in 2024 and 1.2% sup. in 2027
Intermediate tone lines: Fiscal eq. in 2023 and 1.2% sup. in 2026
Soft lines: Fiscal eq. in 2022 and 1.2% sup. in 2025

Source: BBVA Research.

Substantial fiscal consolidation will be required to be a high probability that debt will be sustainable. Otherwise, debt becomes highly vulnerable to exchange rate leaps. If the IMF remains firm about ensuring debt sustainability (even with a low probability), a path of fiscal adjustment will be required that will not be easy to accept months before the elections.

… but the government will always remain at the negotiating table to avoid a new wave of financial tensions

MONTHLY MATURITIES IN USD WITH PRIVATE AND MULTILATERAL CREDITORS
(USD MILLIONS)



Source: BBVA Research and Ministry of Economy.

- The next major maturity in foreign currency is in May, with the Paris Club.
- Negotiations with the IMF need to be at least at an advanced stage by then to refinance that payment.
- For this reason, we believe that there will be substantial announcements during April about the new program with the IMF.
- The Government is requesting an "EFF" program, which is longer term than the current "SBA." In return, the IMF will likely demand tougher conditions, in terms of fiscal-monetary-exchange rate consistency and medium-term reforms (tax, financial, capital mobility).

Macroeconomic forecasts

ARGENTINA	2018	2019	2020e	2021e	2022e
GDP (% Y/Y)	-2.6	-2.1	-11.0	6.0	2.5
Inflation (% Y/Y, EOP)	47.6	53.8	36.1	50.0	45.0
Exchange rate (vs USD, EOP)	37.9	59.9	82.6	121.3	164.6
Monetary policy rate* (% EOP)	59.3	58.5	37.1	45.0	40.5
Private consumption (% Y/Y)	-2.2	-6.6	-13.8	6.2	2.9
Public consumption (% Y/Y)	-1.7	-1.0	-4.9	1.7	0.8
Investment (% Y/Y)	-6.0	-16.0	-16.2	38.0	7.0
Primary fiscal balance (% GDP)	-2.3	-0.4	-6.5	-4.0	-2.0
Current account (% GDP)	-5.1	-0.9	1.1	0.5	-1.3

* As of Dec-19, the monetary policy rate is the weighted average between the LELIQ rate and the repo rate.

Source: BBVA Research.

BBVA Research

Argentina Economic Outlook

1Q21

January 2021

Creating Opportunities