

Fiscal and institutional challenges for the new government

General Information



GDP	USD58.728bn (World ranking 76, World Bank 2014)
Population	15.86mn (World ranking 66, World Bank 2014)
Form of state	Constitutional Democratic Republic
Head of government	Jimmy Morales (FCN)
Next elections	2019, presidential and legislative



Strengths

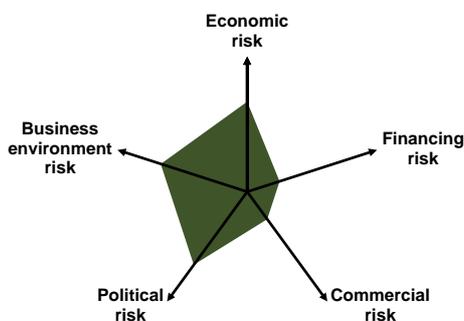
- Generally conservative, prudent macroeconomic policy framework
- Moderate debt ratios and adequate external balance
- Access to international finance support likely, if needed (IMF precautionary standby completed in 2009-10 during height of global financial crisis)
- Functioning democratic process—four handovers of power since end of 36-year civil war in 1996)
- Adequate business environment
- Trade agreement with U.S. (DR-CAFTA)

Weaknesses

- Low growth of medium-term real per capita GDP and highly skewed income distribution
- High dependency on primary commodities and U.S. (trade and workers' remittances) though exports are diversified
- Weak institutional framework, legacy of history of political instability
- Security situation and levels of violent crime, regional hub for illegal drug trade

Country Rating

B1



Source: Euler Hermes

Trade Structure

By destination/origin (% of total)

Exports	Rank	Imports
United States	42% 1	38% United States
El Salvador	10% 2	11% Mexico
Honduras	7% 3	7% China
Mexico	6% 4	5% El Salvador
Nicaragua	4% 5	3% Colombia

By product (% of total)

Exports	Rank	Imports
Vegetables and fruits	13% 1	17% Petroleum products
Coffee, tea, cocoa	13% 2	6% Road vehicles
Apparel & clothing	12% 3	6% Textile yarn
Sugar	9% 4	4% Cereals
Metalliferous ores	3% 5	4% Manufactured articles

Source: ITC, Chelem

Economic Overview

Growth to remain steady in 2015 and 2016

After a peak of +4.2% in 2014, real GDP growth is expected to go back to its long-term average, expanding by +3.7% in 2015 and +3.5% in 2016. Private consumption (84% of GDP) will remain the main engine of growth, supported by low inflation and accommodative monetary policy. Consumer prices, which have steadily slowed down over past months, are expected to remain within the inflation range of 4% +/-1pp in 2015 and 2016, while credit should continue to expand above +10% per year. Regarding the external sector, the U.S. recovery will drive up Guatemalan exports, remittances, tourism and FDI inflows, while Guatemala will continue to benefit from low oil prices.

Fiscal and institutional fragilities remain

Public finances are fragile despite low levels of fiscal deficit and public debt. Narrow fiscal revenues (less than 12% of GDP) raise doubts about the sustainability of public finances, as public spending is fairly inflexible. Current expenses account for more than 75% of total spending, of which 45% are for functional expenses, 10% for payment of debt service and 20% for subsidies and other transfers. Implementing a tax reform will be one of the major challenges for the newly elected President Jimmy Morales, who is taking office in January 2016, as he does not hold an absolute majority in Congress.

The external position is broadly sound although vulnerable to external shocks given strong dependency on agro exports (notably sugar and coffee) and linkages to the U.S. (through exports, remittances and investment). The current account deficit is moderate (-2% of GDP in 2015) as the wide trade deficit (-12% of GDP expected for 2015) is mostly offset by remittances inflows (10% of GDP). The external deficit is largely financed by public borrowing and FDI inflows. These are expected to remain strong in coming years due to ongoing investment projects in agriculture, mining and banking sectors. FX reserves are comfortable (above USD7bn or 4 months of imports), allowing the monetary authorities to defend the managed float of the exchange rate against the USD (within a range of 7.8GTQ/USD +/- 0.3). The external debt is moderate (below 30% of GDP).

The business environment is adequate. Guatemala is ranked 81st out of 189 countries in the World Bank's 2016 *Doing Business* survey. However, important shortcomings remain when protecting investors, enforcing contracts and resolving insolvencies, reflecting weak regulatory quality and the complexity of the rule of law. Also, a lack of physical investment, low human capital and worrisome security issues hamper investor confidence.

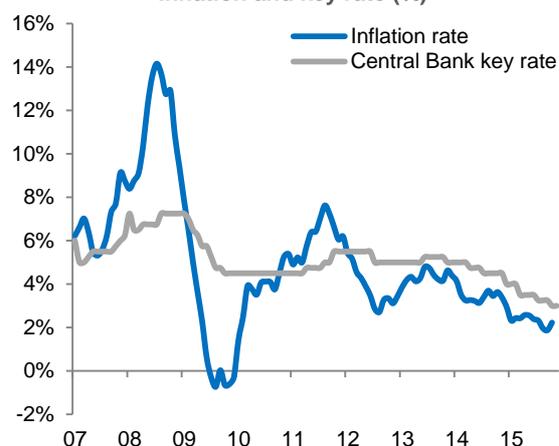
Key economic forecasts

	2014	2015f	2016f	2017f
GDP growth (% change)	4.2	3.7	3.5	3.5
Inflation (% , yearly average)	3.4	2.3	2.9	3.8
Fiscal balance* (% of GDP)	-1.9	-2.3	-2.1	-2.1
Public debt* (% of GDP)	24.3	25.1	25.8	26.3
Current account (% of GDP)	-2.4	-1.6	-2.0	-2.0
External debt (% of GDP)	27.7	28.4	29.1	29.8

*Includes Local Government; Non-financial Public Corporations; Social Security Funds; State Governments

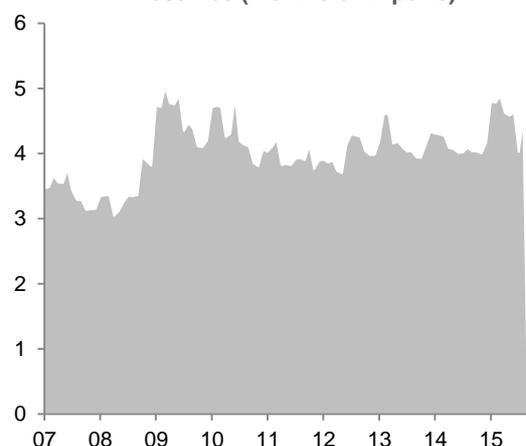
Sources: National sources, IMF-WEO, IHS, Euler Hermes

Inflation and key rate (%)



Sources: IHS, Euler Hermes

FX reserves (months of imports)



Sources: IHS, Euler Hermes

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