

THE WEEK AT A GLANCE

ECONVIEWS
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Editorial: A Small Turn Towards Orthodoxy...but with a Twist

The minister of Economy, Martin Guzmán, announced this morning that he has no intention of asking the Central Bank for more help for the rest of 2020. He will turn to the market to get the money to finance capital and interest maturities and up to 10% more. If he were to get more money, he would reduce the debt with the CB. This is good news and indicates that Guzman's agenda is slowly making its way through with an administration that has had an erratic monetary and fiscal policy so far. This is a small turn towards orthodoxy but burdened by Guzman's pace, which is much slower than what the market would like.

Everything that glitters is not gold. If one were to take the Ministry's announcement at face value, one could assume that there would be virtually no primary deficit in the last two months of the year. No matter how much the accounts might improve, this is technically not possible, especially since in December there is usually a deficit worth at least 1 point of GDP, which is mostly non-deferrable since it is for bonuses for retirees, workers and almost always some kind of bonus for social program beneficiaries. It might be possible to defer subsidy payments or some item of capital expenditure, but that is about it.

The circle is then closed with a probable profits transfer. The wording of the statement does not exclude this practice, which, although different in accounting terms, is equivalent from a monetary standpoint. Profits transferred from the CB arise from nominal devaluation and are not based on cash flow but on the revaluation of assets and therefore money has to be printed to make this transfer. In other words, the economy's surplus of pesos will not be cleaned up this year.

Our primary deficit estimate for the last two months is at least 360 billion pesos. That is to say, that the minimum issuance for profit transfers is 300 billion. Guzman's move has a legal tinge: the CB had little margin left to increase loans to the Treasury, but it has plenty of room to transfer profits due to the securities revaluation in the last balance sheet.

The certainty that the local market will refinance principal, interest and perhaps a bit more, entails an implicit rise in interest rates. The last auction was with rates lower than the market ones and the only interested parties were public sector agencies. At the very least, the Treasury will have to come out with market rates. The question is if there will be coordination and whether the CB will follow. This would be reasonable since inflation in October will have had a new rise and November and December are likely to follow the trend. Increases in health insurance have already been authorized and the market is getting ready for hikes in public services tariffs, in addition to the shortages resulting from restrictions on imports. If they announce positive rates in pesos, even though there is no uniform criterion to calculate them, the policy rate would not be meeting the criterion.

Will this set of policies quench the dollar frenzy? It is difficult to know, but it seems that the Government now understands more clearly that it needs to hasten a deal with the Fund. If the market begins to see it as the high-stakes scenario, it is most likely that we will not see out-of-control spreads again. **For the "exchange calm" to continue, two important things must happen. The first is the Central Bank stop losing reserves. The second is politics stop sending contradictory messages. None of the them are guaranteed.**

What's coming up this week...

- ✓ On **Wednesday 4th**, ADEFA will report **vehicle production, sales, and export** data for October.
- ✓ **During the week**, October's **retail sales and cement production** will also be reported.
- ✓ On **Thursday 5th**, September's **industry and construction data** will be released.
- ✓ On **Thursday 5th**, the CB will release October's **market expectations survey** (REM in Spanish).

Stoplight for Economic Activity

Seasonally adjusted variations

		m/m	q/q	Last data vs previous quarter	
Industrial production - INDEC	Aug-20	-0.9%	25.8%	7.1%	●
Automobile production - ADEFA	Sep-20	32.6%	248.8%	39.7%	●
Steel production- Chamber of steel	Sep-20	8.8%	72.1%	15.1%	●
Poultry production - Min. of Agriculture	Sep-20	15.5%	-2.3%	10.9%	●
Dairy production - Min. of Agriculture	Sep-20	-2.2%	-1.8%	-3.5%	●
Beef production - Min. of Agriculture	Sep-20	6.2%	-1.3%	1.4%	●
Real Estate transactions City of BA	Aug-20	162.3%	67.0%	61.2%	●
Flour Production - Min. Of Economy	Sep-20	2.2%	0.3%	-2.0%	●
Oil production - Min. of Production	Sep-20	-0.9%	0.9%	-2.1%	●
Gas production - Min. of Production	Sep-20	6.1%	1.9%	5.0%	●
Cement production - AFCEP	Sep-20	16.2%	32.8%	15.0%	●
Construction activity - INDEC	Aug-20	-1.0%	83.7%	12.8%	●
Retail sales - CAME	Oct-20	-2.1%	24.2%	5.4%	●
Gas sales - Min. of Economy	Aug-20	0.8%	24.8%	8.9%	●
Motorcycle licenses - ACARA	Oct-20	-4.0%	13.5%	4.1%	●
Use of electricity - CAMMESA	Sep-20	1.8%	24.3%	4.3%	●
Subway rides - City of Buenos Aires	Sep-20	35.0%	-4.9%	-8.8%	●
Imports CIF - INDEC	Sep-20	22.7%	12.3%	26.4%	●
Exports FOB - INDEC	Sep-20	-4.7%	3.0%	-2.0%	●
Loans in ARS to private sector (real) - BCRA	Sep-20	0.8%	5.6%	2.6%	●
VAT-DGI Revenues - AFIP	Oct-20	4.4%	11.4%	8.8%	●
Formal private jobs - SIPA	Aug-20	0.0%	-1.2%	-0.3%	●
Formal private jobs - Min. of Labor	Sep-20	-0.2%	-0.3%	-0.2%	●
Consumer confidence - UTDT	Oct-20	-3.7%	3.8%	-2.8%	●
Government confidence - UTDT	Oct-20	-12.1%	-20.0%	-16.9%	●

Note: stoplight color depends on last data vs previous quarter

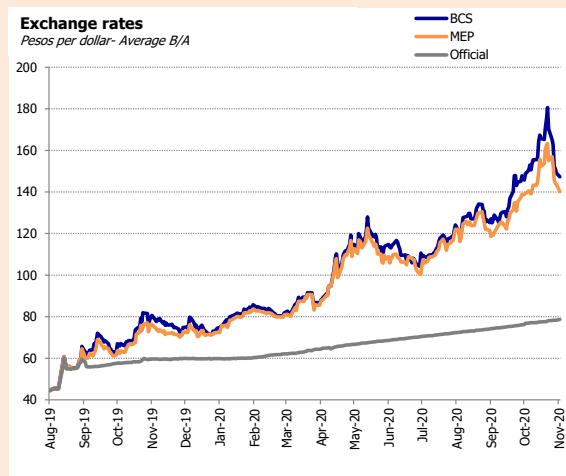
Lower Spread... but at What Cost?

- The FX spread, which had peaked at 132%, closed at 87.2% yesterday, with the blue chip swap at ARS 147.41
- The new dollar-linked bond issued last Tuesday raised ARS 129.8 billion, and the CER bond maturing in December raised another ARS 66.5 billion
- The Government announced that it will not request assistance from the CB as temporary advances for the rest of the year; should it manage to obtain net financing for 110% of maturities in the market, it will still have to get ARS 300 billion
- Time deposits of the private sector continue to decline and contracted 4.4% in the last 30 rolling days

The Government finally got the spread under 100%. But last week was far from calm on foreign exchange issues. The Central Bank continued to sell reserves in the official exchange market, it continued to intervene in the futures market and, jointly with ANSES, sold bonds to provide liquidity to the blue-chip swap once again. Import restrictions remained firm and there were rumors of controls and "friendly bidders" in the informal market that will help lower the price of the informal dollar. Last Tuesday's auction brought some financial respite but at the high cost of issuing debt indexed to the evolution of the exchange rate and inflation.

The official exchange rate scarcely grew 30 cents last week, closing at ARS 78.33 on Friday. Yesterday the Central Bank sped up the daily depreciation rate to 0.46% and closed at ARS 78.69 for wholesale. In turn, **the public sector continued to sell bonds to intervene in the blue chip swap, which also benefited from the lower pressure achieved by the dollar-linked auction on Tuesday, falling over 21 pesos in the week.** Yesterday the blue chip swap dollar lost another ARS 2.5 compared to Friday, to ARS 147.41 ask. This way, **the spread with the official dollar, which had reached a maximum of 132%, was reduced to 87.2%.** Meanwhile, **the MEP dollar closed yesterday at ARS 140 (78.1% spread) and the informal one at ARS 166 (111% spread).**

As expected, the dollar-linked bond and the CER-adjusted bill maturing at the end of the year, turned out to be the most attractive instruments for the private sector in last Tuesday's auction and relieved pressure on the financial dollar markets. In search of coverage due to the current uncertainty, they amounted to ARS 129.8 and ARS 66.5 billion, respectively. Although it helped to decompress some of the upcoming maturities, the auction increased the Treasury's risk by indexing much of the debt. **The Rofex futures market is validating an average implicit rate of 80%, while the TX21 and T2v1 bonds are reflecting an expected break-even devaluation of 70% and an annualized inflation of 54% as compared to the 2021 fixed rate.**



Auction of peso-nominated titles, Oct 27th

Instrument and amount issued, in million ARS

	Type of instrument	Amount issued	Interest rate	Maturity date
X04D0	Tied to CER	66,559	CER + 1%	4-Dec-20
S30D0	Fixed-rate	48,473	35.0%	30-Dec-20
T2X1	Tied to CER	8,827	CER + 1.5%	17-Apr-21
TB21	Badlar	1,009	36.1%	5-Aug-21
DOLLAR-LINKED 2022	Tied to FX rate	129,804	Devaluation + 0.1%	29-Apr-22
Total:		254,672	-	-

Source: Econviews based on Ministry of Economy

In this scenario, and in order to send signals of monetary and fiscal consistency, **yesterday the Treasury announced that it will not be asking the CB for assistance via temporary advances for the rest of the year.** It is committed to renewing all principal and interest maturities and obtaining net market financing of up to 10%. Moreover, with part of the funding obtained in Tuesday's auction, it returned another ARS 100 billion in temporary advances to the Central Bank. We estimate that around ARS 480 billion in maturities of principal and interest remain to be financed in pesos with the private sector in the next two months, while the primary deficit will add up to an additional ARS 350 billion. In other words, if the Treasury succeeds in its task, **it will still have to finance around ARS 300 billion with the private sector, which will probably be covered by transfers from the Central Bank's remaining profits, which amount to ARS 400 billion.**

As a counterpart to this greater appetite for bonds tied to the exchange rate and the CER, **private sector time deposits contracted by 4.4% in the last 30 days** (data up to the 27th). With the Badlar and TM20 rates above 31.5%, additionally, with a leliqs rate of 36% and repos of 31% and 34.5% depending on their duration, the profitability for banks taking time deposits is very low.

The government has been taking steps in the right direction, although somewhat untimely. Tuesday's good auction and the announcement regarding the Central Bank's assistance should help moderate the issuance of pesos in a context where demand remains anemic. But the problem is that **the Treasury is not rebuilding the curve in pesos but is creating a new "indexed curve" that the market is validating at high rates. The benefits are great, but so are the risks.**

The FX Market Reflected the Increased Restrictions and Growing Spread in September

- *Cash-based exports were again below those accrued for the eighth consecutive month; in contrast, the amount actually paid for imports was higher than the accrued one*

- *Export collections fell again compared to a year ago (-14.3%) while import payments increased 51.4% spurred by the FX spread; in September, the balance of the goods account was almost nil, with a net income of USD 7 million*

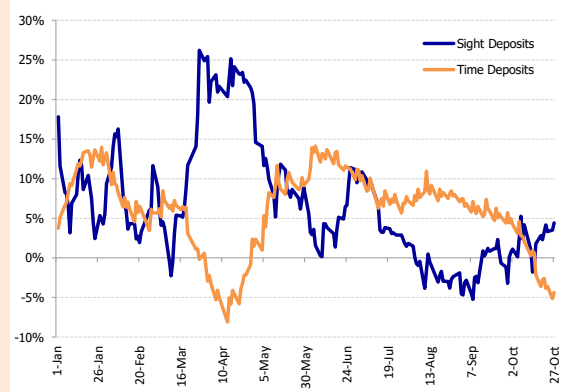
- *Even without foreign tourism, the services balance continues to increase its deficit: USD 278 million that mainly came from card operations and remote payments to foreign suppliers*

Financial gap in ARS with the private sector
In billion ARS

	November	December	Total
Primary deficit	92.6	264.7	357.3
Capital maturities	203.8	229.0	432.7
Interests	20.3	20.8	41.1
Total	316.7	514.5	831.2

Note: excludes dollar debt with International Organisms and intra-public sector debt

Private sector deposits
Var. %, last 30 days



FX balance - Central Bank
In million of USD

	Sep-19	Sep-20	YTD 19	YTD 20
Current account (1)	1,422	-601	4,867	751
Goods	2,248	7	17,738	7,071
Services	-224	-278	-4,439	-920
Interests and dividends	-627	-334	-8,544	-5,468
Transfers	25	5	112	69
Capital account (2)	-47	5	73	69
Financial account (3)	-6,659	-952	-26,315	-5,737
FDI (non-residents)	96	60	2,085	854
Portfolio investment (non-residents)	3	3	-4,522	38
Financial loans, bonds and credit lines	-1,416	-566	-4,336	-5,734
Operations with the IMF	0	0	16,226	0
Loans from Int. Organizations and others	-70	-196	-1,143	61
Swaps for transfers with the rest of the world	1,048	-133	4,939	325
Private sector's net purchase of ext. assets	-3,013	-434	-22,754	-2,831
Financial sector's net purchase of ext. assets	501	246	935	1,017
Pub. sector's net purchase of external assets	66	8	1,837	-77
Securities	-20	0	-8,845	-6
Other operations of the nat. pub. sector (net)	-957	-89	-9,703	-245
Others	-2,896	149	-1,033	860
Non-reported by clients (net) (4)	1	0	4,732	0
Var. of int. res. (5) = (1) + (2) + (3) + (4)	-5,283	-1,548	-16,642	-4,917

Source: MULC - BCRA

- Due to greater restrictions and a whole week without operations, dollar purchases totaled USD 643 million and halted its monthly growth after half a year, with 600,000 fewer buyers than in August

- It was another month of record reserve sales for the CB; foreign exchange intervention amounted to USD 1.6 billion, most of it in the first fortnight, while gross international reserves fell by USD 1.4 billion ending the month at USD 41.7 billion

The FX market once again echoed the greater restrictions to dollar purchases and the widening of the exchange spread. These two major distortions boosted both under-accounting of exports as well as over-accounting of imports, as part of the rush to dollarize portfolios and access the official dollar in any possible way.

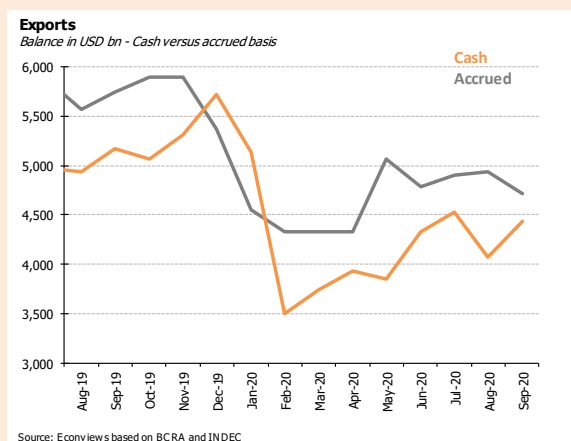
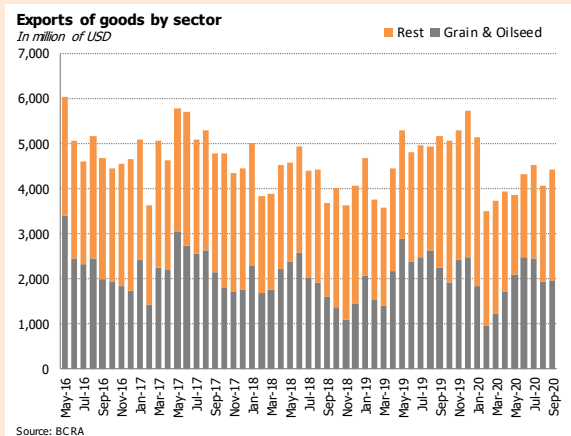
On the commercial trade side, **export collections amounted to USD 4.4 billion in September**, a figure that means a **14.3% yearly contraction**. With the harvest months passed, **exports of oilseeds and cereals contributed USD 1.9 billion**. With a spread between the official and parallel exchange rate around 80%, and off-the-chart devaluation expectations, many exporters were tempted to postpone their dollar sales at the official rate, this contributed to a **12.6% lower balance than a year ago**.

During the month, **USD 4.4 billion were paid in imports**, the highest record since January 2018 and way over the 2020 average of around 3 billion. As **devaluation expectations encouraged advancing cash payments, imports according to the FX market (cash basis) again exceeded the balance recorded by customs (accrual basis) in the INDEC's Trade Exchange Report (ICA)**, this time by almost USD 300 million. Thus, payments **grew a whopping 51.4% compared to September 2019**.

Thus, payments for imports practically equaled collections from exports and **the goods balance in dollars was scarcely positive, by USD 7 million**. Even though the balance remains favorable, it is the lowest record since March 2018, when the goods account recorded its last deficit.

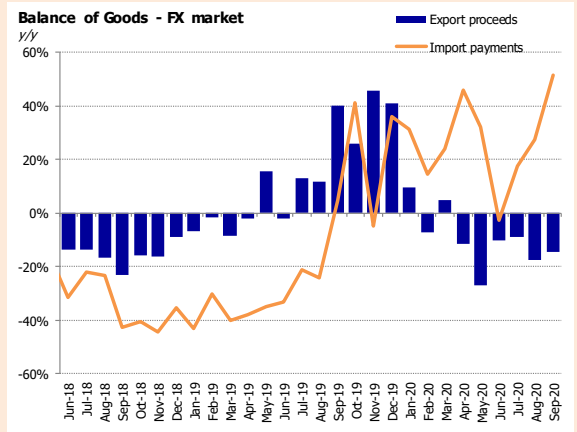
The deficit in the **services balance** continues to grow, with **USD 278 million net outflows in September**. With almost no tourism movement, the greatest foreign exchange pressure came from card operations, such as remote purchases from foreign suppliers, together with freight payments, while the greatest inflow was through the "Business, professional and technical services" category. **The USD 326 million that outflowed as interest** mainly corresponded to the private sector, although **the Government made payments to international organizations for USD 90 million**.

The financial account deficit totaled USD 952 million, mainly due to the net cancellation of 511 million in non-financial private sector debts. In the 13 months since the implementation of FX controls, businesses have cancelled debts for 10 billion dollars in net terms. The foreign exchange outflow in foreign asset formation was USD 434 million, slightly less than that recorded



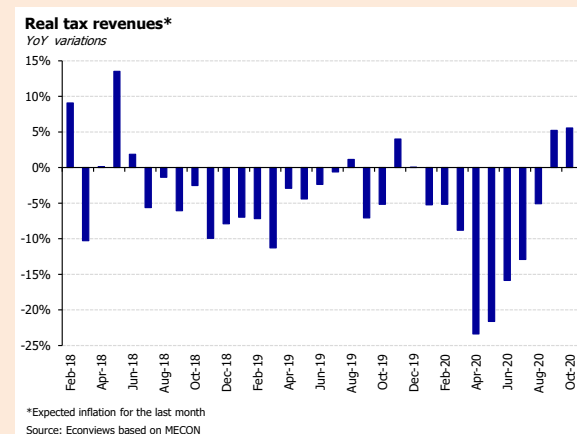
in August. With greater restrictions and with the operation stopped for a week after the implementation of harsher restrictions in mid-September, **the purchase of dollars was reduced to USD 643 million**, against USD 750 million in August. With around 3,400,000 buyers in September (600,000 less than in August), after half a year the demand for dollars fell compared to the previous month. We expect these sales to continue falling in October, with even greater restrictions.

On the other hand, the **CB's gross international reserves fell USD 1.4 billion and closed September at USD 41.7 billion**. Throughout the month, the monetary entity intervened in the exchange market with net sales of USD 1.6 billion, most of them in the first fifteen days.



Revenues Grew in Real Terms for the Second Month in a Row

- *Taxes linked to activity are still 7 points below last year, but they improved compared to previous months in seasonally adjusted terms*
- *Personal assets and Income Tax were the stars of the show this month, greatly due to increases in rates or low comparison levels*
- *Foreign trade is losing weight, given that the farming sector paid export taxes in advance and restrictions on imports seem to have played a key role in revenues. The PAIS Tax fell to less than half of previous months*



October's revenues grew 43.9% y/y, a 5.6% increase in real terms, considering a 3.2% inflation in October. It was the second real rise in a row after 12 months without any improvement.

Taxes linked to economic activity still showed significant y/y falls as expected, but they improved compared to previous months. For example, VAT-DGI fell 7.4% in real terms (its lowest fall since last November), but increased for the fourth month in a row in seasonally adjusted terms. Something similar happened with the tax on Credits and Debits: it fell 7.8% net of inflation compared to October 2019, but it grew 5.6% compared to September in seasonally adjusted terms.

The tax that grew the most was personal assets due to its rate going up and the number of allowed deductions going down, which allowed it to six-fold its revenues. Income Tax jumped 76%. Here, the comparison basis was lower because the previous administration had reduced Income Tax after the primaries. They also started to collect taxes on spending in dollars and

Tax revenues
Up to October 2020 - Central Government

	In BN AR\$ up to Oct-20	YoY	
		Oct-20	Oct-19
Total	642.10	43.9%	42.8%
Income	140.67	76.0%	25.4%
VAT	188.02	28.6%	32.0%
VAT DGI*	123.23	26.4%	31.9%
VAT DGA	68.52	28.9%	35.1%
Credits and debits	38.88	592.3%	335.4%
Personal assets	8.53	-	-
P.A.I.S.	125.71	32.4%	27.3%
Social security	125.71	32.4%	27.3%
Exports tax	39.47	1.8%	176.1%
Imports tax	20.71	7.6%	66.2%
Others	37.37	-	-

*Gross of refunds
Source: EconViews based on MECON

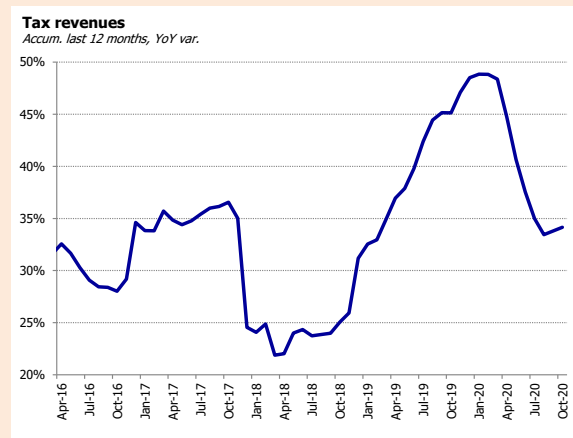
purchases of dollars for savings. Thus, this rise is quite unrelated to the activity level.

Taxes levying foreign trade grew way below inflation or the dollar rate. Exports taxes went up 1.8% because the farming sector made payments in advance by the end of 2019 to beat the increase in rates. As for imports taxes, their 7.6% rise is probably the reflection of the restrictions. The nominal growth had been higher in August and September.

Contributions and taxes linked to social security fell slightly in real terms (-3% y/y), which is logical with wages falling more than that, but with less deductions than last year. The tax on fuels also had a worse performance, something that was already on paper since gas sales are around 30% than last year.

The PAIS tax was a victim of its own success. After ending savings dollar purchases for most individuals, its revenues went from over 20 billion in previous months to 8.7 billion. This tax is not distributed to provinces, making it a big loss for the Treasury.

The big winners in October were the provinces. According to the Chart by the Ministry of Economy, the part of revenues assigned to them increased 58.1%, while the Federal Government will take about 35% more considering the money destined to the Treasury and ANSES jointly.



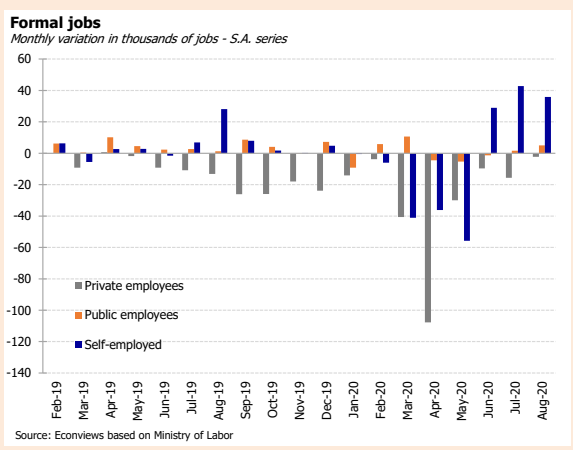
No Signs of Recovery in Wage Employment

- *Wage employment in the private sector was stagnant in August compared to July; it is still 3.2% below February's level, before the pandemic. In y/y terms, the fall is 5.0%*

- *Independent work kept recovering after the slumps in March, April, and May: "Monotributistas" (single-system taxpayers) were the most "dynamic" by far, growing 2.1% monthly, which meant about 33,900 new jobs*

- *Thus, total formal employment increased 0.3% monthly in seasonally adjusted terms, 33,500 new jobs with 90% of them coming from newly registered Monotributistas. 1,300 private employees lost their jobs, making it the 28th consecutive month in decline*

- *In August, real wages fell 0.1% monthly and were 4.9% below August 2019. In September, the union-negotiated wage –nominal– grew 36% y/y, slightly below inflation (36.6%)*



The budding recovery of economic activity after April's historic collapse has not yet impacted formal wage employment. Despite EMAE –seasonally adjusted series– recording continuous increases since May (although without being able to attain its pre-pandemic levels), April 2018 was the last time the private sector saw a significant monthly increase in its formal jobs.

The prohibition to lay employees off together with the doubled severance payments did not obtain the expected results after the quarantine was imposed, which paralyzed activities in a large portion of the economy. **Over 200,000 wage jobs were lost in the private sector** (seasonally adjusted). However, the good news is that August was the first month of the year with a minimum fall: compared to July, 2,305 less jobs were recorded (-0.04% m/m), counting domestic employees. If we exclude them, the fall represented 1,300 jobs. In April, the collapse had totaled over 100,000 jobs (and this figure rises if not seasonally adjusted). In y/y terms, the fall amounts to 4.9%.

At a sectoral level, the performance of private wage employment was heterogeneous in the monthly comparison (seasonally adjusted). Out of the 14 branches economic activity is split in, only 5 of them scored positive variations compared to July. The best performance was shown by the “Real Estate, Business, and Rental” sector which scored over 6,000 new jobs (0.8% m/m). Trailing behind came industry (+1,540 jobs, 0.1% m/m) and construction (+946 jobs, 0.3% m/m). The Labor Indicators Survey (EIL in Spanish), carried out in the main urban areas, forecasts another increase of formal employment in the latter for September.

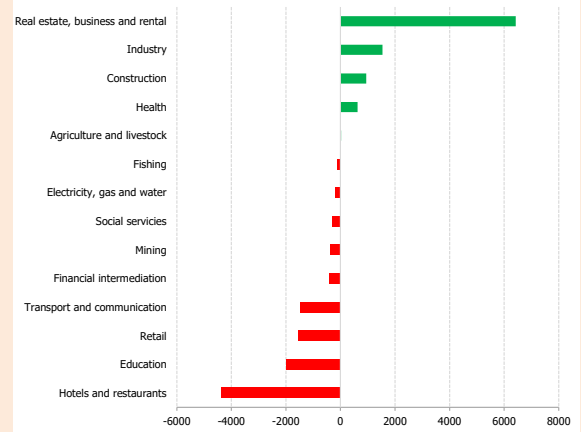
Conversely, employment in hotels and restaurants keeps falling and around 4,400 more jobs were lost in August (-1.9% m/m). The sector is the most struck by the lockdown: in August, economic activity contracted 56% compared to one year ago. The reopening of bars and restaurants in the City of Buenos Aires will help decrease the fall, but with numerous establishments permanently closed, the recovery will probably take years. As for the education sector, about 2,007 formal jobs were lost here (-0.5% m/m), while commercial activity, despite the gradual reopening of the economy, lost another 1,574 jobs (-0.1% m/m).

At a provincial level, the performance of wage employment was also varied in August. In relative terms, the province with the best performance was Jujuy, with a 2.8% monthly increase (+1,519 new jobs), followed by Santa Cruz (1.3% m/m), and Corrientes (0.8% m/m). Conversely, the greatest monthly falls were recorded in La Rioja (-1.8%), Misiones (-1.5%), and Tucumán (-1.1%). Despite this drop, Tucumán is the only province apart from Misiones where formal employment is over its pre-pandemic levels (7.4% over February's record).

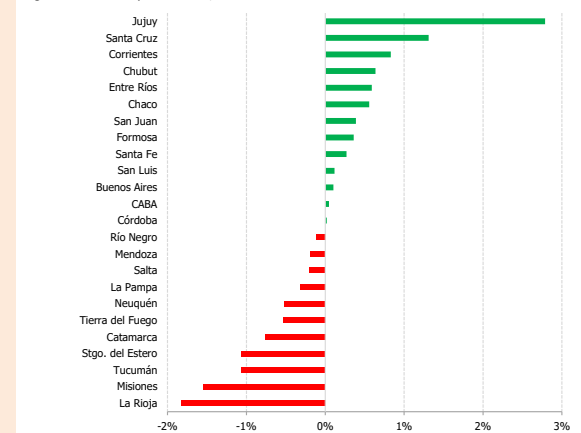
For September, EIL's data anticipate a 0.2% m/m drop nationwide (own seasonal adjustment). However, while the fall amounts to 0.5% in the Greater Buenos Aires, a 0.3% rise took place in the interior of the country.

The performance of independent work was very different from wage employment. In August, it managed to grow for the third month in a row (1.5% m/m, seasonally adjusted). The rise was led by *monotributistas*: about

Private wage employees by economic sector
August 2020 - Monthly variation, s.a.

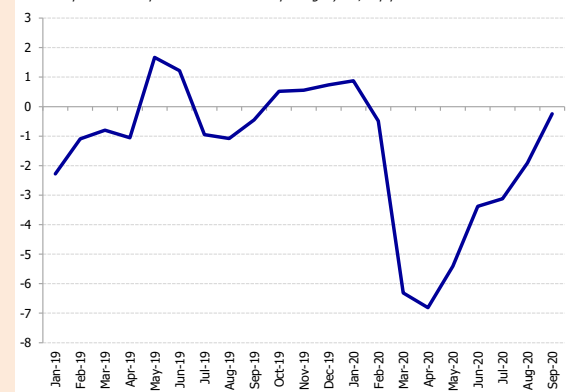


Private wage employees per province
August 2020 - Monthly % variation, s.a.



Expectations of the private sector

% of companies that expect to hire minus % expecting layoffs, in p.p.

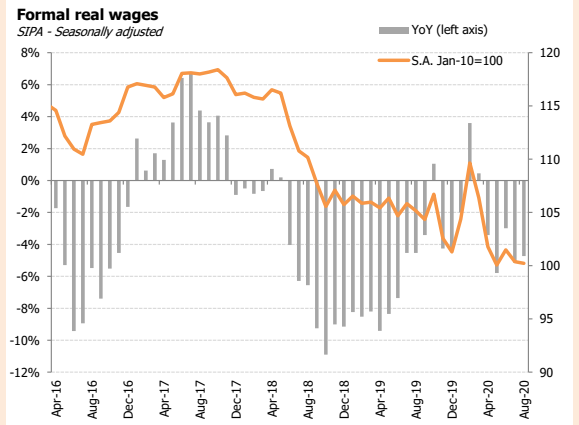


33,900 new people registered under this regime, which meant a 2.1% monthly increase. However, independent work is still 1.5% below February levels, although only 0.7% less than a year ago. **Public employment is the only one managed to stay at its pre-pandemic levels.** With a monthly increase worth 5,014 jobs in August alone (+0.2%), the total number of public wage earners was 0.19% over February and 0.7% over August 2019.

This way, total formal employment went up 0.3%, which meant that 38,500 jobs were created: about 90% of this increase came from *monotributistas*. In y/y terms, the fall equals 2.6%.

As for wages, they fell again in real terms in August, 0.1% compared to July (seasonally adjusted series) and 4.7% compared to one year ago. Year to date, real wages have only grown in y/y terms in February and March –with the fixed amount increases set by decree and the revision of 2019 wage negotiations. Postponing 2020 wage negotiations in several sectors fully impacted the performance of wages, but, with the greater number of closed wage agreements, we should see an improvement in the coming months. **According to the Ministry of Labor, the nominal union-negotiated wage grew 36% y/y, slightly below inflation (36.6%).**

With increased flexibility in the lockdown, we expect a certain improvement in the most-struck sectors. Nonetheless, the rigidity of the labor market makes it difficult to recover as quick as economic activity. According to the EIL, layoff expectations have been greater than hiring for 7 months in a row –though the difference has been dropping. As for real wages, we expect them to fall 3.6% on average in 2020, after plummeting 6.0% in 2019.



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