MONTHLY REPORT

ECONVIEWS
ECONOMÍA Y FINANZAS

July 2023
Issue #229

THE MONTH AT A GLANCE

RECENT DEVELOPMENTS

- On July 26th the Federal Reserve hiked its policy rate 25 bps again to 5.50%, the highest in 22 years. Markets are pricing this as the terminal rate, but with 2.4% GDP growth in Q2 and unemployment still at 3.6%, we think there could be one more hike this year.
- Argentina's monthly CPI slowed to 6% in June, helped by seasonal effects in fruits, vegetables and meat and a calmer FX market. Year-on-year inflation is running at 116%.
- The BCS heated up from ARS 497 to 551 in July and the informal dollar leapt 11% to ARS 551, widening the FX spread to 100%. The BCRA is devaluating the official rate at a 6.9% monthly pace.
- In late July, Economy applied new import taxes: 7.5% on non-essential goods and freight and 25% on services. It also extended the preferential ARS 340 exchange rate for corn and regional economies until August 31st, in a bid to build up reserves, coded as a "fiscal devaluation".
- CER (inflation-adjusted) bonds yield 10% in the secondary market, while dollar-linked bonds are paying a 6-7% premium. This means the market thinks devaluation will outpace inflation by a lot in the first months of 2024.

FIGURE OF THE MONTH

The Central Bank lost nearly

20bn

of its international reserves so far in 2023.

TO BE ALERT

With the new import taxes, only

46%

of Argentina's trade is priced at the ARS 273 official exchange rate.

WHAT'S COMING NEXT?

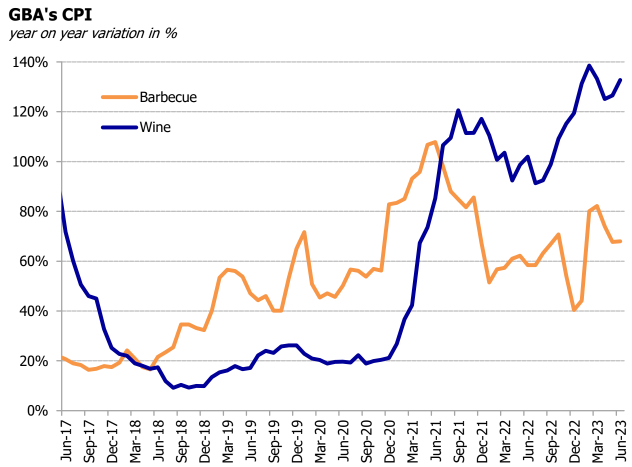
- Due to the combination of new import taxes (0.3% of GDP), the corn dollar (0.1% of GDP) and a reduction in energy subsidies and CAPEX in the second semester, we lowered our primary deficit forecast for 2023 from 3.3 to 2.4% of GDP.
- We see July's inflation around 7.2%. The "fiscal devaluation" and 11% leap in the informal dollar will push August's print closer to 7.8%. We expect inflation to stay in this range until November and December, when fears of the new administration sinking the peso could take it to 9-12% monthly. We expect 2023's yearly inflation to close around 148%.
- Primary elections will take place on August 13th. In this year's provincial elections, JxC has beat Peronist forces by 39-26, although the key Buenos Aires Province has not voted yet. Most polls have an opposition win but are split on whether Mayor of BA Rodriguez Larreta or former Minister Bullrich will take the primary, and on whether the margin will be enough to avoid a run-off in November.
- The IMF is negotiating a bridge deal for the next months. Unless it advances disbursements the Government will likely keep using CNY from the China swap to cover maturities, which amount to USD 3.5 billion in October and November. Argentina also owes July's 2.6 billion maturity, which should be paid in the next days.

SUMMARY OF MAIN INDICATORS

	Last	Previous		Last	Previous
Economic activity			**Financial data**		
Economic activity (MoM s.a.)	-0.1%	-1.8%	Inflation (monthly)	6.0%	7.8%
Consumer confidence (MoM)	4.3%	9.1%	FX spread (21day avg.)	98.8%	102.8%
Industrial activity (MoM s.a.)	-1.5%	1.1%	Country risk (bps 21day avg.)	2,033	2,419
International accounts			**External data**		
Current Account (USD BN)	-5.64	1.75	Soybean price (per ton, 21day avg.)	553.2	503.7
CB Reserves (USD BN 21day avg.)	27.31	32.52	Brazilian activity (MoM s.a.)	-2.0%	0.8%
Primary balance (ARS BN)	-611.74	-247.65	Financial Conditions Index	17.4	19.4

Source: Econviews based on multiple sources - working days only

GRAPH OF THE MONTH:



Source: Econviews based on INDEC

RECENT ECONOMIC DEVELOPMENTS

JUN 30th	JUL 7th	JUL 9th	JUL 16th	JUL 23rd	JUL 24th	JUL 28th
Econviews Monthly #228: The candidates for the 2023 elections + special report on the legacy for 2024	**Goverment postpones maturity with IMF,** extends talks with net reserves deep in negative territory.	**Key gas pipeline inaugurated**, with President Fernandez, VP Cristina Kirchner, and Minister Massa all present in sign of unity.	In primaries for governor of Santa Fe Province, **JxC and allies beat incumbent Peronists by a record 63-35.**	**IMF says it is near staff level agreement on Argentina EFF,** expects to finish defining details in the following days.	**Economy applies new import taxes**: 7.5% for goods and freight and 25% for services. Parallel dollar up 11% to 543.	**Econviews Monthly #229**

POLITICS

Two weeks away from the primaries, polls and provincial elections point towards a JxC opposition win. **Key takeaways on the eve of August 13th**: 1) who wins the JxC primary. Patricia Bullrich, read as a hawk, is the favorite in polls, but may have trouble retaining more moderate Mayor of BA Rodriguez Larreta's votes in October. 2) To avoid a run-off, the winning force needs to reach either 45% of affirmative votes or 40% and a 10-point lead. 3) Libertarian Javier Milei and dissident Peronist Schiaretti's votes could define an eventual run-off and also shape the upcoming Congress. 4) There is no run-off election in the key Province of Buenos Aires, so a one-vote margin is enough to re-elect Peronist Kicillof.

IMF

Until the last minute, the government entering into arrears with the IMF appeared like a possibility, but today the Fund announced a technical agreement between Argentina and the staff. Although board revision will take place after the August 13th primaries, this will permit the disbursement of USD 7.5 billion, enough to cover maturities until December. By then, the political scenario will be much clearer. The main obstacle to negotiations was exchange rate policy, and the executive decree raising import taxes on services, freight and some goods appears to be a halfway compromise. The IMF criticized the failure to meet reserve, fiscal and monetary targets.

ECONOMIC ACTIVITY

Activity stagnated in May (-0.1%), after falling 1.8% between March and April. In year-on-year terms the economy slumped 5.5% and accumulated a 1.3% contraction in five months of 2023. Agriculture is 44% down due to the drought, and June should be the worst month for the sector. However, manufacturing also slid 1.5% monthly in May, and construction activity fell by 2.2%. Initial data for June was sour: output kept shrinking in the cement (-3.2%) and auto (-3.9%) industries, and electricity consumption fell 1.3%. But with the worst of the drought having passed, the outlook for coming months is mixed. We corrected our GDP forecast for 2023 upwards from -3.8 to -3%, but lowered 2024 from 0 to -0.5%.

INFLATION

Surprisingly, inflation eased for the second straight month from 7.8% in May to 6% in June, well below any market forecast. Seasonal prices increased 1.8% and meat only 0.3%, helping food inflation lower from nearly 10% in April to 4.1% in June. This partly offset the 7.2% rise in regulated prices, as electricity rates in the GBA area adjusted again. Monthly core inflation was slightly higher, at 6.5%. In year-on-year terms, inflation is still running at 116%. July's CPI print should be closer to 7.2%, but the new taxes on imports and the 11% rise in the informal exchange rate will weight on August's inflation, which we see around 7.8%. We slightly lowered our full year forecast from 150 to 148%, but still see 2024's inflation at 140%.

MONETARY SECTOR

With 6% inflation in June, the Central Bank kept its policy rate at 97%. Unless there is a black swan in the primaries which destabilizes the BCS, we expect it to stay there until the new administration takes over in December. At an 8% effective per month, the current Leliq rate is slightly positive *ex ante*. Waiting for a new IMF deal, net reserves fell deeper into negative territory, from USD -5.2 billion in late June to -7.7 bn now. The new taxes may discourage imports, but the ARS 273 official rate is still around 30% overvalued, and this (plus the drought) has turned the BCRA into a net seller of USD 1.4 billion in the FX market during July. Between these sales and debt payments, it has lost almost 20 billion in reserves so far in 2023.

FISCAL ACCOUNTS

June's primary deficit stood at ARS 612 billion, accumulating 1.1% of GDP in the first half of 2023, missing the IMF target of 0.8%. After 7 months of contractions, real revenues grew 1% year-on-year helped by a 14% increase in VAT and a 0.4% recovery in export taxes, which collapsed 53% in the full semester. Other taxes liked to the level of activity like credits and debits (-2.8%) or social security (-1.4%) have lost steam. Spending fell 2.7% year-on-year, mainly due to a 10.7% fall in pensions and other social items. Economic (energy and transport) subsidies leapt 15% in June, but a large part was paying off debts with providers. With a 0.3% of GDP boost from the new import taxes, we lowered 2023's primary deficit from 3.3 to 2.4%.

I. Argentina Averted the Chasm With the IMF Agreement, Though Fragility Is Still the Name of the Game

The economic discussions have been dominated by the day-to-day developments in the negotiations between Argentina and the IMF. The other key piece of analysis is on the impact that the primaries (the PASO) might have on key variables such as the parallel exchange rate, inflation, the country risk and on overall financial stability. The latest news is that there is a technical agreement between the IMF staff and the government and is almost a certainty that the IMF Board will approve it sometime in the second half of August. This will be the last review until November.

The agreement will pave the way for the much-awaited disbursement that will provide some relief on the international reserves front, though not enough to navigate the turbulent waters that are expected till the change in government takes place in December.

The disbursement of 7.5 billion dollars will probably be used in part to repay China for that bridge loan that it gave through the currency swap to remain current with the IMF and the rest to make the September and October payments to the IMF. There is no fresh money to strengthen reserves as the government was expecting and in order to make the payment to the Fund in December Argentina will need a new agreement, which will be negotiated with the next administration.

The exchange rate policy was once again the main sticking point that delayed the agreement. However, this time the IMF highlighted that the negotiations were also delayed due to the policy slippages, mainly that none of the targets were met in the fifth and sixth reviews of the program.

The government has been vehemently opposed to any changes in the exchange rate policy, especially at this stage when the primary elections are around the corner. The IMF, on the other hand, continues to be uncomfortable with the current exchange rate regime, but decided to compromise on this issue in order to reach an agreement.

The compromise solution was to implement a "fiscal devaluation" (executive decree 377/2023) by increasing taxes on some imports, which in practice was equivalent to a devaluation of around 7.5% for some goods which looks as too little, too late. There is little hope that that these measures will improve the external situation so we should expect a further drain on reserves as well as new measures such as tightening controls or variations on the recent agro-dollars.

There was some urgency to reach an agreement because Argentina has to make large payments on July 31st and August 1st and can only be done if China activates de currency swap. It is very likely that China wanted some assurances that there would be an IMF program, especially if this was a bridge loan. At the same time the government was concerned that in the absence of an agreement there would be turmoil

Projected cash flow with the IMF
In million USD

	Disbursements	Repurchases	Charges
Jul-23		-2,659	
Aug-23	7,405		-809
Sep-23		-926	
Oct-23		-2,659	
Nov-23			-721
Dec-23	3,366	-926	
Jul-Dec 2023	10,771	-7,169	-1,531
Jan-24		-1,969	
Feb-24			-652
Mar-24	1,077		
Apr-24		-1,969	
May-24			-589
Jun-24	1,077		
Remainder of 2024	1,096	-656	-1,128
Total 2024	3,250	-4,594	-2,369

Source: Econviews based on IMF

Executive decree 377/2023

Official exchange rate + taxes (for hoarding)	**Raises income tax from 35 to 45%**, unifying with credit card exchange rate (30% PAIS + 45% income tax)
PAIS tax	
Freight	**7.5% tax rate**
Other imports of services	**25% tax rate**, exc. healthcare and education (0%) and tourism/entertainment (30% rate already in place)
Imports of goods	**7.5% tax rate**, exc. food staples, energy, drugs, fire control material, car parts and agroind. inputs (0%) and luxury goods (30% rate already in place)

Source: Econviews based on Ministry of Economy in the FX market and hence that the parallel rates could be very volatile just before the PASO, an unwelcome event.

The bottom line is that once again the IMF agreed to a very light program. Perhaps its thinking is that it is better to have a weak program and avoid a default than pushing Argentina into arrears in the midst of a Presidential election. It seems clear that it does not expect Argentina to meet the program targets, and that the relevant policy discussions will take place with the next administration.

The fact that there is an agreement is good news for the markets, as a default was averted. However, they will still keep an eye on day to day developments. The primaries (PASO), that will take place on August 13th, are likely to shed some light on the result of the general elections and hence on who could be the next president. The opinion polls are difficult to trust given the numerous wrong calls that they have been making all over the world. In Argentina, they failed to predict Pullaro's victory in Santa Fe, where they missed the results by a large margin.

The first thing to look will be whether Juntos por el Cambio (JxC) manages to strike a victory over Union por la Patria (UP) and what is the size of the margin. If JxC wins by a margin of five percentage points or more and there are signs that it could win in the general election, perhaps in the first round, would be good news for the markets. The second issue is whether the candidate is Horacio or Patricia, which probably does not mean a big difference in terms of economic policies, but it could indicate the chances of JxC winning the election in the first round. One should also look at the results in the province of Buenos Aires, and in this respect, it will be important the performance of Milei, given that in that province there is not a ballotage.

On the economic front the main question is how the economy is likely to perform during the election period and what are the risks. The agreement with the IMF has remove one of the biggest risks, a default that would have been disruptive and could threaten the transition. True, there could be volatility in the exchange rate, especially if there are unpleasant surprises in the PASO, but a very difficult scenario has been avoided.

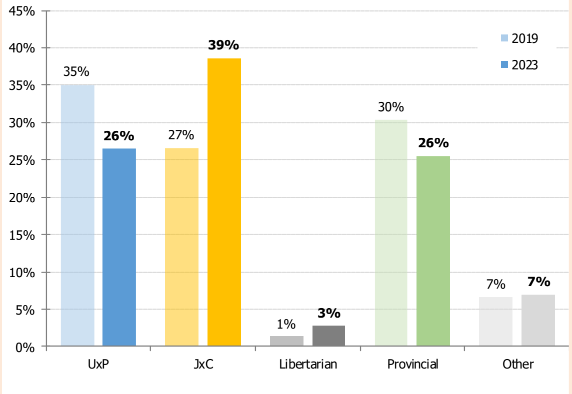
There are still risk on the reserves front, as the policy measures adopted are not enough to turnaround the situation. Net reserves will continue to be negative this year. The main risk is that the government runs out of liquid dollars to keep making the payments abroad. A longer-term solution can only be implemented by a new administration that will probably receive a Central Bank with no reserves and a large debt with China.

Inflation could be another risk, however, the 6% rate of inflation of June and the agreement with the Fund dispels the worse concerns about a situation of runaway inflation. That was seen as a distinct possibility in April when inflation reached 8.4%, but now it seems that we can expect inflation rates in the range of 7.5% in the coming months, that will rise towards the end of the year when there will be expectations that the devaluation would take place soon.

Main electoral dates

24-Jun-23	Start of primaries campaign
13-Aug-23	**Primaries elections**
2-Sep-23	Start of general elections campaign
1-Oct-23	First presidential debate
8-Oct-23	Second presidential debate
22-Oct-23	**General elections**
19-Nov-23	**Possible ballotage**

Provincial elections 2019 vs 2023
% of affirmative votes - so far 44% of the voters have voted



Net International Reserves
In billion USD

Gross reserves	**25.3**
Reserve requirements in USD	10.0
Swap (China)	18.2
SEDESA	1.8
BIS	3.0
Net reserves	**-7.7**

Source: Own estimates based on BCRA and IMF
Up to Jul-26

II. Another Legacy: The Curse of High Chronic Inflation

Inflation will be one of the biggest challenges for the next administration, as this year it is likely to end up in the range of 150%, a huge number under by any standard. This places Argentina among **the countries with the highest rates in a world at a time when price stability is the norm rather than the exception**.

Inflation is not a new problem in Argentina, as it was in three digits in the seventies and eighties, and it even suffered a hyperinflation with rates that exceeded 5,000% per annum in 1989. In those years the country implemented numerous stabilization programs, **and almost all of them ended in tears**. The main reason was that they did not address the fiscal imbalances in a decisive way while **they failed to find the appropriate nominal anchors through the combination of monetary and exchange rate policies to guide expectations**.

In those years many Latin American countries such as Brazil, Chile, and Uruguay were also facing high rates of inflation, but over the years they managed to bring them down to one digit. Furthermore, since the mid-eighties they have been able to maintain price stability. **Why has Argentina been different?**

This is a question that does not have a simple answer. On the one hand, Argentina joined the club of low inflation countries during the nineties thanks to the implementation of the convertibility plan that helped the country to enjoy price stability for a whole decade. But on the other hand, the experiment ended in one of the largest crises in Argentine history, when unemployment reached 25%, 55% of population dropped below the poverty line. It was Argentina's Great Depression.

The Kirchner administration implemented expansionary policies in an economy that was recovering quickly form the depression and in an extremely favorable international environment, circumstances that led to a revival of inflation. The population at large accepted inflation at first because they perceived that the alternative was a new increase in unemployment which appeared to be more costly. The rise of inflation between 2003 and 2011 took place while the country did not have fiscal deficits. At that time, **it was entirely the result of an expansionary monetary policy to stimulate growth**.

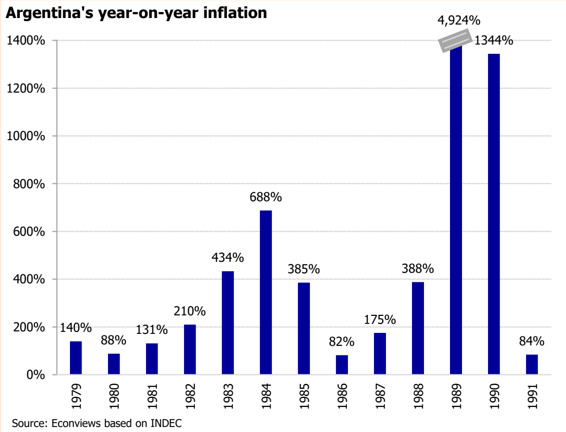
By 2011 inflation reached 20%, and the biggest problem was that the government did not make any efforts to bring it down. There were no red lights that justified a stabilization program. On the contrary, **it manipulated statistics to conceive the actual rate of inflation**. History and economic theory show that if inflation is left unchecked the most likely outcome is that it will only go up, which is precisely what has been happening since the turn of the Century.

Argentina now faces what is generally known as chronic high inflation, a process that is particularly difficult to fight and where the traditional medicines applied in developed countries are not very useful. The process is also different from hyperinflations, which typically have been

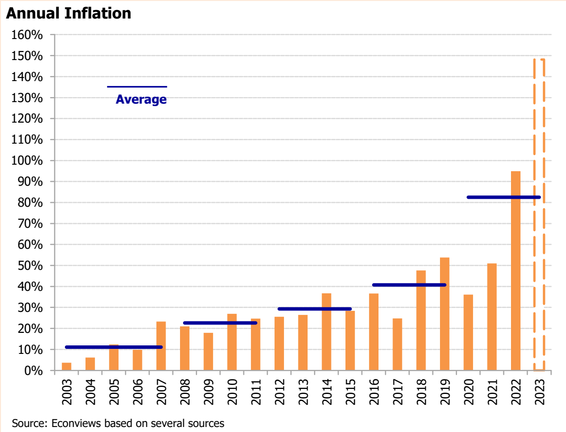
Inflation
Simple avg.

Period	Inflation rate
50-60's	26%
70's	136%
80's	750%
90-92	482%
93-2005	5.6%
2006-09	18.0%
2010-13	25.9%
2014-17	31.6%
2018-23	71.9%

Source: Econviews based on several sources

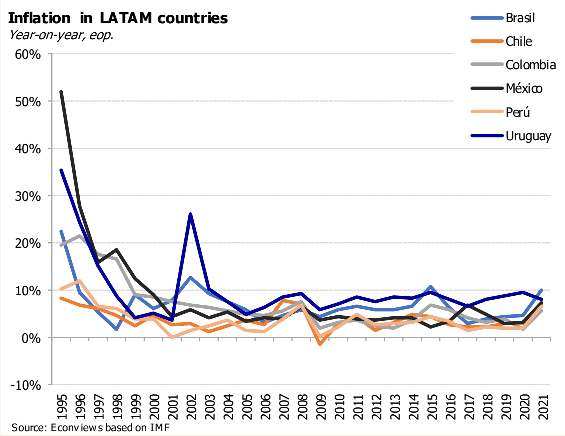


Source: Econviews based on INDEC



Source: Econviews based on several sources stopped overnight and where the traditional orthodox recipe of tight money and tight fiscal has been effective to deal with it.

The relevant experiences are countries like Chile, Brazil, Uruguay, Israel and to a lesser extent Mexico which suffered chronic high inflation. In these countries inflation displayed significant persistence. In addition, given that they had very high levels, the approach to achieve rapid reductions in inflation were very different from the traditional ones, they required a different type of medicine.

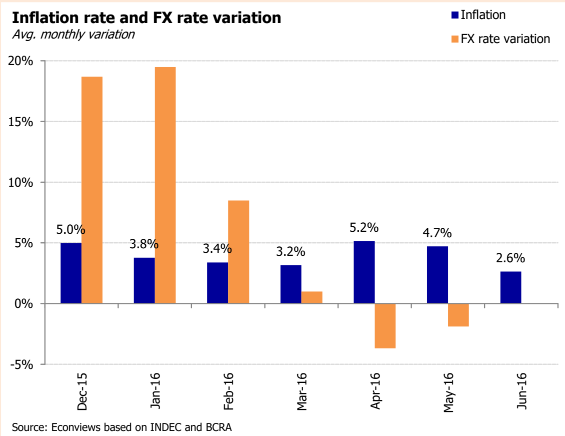


The main difference in these economies is that there is typically a high degree of inertia in the inflation process due to formal or informal indexation, which tends to generate persistence. In addition, **high inflation is more volatile** and tends to be destabilized relatively quickly by nominal shocks such as devaluations, large increases in commodity prices or utility rates mainly because adjustments in prices and wages are more frequent and hence these shocks are very quickly transmitted to inflation. A third problem is that **the inflation process in these economies is asymmetric**, it goes up very quickly in response to a negative shock, and very likely it jumps and stays one step higher, while it does not drop in response to positive shocks.

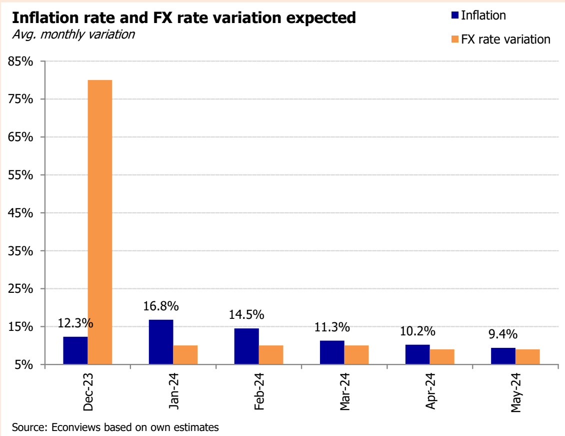
For these reasons It will be very challenging to bring down inflation in Argentina, not only because it is clearly a chronic high inflation country, but also because **it needs first to effect a devaluation and increase utility rates, two shocks that are likely to move inflation one step higher.** Of course, it also needs to implement a reduction in the fiscal deficit to **stop fiscal dominance**, namely, to end years in which monetary policy has been subordinated to the needs to finance the Treasury.

A plan to bring down inflation in two steps

1. Getting the pre-conditions for disinflation



It ain't going to be easy. The next administration will receive numerous imbalances, and many of the policy measures that are needed conspire with the efforts to bring down inflation. For instance, the required devaluation to increase international reserves will put upward pressure on prices. Likewise, the efforts to bring down the fiscal deficit, which include hikes in utility rates, will have a similar effect. **Things are going to get worse before they get better.**



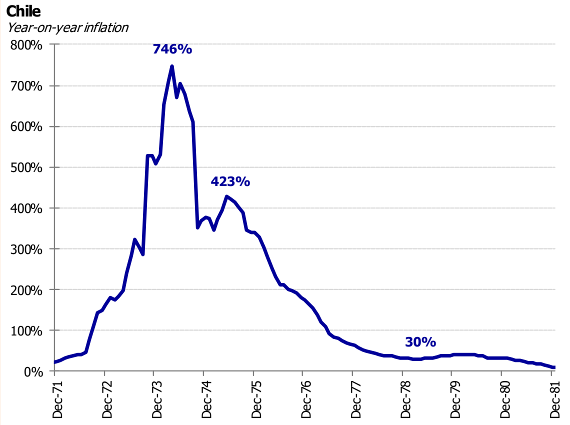
The roadmap to bring down inflation indicates that it needs to be implemented in two steps. In the first one there will be a need to realign relative prices (primarily the exchange rate, utility rates and other regulated prices) and to reduce the fiscal deficit. These represent the pre-conditions to implement a disinflation program.

The first step is risky, because the passthrough of the devaluation combined with the increases in regulated prices could lead to a doubling in the rate of inflation, as it happened following the devaluation of 2015 from 2% to 5% and stayed above the 2% trend for almost five months. If the starting monthly rate is 8% one cannot rule the possibility that it moves to 16% (or even higher) and remains in two digits for various months, an outcome that is develop in some detail in our base case scenario.

The second risk is that due to the asymmetric characteristics of high inflation and to the existence of inertia, inflation might get stuck at those higher levels through most of 2024 instead of quickly returning to the pre-devaluation rates.

2. Alternative disinflation strategies

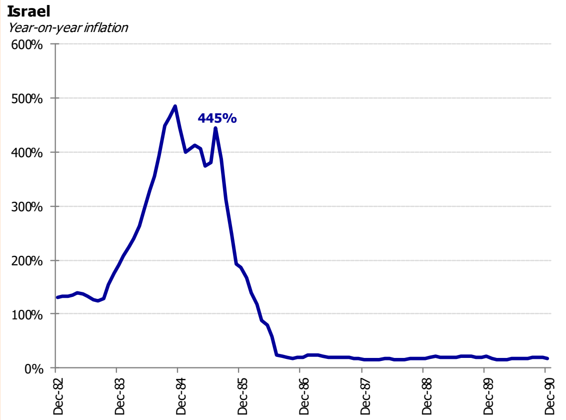
The second step in the roadmap is the disinflation program, **which will probably be implemented with an annual rate of inflation above 150%**. This scenario will open several options to bring it down. One of them is to **implement a money-based program**, of the type that have been successfully recently implemented in some Latin American countries such as Chile or Brazil and have succeeded in bringing down annual inflations to the range of 10%, the aftermath of the pandemic. **Those programs were based on tight money and high interest rates.**



Source: Econviews based on BCC

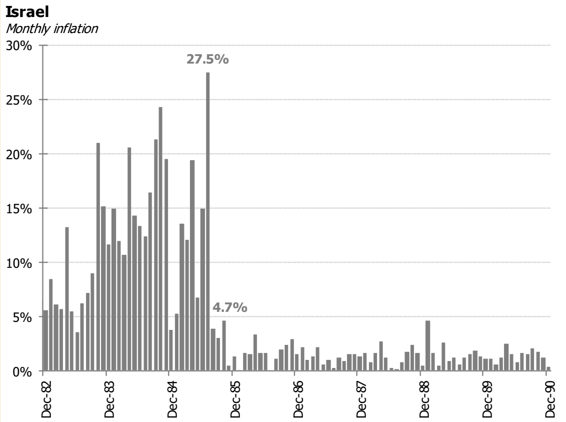
The experience with this type of programs, based on tight fiscal and monetary policies, in chronic high inflation economies has been, by and large, poor. The main problem is that **they work very slowly due to price inertia**, and hence they are difficult to maintain over long periods, mainly because it is politically difficult, especially in a country that has elections every two years. The best example of this type of program was the effort to bring down inflation in Chile under Pinochet, following the military coup that overthrew the socialist Allende government in 1973. The new government put in place one of the most orthodox programs ever implemented in the region, and yet inflation almost did not bow; it was 163% in 1972 and it was 174% in 1976, following three years of inflation of more than 350%. True, the program avoided a runaway inflation, but it clearly failed regarding its main objective, namely, to bring down inflation in a drastic manner. And this was an authoritarian dictatorship that did not have to face elections.

The message from this experience is loud and clear, **tight money can only work gradually, and in high chronic inflation countries it simply takes too much time and too much sacrifice to bring it down.**



Source: Econviews based on BOI

A second approach is the so-called **exchange rate/income policies strategy** (ER-IP), where the best example is the program implemented in **Israel in 1985**. The Israeli program was implemented in a country that had experienced many years of high inflation, which remained at over 100 since the early 1980, that peaked at 445% in 1985. How long would it have taken to bring down inflation down from 445% to single digits with a traditional program?

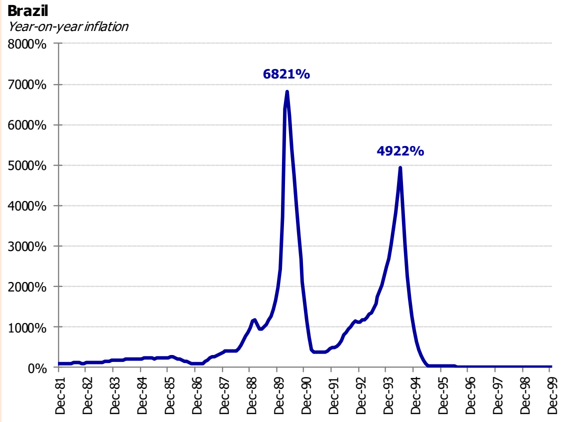


Source: Econviews based on BOI

In Israel the strategy was to implement a **shock program** plan that had an important orthodox component, mainly **a large reduction in the fiscal deficit** as well as **high interest rates** that were several points above the inflation rate. In addition, there were **structural reforms** that were critical to support the program and restart growth. The Central Bank fixed the exchange rate, which was used as the program's nominal anchor to affect inflation expectations. But unlike other plans, **it also includes unorthodox elements**, such as setting public utility rates and price and wage controls, which **served to coordinate the process of a rapid drop of rates** that were in the range of 15% per month to just 2% three months later. Price controls were not imposed in a "repressive" way, but basically functioned as a **coordinating mechanism**, which was **critical to anchor expectations**.

Argentina in 1985 implemented the Austral plan, whose design was very similar to the Israeli program and that initially was successful in bringing down inflation, in a similar way to Israel. For nine months it worked well, but eventually was abandoned mainly because **the Central Bank departed from the initial plan and of a prudent monetary stance while the fiscal accounts deteriorated rapidly**.

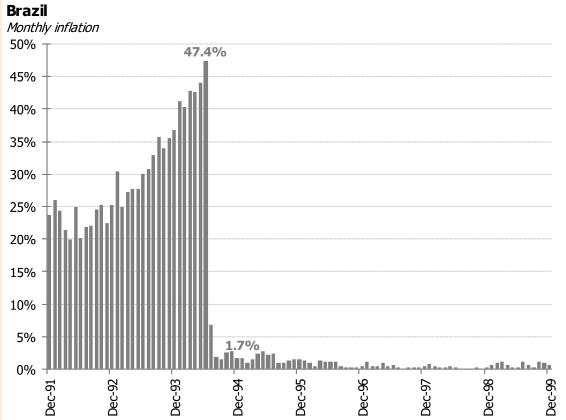
What was original and effective about in these programs is that they sought to lower inflation through a shock policy, which worked because the fixed exchange rate (reinforced by controls) **was part of a comprehensive program that forcefully attacked fiscal and monetary imbalances**.



Source: Econviews based on BCB

The **real plan, adopted in Brazil in 1994** following several programs that had ended in failure did succeed in bring inflation down from 5,000% per year to just 16% two years later. This was an original approach that finally stopped inflation on its tracks. Once again, a plan that combined orthodoxy with income policies worked to lower inflation.

The Real plan was primarily a variation of the Israeli/Austral plans that worked in two stages. First, **it introduced a stable currency that was used a unit of account and linked to the US dollar**. Prices were set in the stable currency, the real, but the means of payment continued to be the cruzado. In other words, **the two currencies were used simultaneously**, one stable and the other where inflation remained high. The interesting part of this plan was that the stable currency made it easier to track relative prices. The real worked similarly to the dollar in Argentina, where many prices are set in dollars and paid in pesos.



Source: Econviews based on BCB

The second stage of the plan was to remove the cruzados and had all prices set in reales, which had a stable relationship with the dollar. Once the real became the currency inflation stopped on its tracks.

Would this be a feasible option in Argentina? Perhaps, though one could be skeptical because the Argentine economy is much more dollarized and at first glance it seems that the dollar is the natural "stable currency".

Among the lessons of these experiences, added to others such as the Israeli plan among others, show that **fiscal balance is essential for any stabilization**, but that **the fiscal deficit itself is not a nominal anchor** and is not enough to stabilize. Second, that **the nominal anchor that has worked best in countries with high inflation is the exchange rate**, and probably in an economy as dollarized as Argentina at some point when there are reserves it will be necessary to use it. Finally, all **these countries kept their currency, did not have to resort to dollarization to curb inflation, and have managed to regain confidence in it.** The Real, the Shekel and the Chilean Peso are used to make transactions and to save even though they were once as unreliable as the Argentine peso is today.

Finally, if the previous options eventually failed, one could think in implementing a new convertibility plan, or more likely to the dollarize of the economy. These should be the last resort options, because **dollarization, while it is perhaps the strategy that has the best chances of bringing down inflation, it has several weaknesses that make the economy vulnerable**. First, it limits the ability of the government to **respond to adverse external shocks**, such as a sharp decline in commodity prices that is typically compensated through a depreciation of the currency. Second, it limits the ability of the Central Bank to **respond to a liquidity crisis**, which in today's world not only includes the banking sector but money market funds and short-term capital instruments that are used to manage liquidity. Last but not least, **in Argentina the Central Bank and the Treasury have no dollars**, which makes dollarization a theoretical option that cannot be implemented.

The bottom line is that within the two-stage stabilization strategy. The first step, which should be implemented upfront, is to **correct the main imbalances that are necessary to bring down inflation and restore growth**, where the priorities will be to achieve a fiscal primary balance and adjust relative prices, namely the exchange rate and utility rates. The second stage is to **bring down inflation**. This stage will be implemented **with a shock program that combines tight monetary and fiscal policies and realigned relative prices**, **plus specific policies to deal with price and wage inertia** along the lines of successful stabilizations that were implemented in Israel and Brazil among other countries.

Base Scenario

	2019	2020	2021	2022 E	2023 E	2024 E
Inflation (eop)	53.8%	36.1%	50.9%	94.8%	148.0%	140.0%
Exchange rate ARS/USD (eop)	59.9	84.1	102.8	177.1	664.2	1,295.3
Exchange rate ARS/USD (eop, YoY)	58.4%	40.5%	22.1%	72.4%	275.0%	95.0%
Real exchange rate ARS/USD (eop, Dec-01=100)	151.5	158.3	137.1	129.4	200.2	167.6
Paralell exchange rate ARS/USD (eop)	74.6	140.3	203.1	340.8	863.5	1,295.3
Spread with official exchange rate (eop)	24.6%	66.8%	97.7%	92.4%	30.0%	0.0%
Gross reserves (USD billion, eop)	44.8	39.4	39.7	44.9	34.0	41.5
Net international reserves (USD billion, eop)	12.6	3.8	2.3	7.7	0.0	6.0
Policy rate (eop)	55.0%	38.0%	38.0%	75.0%	120.0%	50.0%
GDP (YoY)	-2.0%	-9.9%	10.7%	5.0%	-3.0%	-0.5%
Formal wages in real terms (aop, YoY)	-6.0%	-1.9%	0.4%	0.3%	-2.5%	-2.5%
Primary result (% GDP)*	-0.2%	-6.4%	-3.3%	-2.7%	-2.9%	0.0%
Fiscal result (% GDP)*	-3.6%	-8.4%	-4.8%	-4.1%	-4.9%	-2.0%
EMBI Argentina (spread in bps, eop)	1,770	1,372	1,703	2,196	1,500	800
Public net debt (% GDP)	43.6%	52.7%	42.1%	35.2%	38.8%	44.4%
Current account (% GDP)	-0.8%	0.8%	1.4%	-0.6%	-3.1%	3.1%

Source: EconViews

*Excludes rents from primary debt issuance in 2022; PIPs below the line in 2019

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