# THE WEEK
# AT A GLANCE

ECONVIEWS

ECONOMÍA Y FINANZAS

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## Editorial: After a Good Week for the Government, on to a New Phase

**The week ended on a positive note.** Inflation was the lowest in 24 months and beyond the rise in utilities, the core CPI at 3.7% was a goal from the middle of the field. The OK from the IMF board was a given, but it is always good to confirm it. And the approval of the “Ley Bases” reform bill is the crowning of a 6-month process in which the project was reduced by 60% and where many things that the government wanted to do were left along the way. The government could not bend the will of the lovers of the status quo (politicians, businessmen and unions) on some issues. Surprisingly, it could not restore income tax for the wealthiest workers, something that lacks common sense and can generate fiscal problems.

**But the important thing is that the government demonstrated that it was able to work with politics to pass a law.** The market celebrated that, and this closes the first part of Milei's government that coincided with the anniversary of the first semester in office.

**Although this second phase begins with an encouraging CPI print and a key law approved by Congress**, it comes with many challenges on the economic front, none of which are easy. The slow reactivation of the economy is still taking baby steps and the fall in inflation in May cannot necessarily be extrapolated to the coming months. Without a new income tax and with a (hasty?) promise of a reduction in the PAIS tax on dollar purchases, fiscal consolidation is a tough battle, even though the conviction is strong. The exchange rate is another issue to be faced, although for us the solution may be less serious than it seems. In any case, we do understand the fears of floating.

**There is a philosophical consensus that FX controls have to be lifted so that Argentina begins to normalize its economy.** Timing is key because the lifting of controls concentrates a dose of positive expectations (“the day of liberation”), with some cost linked to an exchange rate adjustment. The sizes of the positive and negative effects are very difficult to think about ex ante, but we know that credibility is an input for that account. With the approved “Ley Bases”, credibility improves. Furthermore, although the results will not be immediate, we believe that if the restriction is not lifted, it will be almost impossible to attract investments. In this sense, we believe that the restriction is more important than the famous RIGI investment regime that was approved with the reform bill.

**Now, the delay between the lifting of F controls and the realization of investments may be long for the times of politics, which are by nature impatient**. That is, there are not so many quick gains now that inflation is no longer so high. All this implies that the challenges that the government will face are complex, even for prepared people, with a correct diagnosis and experience, such as the teams at the BCRA and the Ministry of Economy.

**Our view is that to the extent that the government can consolidate fiscal surpluses, the dose of credibility will be sufficient to lift the restriction, to let the currency float with costs on inflation and the level of activity that will be politically manageable.** We are not suggesting that there are no costs or that there are no risks, but our view is that it is worth paying the costs and taking the risks at some point in the next few months. Of course, we understand the view regarding the fear of floating in an environment where stability is not assured. But we believe that once the law is in effect and the various issues begin to be regulated, there will be credibility to think about the strategy of lifting FX controls, which will turn 5 years old in September.

# LAST WEEK IN REVIEW

**The "Bases" Law was approved in the Senate, with several changes involved.** The repeal of the pension moratorium was eliminated from the project, and the Proportional Retirement Benefit for those who turned 65 and did not complete the contributions. Aerolíneas Argentinas, Correo Argentino, and RTA were also excluded from the list of public companies to be privatized, and **changes were introduced in the Incentive Regime for Large Investments (RIGI):**

- The base amount for investments of US$200 million is maintained, but **the industries included were restricted**. Forestry-industry, infrastructure, mining, energy, technology, tourism, oil and gas, and steel are considered strategic sectors.
- The projects included in the RIGI assume the **commitment to allocate at least 20% of the total investment to hire national suppliers** as long as the offer is available and in good condition.
- Although the benefit will apply throughout the national territory, **it will be subject to local regulations**.
- The deadline to adhere is two years from the entry into force of the regime. However, **the Executive can extend the validity only once for up to one year.**

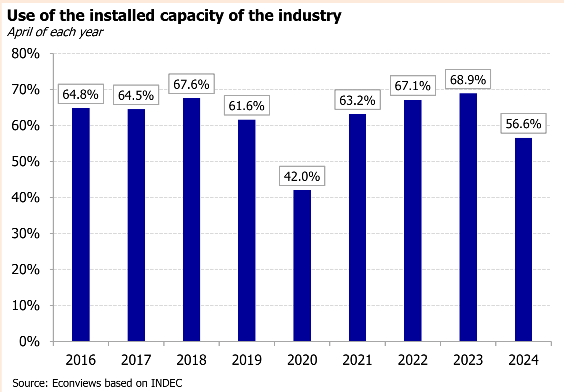
**The fiscal package was also discussed and approved, but with key rejections**:

- **Income tax**: Reestablishing the tax for employees in a dependency relationship was rejected. The project established a non-taxable minimum of AR$ 1.8 million for singles and AR$ 2,340,000 for married people with 2 children. If there are no new changes in Deputies, those who received a gross salary greater than AR$ 3,514,725 (15 minimum wages) will continue to pay.
- **Tax on Personal Property**: The increase in the floor for payment of the tax was rejected, from AR$ 27 to AR$ 100 million, and a reduction in rates ranging from 0.5% to 1.5% (today it is 1. 75%). In addition, the differences between local and foreign goods were eliminated (they pay 2.25%), and the benefits for those who pay in advance.

- **The industry's installed capacity utilization was 56.6% in April.** This figure is 3.2 p.p. higher than that of March, but still below previous years for the month of April, with the exception of the pandemic.

- **All items decreased their use compared to the same month in 2023.** The least affected were Paper and cardboard (-5.1 p.p.), Food (-4.8 p.p.) and Oil refining (-4.6 p.p.).

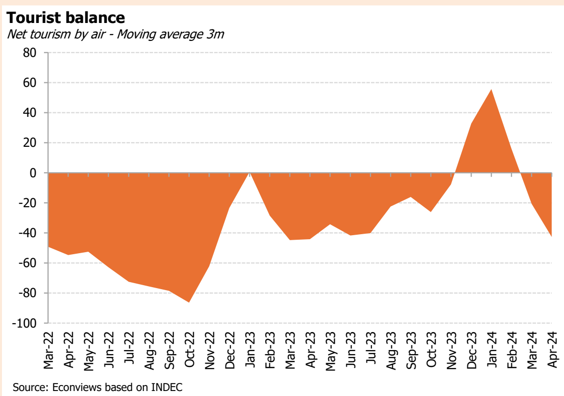
- **The item with the worst performance was Non-metallic mineral products (-29.6 p.p.).** The metal industry (basic metals, automotive, metalworking) is also greatly affected.




- In April, **foreign tourism by air rose 7% year-on-year, while outbound tourism increased 17%.** Taking all avenues, the foreign currency fell 23.4% while the emissive currency rose 33.6%.

- **The tourist balance becomes more negative**. The best time for inbound tourism was between November 2023 and January 2024, when local prices were still attractive to foreigners. Since March, outbound tourism exceeds incoming tourism.

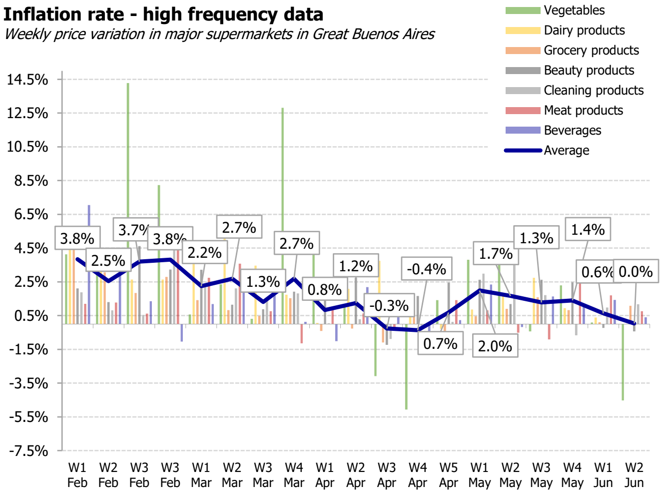
- **The destination most chosen by Argentines is Chile**. The number of Argentine tourists in Chile increased by 101.6% compared to April 2023.



# WEEKLY INFLATION

**Inflation rate - high frequency data**

*Weekly price variation in major supermarkets in Great Buenos Aires*




Note: The variations are based on the average price per week, from Friday to Thursday.
Source: Econviews based on own estimates

# NEXT WEEK'S HIGHLIGHTS

- On **Tuesday 18**, the INDEC will publish the **wholesale price data** (SIPM) and the **construction cost index** (ICC) corresponding to May 2024
- On **Tuesday 18**, the **monthly valuation of the INDEC breeding basket** for May will also be published.
- On **Wednesday 19**, the results of the **surveys of supermarkets, wholesalers and shopping malls** corresponding to May will be published.
- On **Wednesday 19**, INDEC will report the **Argentine commercial exchange** (ICA) for May.

## Market dashboard

*Weekly, monthly and yearly variations*

| | Last data | w/w | m/m | y/y | |
|---|---|---|---|---|---|
| Official exchange rate ARS/USD | 902.7 | 0.4% | 2.0% | 264.3% | ↑ |
| MEP | 1243.7 | -2.8% | 19.4% | 161.9% | ↓ |
| Blue Chip Swap | 1261.7 | -3.6% | 76.9% | 285.1% | ↓ |
| Parallel | 1260.0 | 1.2% | 20.0% | 156.6% | ↑ |
| Official exchange rate BRL/USD | 5.4 | 0.6% | 4.8% | 11.7% | ↑ |
| CB reserves (USD million) | 29,166 | -134 | +798 | -3,170 | ↓ |
| Policy rate (Leliq) | 40.0% | 0 p.p. | 0 p.p. | -57.00 p.p. | = |
| Badlar rate (private banks) | 33.6% | +0.69 p.p | -5.56 p.p. | -58.88 p.p. | ↑ |
| Private Deposits (trillion ARS) | 51.4 | -2.1% | 2.1% | 135.5% | ↓ |
| Private Loans (trillion ARS) | 24.9 | 1.2% | 15.7% | 169.1% | ↑ |
| Merval (in ARS) | 1,582 | 4.2% | 12.2% | 317.8% | ↑ |
| Merval (in USD) | 1,254 | 8.0% | -36.6% | 8.5% | ↑ |
| Country Risk (spread in %) | 1,382 | -12.6% | 11.2% | -40.8% | ↓ |
| Soybean (USD/tn) | 433.5 | 0.0% | -1.6% | -15.0% | ↑ |
| Corn (USD/tn) | 177.2 | 0.3% | -0.8% | -26.0% | ↑ |
| Wheat (USD/tn) | 225.1 | -2.4% | -6.7% | -2.8% | ↓ |
| Oil - Brent (USD/barrel) | 82.6 | 4.3% | 0.6% | 11.1% | ↑ |
| Oil - WTI (USD/barrel) | 79.4 | 3.8% | -0.3% | 16.4% | ↑ |
| LNG (USD/MMBTU) | 12.6 | 5.0% | 20.0% | 40.0% | ↑ |
| Gold (USD/oz.) | 2,332.5 | 1.7% | -1.1% | 20.0% | ↑ |

*Note: arrow depends on weekly variation*

## Stoplight for Economic Activity

*Seasonally adjusted variations*

| | | m/m | q/q | LD vs previous Q |
|---|---|---|---|---|
| Industrial production | *Apr-24* | 1.8% | -7.1% | -1.5% |
| Automobile production | *May-24* | -9.8% | -4.5% | -4.5% |
| Steel production | *Apr-24* | 44.3% | -13.0% | -0.5% |
| Poultry production | *Apr-24* | 5.2% | 1.3% | 1.1% |
| Dairy production | *Apr-24* | 9.8% | -3.5% | -0.1% |
| Beef production | *May-24* | 0.4% | -3.6% | 2.0% |
| Real Estate transactions (CABA) | *Apr-24* | 7.9% | 15.1% | 13.5% |
| Flour Production | *Apr-24* | 4.9% | -1.6% | 2.3% |
| Oil production | *Apr-24* | 0.6% | 1.9% | 0.4% |
| Gas production | *Apr-24* | 2.4% | 14.0% | 4.9% |
| Cement production | *May-24* | 14.2% | -15.9% | 11.6% |
| Construction activity | *Apr-24* | 1.7% | -22.7% | -10.3% |
| Gas sales | *Apr-24* | 0.1% | -4.0% | -1.7% |
| Motorcycle licenses | *May-24* | 0.6% | -11.0% | 13.2% |
| Use of electricity | *Apr-24* | 0.9% | -4.2% | -2.7% |
| Train rides (AMBA) | *Mar-24* | 3.2% | 0.7% | 2.7% |
| Imports CIF | *Apr-24* | -0.4% | -7.9% | -2.2% |
| Exports FOB | *Apr-24* | 1.0% | 11.4% | 2.3% |
| Loans in ARS to private sector | *Apr-24* | -1.2% | -16.6% | -2.2% |
| VAT-DGI Revenues | *May-24* | -1.6% | -1.5% | -2.0% |
| Formal private jobs (SIPA) | *Mar-24* | -0.4% | -0.5% | -0.4% |
| Formal private jobs (EIL) | *Apr-24* | -0.3% | -1.1% | -0.8% |
| Consumer confidence | *May-24* | 3.1% | 0.6% | 4.6% |
| Government confidence | *May-24* | 2.4% | -6.5% | -0.7% |

*Note: stoplight color depends on last month vs previous quarter variation*

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# May Inflation Was the Lowest in 28 Months

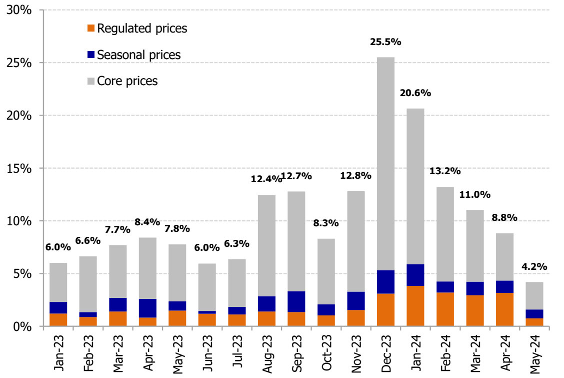
- *Electricity users in May paid only 40% of the cost against more than 60% in April. Healthcare price drops also helped.*
- *Compared to 2018, public services are 38% behind and education 30%.*
- *We think that in June inflation will return to the 6% area and it will be around 160% for all of 2024.*

**May inflation was 4.18%, once again below expectations.** This is the lowest monthly figure since January 2022. With this increase, the year-on-year inflation reached 276.4%.

**Within the categories, core inflation was 3.73%. This data is important because core inflation usually marks a trend of how inflation is going on and how it may continue.** We estimate that much of this decline has to do with what happened within the food item. Here the crawling peg at 2% helped. Although total foods rose 4.85%, most components had increases of less than 3%. In the same sense, taking the GBA prices basket published by INDEC, we see that 36% of products rose less than 2% and another 39% between 2 and 5%. That is to say, no particular item brought it down, but in general, the increases were moderate, a good sign.

**Graph 1. Monthly inflation**

*Contribution of each category*




Source: Econviews based on INDEC

**Chart 1. Utility rates helped in May**

*Contribution to monthly inflation - Own estimates at national level*

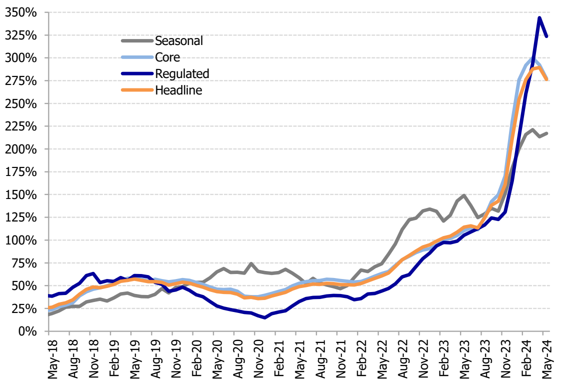
| | Dec-23 | Jan-24 | Feb-24 | Mar-24 | Apr-24 | May-24 |
|---|---|---|---|---|---|---|
| Electricity, gas y other fuels | 0.45% | 0.55% | 0.46% | 0.36% | 1.06% | 0.05% |
| Healthcare | 0.54% | 0.54% | 0.44% | 0.37% | 0.26% | -0.07% |
| Fuels and lubricants | 1.52% | 1.55% | 0.40% | 0.35% | 0.30% | 0.20% |
| Public transport | 0.64% | 0.82% | 0.31% | 0.80% | 0.33% | 0.23% |
| Communication | 0.25% | 0.42% | 0.88% | 0.31% | 0.16% | 0.18% |
| Education | 0.15% | 0.13% | 0.10% | 0.52% | 0.13% | 0.14% |
| Total | 3.55% | 4.01% | 2.59% | 2.70% | 2.24% | 0.72% |
| Headline inflation | **25.47%** | **20.61%** | **13.24%** | **11.01%** | **8.83%** | **4.18%** |

Source: Econviews based on INDEC

**In total, core inflation contributed 2.6 points to the rise in the monthly CPI (see graph 1).** Although this number implies a considerable drop compared to previous months, the novelty was in the regulated ones. This category rose 4.02%, a figure much lower than the 18 points that had risen in the previous two months. The contribution to total inflation was 0.75 percentage points, while in previous months the contribution was around 3 points. We believe that this is the key to explaining why general inflation was so low.

**Graph 2. National inflation**

*Annual variation*




Source: Econviews based on INDEC

**That the regulated prices have risen so little is the result of the utility rates freezing that had been established in May.** We estimate that electricity, gas, and other fuels had added just over one point to inflation in April, while in May the contribution was just 0.05 points (see table 1). Healthcare companies were also recovering margins in previous months but following the decision of the Ministry of Economy to roll back the increases, they had to lower their prices, and this was reflected in the index with a negative contribution. In fuel and public transportation, the contribution in May was also lower than in April. Communication and education had a marginally greater contribution.

**Our view is that this help from the regulated prices cannot last much longer.** To make the disinflation sustainable, relative prices must be correctly aligned. Taking the average for the second half of 2018 as a basis for comparison, the item containing utility rates is 38% behind the general level, although it improved compared to November. Education is 30% below headline inflation and communication 21%. Two other important prices in the economy, such as the official exchange rate and formal wages, also have lost ground against inflation (see graph 3).

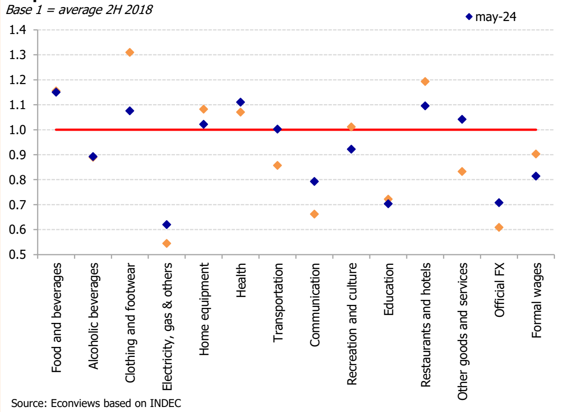
**The good thing is that by adding all categories, the difference with respect to the general price level was reduced by half between November and May.** That is to say, while there is still work to do, there has been significant progress. This issue is precisely what makes us think that inertia will not be easy to break, and that lowering inflation will be costly.

**It is still necessary to continue reducing subsidies or, in other words, raising utility rates.** This affects prices. In May, the coverage of the electricity rate was 40.3% of costs, so there is room for further increases (see graph 4). The same reasoning applies to wages, which are low in real terms and would be expected to begin to recover. The discussion about the exchange rate is long, but it is logical to assume that at some point there will be a correction, which will also add pressure on prices.

**In short, a priori it is difficult to think that inertia can be broken without generating greater imbalances than the current ones.** Our vision is that once all the inherited macro imbalances have been corrected and exchange market restrictions are lifted, a shock stabilization plan will be needed to break down expectations. For example, the Austral plan or Convertibility plan managed to lower inflation much faster (see graph 5).

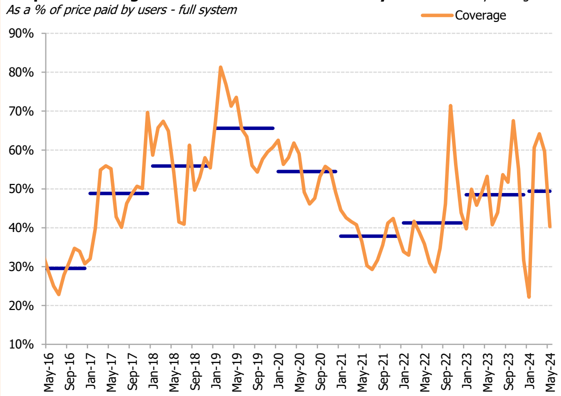
For the next few months, we think of a stabilization of inflation at around 5.5%, ending 2024 at 160%.

**Graph 3. Relative Preces**
*Base 1 = average 2H 2018*



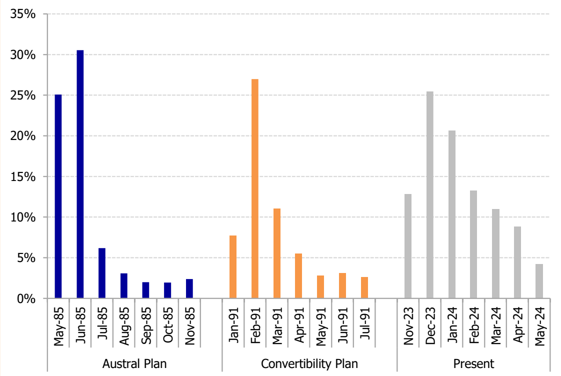

Source: Econviews based on INDEC

**Graph 4. Coverage of wholesale cost of electricity**
*As a % of price paid by users - full system*



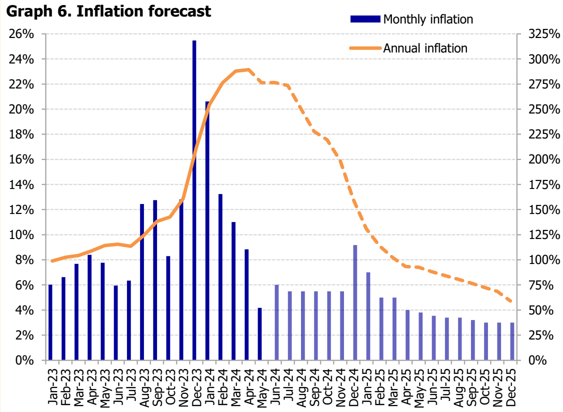

Source: Econviews based on CAMMESA

**Graph 5. Inflation after stabilization plans**
*Monthly variations*




Source: Econviews based on INDEC

**Graph 6. Inflation forecast**




Source: Econviews based on INDEC & own estimates

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# Formal Employment Suffers Due to the Stoppage of Public Works

- *105,000 formal jobs were lost between September and March and 114,000 among formal private employees, 1.8% of the total.*
- *Construction explains 66% of job loss; This crisis is more like 2016 than 2018 or 2001*
- *Real wages recovered half of what was lost but are still 10% below the September 2023 level.*

**105,000 formal jobs have been lost since September.** As of March, the bulk was among private employees (-114,000) and specifically in construction (-75,000), greatly affected by the stoppage of public works. The public sector workforce was reduced by 21,000 employees in those six months. Domestic workers, self-employed and Social programs also contracted, partially offset by 62,000 single tax-payers who registered.

**The job destruction is comparable to 2016 or 2018.** The devaluation at the end of 2015 claimed 66,000 jobs in six months. The 2018 exchange rate took away 106,000. For comparison, at the height of the pandemic, May 2020, 199,000 formal private positions had been lost and in the first half of 2002, more than 260,000.

**It is more concentrated in construction than in other crises**. The loss of 75,000 formal jobs in the sector accounts for 66% of the total. Manufacturing employment (-14,000 jobs, 13% of the total) or in commerce and transportation (-2,000 jobs, 2% of the total) are better weathering the recession.

This is different from 2018, or going further back, from 2001, when construction accounted for only 20% of the formal private job losses. It resembles 2016, when the sector's impact reached 62%. In 2001, construction costs had decreased, but that is not the case currently.

**Hysteresis**. It is a small consolation that the bulk of the layoffs are in construction, a historically pro-cyclical sector with shorter hiring periods, rather than in manufacturing industry, where reintegration tends to be more costly. In 2001 and 2018, the trend reversal in construction preceded the overall recovery of private employment, as shown in charts 3 and 4.

The difference with those crises is that this time a real exchange rate higher than the pre-devaluation rate is not being sustained. As in 2016, the rapid compression of the gap and the rise in dollar costs plays against construction. Added to this is a much tougher public works adjustment than then.

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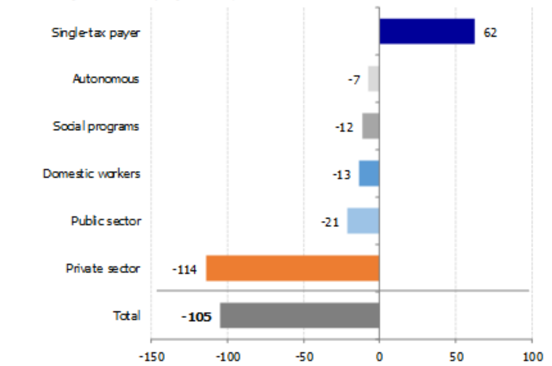
**Graph 1. Loss of formal employment**
*In thousand jobs, seasonally adjusted. Sep-23 to Mar-24*



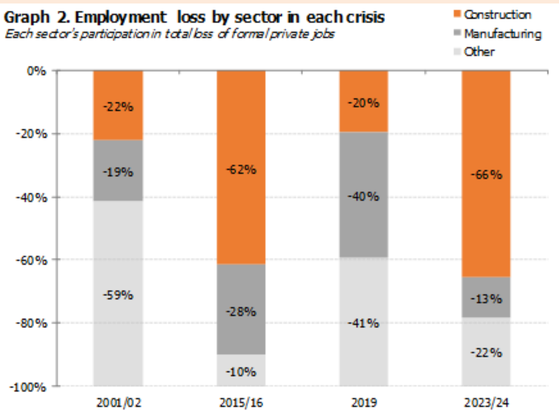

Source: Econviews based on SIPA

**Table 1. Loss of formal employment**
*Variation in thousands of positions and in %, without seasonality*

| | | Loss of employment | |
|---|---|---|---|
| | | In thousands | % of the total |
| 2001/02 | 4Q-2001/2Q-2002 | -262 | -6,9% |
| Removal of exchange controls | nov-15/apr-16 | -66 | -1,0% |
| Currency crisis | may-18/nov-18 | -106 | -1,7% |
| Pandemic | jun-20/jul-20 | -199 | -3,3% |
| **Current** | **sep-23/mar-24** | **-114** | **-1,8%** |

Source: Econviews based on SIPA and Sec. of Labor

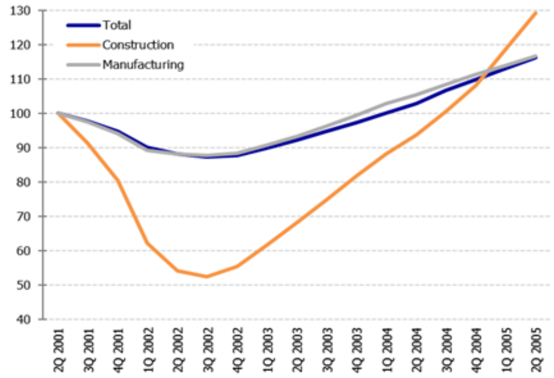
**Graph 2. Employment loss by sector in each crisis**
*Each sector's participation in total loss of formal private jobs*




Source: Econviews based on SIPA and Sec. of Labor

**Graph 3. Employment recovery in 2001/02**

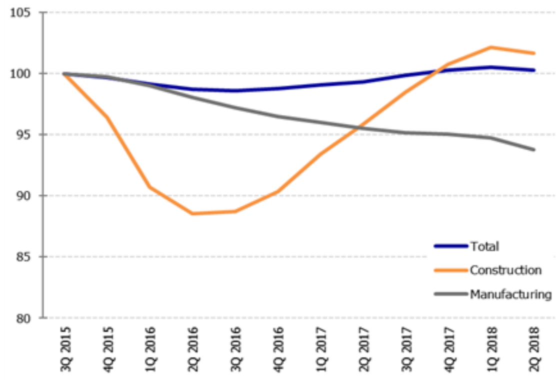
*Formal private employees, index 2Q-2001=100, without seasonality*




Source: Econviews based on Sec. of Labor

**Graph 4. Employment recovery in 2015/18**

*Formal private employees, 3Q-2015 index=100, without seasonality*




Source: Econviews based on Sec. of Labor

At Econviews we have been saying that the economic recovery will be more pipe-shaped than short V-shaped, driven by the export sectors: agriculture, mining, and oil and gas. None is intensive – short-term – employment. The anti-inflationary policy with a strong exchange rate anchor makes it likely that the employment recovery will be even slower.

**The recession hits hardest in the north.** La Rioja (-12%), Formosa (-12%), Tierra del Fuego (-8.7%), Santiago del Estero (-8.5%) and Chaco (-6.7%) lead the loss of formal private employment by province, while that the main urban centers such as Buenos Aires (-1.9%), Córdoba (-1.6%) or CABA (-0.6%) come out comparatively better. In provinces with a less developed private sector, the freeze of public works had a much greater impact.

Looking at the last decade, **Neuquén was the only province to increase private employment significantly**, with 40% more jobs than in the first quarter of 2014. Even in the last six months, it was one of the provinces with the lowest job loss, 0.2%. Vaca Muerta and other investments in mining and oil and gas are not going to change the movie of these months, but they can have a significant impact in the medium term. Salta follows at a distance (+13%), a rate not far above population growth.

Regarding informal employment, there is still no national data for the first quarter. But in the City of Buenos Aires unemployment simultaneously increased (from 6.4 to 7.5%) and the informality rate decreased (from 27.4 to 25.5%), a sign that non-registered jobs are being lost.

**At what speed are salaries recovered.** On Monday the 10th, the government celebrated the data from the RIPTE index of the Ministry of Labor, which shows that in April formal private salaries rose 16.6% against an inflation of 8.8%, a real improvement of 6.6%. At Econviews we had been anticipating that January was a floor for salaries, although it cannot be extrapolated to the RIPTE data for April. To see the evolution of purchasing power, we find it more useful to compare April's salary against May's inflation (which gives a real increase of 11%).

The RIPTE has a lower lag than the other known indices, the SIPA and the INDEC. Its disadvantage is that it only considers the remunerative components of the salary, and up to the limit defined for employer contributions. Faced with the acceleration of inflation, many unions have been negotiating non-remunerative bonuses to improve the out-of-pocket salary with less burden

**Table 2. Variation in employment by province**

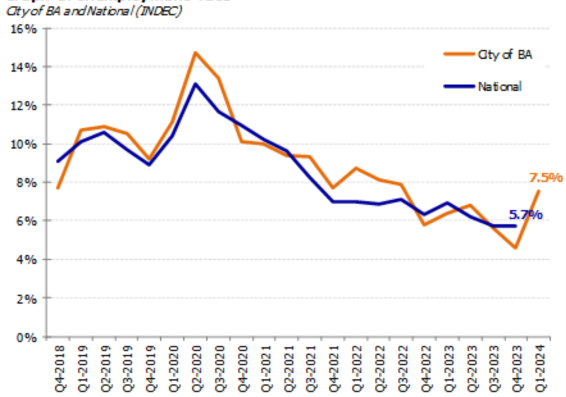
*Formal private employees, without seasonality*

| | | Last 6 months | Last 5 years | Last 10 years |
|---|---|---|---|---|
| 1 | Salta | 1,6% | 10,7% | 13,2% |
| 2 | Neuquén | -0,2% | 18,8% | 39,7% |
| 3 | Río Negro | -0,4% | 7,4% | 5,6% |
| 4 | Tucumán | -0,6% | -6,7% | 1,9% |
| 5 | CABA | -0,6% | -0,2% | 0,2% |
| 6 | Mendoza | -0,6% | 0,1% | 1,7% |
| 7 | Chubut | -1,0% | 3,0% | 1,1% |
| 8 | Entre Ríos | -1,4% | 3,7% | 2,2% |
| 9 | Córdoba | -1,6% | 4,2% | 5,4% |
| 10 | Santa Cruz | -1,7% | 5,3% | -1,3% |
| 11 | Santa Fe | -1,8% | 3,0% | 4,4% |
| 12 | Buenos Aires | -1,9% | 3,9% | 3,3% |
| 13 | Corrientes | -2,4% | 2,8% | 9,9% |
| 14 | La Pampa | -2,7% | 9,1% | 12,5% |
| 15 | Misiones | -3,6% | 1,9% | 4,2% |
| 16 | Jujuy | -4,4% | -3,4% | 4,4% |
| 17 | Catamarca | -4,9% | 29,1% | 20,1% |
| 18 | San Juan | -5,4% | -1,9% | -6,8% |
| 19 | San Luis | -5,6% | 0,5% | -7,5% |
| 20 | Chaco | -6,7% | 2,6% | 3,1% |
| 21 | Santiago del Este | -8,5% | -1,1% | 0,4% |
| 22 | Tierra del Fuego | -8,7% | 2,6% | -8,6% |
| 23 | Formosa | -11,5% | -6,2% | -15,9% |
| 24 | La Rioja | -11,9% | 4,9% | 3,7% |

Source: Econviews based on SIPA

**Graph 5. Unemployment rate**

*City of BA and National (INDEC)*




Source: Econviews based on INDEC and GCBA

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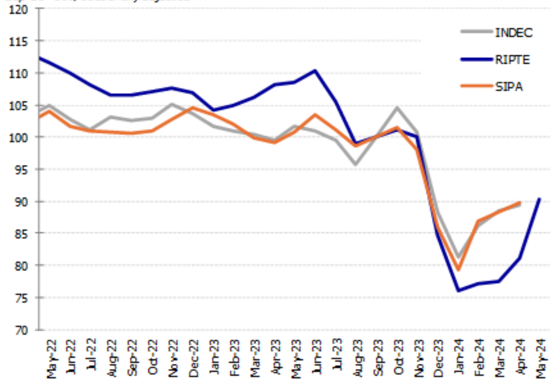
on the employer, which are incorporated into the basic salary at the close of the joint wage cycle in April.

For this reason, in April the RIPTE index did catch-up with its SIPA or INDEC peers, which do include bonds. Now, all three show that **real salaries are 10% below September 2023.** They were 20% below in January, **meaning they cut half the loss.**

**Graph 6. Real wages according to different indexes**
*Sep-23=100, seasonally adjusted*




Source: Econviews based on Sec. of Labor and INDEC