ARGENTINA

IMPRESSIVE STABILISATION

Argentina's economy is back on track. Since mid-2024, growth has returned and inflation has slowed significantly. There has been a high social cost to the severe cuts in public spending, but the government budget is in surplus for the first time since 2010. With the recessionary impact of fiscal austerity, the current account balance has turned into a surplus as well. But exports have also been rebounded , despite low prices of agricultural commodities. For the time being, the central bank's foreign exchange reserves are still insufficient for exchange controls to be lifted before the mid-term elections in October. The renewal of an agreement with the IMF is already a prerequisite. The economic recovery should be confirmed in 2025, especially as the change of government in the United States could have positive effects.

GROWTH: THE END OF RECESSION

Real GDP rebounded strongly in Q3 2024 (+3.9% q/q) after three quarters of consecutive declines. All of the components of private demand made a positive contribution to the upturn in activity, including net foreign trade thanks to stronger growth in exports than in imports. By sector, the rebound has been particularly noteworthy in construction (+11%) and industrial production (+3.4%), but it only very partially corrects the fall in late 2023-early 2024 (see chart). Measured over a year, GDP growth is still negative (-2%) and remains almost 5% below its previous high in Q4 2018.

Over the last months of the year, trends in industrial production and in agricultural and industrial manufacturing exports in dollars (75% of total exports) confirmed the return to growth. Only construction activity contracted again, but this does not reflect a trend, as data are highly volatile, even when seasonally adjusted. Household confidence, which had fallen sharply in the first half of the year, returned to its late 2024 level, reinvigorated by the progress of disinflation (see below). Between January and October 2024, wages actually recovered. However, over the year as a whole, wage trends remained negative, especially in the public sector (-18% compared with -2.5% for registered private-sector employees). As job losses increased at the same time, and social benefits were cut in real terms, the rebound in household consumption was based largely on a falling saving rate.

For 2025, the return to full-year growth is based on i/ continuing disinflation, which would enable household disposable income to recover and provide a more solid basis for consumption ii/ rebounding investment as a result of deregulation and the tax incentive programme (RINGI programme). On the other hand, the positive contribution of foreign trade could be reduced or even reversed due to the very strong appreciation of the real exchange rate. In addition, the prices of the main exported agricultural commodities (soybean, corn and wheat) are not buoyant.[1]

FORECASTS

	2022	2023	2024e	2025e	2026e
Real GDP growth, %	5.3	-1.6	-2.6	3.9	2.8
Inflation, CPI, year average, %	72.4	133.5	219.9	42.0	29.0
General gov. balance / GDP, %	-3.8	-4.4	-0.0	0.2	0.9
General gov. debt / GDP, %	85.6	156.5	87.4	74.8	69.4
Current account balance / GDP, %	-0.6	-3.2	1.5	0.7	-0.0
External debt / GDP, %	43.8	44.4	51.4	40.4	33.1
Forex reserves, USD bn	41.2	19.0	22.0	34.8	46.7
Forex reserves, in months of imports	5.1	2.5	3.4	5.0	6.3

e: ESTIMATES & FORECASTS

TABLE 1 SOURCE: BNP PARIBAS ECONOMIC RESEARCH

ARGENTINA: ACTIVITY INDICATORS

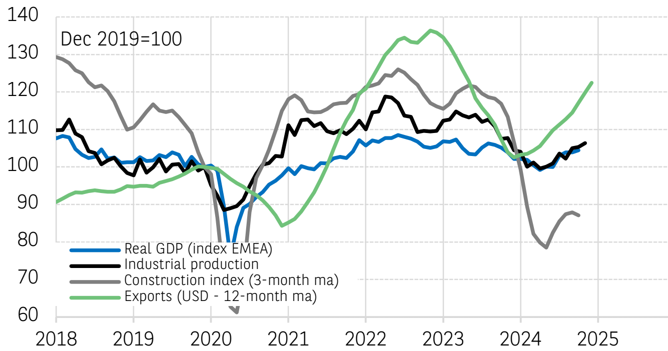

CHART 1 SOURCE: INDEC, ISAC, BNP PARIBAS

INFLATION: FIRST SUCCESS FOR THE ANCHORING STRATEGY

Inflation has slowed significantly in recent months, from an average of 4.2% per month between May and August to 2.8% between September and December. This disinflation is mainly due to i/ an appreciation of the real exchange rate, as a result of the setting of a nominal depreciation rate for the official exchange rate against the dollar of only 2% per month and the reduction in the gap between the main parallel exchange rate used for market instruments (the Blue Chip swap rate) and the official exchange rate, which was reduced to 30% on average in 2024 (17% in mid-January 2025) compared with more than 200% before devaluation ii/ the slowdown in money supply growth since July 2024. This strategy of anchoring expectations to the real exchange rate and controlling the monetary base has been facilitated by falling real wages and the extreme fiscal discipline imposed by Javier Milei's government.

1 Only corn prices have recovered since mid-2024, and are currently 11% above the 2024 average. Conversely, soybean prices are stagnating and wheat prices are depressed, down 2% and 9% on 2024, respectively.

PUBLIC FINANCES: AUSTERITY

Fiscal adjustment was spectacular in 2024. The central government budget recorded a surplus of 0.3% of GDP for the first time since 2010. The primary balance surplus hit 1.9% of GDP, compared with a deficit of 2.7% in 2023. The bulk of this spectacular improvement has come from a drastic cut in spending of 4.5 points of GDP. Social benefits and current transfers alone shrank by 2.6 points of GDP. The social cost is high, with the official poverty rate hitting a record 52.9% in June 2024. Thanks to disinflation, it is estimated to have fallen below 40% during the second half of the year[2]. However, according to calculations by the UCA Catholic University's social debt observatory, the poverty rate has actually risen over the past year and is still above 40% due to rising prices for services (electricity, water, gas and transport) and cuts in basic social benefits.

Revenue as a % of GDP remained more or less stable between the end of 2023 and the end of 2024, thanks in particular to the increase in real terms in taxes on foreign trade. Finally, the net interest burden also remained stable at 1.6% of GDP.

For 2025, the government aims to maintain a balanced budget and therefore to maintain a primary surplus of at least 1.5% of GDP. However, the abolition of the *Impuesto Pais* on imports and tourist spending by Argentines is likely to result in a loss of 1% of GDP in revenue. Further spending cuts will therefore be necessary.

The public debt ratio as a % of GDP is still very high at 94%. The change between the end of 2022 and the end of 2024 (see forecast table) almost exclusively reflects the impact of changes in the real exchange rate (+190% against the dollar in 2024 after -40% in 2023). With foreign currency debt still accounting for the majority of total debt (56% at the end of 2024), the ratio should continue to fall sharply over the next two years if the monetary authorities maintain a target rate of nominal exchange-rate depreciation significantly lower than the inflation rate, and if convergence between the parallel rate and the effective rate continues, or at least does not reverse. These last two conditions presuppose the maintenance of fiscal credibility and the strengthening of external liquidity and solvency, and, therefore, a lasting improvement in the current account.

EXTERNAL ACCOUNTS: FOREIGN EXCHANGE RESERVES REMAIN INSUFFICIENT DESPITE THE RECESSION SURPLUS

The current account balance returned to surplus last year (+USD 5 billion in Q1-Q3 2024). This is mainly a recession surplus following the extreme tightening of fiscal policy; imports excluding petroleum products contracted by 14% and the energy balance recorded a significant surplus of USD 4 billion. However, the surplus is also due to very dynamic exports, given the sluggish growth in global trade (3.4%). Exports of manufactured agricultural and industrial products rose by 16%, largely offsetting the fall in exports of raw agricultural products. In October and November, the trade balance (customs source) was still clearly in surplus (USD 1.6 billion cumulatively).

Over Q1-Q3 2024, net inflows of direct investment (USD 8.9 billion) largely offset net outflows of portfolio investment (USD -5.1 billion). Net capital flows from Argentinians (not included in FDI and PI) were negligible after massive net outflows in 2023 (USD 15.3 billion).

However, foreign exchange reserves only increased by USD 6 billion between the end of 2023 and the end of 2024, mainly due to the repayment of foreign public debt (USD 5.7 billion). The tax amnesty on dollars kept under the mattress or as deposits abroad enabled up to USD 15 billion to be repatriated, but these remained in the form of deposits in local banks. At the end of January, official foreign exchange reserves stood at just 30 billion.

In 2025, the amortisation of public foreign debt will almost double (USD 11.1 billion) despite the absence of repayments to the IMF. The budget surplus in 2024 enabled the Treasury to rebuild its foreign currency reserves, purchased from the central bank, enabling it to cover the international bond maturities in January and July 2025 (USD 5.8 billion amortisation, USD 3.1 billion interest).

Monetary and exchange rate policy: Argentina moves towards lifting exchange controls after the mid-term elections

The central bank has made only two moderate cuts to its key rate since the end of April 2024, bringing it down to 32% since the beginning of December. The BCRA had been forced to raise it very sharply during the devaluation at the end of 2023, and then to cut it markedly once the stressful period in late 2023-early 2024 had passed. The level of the key rate is in line with inflation expectations (26% according to the BCRA's December survey).

The exchange rate policy closely drives the nominal exchange rate in order to consolidate the convergence of the various rates before lifting exchange controls. The BCRA has lowered the rate of depreciation of the official exchange rate to 1% per month for 2025. However, exchange controls will not likely be lifted before the mid-term elections in October; the government team estimates that between USD 11 billion and USD 20 billion are needed for the lifting of exchange controls to be successful. Tthe renewal of the IMF agreement (which has been secured, but with very little additional funding) is a prerequisite in order to attract sustainable private investment.

TRUMP 2.0: A BONANZA?

The change of government in the United States could have positive implications for Argentina. The threat of a 10% or 20% increase in customs tariffs would only affect 8% of the country's exports. In addition, Argentina's trade balance with the United States is usually in deficit (the surplus in 2024 – USD 229 million - was an exception) and the Argentine monetary authorities cannot be suspected of manipulating the exchange rate to boost their competitiveness, quite the contrary. Javier Milei and Donald Trump have a very cordial relationship, and Javier Milei may even seek to negotiate a bilateral free trade agreement, even if it means leaving Mercosur, which he has described in the past as a "protectionist prison". The United States is the largest direct investor in Argentina, and the very liberal economic policy of the Milei government should attract US investors.

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2 38.9% in Q3 according to the Consejo Nacional de Coordinación de Políticas Sociales (CNCPS), 34.8% in Q4 2024 according to a study by an economist at the Università Torcuato di Tella.