Guatemala

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Research & Analytics

COUNTRY

Real GDP growth (%) 2016	3.60%
Next General Election	Oct 2015
Exchange Rate	GTQ 7.675
	stable

CREDIT RATING

S&P Foreign Currency	BB (Stable)
Fitch Foreign Currency	BB (Stable)
Moody's Foreign Currency	Ba1 (Neg)

Major Trade Partners	US 36.1%, El Salvador 11.8%, Honduras 8.3%, Nicaragua 4.8%
Major Exports	Sugar, coffee, petroleum, apparel, manuf. products, minerals
GDP Composition	Agriculture: 13.3%, industry: 23.5%, services: 63.2%

RECENT ECONOMIC DEVELOPMENTS

ECONOMIC OUTLOOK

The Guatemalan economy expanded by 3.5% in the second quarter of 2015 following a revised 5.0% expansion in the first quarter. Economic growth in 2015 is estimated at 4.5%, supported by several infrastructure projects and pre-election spending. The energy ministers of Guatemala and Mexico have announced a USD1.2 billion natural gas pipeline between the two countries which is expected to take around four years to be completed.
The Guatemalan economy is driven by its services sector, accounting on average for approximately 50% of economic activity. The main service activities include financial services and transportation and communication. After the services sector, manufacturing is the second largest economic sector, accounting for approximately 24% of GDP. Within this sector, the food and beverages industry accounts for about 45% of total activity. Construction accounts for a relatively small percentage of economic activity at just 2.8%. Agriculture accounts for approximately 10% of economic activity. Guatemala is the biggest Central American coffee producer after Honduras. Guatemala is also a significant sugar producer. The agricultural sector accounts for about 40% of exports.

LABOUR, INFLATION AND THE FINANCIAL SYSTEM

In December 2015, the rate of inflation measured 3.07% which was within the Central Bank's target inflation rate of 4% ± 1. Inflation continues to be influenced by the fall in global oil prices and will likely be at the lower end of the target range as long as low oil prices persist. The agricultural sector provides employment for 50% of the labor force. The Guatemalan unemployment rate was reported at 2.9% during the first quarter of 2014 and is forecasted at 3.0% in 2015 and 2016. In November 2015, the central bank reduced its policy rate to 3% from 3.25% and no significant monetary changes are expected in the next two years.

EXTERNAL ACCOUNTS

Guatemalan exports are dominated by coffee (21%) and sugar (7.5%), however nontraditional exports (cut flowers, and berries, shrimp, and assembly) are said to be of growing importance to the economy. The country is growing and exporting an increasing amount of raw materials for biofuel production, especially sugar cane and palm oil. Most Guatemalan exports go to the US (40%) followed by El Salvador, Honduras and Mexico.
The current account deficit is expected to average 2.3% of GDP annually for 2015-2017 and will continue to be funded by FDI, which has averaged 95% of the deficits over the last three years. Growth in current account receipts will be dependent on growth in the US economy, its main trading partner. Remittances are an important source of foreign income with most originating in the United States. In 2012, Guatemalans in the US provided USD4.8 billion in remittances, accounting for approximately 10% of GDP. Remittances have increased as the U.S. economy improves and is the largest single source of foreign income and forecasted to continue growing approximately 10% a year. Foreign currency debt has steadily declined to represent less than 50% of total debt at the end of 2014 from 57% five years ago, while central bank reserves reached USD7.4 billion as of Oct. 23, 2015, from USD4.9 billion in 2009. Guatemala's international reserve position has remained strong and represented about four months of current account payments during 2015. The Guatemalan quetzal saw some significant appreciation against the US dollar in 2014 and has remained relatively stable in 2015. The central bank has indicated that the appreciation was due to increased remittances, private capital inflows, payment of certain obligations which increased the supply of currency and the reduction in the price of oil which reduced import costs.

FISCAL PROFILE

The fiscal deficit is expected to remain low averaging 2.3% in 2016 and marginally trending upwards to 3.0% in the coming years due to expenditure pressures on the incoming government. Guatemala is not expected to substantially reduce its fiscal deficit in the coming years. Expenditure is forecast to increase on account of higher social and security-related spending while revenue growth will remain constrained by an inefficient taxation system and continued opposition to tax reforms (Guatemala's tax revenue as a percentage of GDP is one of the lowest in Central America due to ineffective tax collecting). Fiscal reform in the next couple of years is unlikely due to the highly fragmented Congress.
Guatemala's debt is expected to stay below 23% of GDP until 2017 as it has hovered at 21.5% of GDP for the past three years. Also interest payments are forecasted to stay below 1.6% of GDP and to account for 13% of general government revenues in 2015.

CREDIT RATING

In June 2014, Fitch Ratings downgraded Guatemala's long-term foreign and local currency credit ratings to 'BB' from 'BB+'. According to Fitch, Guatemala has not been able to make sufficient progress to materially enhance its growth prospects, widen its revenue base and improve its fiscal flexibility. As a result, Guatemala's relative standing in Fitch's 'BB' category has been eroded over the years in terms of its revenue base, average growth rate and aggravated by weak governance and human development indicators.

OUTLOOK

In October 2015, Jimmy Morales of the FCN Nacion party won a landslide victory in second round voting. The new president based his campaign on fighting corruption and reform but as in the case of other Latin American countries he will face difficulties in implementing reforms due to a fragmented congress. The FCN hold only 11 out of the 158 seats in the unicameral legislature and this coupled with the inexperience of the President will make policymaking very difficult and sway investor sentiment. With 40% of the country's exports going to the US and 94% of Guatemalans living abroad residing in the US, the health of the external account is strongly related to the health of the US economy. A strengthening U.S will bolster remittance inflows and manufactured exports and depressed oil prices will also provide additional tailwinds to the economy. Guatemala remains vulnerable to external shocks with close to 50% of total debt denominated in foreign currency. Political uncertainty, contraction in capital spending and a decline in the agricultural industry due to adverse weather condition are expected to temper growth to 3.7% in 2016.