



PARAGUAY

2016 ARTICLE IV CONSULTATION—PRESS RELEASE; AND STAFF REPORT

May 2016

Under Article IV of the IMF's Articles of Agreement, the IMF holds bilateral discussions with members, usually every year. In the context of the 2016 Article IV consultation with Paraguay, the following documents have been released and are included in this package:

- A **Press Release** summarizing the views of the Executive Board as expressed during its April 29, 2016 consideration of the staff report that concluded the Article IV consultation with Paraguay.
- The **Staff Report** prepared by a staff team of the IMF for the Executive Board's consideration on April 29, 2016, following discussions that ended on February 26, 2016, with the officials of Paraguay on economic developments and policies. Based on information available at the time of these discussions, the staff report was completed on April 15, 2016.
- An **Informational Annex** prepared by the IMF staff.

The documents listed below have been or will be separately released.

Selected Issues

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IMF Executive Board Concludes 2016 Article IV Consultation with Paraguay

On April 29, 2016, the Executive Board of the International Monetary Fund (IMF) concluded the Article IV consultation¹ with Paraguay, and considered and endorsed the staff appraisal.

Paraguay's economy remains relatively resilient against the backdrop of a regional slowdown. Growth is estimated at 3 percent in 2015, among the strongest in Latin America. This reflects a milder terms-of-trade shock relative to comparators; stable growth in investment and consumption; and modest fiscal stimulus. However, the economy experienced some loss of momentum over the past year. Growth below potential helps contain inflation pressures, including from past exchange rate depreciation. In the first two months of 2016, headline inflation was temporarily elevated, mainly due to volatile food prices. Since then, it has moderated below 5 percent in March and is expected to decline to the mid-point of the central bank's target range (4.5 percent) over the course of 2016.

The external position deteriorated in 2015, due to a negative terms-of-trade shock and weakness in major trading partners. Furthermore, credit growth has moderated from a rapid pace, as economic activity has slowed and financial conditions have become less favorable. Credit quality has been deteriorating. Specifically, banks' non performing loans have been rising, albeit from low levels, since mid-2015. Notwithstanding potential vulnerabilities from past rapid credit expansion, the financial system appears sound. Most banks posted positive net income in 2015, although profitability measures (returns on assets and equity) were in most cases below 2014 levels. Relative to the region, Paraguay's banks compare favorably in terms of their balance sheets and profits.

Macroeconomic policies remain accommodative in light of subdued inflation and slower growth. Notwithstanding the BCP's 25 basis point interest rate hike in January 2016, monetary policy continues to be somewhat accommodative, following an easing cycle in mid

¹ Under Article IV of the IMF's Articles of Agreement, the IMF holds bilateral discussions with members, usually every year. A staff team visits the country, collects economic and financial information, and discusses with officials the country's economic developments and policies. On return to headquarters, the staff prepares a report, which forms the basis for discussion by the Executive Board.

2015. Meanwhile, fiscal policy has been supportive of economic activity. The fiscal deficit at the central government level is estimated to have reached 1.7 percent of GDP—marginally above the 1.5 percent ceiling set by the fiscal responsibility law (FRL).

Paraguay's economy is expected to remain relatively resilient this year and next despite challenging external conditions. Staff expects solid growth near 3 percent in 2016 and 3.25 percent in 2017. Given favorable weather and strong yields, the soy harvest—Paraguay's main agricultural crop—is likely to see strong growth from last year. Sound macroeconomic fundamentals, favorable demographics, lower cost of oil imports and a very competitive electricity sector are additional factors sustaining growth in the near-term. Lower credit demand from subdued investment plans and tighter credit conditions will contribute to slower, but still positive, credit growth in 2016, more in line with economic fundamentals.

Downside risks to growth have risen, mainly from the external side. A further slowdown in Brazil or deeper decline in agricultural commodity prices represents the major risks to the outlook. Domestically, rapid credit expansion in the banking system in the context of slower economic activity represents a potential macrofinancial vulnerability that could amplify the effects of adverse external shocks. Finally, limited capacity for administering and executing public investments also represents a downside risk to growth.

Executive Board Assessment²

Executive Directors commended the Paraguayan authorities for maintaining solid macroeconomic fundamentals, including low inflation, sustained growth and sound public finances. Nevertheless, Directors noted that downside risks to growth have risen, mainly from the external side. They emphasized the need to maintain macroeconomic stability and to strengthen implementation capacity and policy frameworks, address structural weaknesses, increase productivity, reduce poverty and promote inclusive growth.

Directors welcomed the authorities' commitment to sound fiscal policy. They emphasized the need for continued efforts to mobilize revenue and contain current expenditure while making space for capital spending, especially on infrastructure. In this context, they welcomed the signs of increased effectiveness of the fiscal responsibility law, but noted the importance of fully internalizing it in the budget process to help establish a track record and bolster the credibility of the fiscal anchor. Directors stressed that if amendments to the law are sought, changes to grant flexibility should be balanced by safeguards which enhance its credibility and are communicated carefully.

² At the conclusion of the discussion, the Managing Director, as Chairman of the Board, summarizes the views of Executive Directors, and this summary is transmitted to the country's authorities. An explanation of any qualifiers used in summings up can be found here: <http://www.imf.org/external/np/sec/misc/qualifiers.htm>.

Directors concurred that the moderately accommodative monetary policy stance remains appropriate given the uncertain international context and contained inflationary pressures. Monetary policy, coupled with a flexible exchange rate, should be the principal tool if growth were to weaken further, within the limits of meeting the central bank's price stability objective. Limiting discretionary foreign exchange market interventions to exceptional circumstances of disorderly market conditions would reinforce the inflation targeting regime and reassure markets. Reforms to deepen interbank markets and improve liquidity management could help strengthen monetary policy transmission.

Directors considered the exchange rate and external position to be broadly in line with fundamentals. They noted that the ample international reserve cover is appropriate considering Paraguay's openness, the level of dollarization, and vulnerability to shocks.

Directors agreed that the financial system appears to be sound, despite weaker economic growth and recent bank performance. In light of past rapid credit growth, vigilance over potential vulnerabilities remained critical to contain financial sector risks. Efforts to bolster the financial sector should include closely scrutinizing banks' loan classification practices and strengthening supervision of the cooperative sector. Directors welcomed progress towards introducing risk-based supervision and encouraged the authorities to continue upgrading monitoring and analytical capacity and strengthen institutional arrangements to carry out these functions.

Directors commended the authorities for progress on implementing their structural reform agenda covered in the National Development Plan. Directors stressed that infrastructure remains a key priority, especially improving electricity distribution and transportation. They welcomed steps that have been taken to strengthen government transparency, including implementation of the Law of Free Access to Public Information.

Directors commended the authorities for their efforts to continue to strengthen anti-corruption and AML/CFT measures to improve the business climate. They welcomed recent passage of the law on asset declaration.

Paraguay: Selected Economic and Social Indicators

I. Social and Demographic Indicators								
Population 2014 (millions)	6.9					Gini index (2014)		48.0
Unemployment rate (2014)	6.0					Life expectancy at birth (2013)		72.0
Percentage of population below the poverty line (2014)	22.6					Adult illiteracy rate (2014)		5.4
Rank in UNDP development index (2014)	112 of 186					GDP per capita (US\$, 2014)		4,481
II. Economic Indicators								
	2010	2011	2012	2013	2014	Est. 2015	Proj. 2016	Proj. 2017
(Annual percent change, unless otherwise indicated)								
Income and prices								
Real GDP	13.1	4.3	-1.2	14.0	4.7	3.0	2.9	3.2
Nominal GDP	20.0	10.8	3.4	15.0	10.1	6.4	8.1	6.9
Per capita GDP (U.S. dollars, thousands)	3.1	3.8	3.7	4.3	4.5	4.0	3.8	3.9
Consumer prices (end of period)	7.2	4.9	4.0	3.7	4.2	3.1	4.5	4.5
Nominal exchange rate (Guarani per U.S. dollar, eop)	4,558	4,478	4,224	4,585	4,629	5,807	...	...
Monetary sector								
Currency issue	18.5	11.6	17.5	13.2	8.9	2.9	3.1	3.4
Credit to private sector 1/	37.9	25.6	15.8	19.4	19.9	8.8	4.6	5.2
Liabilities to private sector	19.9	19.3	14.0	20.0	15.9	4.2	6.6	6.2
External sector								
Exports (fob, values)	35.1	20.7	-7.8	16.7	-3.7	-14.6	-5.1	5.1
Imports (cif, values)	44.7	22.9	-5.9	7.8	1.1	-14.9	-6.7	7.1
Terms of trade	8.2	14.3	-10.2	11.4	9.8	-2.8	1.7	-2.5
Real effective exchange rate 2/	1.9	11.8	-1.6	5.2	3.2	-1.1	...	...
(In percent of GDP, unless otherwise indicated)								
Current account	-0.3	0.4	-2.0	1.7	-0.4	-1.8	-1.4	-1.2
Trade balance	4.4	3.4	2.3	5.7	3.3	3.2	3.8	3.1
Exports	52.2	50.3	47.4	47.0	42.4	39.8	39.6	39.9
Electricity	9.8	9.0	9.1	7.7	7.1	7.4	7.8	7.8
Other registered	22.6	21.9	20.5	24.9	24.1	22.6	22.5	23.3
Unregistered	19.8	19.4	17.8	14.3	11.2	9.9	9.3	8.9
Imports	-47.8	-46.9	-45.1	-41.2	-39.1	-36.6	-35.8	-36.8
Of which: Oil imports	-5.4	-6.0	-6.7	-6.0	-5.5	-3.2	-2.0	-2.4
Capital account and financial account	1.0	1.9	3.7	0.3	5.5	0.8	1.5	0.8
General government	0.3	-0.2	-0.1	1.8	3.2	1.4	3.5	0.7
Private sector	0.6	2.1	3.9	-3.0	1.0	-0.6	0.2	0.1
Of which: Direct investment	1.1	2.2	1.9	0.2	1.1	1.3	1.6	1.8
Errors and omissions	0.9	0.8	-1.8	1.6	-1.4	-1.0	0.0	0.0
Gross international reserves (in millions of U.S. dollars)	4,168	4,984	4,994	5,871	6,891	6,329	6,360	6,254
In months of next-year imports of goods and services	3.9	5.0	4.6	5.3	7.3	7.1	6.7	6.2
Ratio to short-term external debt	2.4	2.7	2.8	3.2	3.8	3.4	3.3	3.1
Gross domestic investment	16.2	17.1	15.1	15.4	16.2	16.5	16.0	16.1
Gross national saving	15.9	17.5	13.0	17.1	15.8	14.7	14.7	14.9
Central government revenues 3/	17.1	18.0	19.0	17.1	17.9	18.1	18.0	18.2
Of which: Tax revenues	12.0	12.6	12.7	11.8	12.7	12.3	12.2	12.4
Central government expenditures 3/	15.8	17.0	20.6	18.8	19.0	19.8	20.1	20.2
Of which: Compensation of Employees	7.2	7.5	9.4	9.1	8.8	9.0	8.9	8.9
Of which: Net Acquisition of Non Financial Assets	2.4	2.3	2.6	2.3	2.4	2.6	2.7	2.7
Central government net lending/borrowing	1.3	1.0	-1.7	-1.7	-1.1	-1.7	-2.1	-2.0
Central government primary balance	1.7	1.3	-1.4	-1.4	-0.7	-1.1	-1.3	-0.9
Public sector debt (excl. central bank bills)	15.6	13.0	16.2	17.0	20.2	23.8	26.5	27.2
Of which: Foreign currency	13.2	11.1	10.9	11.6	14.5	18.0	21.4	21.2
Of which: Domestic currency	2.4	1.9	5.3	5.4	5.8	5.8	5.1	6.0
Memorandum items:								
GDP (billions of Guaranies)	94,934	105,203	108,832	125,152	137,798	146,566	158,409	169,324
GDP (US\$ billions)	20.0	25.1	24.6	29.0	30.9	28.1	...	...

Sources: Central Bank of Paraguay; Ministry of Finance; and IMF staff estimates and projections.

1/ Includes local currency credit and foreign currency credit valued at a constant exchange rate.

2/ Average annual change; a positive change indicates an appreciation.

3/ According to the GFSM 2001 presentation.



PARAGUAY

STAFF REPORT FOR THE 2016 ARTICLE IV CONSULTATION

April 14, 2016

KEY ISSUES

Context: Paraguay has solid macroeconomic fundamentals, with low inflation, sustained growth and sound public finances. Over the course of last year, however, the economy experienced a loss of momentum—largely linked to weak commodity prices and adverse regional spillovers. Downside risks to growth, mainly external, have risen. Over the medium term, authorities face challenges, including limited implementation capacity and political economy constraints, in the pursuit of their reform agenda to address structural weaknesses, reduce poverty, strengthen policy frameworks, increase productivity and promote inclusive growth.

Focus: The consultation focused on policies to support macroeconomic resilience, contain financial sector vulnerabilities, and advance economic development.

Key policy issues:

- On the fiscal front, there are clear signs of increased effectiveness of the fiscal responsibility law (FRL), and it is important that the law is fully internalized in the budget process. Staff projects a broadly neutral fiscal stance for 2016 and some tightening of current primary expenditures would be advisable to avoid exceeding the FRL's deficit ceiling by a wider margin while safeguarding needed public investment. Caution is warranted when considering any modifications to the fiscal anchor. If amendments to the law are sought, changes to make the fiscal rules more flexible should be accompanied by safeguards that enhance credibility.
- Monetary policy remains accommodative given the uncertain international context and contained underlying inflationary pressures. On the external front, staff continues to assess the currency and external position as being broadly in line with fundamentals and reserves remain broadly adequate. Monetary policy coupled with a flexible exchange rate should be the principal tool if growth were to weaken further, within the limits of meeting the central bank's price stability objective.
- The banking system appears to be sound and authorities are moving forward with efforts to enhance financial supervision. Reducing still-elevated financial sector dollarization through macroprudential instruments could help limit risks from exchange rate fluctuations and possibly curb the need for foreign exchange interventions. To manage risks emanating from somewhat weaker credit quality, particular scrutiny is warranted in examining banks' loan classification and provisioning, particularly to the agricultural sector.

Approved By
**Jorge Roldos and
 Vikram Haksar**

Discussions took place in Asunción during February 15–26. The staff team comprised H. Faruqee (head), A. Santos (senior resident representative), A. David, G. Keim, N. Novta, and M. Santoro (all WHD) with research assistance from E. Tawfik and editorial support from J. Meza-Cuadra and A. Herrera. J. Corvalan (OED) also participated in the meetings. The team met with BCP President Carlos Fernández, Minister of Finance Santiago Peña, Minister of Public Works and Communications Ramón Jiménez, Minister of Industry and Commerce Gustavo Leite, Minister of Planning José Molinas, Social Action Minister Héctor Cárdenas, and other senior officials, and representatives from the private sector, think tanks, and the donor community.

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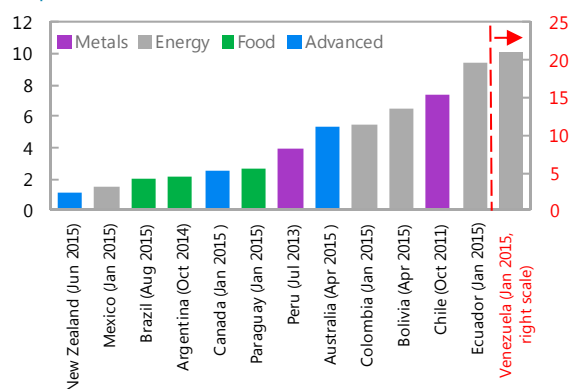
RECENT DEVELOPMENTS: RELATIVE RESILIENCE TO A REGIONAL SLOWDOWN

1. Against the backdrop of a regional slowdown, Paraguay's economy remains relatively resilient. Staff estimates growth at 3 percent in 2015, among the strongest in Latin America (Table 1). This reflects: (i) a milder adverse terms-of-trade shock relative to comparators;¹ (ii) stable growth in investment and consumption; and (iii) modest fiscal stimulus.

2. The economy experienced some loss of momentum over the past year due to unfavorable external shocks. For three consecutive quarters, Paraguay's real GDP growth has progressively slowed down, reaching 1.1 percent year-on year (y/y) in the fourth quarter, from 6 percent in the first quarter (Figure 1). Real exports contracted by just below 10 percent (y/y) in the first three quarters of 2015. Prices of its two major exports, soybeans and beef, fell 24 and 10½ percent respectively in 2015, while a deepening recession in Brazil affected re-exports and commercial activity in Paraguay's border cities.

3. Inflation pressures remain contained despite significant depreciation of the guaraní against the U.S. dollar. Core inflation remained subdued during most of 2015 (Figure 1),² despite a 25 percent depreciation against the U.S. dollar (although depreciation of the guaraní in effective terms was more modest). However, core inflation increased towards the end of the year. A limited degree of exchange rate pass-through resulted in higher prices. Services and housing have also contributed to higher core inflation. In the first two months of

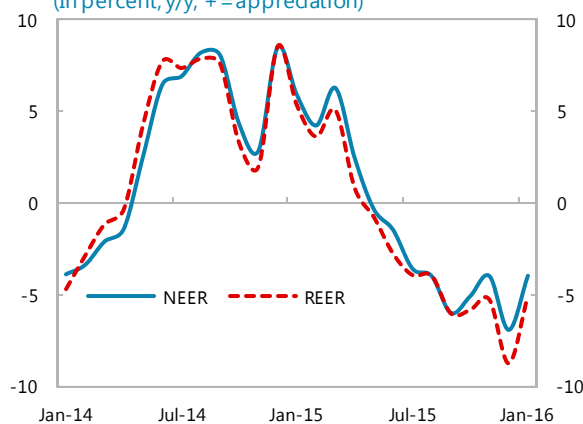
Peak to Trough Change of Commodity Terms of Trade
(In percent of GDP)



Sources: Gruss (2014); and IMF staff calculations.

Note: Trough period of current commodity terms of trade cycle in parentheses for each country. Exclude precious metals, except for Bolivia, Colombia and Peru.

Effective Exchange Rates
(In percent, y/y, += appreciation)



Source: IMF INS.

¹ Terms-of-trade deteriorated as soy and beef export prices dropped in 2015, but import prices of oil products and capital goods also decreased to provide some offset. Capital goods import prices fell in U.S. dollar terms mainly from neighboring countries, Brazil and Argentina, whose currencies have depreciated significantly against the U.S. dollar.

² BCP's preferred measure of underlying inflation ("nucleus") averaged 2.9 percent for 2015 (y/y) and 3.7 percent in December, whereas core inflation (X1) averaged 3.7 percent for 2015 and 4.9 percent in December.

2016, headline inflation remained temporarily elevated, mainly due to volatile food prices. Staff expects inflation to decline to the mid-point of the central bank's target range (4½ percent) over the course of 2016, as growth below potential helps contain inflation pressures, including from past exchange rate depreciation. Moreover, recent currency appreciation since February, low oil prices, moderating inflation for services and housing, and anchored inflation expectations, further point to more subdued or easing inflationary pressures going forward, also reflected by moderating inflation in March 2016.

4. Macroeconomic policies remain accommodative in light of subdued inflation and slower growth. Notwithstanding the BCP's unexpected 25 basis point interest rate hike in January 2016 to 6 percent, monetary policy continues to be somewhat accommodative, following an easing cycle over March-July 2015 (Figure 2). Meanwhile, fiscal policy has been more supportive of economic activity. Staff estimates that the fiscal deficit at the central government level reached 1.7 percent of GDP—marginally *above* the 1.5 percent ceiling set by the fiscal responsibility law (FRL). The estimated deficit would imply a positive fiscal impulse of 1.2 percent of potential non-agriculture non-energy GDP³ (Figure 3, Table 2, and Table 3).

5. In the first year of implementation, FRL compliance has been challenging. Amid legitimacy questions about the scope of the FRL to limit the legislative power of congress to enact budgets that are not in line with the law's provisions, the 2015 budget approved by congress exceeded the deficit ceiling by 1.3 percentage points of GDP after modifications were introduced to the executive's budget proposal. Moreover, the approved budget law, allowed for the exclusion of capital expenditure financed by sovereign bonds from the calculation of the deficit ceiling on a one-off basis. Staff estimates an adjusted fiscal balance of -0.6 percent of GDP for 2015, below the FRL deficit ceiling if such expenditures are excluded. Furthermore, real current primary expenditures are estimated to have grown by 4.7 percent, exceeding the FRL ceiling of 4 percent on an ex-post basis.

6. In 2016, however, there have been signs of increased effectiveness of the FRL in the budget process. The draft 2016 budget submitted to congress complied with the numerical targets of the law. While the final approved version still respected the deficit ceiling, modifications introduced by congress altered the composition of spending. Staff still expects real current primary expenditure growth for the central government to be below the FRL ceiling when comparing outcomes for 2015 and 2016, but the growth of these expenditures would exceed the 4 percent limit when comparing the approved budget to the 2015 outturn.⁴

7. The external position deteriorated modestly in 2015, due to a negative terms-of-trade shock and weakness in major trading partners. The current account balance moved further into negative territory and is expected to remain in deficit at -1.8 percent of GDP in 2015 (Figure 4, Table

³ The primary balance is estimated to have deteriorated by 0.4 percent of GDP.

⁴ Note that authorities do not use fiscal outcomes to assess compliance with the FRL. Instead, compliance is based on a comparison of the implied growth in current primary expenditures for the public sector in the approved budget for year $t+1$, relative to the prevailing budget in year t , deflated by the mid-point of the BCP inflation target band.

4), as exports receipts (particularly, from Asia) have fallen due to lower commodity prices, as well as from weaker economic activity in trading partners—notably, Brazil and Russia. Recent indicators also point to weaker exports and, consequently, a smaller trade surplus last year. With respect to the financial account, foreign direct investment has grown more modestly, about 10 percent through Q3 2015, than its average over the last 10 years given generally tighter financial conditions externally. The deterioration of the current account position and reduced capital inflows has reduced international reserve holdings. Staff continues to assess the currency and external positions as being broadly in line with fundamentals given changes in the external environment (Annex II). The assessment is mainly based on external adjustment consistent with weaker terms-of-trade and partner activity, and real effective exchange rate (REER) depreciation, which is more in line with its ten-year average. EBA-lite estimates of current account and REER gaps continue to present mixed results, with poor empirical fit and almost no share of the misalignment explained by policy gaps.

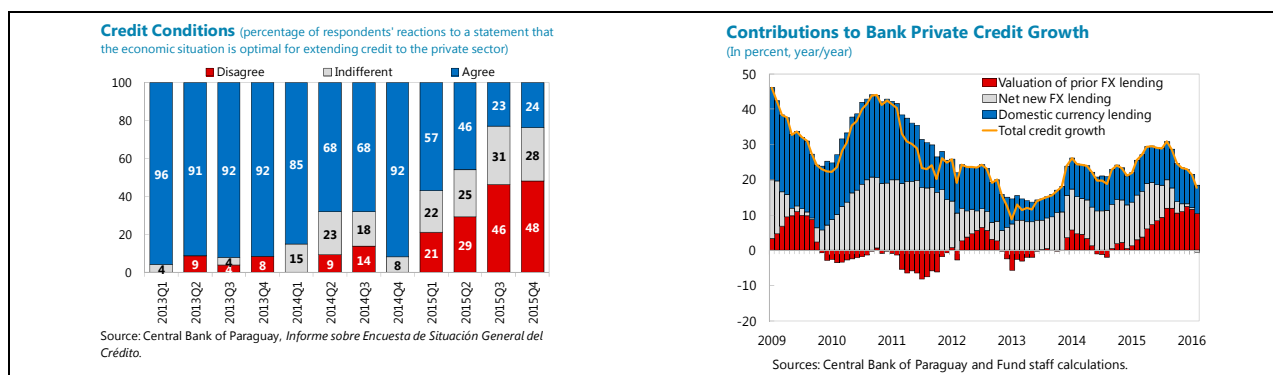
Exchange Rate Assessment - 2015					
	EBA- Current account				EBA - REER
	Norm ^{1/}	Balance ^{1/}	Gap	REER ^{2/}	REER ^{2/}
EBA-lite methodology	-5.2	-1.8	3.4	-12.8	17.7
Diagnostics	EBA CA		EBA REER		
Fitted	-5.2		4.6		
Residual	3.4		0.2		
Policy gap	0.1		0.0		
Constant	-4.0		4.2		
1/ Percent of GDP					
2/ In percent. + indicates overvaluation with respect to implied benchmark.					

8. Reserves remain broadly adequate. The BCP's reserve position at 23 percent of GDP covers 7 months of imports (Table 5). Reserves are expected to increase in 2016, relative to 2015, partly as a result of the issuance of a US\$600 million government bond. Reserves are assessed to exceed the IMF's standard adequacy metric for floating exchange rate economies. However, staff believes that ample reserve coverage is appropriate for Paraguay considering the economy's openness, significant dollarization, and high vulnerability to weather and commodity price shocks.

9. Recently, credit growth has moderated, but credit quality has deteriorated. Over 2015, financial intermediaries have become increasingly less optimistic about economic conditions and extending credit. In parallel, growth in bank credit to the private sector in local currency terms peaked at 29½ percent last May but stood at about 18 percent by February 2016 (Table 6). This largely reflects stagnant FX lending volumes, which more than offset the valuation effects of exchange rate depreciation.⁵ Stagnant FX credit volumes coincided with reduced demand for investment loans in the largely dollarized agriculture sector, owing to the drag on profitability from

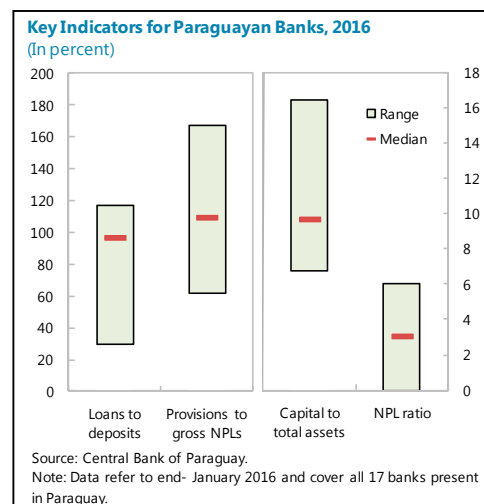
⁵ When FX credit is measured in constant January 2014 exchange rates, growth of total credit to the private sector stood at 7½ percent in February 2016, down from a recent peak of 22½ percent in March 2015.

lower commodity prices. In contrast, local currency lending growth remained strong, even as changes to credit card regulations appear to have restrained consumer lending. Credit quality has been deteriorating recently, with banks' non performing loans (NPLs) rising to a still-moderate 2.9 percent in February 2016 (Table 7). Moreover, loan restructuring and refinancing, outside of NPLs, also rose over the year to 2.3 percent of total loans, in some cases benefitting from the BCP's decision to grant temporary relaxations in loan classification to mitigate the effects of shocks facing the agriculture and livestock sectors.



10. Notwithstanding potential vulnerabilities from rapid credit expansion, the financial system appears sound (Figure 5).

Most banks, including large institutions, posted positive net income in 2015, although profitability measures (returns on assets and equity) were in most cases below 2014 levels. Reduced profitability largely reflected higher provisioning expenses, which continued to provide ample coverage for nonperforming loans. Reported system-wide capital ratios were strong, with the tier 1 capital ratio at 11.3 percent (Table 8). The equity-to-asset ratio dipped slightly, as share capital issuance by many banks offset still-rapid asset growth. Relative to the region, Paraguay's banking sector compares relatively favorably on profitability, capitalization, liquidity, and loan quality.



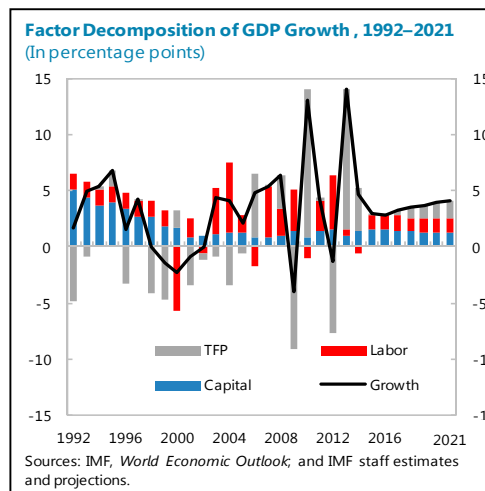
NEAR-TERM OUTLOOK AND RISKS TO RESILIENCE

11. Paraguay's economy is expected to remain relatively resilient this year and next, withstanding the adverse impact of sizeable external shocks. Despite a prolonged regional slowdown and weaker commodity prices, staff expects solid growth near 3 percent in 2016 and 3¼ percent in 2017, led by agriculture and construction. Given favorable weather and strong yields, the soy harvest—Paraguay's main agricultural crop—is likely to see strong growth from last year. This boost in volumes in agriculture in the first quarter should provide

Projected Real GDP Growth 1/	
	2016 2017
	(in percent)
BCP Forecast	3.2 ..
BCP Survey	3.0 3.8
Consensus Forecast	3.4 3.6
IMF	2.9 3.2

Sources: Central Bank of Paraguay; Consensus Forecast; and IMF.
1/ As of March, 2016.

an offset to negative carryover effects from weakening momentum elsewhere over the course of last year—led by decelerating activity in other trade-related sectors (industry, commerce and livestock). From the demand side, consumption growth is expected to remain solid, but investment in agriculture is likely to weaken further given lower prices and tighter margins, subdued outlook for commodity prices, and slower declines in costs and prices of machinery and equipment. Sound macroeconomic fundamentals, favorable demographics, lower cost of oil imports and a very competitive electricity sector are additional factors sustaining growth in the near-term. Following rapid credit growth in 2015, lower credit demand from subdued investment plans and tighter credit conditions will contribute to slower, but still positive credit growth in 2016, more in line with economic fundamentals.



12. But downside risks to growth have risen mainly from the external side (see Risk Assessment Matrix). These risks are underscored by a noticeable deceleration in the quarterly path of GDP in 2015. A further slowdown in Brazil and deeper decline in agricultural commodity prices represent the major risks to the outlook. Staff analysis suggests that growth spillovers from Brazil can be sizeable but the confidence range around point estimates is large (Box 1, Annex V). Albeit of lesser importance, lower growth in the euro area and Russia—market destinations accounting for about 25 percent of Paraguay’s exports—could dampen domestic growth to some degree. The recent removal of exchange controls and trade taxes in Argentina could be a source of upside risk, but its effects are uncertain (see Box 1). Rapid credit growth in the banking system in the context of slower economic activity represents a potential macrofinancial vulnerability that could interact with external risks, such as the deterioration of external financial conditions.⁶

13. On the domestic front, limited capacity for administering and executing public investments also represents a downside risk to growth. With indicators of its capital stock and infrastructure quality typically in the bottom quartile among emerging markets, Paraguay’s planned infrastructure build-out is a necessity. However, the efficiency of public investment management and experience with large projects is relatively low—raising risks associated with any ramp-up in infrastructure spending, including private sector participation in infrastructure projects (PPPs).

⁶ As a potential mitigating factor, lending rates remained quite stable during previous episodes of financial turbulence, including during the taper-tantrum in mid-2013.

Risk Assessment Matrix

Nature of the shock (color = likelihood)	Sources of Risk	Impact if Realized (color = severity)	Policy Response
	Vulnerabilities/ Channels of transmission		

DOMESTIC

Weak administrative capacity and execution of public investment	➔	Real: Low administrative capacity would translate into slower or less effective implementation of crucial infrastructure investment.	A weaker-than-expected infrastructure investment would depress growth in the near and medium term.	<ul style="list-style-type: none"> - Accelerate efforts to address institutional weaknesses and improve transparency. - Encourage private sector investment.
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EXTERNAL

A further slowdown in Brazil and other trading partners	➔	Financial: Banks have large exposure to the exporting sectors. <div style="text-align: center; margin: 5px 0;"> ↑ Leverage ↑ </div> Real: Exports to Brazil represent around 30 percent of Paraguay's total exports. FDI inflows from Brazil are also large, especially in the maquila industry. Europe and Russia account jointly for 25 percent of total exports.	Slower than expected growth in trading partners would impair export sales and spill over to banking sector and other sectors related to export production.	<ul style="list-style-type: none"> - The floating exchange rate represents the first line of defense. FX intervention could be used to avoid excessive volatility. - Let monetary conditions ease, consistent with IT framework. - Let automatic stabilizers operate.
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A more persistent decline in agricultural commodity prices	➔	Financial: Banks have large exposure to the exporting commodity sectors. <div style="text-align: center; margin: 5px 0;"> ↑ Leverage ↑ </div> Real: Exports of agricultural products represent about 30 percent of GDP.	More persistent lower commodity prices will curtail profits in the exporting sectors with spillovers to the banking and other related sectors.	<ul style="list-style-type: none"> - The floating exchange rate represents the first line of defense. FX intervention could be used to avoid excessive volatility. - Accelerate measures that promote diversification. - Let monetary conditions ease, consistent with IT framework. - Let automatic stabilizers operate.
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Weather-related shocks to agriculture and energy sectors	➔	Financial: Banks have large exposure to the agricultural sector. <div style="text-align: center; margin: 5px 0;"> ↑ Leverage ↑ </div> Real: Agriculture and hydroelectricity are particularly vulnerable to severe natural shocks.	Disruption in the agricultural sector from weather-related events can have significant impacts on GDP (up to 4 percent, in some cases)	<ul style="list-style-type: none"> - The floating exchange rate represents the first line of defense. FX intervention could be used to avoid excessive volatility. - Accelerate measures that promote diversification. - Let monetary conditions ease, consistent with IT framework. - Let automatic stabilizers operate.
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A further deterioration of external financial conditions	➔	Financial: corporate and non-corporate debt has increased for some time, especially dollar-denominated.	A sharp increase in interest rates, related to the end of US monetary policy easing or persistent dollar strength could impact firms' profitability, impeding loan service. There are, however, significant mitigating factors: - About 45 percent of dollar-denominated debt is concentrated in the agricultural sector, which has significant natural hedges. - Domestic interest rates tend to be resilient to developments in the US markets, including during the taper-trantrum episode in 2013.	<ul style="list-style-type: none"> - The floating exchange rate represents the first line of defense. FX intervention could be used to avoid excessive volatility. - The authorities should enact macro-prudential measures, including by imposing different capital requirement on dollar-denominated loans.
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Note: Colored boxes on left hand side represent shock likelihood and colored boxes on right hand side represent severity of impact. Red = High, Yellow = Medium, and Green = Low.

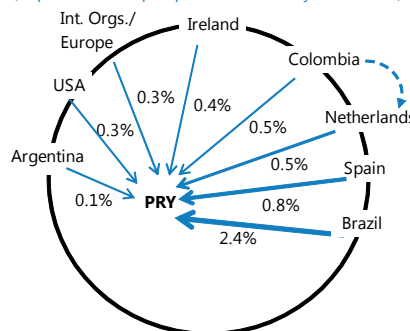
Box 1. Paraguay: Global and Regional Spillovers to Paraguay

Financial linkages between Paraguay and the rest of the World are limited.

Foreign asset holdings by Paraguayan banks are small and banks are largely funded through deposits and capital. Foreign ownership of deposits is also small and foreign equity (mainly from Brazil) represents only 2.5 percent of system assets. Nevertheless, high levels of dollarization in the financial system could render bank balance sheets vulnerable to sharp exchange rate movements, even though currency mismatches are partly offset by natural hedges. Furthermore, foreign investors do not hold domestically-issued government bonds and most portfolio inflows to the country are linked to the issuance of sovereign bonds in international markets. FDI growth in the recent past has been concentrated in the construction and maquila sectors, which benefit from Paraguay’s competitive tax system and energy prices.

Foreign Equity Financing

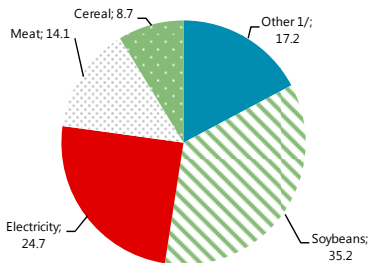
(Capital ownership in percent of total system assets)



Trade channels continue to be the main source of vulnerability to external shocks.

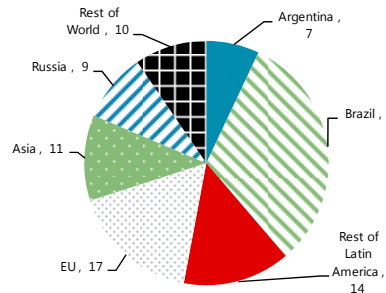
Paraguay is a highly open economy, with total exports and imports at around 80 percent of GDP, but trade is concentrated both in terms of products and export destinations. As a consequence, the economy is vulnerable to demand shocks from major trading partners (in particular Brazil) and to volatility in prices of key commodity exports (soybean, beef). Brazil’s deep recession also had a profound impact on the demand for re-exports, affecting economic activity in border cities. The recent decline in oil prices is likely to have a positive impact on the economy, given that the country is a net oil importer. Spillovers through trade also have a significant impact on asset quality in the banking system. In particular, the effect of Brazil’s GDP growth on NPLs is large and significant (see Selected Issues Paper).

Exports by Main Products, 2015
(In percent of total)

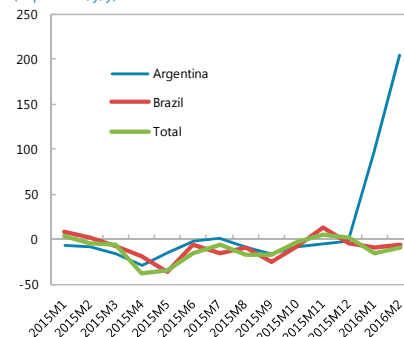


Sources: BCP, and IMF staff calculations.
Note: Date refer to registered exports only.
1. Other includes cotton and wood.

Exports by Key Trading Partners, 2015
(In percent of total)



Registered Exports Growth
(In percent, y/y)



Sources: BCP, and IMF staff calculations.

Vector autoregression (VAR) estimates suggest that Paraguay’s growth rates are affected by shocks to Brazil’s growth as well as shocks to global variables (VIX index, commodity prices).

Staff analysis suggests that growth spillovers from Brazil can be sizeable—about ½ to ¾ percentage point on domestic growth for a one percentage point shock to Brazil’s growth. However, confidence intervals around the estimated spillover coefficients are wide given the underlying variability of the series, including domestic GDP. The estimated cumulative effect on Paraguay’s growth 4 quarters after the shock in Brazil can be as low as zero or as high as over 1 percentage point. Typically, the greatest cumulative effect on Paraguay’s growth is about 3 quarters after the Brazil shock. Given Paraguay’s relatively resilient growth so far, despite almost 8 quarters of recession in Brazil, further negative impact from Brazil may remain subdued. Shocks to the VIX volatility index, a measure of global risk aversion, are also linked to statistically significant decreases in Paraguay’s GDP growth (variance decompositions show that about 11 percent of the forecast errors can be attributed to VIX shocks at the four quarter horizon and beyond). Responses of GDP growth to soybean prices and commodity terms of trade also go in the expected direction although statistical significance varies depending on the model used.

Spillovers from Argentina following the normalization of the exchange rate system in that country remain uncertain.

Foreign exchange controls in Argentina had previously led to a surge in contraband imports, which appears to have subsided. Businesses involved in the formal distribution and retail chain had been negatively affected by contraband trade. Exports from Paraguay to Argentina have surged since December 2015, albeit from a very low level. The effects of recent developments in Argentina on investments in the real estate sector are difficult to ascertain due to the lack of statistics on the sector.

POLICY DISCUSSIONS: SUPPORTING GROWTH THROUGH STRENGTHENED POLICY FRAMEWORKS

14. Discussions focused on the structural reform agenda and measures to further strengthen fiscal, monetary, and financial sector policy frameworks. The National Development Plan comprehensively outlines the authorities' structural reform priorities and tracking of implementation progress was discussed, particularly with respect to infrastructure. Improvements in government accountability were seen as encouraging initial steps. The current mix of macroeconomic policies was viewed as broadly appropriate. Monetary policy remains accommodative and the BCP kept interest rates on hold at its policy meeting at the time of the mission—citing a more complex external environment. Steps to reinforce credibility of the inflation targeting regime were also discussed. On fiscal policy, there were clear signs of increased effectiveness under the fiscal responsibility law in the 2016 budget process, but a longer track record of compliance is needed to cement it as a credible fiscal anchor. The fiscal stance appears broadly neutral in 2016, but tax revenues are likely to be weaker than in the budget, and tightening current expenditures would be advisable to avoid exceeding the FRL's deficit ceiling ex-post by a wider margin. Improvements to the medium-term fiscal framework and pension reform were still needed.

A. Structural Reforms: Laying Foundations for Durable Growth

15. Paraguay has embarked on an ambitious reform agenda to raise living standards and boost potential growth (Figure 6). The authorities' national development plan (NDP) for 2014–30 rests on three axes: (i) poverty reduction and human capital development; (ii) infrastructure and inclusive growth; and (iii) insertion of Paraguay into global value chains. The mission discussed implementation progress with respect to the NDP and key strategic reform priorities. Deficiencies in transportation and electricity distribution were seen by staff as key bottlenecks,⁷ constraining productive capacity

Structural Reforms: National Development Plan		
Axis	Reform Areas	Main Measures
I	Poverty reduction	Eradicate extreme poverty
	Education	Improve education quality and enrollment
	Health	Reduce infant malnutrition
		Increase life expectancy
	Urban planning	Universal access to water and sanitation
Eradicate unhealthy living conditions		
		Increase registration of urban and rural plots
II	Employment	Increase employment among the young and disadvantaged
	Financial	Universal social security coverage
		Improve financial inclusion
	Transportation	Improve road maintenance
	Communications	Improve fluvial transportation through dredging and nocturnal navigation
		Increase broadband internet coverage
	Productivity	Increase agricultural productivity on family-owned farms
	Environment	Eradicate illegal deforestation
Increase renewable energy consumption		
III	Social integration	Incentivize return of distinguished Paraguayans
		Support return of Paraguayan migrant workers
	Economic integration	Increase exports
Increase tourism		

⁷ Improved navigability of the Paraguay-Parana Waterway, through dredging, as well as investment in port terminals and key road segments would relieve traffic congestion, reduce logistics costs and facilitate trade. Existing electricity transmission and distribution systems are inadequate to meet the growing demand for energy. Paraguay shares with Brazil the second largest hydroelectric power plant on earth, Itaipu, yet hydro power represents less than 20 percent of domestic energy consumption.

and quality of public services. Staff and authorities agreed on the need to prioritize infrastructure investment in these areas—including through PPPs.

16. The national development plan places emphasis on inclusive growth and poverty reduction.⁸ The authorities highlighted the “Sowing Opportunities” umbrella program aimed at poverty reduction and inclusive growth. It includes *Tekopora*, the longstanding conditional cash-transfer program, as well as several new programs such as *Tenondera*, an income-generating program to empower those graduating from *Tekopora*; and *Tekoha*, a program to assist the poor to legally acquire property on which they live. At the same time, authorities noted that efforts have been made to improve targeting and coverage by collecting more information about the economic conditions of potential recipients via the “*Ficha Social*” survey.

17. Government performance is now more accountable due to the transparency law and via internal scorecards. The general public has online access to the wages of all public officials, as well as assets for many of them.⁹ There is also free access to public procurement data. Authorities across institutions expressed their satisfaction with the implementation of the Law of Free Access to Public Information, seeing it as a fundamental change in the country. Thanks to its implementation, there is more involvement of civil society in government affairs. In addition, the government uses internal scorecards (“*Tablero de control*”) to improve accountability and monitor performance in different ministries and agencies. The authorities are improving human resource management, with merit-based selection processes in 96 institutions (up from 24 in 2013). The authorities also noted that there are ongoing efforts to reform the judicial system and improve the AML/CFT legislation.

Recent achievements in fighting corruption:
I Methods to ensure free access to public information
<ul style="list-style-type: none"> Anticorruption portal (to make a denouncement, seek verification) Unified portal to access public information (public sector payroll, asset declarations, or request other public information) National public procurement directorate, with online access
II Strengthened administrative control
<ul style="list-style-type: none"> Internal scorecards (“<i>Tablero de control</i>”) Biometric control of public employee presence at work Use of magnetic card to charge fuel for public sector vehicles Electronic payment of social services (<i>Tekopora</i>, pensions for poor)

B. Fiscal Policy: Balancing Credibility and Flexibility

18. Options to enhance the credibility and effectiveness of the Fiscal Responsibility Law were discussed. While the FRL has not had the expected traction on the budget process, there are signs of increased effectiveness as evident in the 2016 budget approved by congress. Crucially, ad-hoc provisions for the exclusion of capital expenditures from the deficit ceiling have not been added

⁸ In addition, programs under each of the three NDP axes can further be divided into: 1) promoting equality of opportunities, 2) efficient and transparent public management, 3) land use planning, and 4) environmental sustainability. The greatest resources are devoted to the first two subcategories.

⁹ The constitutional requirement (Article 104) that public officials declare their assets was clarified via regulatory Law 5033 in 2013.

to the Budget law this year. Overall, despite notable progress, questions about the FRL as a credible fiscal anchor remain. Part of the issue concerns legal ambiguity between the obligations under the FRL and constitutional budget authority of congress under the current legal framework. To build credibility of the fiscal framework and establish a track record, staff argued that it was important to fully internalize the constraints of the FRL in the budget process.

Compliance with the FRL			
	2015	2016	
	Est.	Staff Proj.	Approved Budget
<i>(in percent of GDP, unless otherwise stated)</i>			
Total Revenue	18.1	18.0	20.1
Expense	17.3	17.3	18.4
Net Acquisition of non-financial Assets	2.6	2.7	3.3
Net lending/Borrowing	-1.7	-2.1	-1.5
Net lending/Borrowing (excl. bond financed capital expenditures)¹	-0.6	...	...
Real current primary expenditure growth (percent change), Staff²	4.7	2.2	8.2
Real current primary expenditure growth (percent change), Authorities³	6.2	...	-2.5
<i>Memo items:</i>			
Nominal GDP, G\$ bn.	146,566	158,409	162,819
Current primary expenditure (Central Government), G\$ bn	22,385	24,040	25,433

Sources: Authorities and staff calculations.

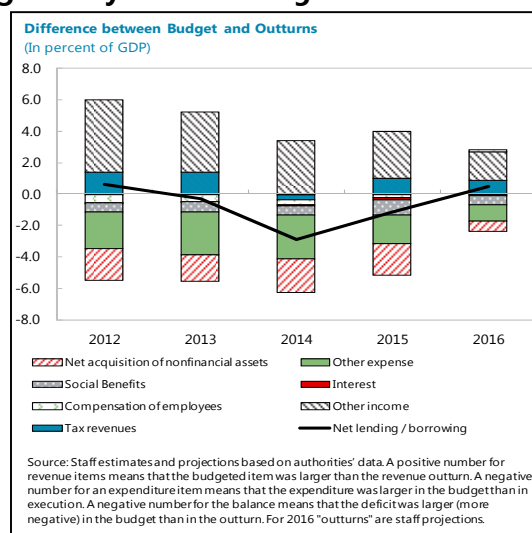
¹ Article 241 of the 2015 budget law (Ley 5.386/15) states that capital expenditure financed by sovereign bonds can be excluded from the calculation of the deficit ceiling in the FRL.

² Deflated using GDP deflator. Based on outcomes for 2015 and staff projections and approved budget numbers for 2016 for the central government.

³ Deflated using the mid-range of the CPI inflation target band. Follows authorities' methodology and compares current primary expenditure for the entire public sector in the approved budget for year t+1 to current primary expenditures in the prevailing budget as of June of year t.

19. In terms of fiscal outcomes, staff sees challenges this year in meeting the deficit ceiling.

While public investment spending is expected to be under-executed relative to the budget (due to ongoing implementation capacity constraints); those savings are likely to be outweighed by weaker-than-budgeted tax revenue. As a result, staff projects that the deficit will increase to around 2 percent of GDP in 2016, implying a broadly neutral fiscal stance. (Table 2 and Figure 3). Given that some fiscal tightening is likely needed, staff suggested that tightening current primary expenditures, while safeguarding needed public investment, would be advisable to avoid exceeding the FRL's deficit ceiling ex post by a wider margin. Authorities affirmed that they remain committed to restraining the growth of current expenditures, in particular compensation of employees in the public sector.



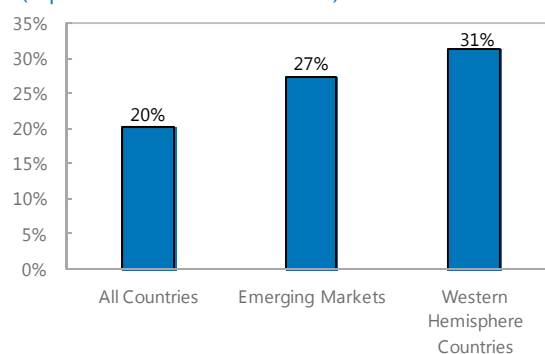
20. The mission urged caution when considering any modifications to the fiscal anchor.

The government strives to meet its constraints under the FRL in the budget, but is considering amending the law going forward given both design and implementation issues. This may include revisiting the deficit ceiling, moving to a structural balance rule, as well as reviewing the treatment of public investment in the numerical targets. Staff advised following a balanced approach in considering any reforms given important potential credibility and reputational costs to amending the framework. If changes are sought, staff recommended that reforms should balance credibility and flexibility considerations to avoid perceptions of dilution of the current law. Any modifications should be accompanied by concrete measures to strengthen fiscal institutions and preserve sustainability of public finances (See Box 2). For example, correction mechanisms can help cement the FRL as a credible fiscal anchor and ensure greater observance of fiscal targets over time. A transition to a new fiscal anchor though would also need to be carefully managed (see Selected Issues Paper).

21. Comparing the implications of alternative fiscal rules, based on the experience of other countries, was also part of this fiscal policy discussion.

A “golden rule”—to exclude, for example, public investment expenditure from the deficit ceiling—is part of fiscal rules in other countries in the region. However, such exclusions typically complicate the implementation of fiscal rules and can weaken fiscal discipline, and in some cases have led to higher public indebtedness (see Selected Issues Paper). If the authorities were to consider adopting a golden rule, staff argued that to mitigate risks to sustainability,¹⁰ a debt ceiling should be added to the existing framework (Box 2). A possible move towards a golden rule should also be accompanied by a number of other safeguards. In particular, authorities need to intensify efforts to enhance public investment management efficiency. If such changes were made, it would also be desirable to retain the current expenditure rule, which would contribute to achieve sustainability and would moderate some of the reputational costs of amending the FRL. Finally, the introduction of a structural balance rule would be a sensible approach to avoid procyclical policies, but staff believed it is likely to face implementation and communication challenges—including the estimation of unobservable variables such as the output gap and structural revenues.

Countries that Exclude Capital and Other Priority Expenditure from Rule, 2014
(In percent of countries with rule)



Sources: IMF Fiscal Rules Dataset.

¹⁰ The debt sustainability analysis presented in Annex IV shows that public debt is sustainable under current policies over the medium term.

Box 2. Paraguay: A Balancing Act: Reform Options for Paraguay's FRL

The Fiscal Responsibility Law, which came into force in 2015, was an important achievement toward strengthening Paraguay's fiscal framework. In addition to numerical targets, the law introduced elements of medium-term budgeting and greater transparency.

However, fundamental issues have emerged with respect to the law's implementation and design. First, there is some legal ambiguity surrounding the FRL given the fact that annual budget laws are on equal legal footing with the FRL. Thus, implementation of the FRL has proven complex with the annual budget law in 2015 affecting how deficit compliance would be assessed last year (the 2015 budget law excluded capital expenditure financed by sovereign bonds from the calculation of the deficit ceiling). Second, there is growing concern that under the current design of the rule, with its comparatively low deficit ceiling, capital expenditure plans may be constrained despite large infrastructure investment needs. Finally, the prevailing deficit ceiling (expressed in headline terms) and limited escape clauses can limit the space for countercyclical policies.

Consequently, the authorities are considering amending the FRL depending on the trade-offs involved with moving to an alternative fiscal rule. With improved implementation under the FRL in 2016, staff favored retaining the current deficit rule and establishing a solid track record of compliance, but also provided analysis of alternative fiscal rules to inform this discussion (See Selected Issues Paper). Specific alternatives considered included adopting a "golden rule" which excludes public investment from the deficit ceiling; increasing the headline ceiling; making the deficit rule more flexible by moving to a structural balance rule; and removing the deficit ceiling and effectively changing the FRL to an expenditure rule.

Staff analysis highlights that different fiscal rules offer certain advantages, but also various drawbacks. The general ranking of different rules with respect to debt trajectories is stable, but the composition of expenditures can vary significantly. For example, if the authorities decide to adopt a "golden rule", which is associated with the highest debt levels in staff simulations, strictly adhering to the current expenditure rule and adding a debt ceiling would be crucial for preserving fiscal sustainability. Furthermore, as practical experience has shown, a golden rule should be accompanied by efforts to enhance public investment management efficiency and public accounting to ensure correct classification of capital expenditures. If the authorities consider raising the headline deficit ceiling, efforts to strengthen the budgetary process and FRL provisions on sanctions and enforcement would help to cement the authorities' commitment to fiscal responsibility and alleviate concerns of dilution of the law. Should the authorities consider removing the deficit ceiling and keeping the existing expenditure rule, debt sustainability could be compromised in the absence of a debt ceiling, although international experience suggests that expenditure rules have better compliance.

Caution is thus warranted when considering changes to the fiscal anchor and a balanced approach is needed if amendments to the law are sought. To gain credibility, establishing a longer track record of compliance would be preferable to changing the rule at the outset. Potential modifications to make the fiscal rule more flexible should be accompanied by a number of safeguards that enhance credibility of the fiscal anchor.

The effectiveness of the FRL will ultimately hinge upon measures to strengthen legal and institutional aspects of the fiscal framework. Paraguay's public financial management system should be strengthened, particularly in terms of budgetary processes, public investment management framework, credible financial reporting and accounts, and additional fiscal transparency. From a legal perspective, the effectiveness of the FRL is limited, as per Constitutional law, congress appears not to be restrained from actions that modify the FRL. On the operational side, Paraguay's fiscal framework would benefit from the introduction of explicit correction mechanisms to address deviations from the fiscal rules, as well as the path back to compliance. More precise provisions on sanctions and enforcement would be welcome.

Transition to a revised fiscal framework would need to be carefully managed. Given the possibly large costs as well as high political sensitivity, any modification to the FRL needs to be carefully tested and communicated. If a transition to another rule is considered, care should be taken that all relevant stakeholders agree on and "own" the reform.

22. Authorities are also considering introducing an independent fiscal council to provide non-partisan evaluation of fiscal policy. The main objective of the envisaged council would be to assess fiscal policy, but it could also evaluate the fiscal forecasts undertaken by the Ministry of Finance. This would be particularly useful under a structural balance rule. The council would comprise reputable experts that would serve on a voluntary basis. Staff broadly welcomed this potential institutional change but noted that the international experience suggests that the mere

establishment of a fiscal council does not by itself lead to stronger fiscal performance.¹¹ Successful fiscal councils possess certain characteristics such as independence, adequate staffing, or high media impact.

23. Regarding the medium-term fiscal framework, staff emphasized further improving revenue collection and raising public investment as a share of spending. The authorities' three year fiscal plan presented with the 2016 Budget envisages a gradual fiscal consolidation, through

modest increases in tax revenues and significant reductions in grants and fixed investment. Staff believes that base broadening measures such as the recent extension of the VAT to cooperatives are a welcome effort to increase tax collection and more can be done to mobilize fiscal revenues.¹² The country's revenue authority (SET) has made good progress in strengthening institutional frameworks, tax payer registries and administrative capacity, but still faces

problems with tax compliance and enforcement.¹³ Compensation of employees continues to represent a relatively large share of total fiscal expenditures compared to regional peers, underlying the need for civil service reform (Figure 3), which would help create more fiscal space for public investment.

24. The mission also encouraged authorities to monitor and mitigate fiscal risks associated with the scale-up of public private partnerships. Projects already in the pipeline under this modality would amount to close to 2.5 percent of GDP. Nevertheless, Paraguay's PPP framework is relatively recent and the authorities have limited experience with implementation. Staff urged them to accelerate efforts to quantify and mitigate fiscal risks arising from contingent liabilities. Staff also recommended that project selection and implementation should be closely monitored to ensure that investment efforts are efficiently translated into a higher public capital stock.

Recent Revenue Collection Measures and Main Policy Recommendations

Recent Progress	Policy Recommendations
<p>Broadening of the tax base: Introduction of PIT (2013) and income tax on the agricultural sector or IRAGRO (2014). Extension of VAT to cooperatives (2016).</p> <p>Strengthening of tax collection: Improvements in taxpayers' registry. Organizational improvements in the tax revenue authority (SET). Progress on elaboration of new audit and enforcement strategies.</p> <p>Customs administration: Strong information and communications technology (ICT) systems are already in place.</p>	<p>Tax revenue administration: Strengthen legal procedures for imposing sanctions on tax evasion. Enhance legal mechanism to address revenue authority's staff corruption. Streamline procedures for registering taxpayers and policies for authorizing invoices. Improve filing procedures to increase compliance.</p> <p>Customs revenue administration: Enhance rules-based control procedures and transparency as well as better risk management. Development and implement the single-window system and move towards fully electronic records. Revisit administrative budget of the customs authority (DNA) to ensure that enough resources are available for investment in infrastructure.</p>

¹¹ Debrun, X. and Kinda, T. (2014) "Strengthening Post-Crisis Fiscal Credibility—Fiscal Councils on the Rise. A New Dataset" IMF Working Paper WP/14/58, April, Washington, D.C.

¹² According to authorities' estimates this extension is expected to yield additional revenues in the order of 0.2 percentage points of GDP.

¹³ Staff's medium-term fiscal forecast incorporates reforms in revenue administration and base broadening measures that could lead to an improvement in the tax revenue to GDP ratio of close to 1 percentage point.

25. Paraguay's fragmented and unregulated pension funds do not effectively mobilize national saving to finance investment or help develop local capital markets. Meanwhile, actuarial and operational deficits pose substantial risks to public finances through contingent liabilities.¹⁴ Given high levels of informality, coverage is estimated to be very low. Currently, most pension fund resources are simply held as deposits in the banking system, in part because of a lack of legal clarity regarding alternative investment options. Enacting the draft law creating a pension regulator and expanding portfolio management options for pension funds will be instrumental in tackling some of these challenges, but additional efforts will also be needed to address long-term financial sustainability concerns, including parametric reform. The authorities broadly shared this assessment and noted entrenched interests in the pension industry impede reforms.

26. Authorities recognize the main fiscal challenges identified by staff and remain committed to moving ahead with initiatives despite political economy constraints. On civil service reform, authorities are working on amending the Civil Service act with support from the United Nations Development Program (UNDP) to build on changes initiated with the introduction of the new salary scale in 2015. The government will also continue to pursue efforts to enhance domestic tax revenue mobilization with technical assistance support from the IMF. Authorities also pointed to recent successes in combating and dismantling large tax evasion schemes. Authorities acknowledged their limited experience in the management of PPPs and are requesting further technical assistance in quantifying and mitigating risks from contingent liabilities associated with these projects. Finally, pension reform is a politically sensitive issue and authorities have opted for a gradual approach, where the approval of legislation creating the pensions regulator through congress would be an important first step. Subsequently, policy measures to address longer term sustainability concerns could then be contemplated.

C. Monetary and Exchange Rate Policy: Reinforcing the Inflation Targeting Regime

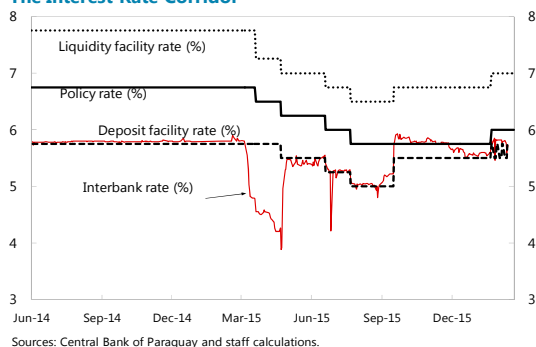
27. Staff and the BCP concurred that accommodative monetary policy remained appropriate given external risks. The policy rate was maintained at 6 percent through March in light of the uncertain international economic context and the view that inflation pressures are contained and inflation expectations anchored (Figure 2). Staff assesses the monetary stance as still accommodative considering that the policy rate remains at the lower end of its historical range and is slightly below the BCP's estimate of the neutral rate. Staff views this stance as broadly appropriate and expects inflation to decline to the mid-point of the target range over the course of 2016.

¹⁴ The system comprises eight defined-benefit funds with independent administrative structures, the largest of which are the Instituto de Prevision Social (IPS) (serving private sector workers through mandatory contributions) and Caja Fiscal (which focuses on civil servants). In addition to pension benefits, IPS also provides health services funded by mandatory contributions. The actuarial study for IPS indicates that it could face operational imbalances as early as 2032. Authorities estimate that the present value of the actuarial deficit of the Caja fiscal fund would amount to between 40 to 50 percent of GDP. Among the remaining smaller pension funds, Caja Itaipu and Caja Ande also present actuarial deficits that combined would amount to close to 4 percent of GDP.

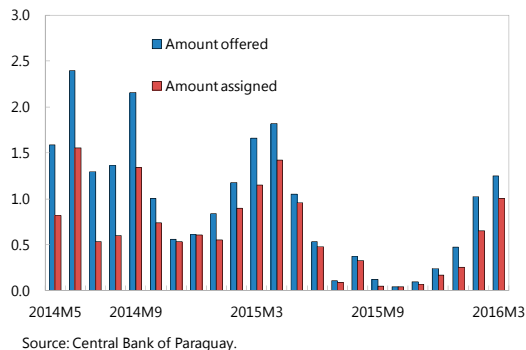
28. The BCP has improved monetary policy operations in pursuit of its inflation objectives.

During the course of 2015, the interest rate corridor around the monetary policy rate (MPR) has been narrowed by lifting the floor to 5.5 percent. At the same time, the central bank increased issuance of monetary regulation instruments (IRMs), used for repos, and reduced the rejection rate of bids in order to steer the overnight rate above the floor of the corridor towards the MPR.

The Interest Rate Corridor



Instruments of Monetary Regulation (IRMs)
(In trillions of Guaraní)



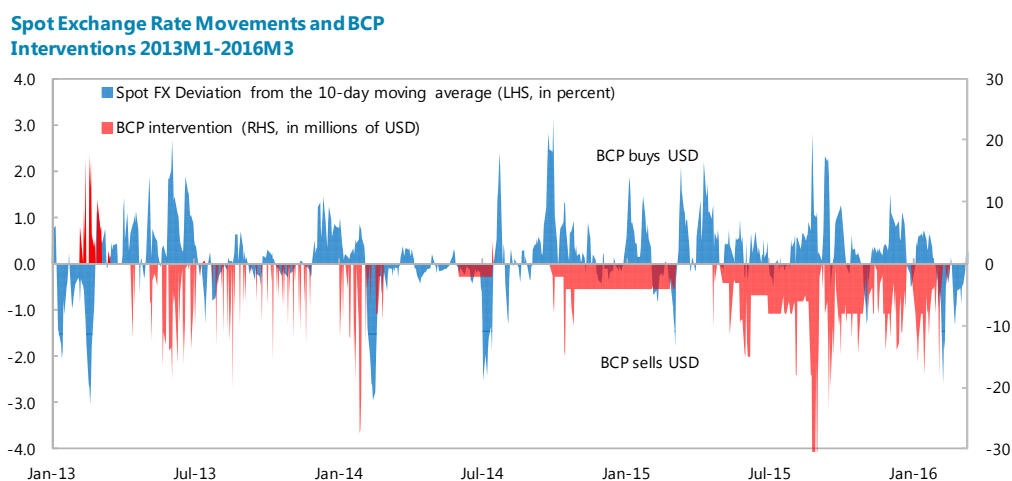
29. Nevertheless, the monetary policy framework can be further reinforced. The mission reiterated some earlier recommendations by staff to further develop interbank markets to improve monetary policy operations and strengthen the policy transmission mechanism through the MPR. This includes widening the set of private counterparties (beyond banks) who can trade short-term liquidity instruments; further discouraging the use of the overnight facility where banks allocate their excessive reserves; improving liquidity analysis and forecasting including of the impact of foreign exchange intervention; and gradually promoting de-dollarization. The latter can include considering macro-prudential measures that introduce differential requirements for dollar loans and deposits.

30. Large FX interventions can interact with regular monetary policy operations and objectives. In September 2015, the BCP conducted discretionary interventions to support the guaraní in response to high market volatility, in addition to regular pre-announced sales of dollars associated with the sterilization of government receipts. The amount of dollars sold through the pre-announced sales also exceeded the dollar amounts purchased from the government. Foreign exchange intervention activity is reported transparently by the central bank. With respect to monetary policy, interventions in the FX markets can affect the operation of the interest rate corridor through the functioning of the interbank market, and ultimately the relative price of FX lending. Depending on the macroeconomic circumstances and market conditions, intervention can thus generate movements in interest rates that may create tensions with policy objectives within the inflation-targeting regime.

31. Staff recommended limiting interventions in the foreign exchange markets to exceptional circumstances. Discretionary interventions should be limited to countering possible disorderly market conditions. These are situations in which the exchange rate stops working as a shock absorber and markets stop operating normally. To further reinforce the interest rate as the

main policy instrument, the BCP should maintain predictable, rules-based dollar sales of government receipts avoiding frequent adjustments to the amounts to be sold and temporary suspensions. Clear communication of the central bank's approach to discretionary intervention may help reinforce the primacy of the inflation-targeting regime and reassure markets. Finally, developing a liquid FX market is an important requirement for a floating exchange rate regime to allow normal fluctuations in demand and supply without disorderly situations (e.g., liquidity running short and markets becoming suddenly one-sided). Avoiding frequent regulatory changes and tight limits on FX operating positions would be helpful in this regard.

32. Authorities broadly agreed with many of staff's recommendations which they believed were consistent with their policy approach. The BCP agreed on the objective of further improving the monetary framework, interbank markets and liquidity forecasting. The central bank stressed that it does not target an exchange rate level in its FX interventions, evident in the fact that the exchange rate depreciated by about 25 percent against the U.S. dollar in 2015. The BCP emphasized that foreign exchange market interventions are made only during exceptional situations of excessive market volatility. For example, the central bank commented that its "complementary" operations (i.e., those beyond its pre-announced dollar sales) in foreign exchange markets last year were motivated by risks of disorderly market conditions. As a result of their discretionary nature, the authorities argued that these types of interventions were difficult to constrain to a predetermined set of rules.

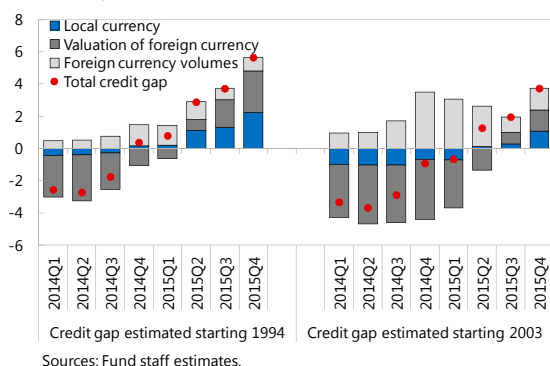


Source: Central Bank of Paraguay.

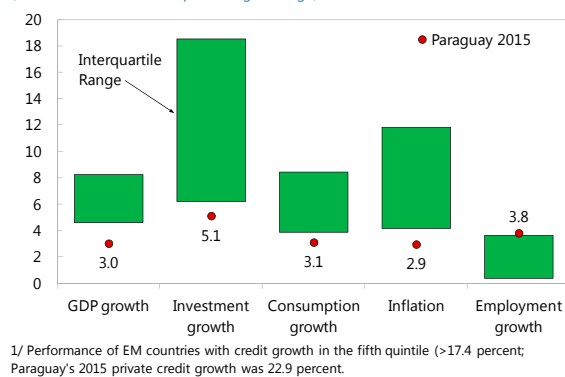
D. Financial Sector Policy: Containing Potential Risks

33. Rapid credit growth partly reflects an extended period of financial catch up and deepening though these effects may be waning. Much of the striking 26½ percent annual average growth in private sector credit over the past decade reflects improved financial stability and macroeconomic fundamentals. With expansion taking place in all broad economic sectors, a large portion of the growth appears attributable to structural factors. Currently, the stock of private credit outstanding is broadly in line with peers with similar per-capita income levels. However, in 2015, economic outcomes were moderate relative to other countries that have experienced high credit growth, suggesting that lending might be running ahead of fundamentals. Similarly, credit gap estimates have turned strongly positive in recent quarters (see Selected Issues Paper).

Credit Gap Estimates, by Component
(Percent of GDP)



Fundamentals of Countries with High Credit Growth
(Percent, variables in real percentage change)



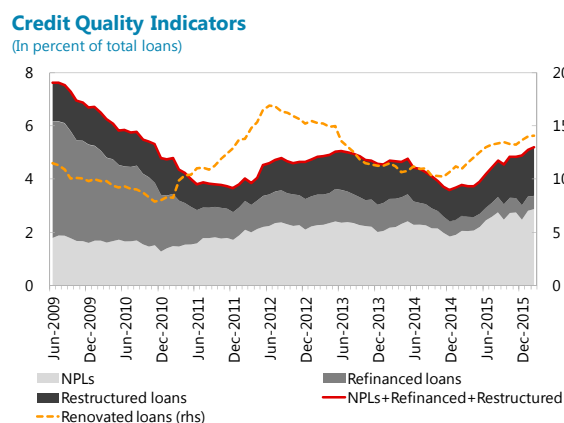
34. At present, certain characteristics of the Paraguayan banking system were helping to contain risks. Both assets and liabilities are split roughly evenly between local and foreign currency denominations, helping to reduce the potential for currency mismatches in the banking system. Risks of an exchange rate driven deterioration in borrowers' ability to repay loans also appeared limited. Natural hedges appeared broadly evident in the sectors that borrowed in FX, with modest shares of borrowers reporting that they lacked income in the currency of the loan. Liquidity risks appeared relevant, given banks' heavy reliance on short-term funding sources, which is reflected in high-interest margins, and a relatively small interbank market; however, large liquid asset holdings could provide safeguards.

35. The framework for financial supervision and regulation is being strengthened. In particular, the authorities have a project to introduce risk-based financial supervision, which has entailed recent actions in various areas:

- *Legislation.* A draft banking law would grant additional powers to the BCP and facilitate the revised regulatory framework. The authorities indicated that passage was a priority and expressed optimism that congressional approval could happen this year. Banks expressed concerns about enhanced BCP powers to revise capital requirements that may cause disruption and regulatory uncertainty. To limit this possibility, continued clear communication will be needed.

- *Capacity building.* The Superintendence of Banks has been receiving technical assistance in a number of areas to better track credit, market, and liquidity risks; assess bank risk profiles; and improve stress testing. Progress has occurred on several fronts, although going forward, additional resources with respect to staffing and information technology may be necessary.
- *Financial stability council.* The authorities plan to introduce a consultative Council of Financial Stability, composed of a high-level committee with the heads of the BCP, Ministry of Finance, and the regulator of cooperatives, INCOOP, and supporting subcommittees.¹⁵ Staff welcomed these steps, noting that good institutional arrangements and adequate information sharing would be essential.

36. Going forward, staff sees scope for enhanced vigilance, particularly with respect to credit. External conditions, including from agricultural product prices, which appear to influence credit quality, are set to remain difficult for some time and could boost already rising nonperforming loans. While loan renegotiations, aided by BCP's temporary relaxation of regulations, may have provided some relief, future potential shocks, for example, those related to the weather, could compound vulnerabilities. Reflecting these risks, staff saw merit in tracking an alternative broader measure of borrower distress, which is composed of nonperforming loans as well as refinanced and restructured loans. The authorities also have plans to strengthen their assessment of risks, including through systemic stress testing in the context of the financial stability council's work.



37. Macroprudential measures can help contain financial sector risks. In particular, to encourage gradual de-dollarization in the banking sector and reduce potential for currency mismatches, staff noted a possible role for differentiated risk weightings or provisioning requirements. For deposits, FX risks could be mitigated by further raising already higher reserve requirements. In addition to the financial stability benefits, these measures could further bolster the inflation targeting regime and monetary policy operations more generally to the extent that de-dollarization is encouraged. Outside of currency risks, the authorities could address potential vulnerabilities from rapid credit growth more directly by introducing regulations related to loan-to-value measures. With respect to liquidity risks, the authorities are working on an ongoing project to construct appropriate liquidity ratios for supervised institutions.

¹⁵ The subcommittees would have responsibility for microsupervision, macro-financial stability, and crisis preparedness.

38. Closer oversight in certain areas would also help prevent a build-up of financial vulnerabilities. In some cases, data gaps needed to be closed, while in others strengthening oversight appeared warranted in staff's view:

- *Cooperatives.* This sector, which reported assets of around 8 percent of GDP as of August 2015, showed higher rates of credit impairment relative to banks (8.6 percent in the largest cooperatives).¹⁶ Characteristics of the credit unions' accounting make it difficult to assess capital adequacy. Nevertheless, the sector's regulator, INCOOP, maintains a monitoring system for compliance—based supervision and specifies corrective actions for breaches of norms. The authorities indicated that they were continuing a project to introduce deposit insurance, which should lead to a process of verifying institutions' health before joining the deposit guarantee fund.
- *Consumer and corporate lending risks and other credit intermediaries.* Ongoing projects, including the Credit Registry, could be leveraged and strengthened to provide a wider range of indicators to assess risks from the household and business sectors. Additionally, reports indicated increasing use of alternative credit intermediaries operating outside of the regulatory perimeter. Close monitoring appeared warranted given concerns over adequate consumer protection as well as the potential for risks to shift away from supervised institutions.
- *Real estate markets.* Reports indicated elevated commercial real estate prices, but decreasing agricultural real estate prices. Staff advised addressing data limitations, which prevent a full assessment of property valuations, rents, and occupancy rates, particularly in light of the widespread usage of real estate to secure loans.

39. The authorities concurred with the need for close financial sector vigilance, although they viewed the rapid credit growth as constituting a lesser risk than staff. In their view, continued rapid local currency growth reflected the relative resilience of the Paraguayan economy, while FX lending growth was distorted by valuation effects. The authorities underscored the priority they attached to the banking law, noting that its passage would broaden their ability to introduce macroprudential measures. On specific macroprudential tools, the authorities noted that identifying an appropriate liquidity ratio measure was a priority, and were open to differentiating risk weights or provisioning requirements; reserve requirements appeared to them as having less relevance. With respect to institutional and information sharing agreements, the authorities emphasized the already good cooperation that existed without the need for formal processes and the consultative process with regards to the draft new banking legislation.

¹⁶ The credit impairment measure is for Type "A" cooperatives, which have assets above 50 billion *guaranies*.

STAFF APPRAISAL

40. Authorities have advanced their structural reform agenda in several areas and important steps have been taken to strengthen transparency and governance. Progress is being tracked through internal scorecards measuring delivery of final goods or services toward meeting social objectives. Infrastructure—notably, improving electricity distribution and transportation—remains a priority. Implementation of the Law of Free Access to Public Information is welcome as having established greater transparency in public processes and greater engagement with civil society, an important step to improve the quality of institutions in Paraguay on a lasting basis.

41. Monetary policy remains appropriately accommodative given the uncertain international context and contained inflationary pressures. Staff expects inflation to decline to the mid-point of the inflation target range by the end of 2016. On the external front, the current account balance is projected to remain in deficit as lower commodity export prices and weaker economic activity in trading partners weigh on export performance. Staff continues to assess the currency and external position as being broadly in line with fundamentals, given changes in the external environment. Reserves remain broadly adequate and exceed the IMF's standard adequacy metric for floating exchange rate economies. Ample reserve coverage is appropriate for Paraguay considering the economy's openness, significant dollarization, and high vulnerability to weather and commodity price shocks.

42. There are clear signs of increased effectiveness of the fiscal responsibility law, but it is important that its ceilings are fully internalized in the budget process. This will help establish a track record and solidify the credibility of the fiscal framework. In 2016, tax revenues are likely to be weaker than expected in the budget, while investment expenditure is expected to be under executed due to persistent implementation capacity constraints. As a result, staff projects a broadly neutral fiscal stance for the year (although the fiscal deficit will exceed the FRL limit). In that context, tightening current primary expenditures would be advisable to avoid exceeding the FRL's deficit ceiling by a wider margin, while safeguarding public investment.

43. Caution is warranted when considering any changes to the fiscal responsibility law. There are potentially important reputational costs to amending the fiscal framework, given the short track record of compliance. If amendments to the law are sought, authorities would be better served by following a balanced approach to any reforms. Modifications to the framework to make the fiscal rules more flexible should be accompanied by a number of safeguards that enhance credibility of the fiscal anchor. In terms of transition, changes to the fiscal anchor would need to be managed and communicated carefully and should be accompanied by concrete measures to strengthen fiscal institutions and preserve the sustainability of public finances. On the operational side, Paraguay's fiscal framework would benefit from the introduction of explicit correction mechanisms to address deviations from the fiscal rules, as well as a path back to compliance.

44. Monetary policy coupled with a flexible exchange rate should be the principal tool if growth were to weaken further, within the limits of meeting the central bank's price stability objective. Certain reforms could help reinforce monetary policy effectiveness. In particular, creating conditions for the expansion of interbank and secondary markets could improve the transmission of monetary operations. In addition, limiting foreign exchange market interventions to exceptional circumstances would help reinforce the primacy of the inflation-targeting regime and reassure markets.

45. The financial system appears to be sound and authorities are moving forward with efforts to enhance financial supervision, including through introducing legislation to strengthen risk-based supervision. Additional key areas of progress have been related to developing monitoring tools and strengthening capacity to monitor credit and liquidity risk. To build upon these gains, key priorities going forward include continuing to upgrade monitoring and analytical capacity as well as strengthening institutional arrangements, and ensuring adequate resources to perform these functions.

46. Other actions could help ensure that market, liquidity and credit risks remain contained in an environment of challenging external conditions. Reducing still-elevated financial sector dollarization gradually, including through macroprudential instruments (such as raising capital and provisioning requirements for foreign currency loans) could help limit financial risks from exchange rate fluctuations and possibly curb the need for foreign exchange interventions. To counter risks emanating from somewhat weaker credit quality, particular scrutiny is warranted in examining banks' loan classification and provisioning to ensure stronger buffers. Additionally, the supervisor of the cooperative sector could be strengthened.

47. Authorities continue to strengthen anti-corruption and AML/CFT measures to improve the business climate. The recent passage of laws on freedom of information and asset declaration are positive developments. Robust use of AML/CFT tools related to politically exposed persons and suspicious transaction reporting can also support efforts to address corruption risks. Authorities are encouraged to progress on amendments to the AML/CFT law in line with international standards.

48. It is recommended that the next Article IV consultation be held on the standard 12-month cycle.

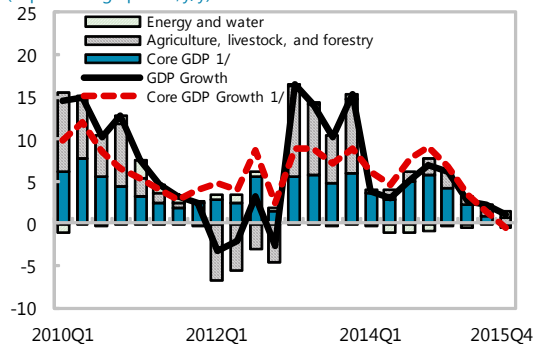
Figure 1. Paraguay: Real Sector Developments, 2010–16

Growth in Paraguay has moderated further in 2015,

but is still buoyed by relatively strong domestic demand.

Contribution to Output Growth by Sector

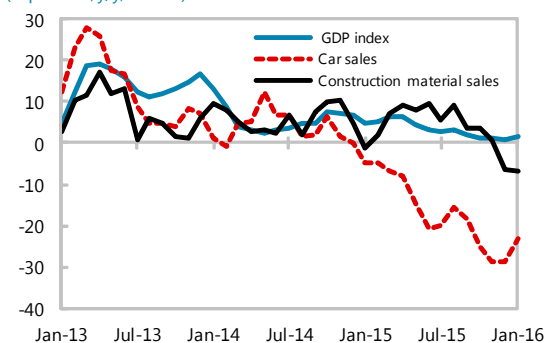
(In percentage points, y/y)



Higher frequency data point to a loss in momentum towards the end of the year, but growth is still positive.

Monthly Economic Activity Indices

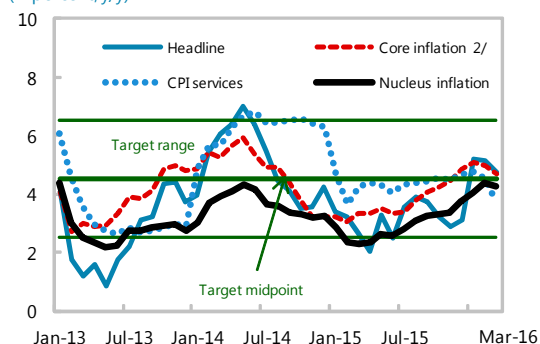
(In percent, y/y, 3mma)



with headline inflation above the 4.5 percent target, but still well within the range...

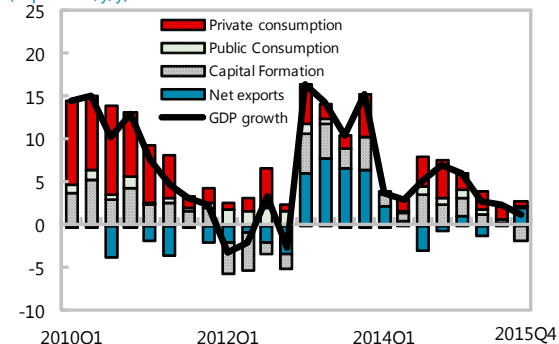
CPI Inflation

(In percent, y/y)



Aggregate Demand Growth Decomposition

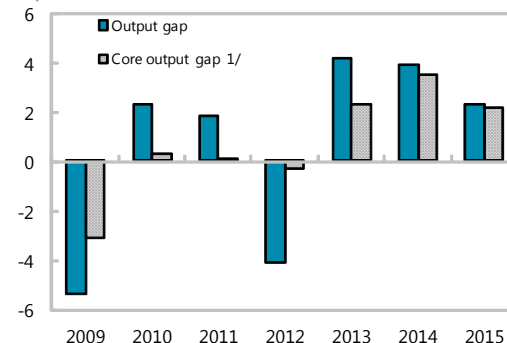
(In percent, y/y)



Despite the recent growth slowdown, the economy is still slightly above potential,

Output Gap

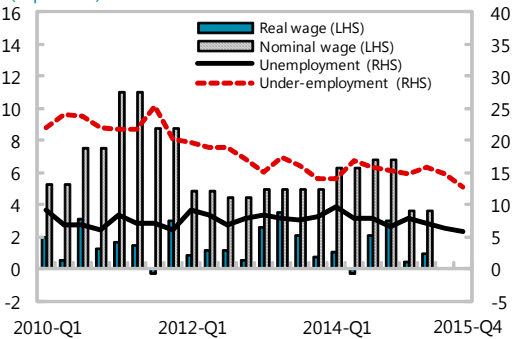
(In percent of trend GDP, HP filter)



... and robust labor markets with continued real wage growth.

Unemployment and Wages

(In percent)



Source: IMF staff calculations based on authorities' data.

1/ Core GDP excludes agriculture, livestock and forestry as well as energy and water.

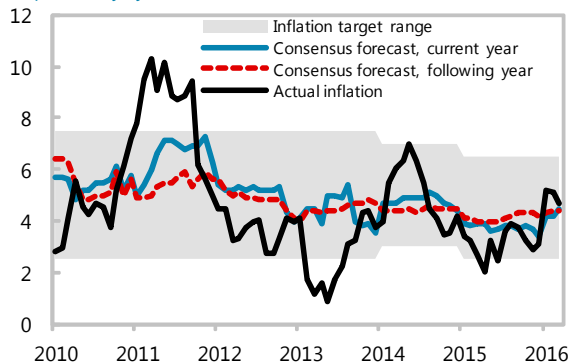
2/ Excludes fruits, vegetables, administered prices, and fuels.

Figure 2. Paraguay: Monetary Developments, 2010–16

Inflation expectations remained anchored and inflation remains in the target range...

Actual and Expected Inflation

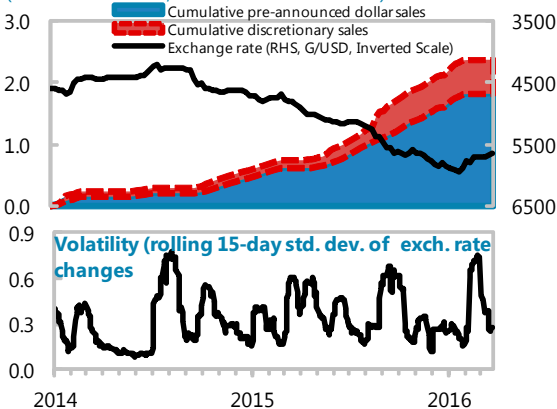
(In percent, yr/yr)



Periodic rises in volatility have resulted in a higher degree of FX market intervention, although the guarani has depreciated in 2015.

Exchange Rates, Volatility and FX Interventions

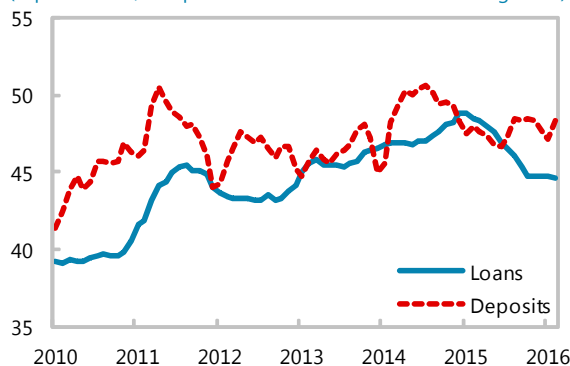
(In billions of USD, unless otherwise stated)



... gradual de-dollarization in the banking sector, which currently reports large shares of foreign currency loans and deposits..

Dollarization of Loans and Deposits

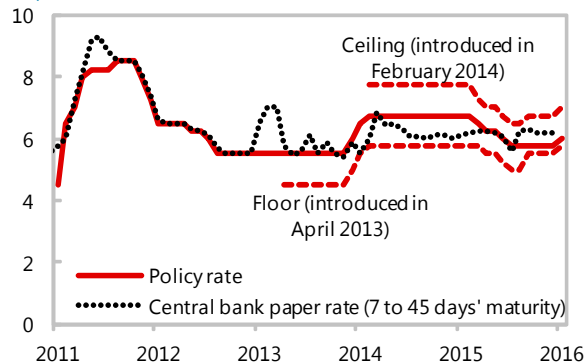
(In pct of total, computed at constant Nov. 2014 exchange rate)



The BCP has only partly reversed its easing, and altered the interest rate corridor to improve monetary policy efficiency.

Central Bank Interest Rates

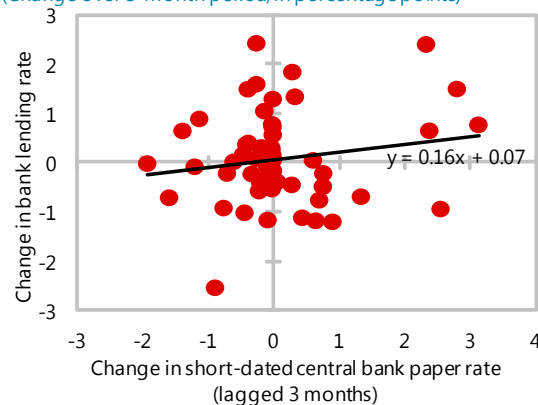
(In percent)



A stronger framework to improve monetary policy transmission may help to encourage...

Interest Rate Pass-Through, April 2011-January 2016

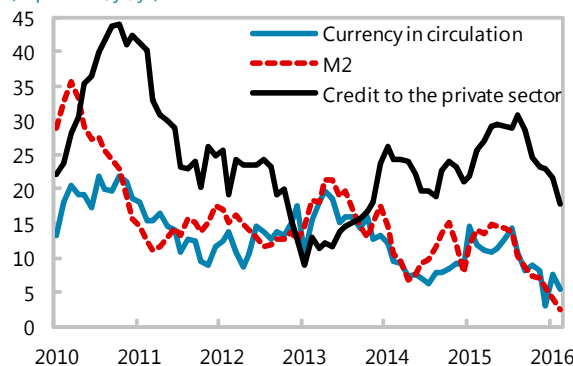
(Change over 3-month period, in percentage points)



The rapid expansion of credit has slowed from its peak earlier this year.

Monetary Aggregates

(In percent, yr/yr)

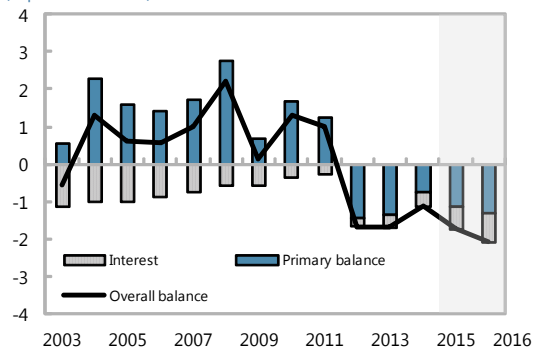


Sources: Central Bank of Paraguay; Bloomberg; Consensus Foreceasts; Haver Analytics; and Fund staff calculations.

Figure 3. Paraguay: Fiscal Sector Developments

The central government switched into deficit in 2012, after an extended period of fiscal surpluses...

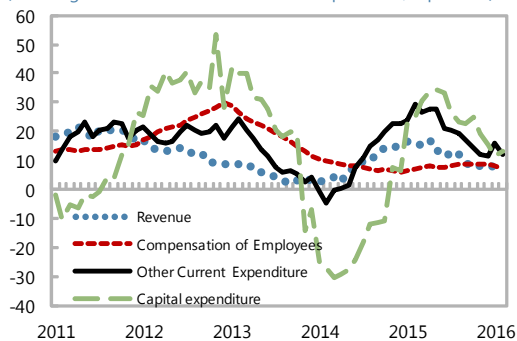
Central Government Overall Balance
(In percent of GDP)



Accelerated spending execution in 2015 and lower than expected tax revenue has caused the headline deficit to widen...

Central Government Operations

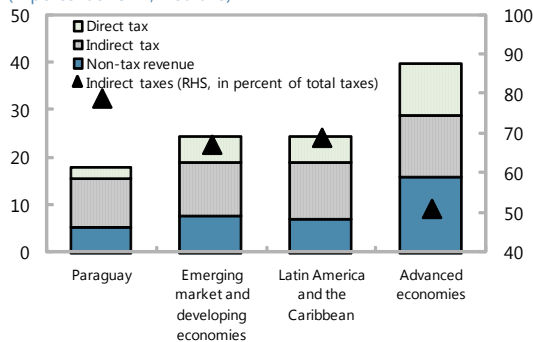
(Annual growth of cumulative 12-month operations, in percent)



Paraguay's tax revenue remains modest by international standards, and tilted toward indirect taxes...

General Government Revenue Structure, 2014

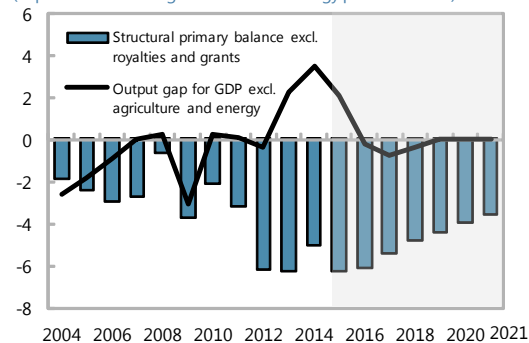
(In percent of GDP, medians)



... but over the medium-term staff expects the fiscal stance to be tightened.

Fiscal Policy over the Business Cycle

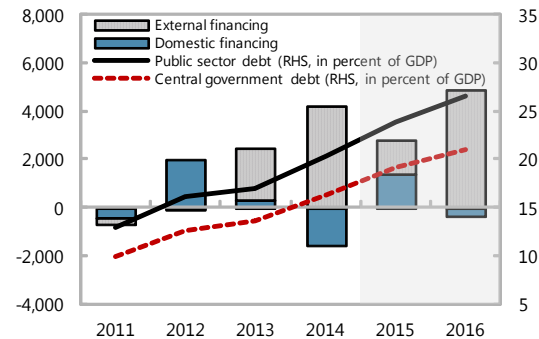
(In percent of non-agricultural non-energy potential GDP)



...leading to an increase in public debt that was compounded by exchange rate depreciation.

Public Sector Financing and Debt

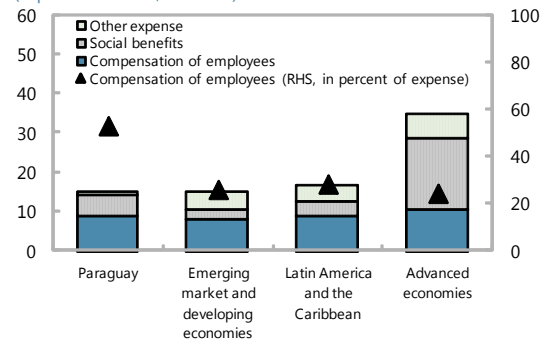
(In billions of Guaranis)



... while wages account for an outsized share of expenditure.

General Government Expenditure Structure, 2014

(In percent of GDP, medians)

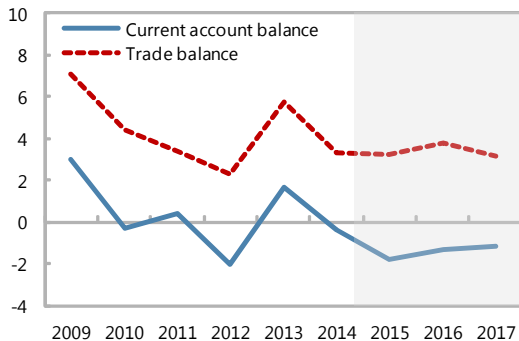


Sources: Paraguayan authorities; IMF, *World Economic Outlook*; World Bank, *World Development Indicators*; and IMF staff estimates and projections.

Figure 4. Paraguay: Balance of Payment Development, 2009–17

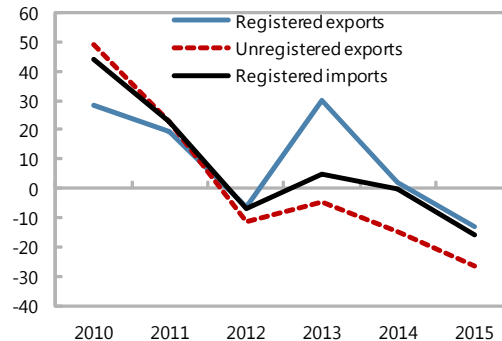
The current account deficit widened in 2015...

Current Account and Trade Balance
(In percent of GDP)



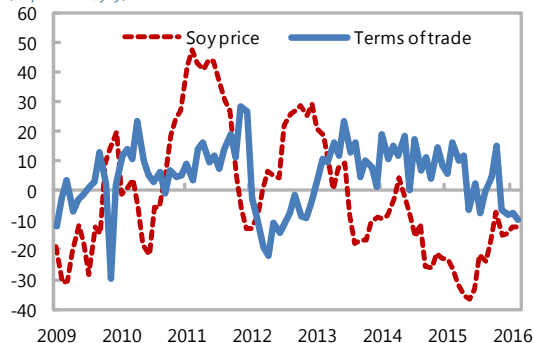
... driven by slowdown in commodity exports and re-exports, amid weak trading partner activity and...

Growth in Registered and Unregistered Trade
(In percent, y/y)



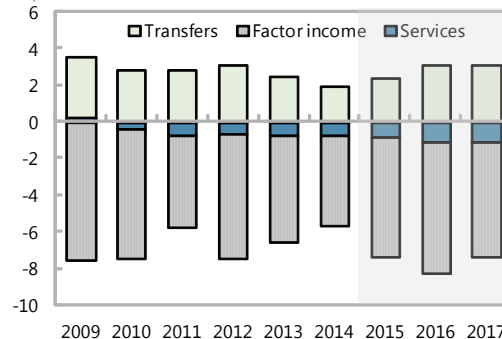
... and lower prices for soy, Paraguay's main export product, although cheaper oil will limit the worsening of the terms of trade.

Terms of Trade and Soy Prices
(In percent, y/y)



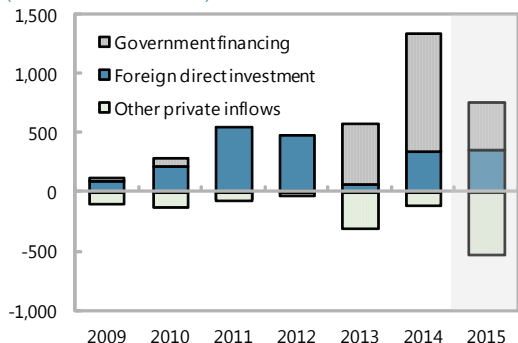
The service and transfer balances should broadly remain stable, while outbound factor payments are projected to grow.

Current Account Components
(In percent of GDP)



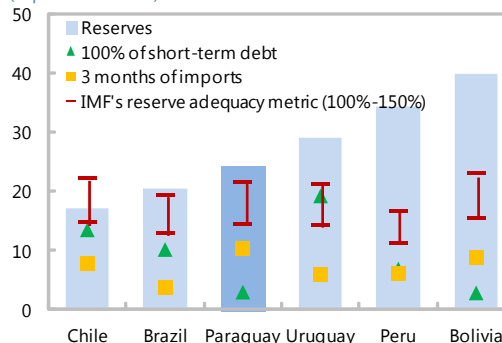
With significant financial inflows in 2014, linked to the issuance of a government bond, reserves have decreased in 2015...

Net Capital Inflows
(In millions of U.S. dollars)



... but somewhat still exceed the typical adequacy range, though less so than in other partially dollarized economies in the region.

Adequacy of International Reserves, 2015
(In percent of GDP)

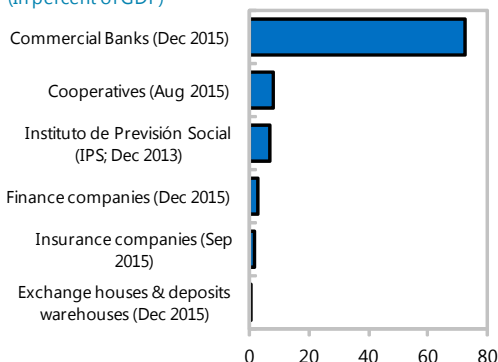


Sources: Central Bank of Paraguay; and IMF staff calculations.

Figure 5. Paraguay: Financial System Structure and Performance

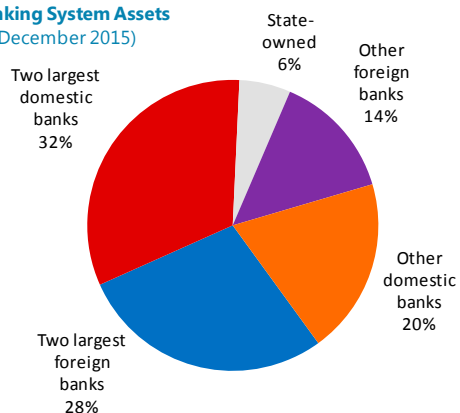
Paraguay's financial system is dominated by commercial banks...

Assets of Selected Financial Sectors in Paraguay
(In percent of GDP)



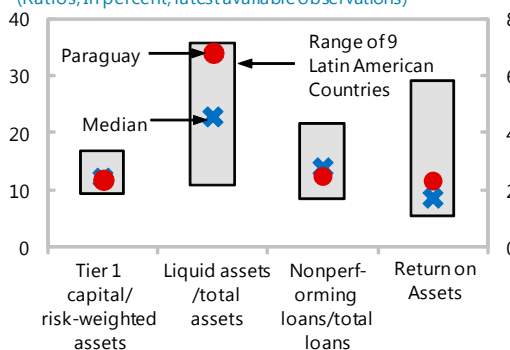
The banking system is concentrated, with foreign banks having a substantial presence...

Banking System Assets
(At December 2015)



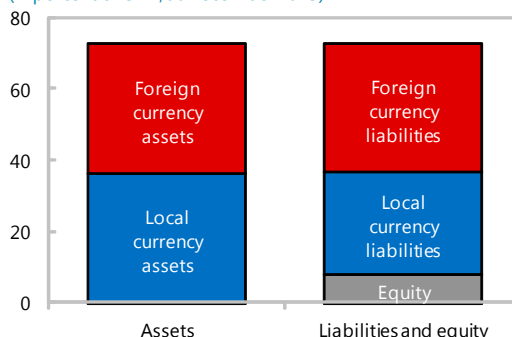
... which report adequate capitalization, strong liquidity, moderate NPLs, and good profitability, compared to the region.

Financial Soundness Indicators
(Ratios, In percent, latest available observations)



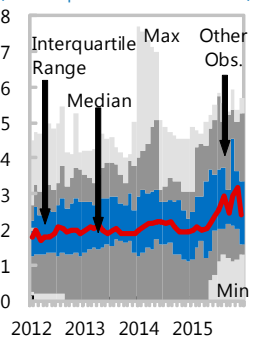
... and balance sheets are heavily dollarized.

Balance Sheet of the Banking Sector, by Currency
(In percent of GDP, at December 2015)

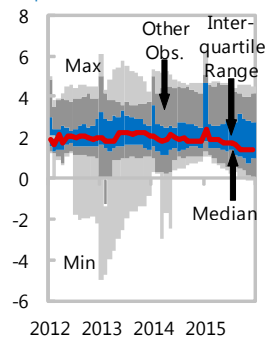


Recently, loan quality has deteriorated a bit, as has profitability, reflecting added provisioning expenses, while net interest margins remain high.

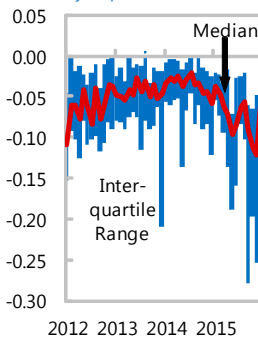
Distribution of NPLs
(NPLs in percent of total loans)



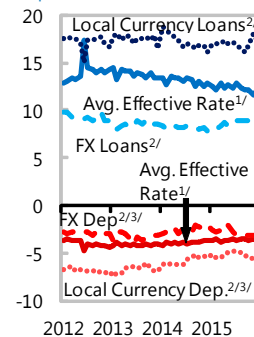
Distribution of ROA
(In percent of total assets)



Provisioning Expenses
(Monthly, in percent of assets)



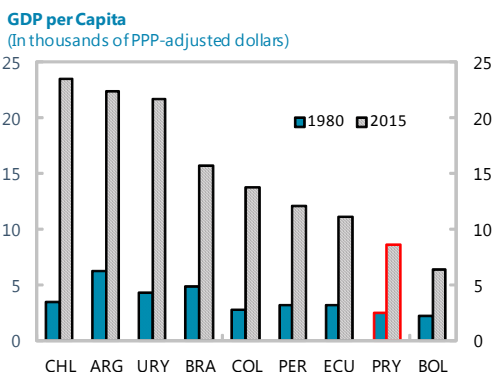
Interest Rates
(In percent)



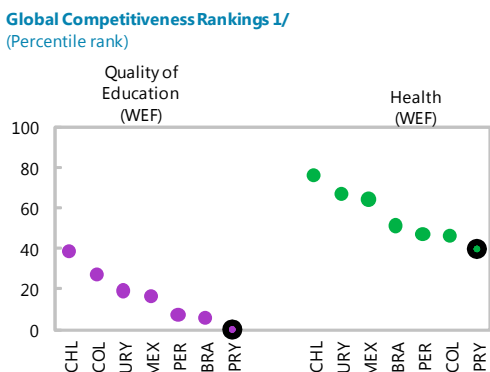
Source: Superintendencia de Bancos, Banco Central del Paraguay, Haver Analytics, and Fund staff estimates and calculations.
 Note: Regional aggregates represent Argentina, Brazil, Chile, Colombia, Costa Rica, Ecuador, Mexico, and Peru. Regulatory data are not consistently defined across countries.
 1/ Calculated from bank-by-bank data. 2/ As reported in Stat. Annex. 3/ Simple average of FX Sight, Time, and CD rates.

Figure 6. Paraguay: Long-Term Growth and Social Outcomes

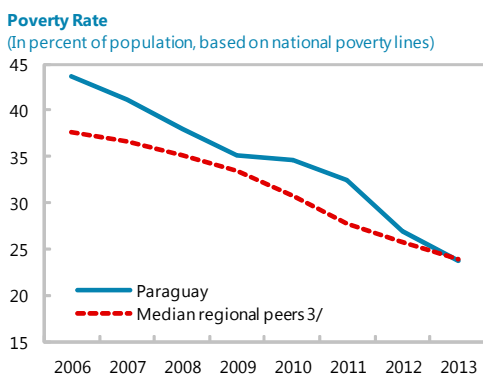
Over the last 35 years, Paraguay has fallen behind its peers in terms of GDP per capita...



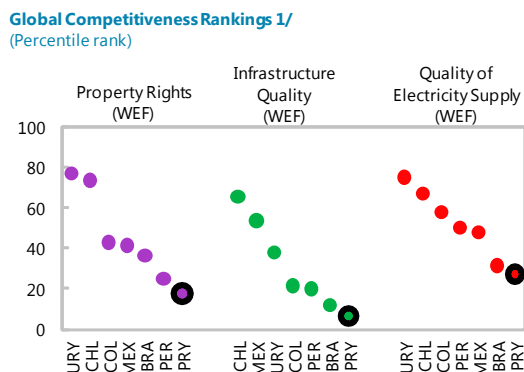
...and low levels of quality of education and health.



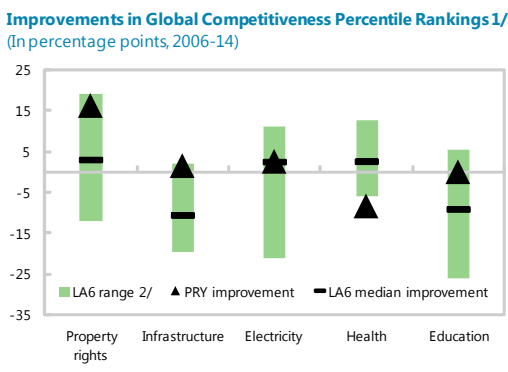
...and has consistently lowered poverty rates,



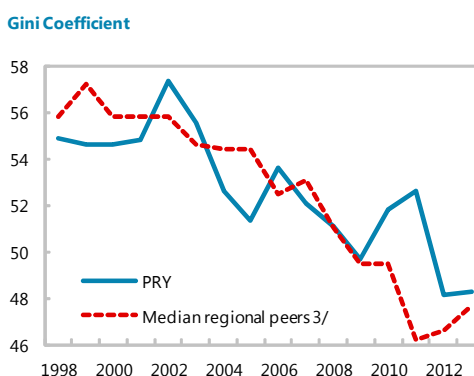
...and is characterized by relatively poor property rights, low quality of infrastructure and electricity supply...



More recently, Paraguay has been catching up, with significant improvements in many of these areas...



...and inequality.

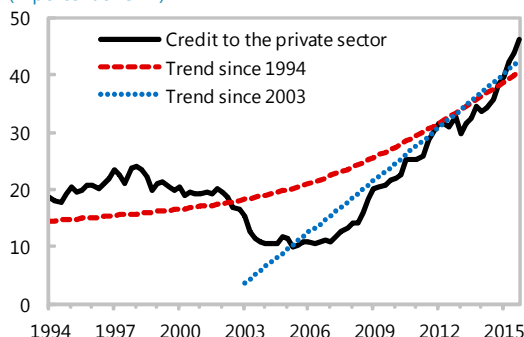


Sources: IMF, *World Economic Outlook*; World Economic Forum, *Global Competitiveness Report (2015-16)*; World Bank, *World Development Indicators*; UNDP Human Development Report; and Fund staff calculations.
 1/ The scale reflects the percentile distribution across all countries in the respective survey; higher scores reflect higher performance; WB: World Bank; WEF: World Economic Forum.
 2/ LA6 includes Brazil, Chile, Colombia, Mexico, Peru and Uruguay.
 3/ Includes Argentina, Bolivia, Brazil, Chile, Colombia, Ecuador, Peru, and Uruguay. Poverty rate data exclude Argentina.

Figure 7. Paraguay: Credit Developments

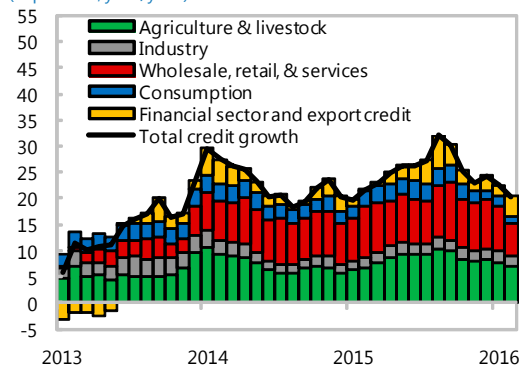
Credit growth has been strong for the past decade...

Credit to the Private Sector (In percent of GDP)



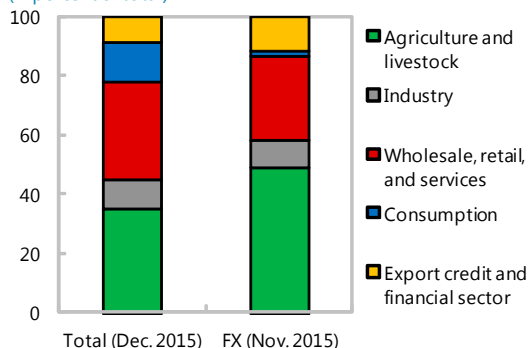
Credit growth has been strong across most sectors...

Contributions to Credit Growth (In percent, year/year)



Total and FX credit is largely directed towards the agriculture sector...

Credit, by Economic Sector (In percent of total)

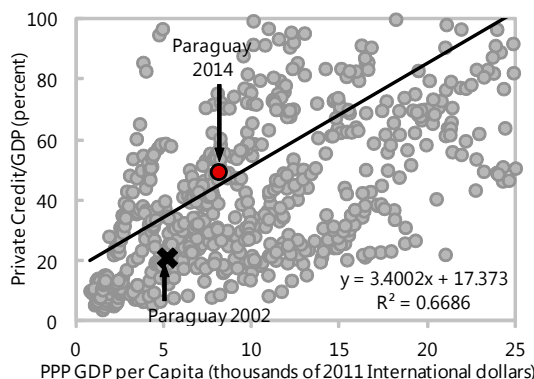


Sources: Superintendencia de Bancos; Banco Central del Paraguay; World Development Indicators; World Economic Outlook; Haver Analytics; and Fund staff estimates and calculations.

1/ The fitted line is estimated with a world sample of 98 non-fuel exporting countries over 2000-14 (depending on data availability), although for illustrative purposes, only countries with real GDP per capita (2011 international dollars) of up to \$25,000 and credit/GDP of up to 100 percent of GDP are shown.

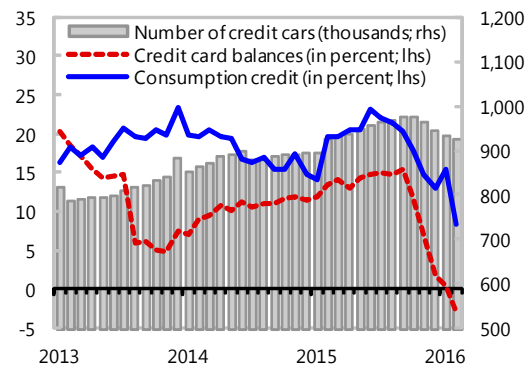
... in part reflecting financial catch-up, with credit now in line with peers with similar levels of per-capita income.

GDP per capita and Private sector credit^{1/}



... but a recent credit card law may have slowed growth in consumer credit.

Credit Card and Consumption Credit Indicators



... which is adjusting to a new reality of much lower prices for its products.

Changes in Agriculture Credit and Soybean Prices (In percent, year/year)

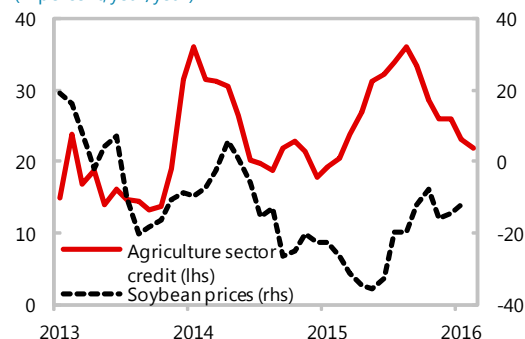


Table 1. Paraguay: Selected Economic and Social Indicators

I. Social and Demographic Indicators								
Population 2014 (millions)	6.9					Gini index (2014)		48.0
Unemployment rate (2014)	6.0					Life expectancy at birth (2013)		72.0
Percentage of population below the poverty line (2014)	22.6					Adult illiteracy rate (2014)		5.4
Rank in UNDP development index (2014)	112 of 186					GDP per capita (US\$, 2014)		4,481
II. Economic Indicators								
	2010	2011	2012	2013	2014	Est. 2015	Proj. 2016	Proj. 2017
(Annual percent change, unless otherwise indicated)								
Income and prices								
Real GDP	13.1	4.3	-1.2	14.0	4.7	3.0	2.9	3.2
Nominal GDP	20.0	10.8	3.4	15.0	10.1	6.4	8.1	6.9
Per capita GDP (U.S. dollars, thousands)	3.1	3.8	3.7	4.3	4.5	4.0	3.8	3.9
Consumer prices (end of period)	7.2	4.9	4.0	3.7	4.2	3.1	4.5	4.5
Nominal exchange rate (Guarani per U.S. dollar, eop)	4,558	4,478	4,224	4,585	4,629	5,807	...	...
Monetary sector								
Currency issue	18.5	11.6	17.5	13.2	8.9	2.9	3.1	3.4
Credit to private sector 1/	37.9	25.6	15.8	19.4	19.9	8.8	4.6	5.2
Liabilities to private sector	19.9	19.3	14.0	20.0	15.9	4.2	6.6	6.2
External sector								
Exports (fob, values)	35.1	20.7	-7.8	16.7	-3.7	-14.6	-5.1	5.1
Imports (cif, values)	44.7	22.9	-5.9	7.8	1.1	-14.9	-6.7	7.1
Terms of trade	8.2	14.3	-10.2	11.4	9.8	-2.8	1.7	-2.5
Real effective exchange rate 2/	1.9	11.8	-1.6	5.2	3.2	-1.1	...	...
(In percent of GDP, unless otherwise indicated)								
Current account	-0.3	0.4	-2.0	1.7	-0.4	-1.8	-1.4	-1.2
Trade balance	4.4	3.4	2.3	5.7	3.3	3.2	3.8	3.1
Exports	52.2	50.3	47.4	47.0	42.4	39.8	39.6	39.9
Electricity	9.8	9.0	9.1	7.7	7.1	7.4	7.8	7.8
Other registered	22.6	21.9	20.5	24.9	24.1	22.6	22.5	23.3
Unregistered	19.8	19.4	17.8	14.3	11.2	9.9	9.3	8.9
Imports	-47.8	-46.9	-45.1	-41.2	-39.1	-36.6	-35.8	-36.8
Of which: Oil imports	-5.4	-6.0	-6.7	-6.0	-5.5	-3.2	-2.0	-2.4
Capital account and financial account	1.0	1.9	3.7	0.3	5.5	0.8	1.5	0.8
General government	0.3	-0.2	-0.1	1.8	3.2	1.4	3.5	0.7
Private sector	0.6	2.1	3.9	-3.0	1.0	-0.6	0.2	0.1
Of which: Direct investment	1.1	2.2	1.9	0.2	1.1	1.3	1.6	1.8
Errors and omissions	0.9	0.8	-1.8	1.6	-1.4	-1.0	0.0	0.0
Gross international reserves (in millions of U.S. dollars)	4,168	4,984	4,994	5,871	6,891	6,329	6,360	6,254
In months of next-year imports of goods and services	3.9	5.0	4.6	5.3	7.3	7.1	6.7	6.2
Ratio to short-term external debt	2.4	2.7	2.8	3.2	3.8	3.4	3.3	3.1
Gross domestic investment	16.2	17.1	15.1	15.4	16.2	16.5	16.0	16.1
Gross national saving	15.9	17.5	13.0	17.1	15.8	14.7	14.7	14.9
Central government revenues 3/	17.1	18.0	19.0	17.1	17.9	18.1	18.0	18.2
Of which: Tax revenues	12.0	12.6	12.7	11.8	12.7	12.3	12.2	12.4
Central government expenditures 3/	15.8	17.0	20.6	18.8	19.0	19.8	20.1	20.2
Of which: Compensation of Employees	7.2	7.5	9.4	9.1	8.8	9.0	8.9	8.9
Of which: Net Acquisition of Non Financial Assets	2.4	2.3	2.6	2.3	2.4	2.6	2.7	2.7
Central government net lending/borrowing	1.3	1.0	-1.7	-1.7	-1.1	-1.7	-2.1	-2.0
Central government primary balance	1.7	1.3	-1.4	-1.4	-0.7	-1.1	-1.3	-0.9
Public sector debt (excl. central bank bills)	15.6	13.0	16.2	17.0	20.2	23.8	26.5	27.2
Of which: Foreign currency	13.2	11.1	10.9	11.6	14.5	18.0	21.4	21.2
Of which: Domestic currency	2.4	1.9	5.3	5.4	5.8	5.8	5.1	6.0
Memorandum items:								
GDP (billions of Guaranies)	94,934	105,203	108,832	125,152	137,798	146,566	158,409	169,324
GDP (US\$ billions)	20.0	25.1	24.6	29.0	30.9	28.1	...	...

Sources: Central Bank of Paraguay; Ministry of Finance; and IMF staff estimates and projections.

1/ Includes local currency credit and foreign currency credit valued at a constant exchange rate.

2/ Average annual change; a positive change indicates an appreciation.

3/ According to the GFSM 2001 presentation.

Table 2. Paraguay: Central Government Operations (GFSM 2001 Presentation)
(In percent of GDP)

	2011	2012	2013	2014	2015	Projections					
						2016	2017	2018	2019	2020	2021
Revenue	18.0	19.0	17.1	17.9	18.1	18.0	18.2	18.3	18.4	18.5	18.5
Taxes	12.6	12.7	11.8	12.7	12.3	12.2	12.4	12.6	12.7	12.9	13.0
Income taxes	2.5	2.7	2.5	2.7	2.7	2.6	2.7	2.7	2.8	2.8	2.9
Excises	1.9	2.0	1.6	1.8	1.7	1.6	1.7	1.7	1.7	1.7	1.7
Value added tax	6.5	6.5	6.3	6.8	6.7	6.7	6.8	6.9	7.0	7.0	7.0
Import duties	1.6	1.5	1.3	1.3	1.1	1.1	1.1	1.2	1.2	1.3	1.3
Other	0.1	0.1	0.1	0.1	0.2	0.1	0.1	0.1	0.1	0.1	0.1
Social contributions	1.3	1.6	1.3	1.7	1.4	1.4	1.4	1.4	1.4	1.3	1.3
Other revenue	4.2	4.7	4.0	3.6	4.4	4.4	4.4	4.4	4.3	4.3	4.2
Grants	1.3	1.1	0.8	0.8	0.9	0.8	0.8	0.8	0.8	0.8	0.8
Itaipu-Yacyreta hydroelectric plants	2.2	2.1	1.9	1.5	2.2	2.4	2.3	2.3	2.3	2.2	2.1
Other nontax revenue	0.7	1.4	1.3	1.3	1.3	1.2	1.2	1.2	1.2	1.2	1.2
Expenditure	17.0	20.6	18.8	19.0	19.8	20.1	20.2	20.1	20.2	20.2	20.0
Expense	14.7	18.0	16.5	16.6	17.3	17.3	17.5	17.5	17.6	17.6	17.5
Compensation of employees	7.5	9.4	9.1	8.8	9.0	8.9	8.9	8.8	8.8	8.7	8.6
Purchases of goods and services	1.6	1.6	1.2	1.5	1.5	1.5	1.6	1.6	1.6	1.6	1.6
Interest	0.3	0.2	0.3	0.4	0.6	0.8	1.0	1.3	1.6	1.7	1.8
Grants	2.6	3.5	3.0	3.1	3.0	3.0	2.9	2.7	2.6	2.5	2.3
Social benefits	1.7	2.1	2.1	2.1	2.6	2.6	2.6	2.6	2.6	2.6	2.6
Other expense	1.0	1.1	0.7	0.7	0.5	0.5	0.5	0.5	0.5	0.5	0.5
Net acquisition of nonfinancial assets	2.3	2.6	2.3	2.4	2.6	2.7	2.7	2.6	2.6	2.6	2.6
Gross operating balance	3.3	1.0	0.7	1.3	0.8	0.7	0.7	0.8	0.8	0.9	1.1
Net lending/borrowing (overall balance)	1.0	-1.7	-1.7	-1.1	-1.7	-2.1	-2.0	-1.8	-1.8	-1.7	-1.5
Net financial transactions	-1.0	1.7	1.7	1.1	1.7	2.1	2.0	1.8	1.8	1.7	1.5
Net acquisition of financial assets	0.3	0.1	0.3	1.2	0.2	0.8	0.8	0.8	0.8	0.8	0.8
Net incurrence of liabilities	-0.7	1.8	2.0	1.9	1.9	2.9	2.8	2.7	2.6	2.4	2.3
Domestic	-0.4	1.8	0.3	-1.1	0.9	-0.2	2.1	2.0	2.1	2.0	1.8
Debt securities	-0.4	0.7	0.7	0.5	0.1	-0.4	1.2	1.6	1.8	1.9	1.8
New TB issues	0.0	1.0	0.9	0.8	0.4	0.3	1.9	2.4	2.7	3.4	1.8
Amortizations	-0.5	-0.3	-0.1	-0.3	-0.3	-0.7	-0.7	-0.7	-0.9	-1.5	0.0
Net credit from the banking system	-0.3	0.9	-0.6	-1.8	0.8	0.2	0.8	0.3	0.3	0.1	0.1
Net credit from the Central bank 1/	-0.3	0.8	-0.6	-1.8	0.8	0.2	0.8	0.3	0.3	0.1	0.1
Net credit from the commercial banks	0.0	0.1	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Other accounts payable	0.3	0.2	0.2	0.2	0.1	0.0	0.0	0.0	0.0	0.0	0.0
Foreign	-0.2	-0.1	1.7	3.1	1.0	3.1	0.7	0.7	0.5	0.5	0.4
Disbursements	0.6	0.8	2.4	3.6	1.5	3.7	1.3	1.2	0.9	0.9	0.9
Amortizations	-0.8	-0.9	-0.6	-0.6	-0.5	-0.6	-0.5	-0.5	-0.5	-0.4	-0.5
Statistical Discrepancy 2/	-0.1	0.0	0.0	0.4	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Memorandum items:											
Primary balance	1.3	-1.4	-1.4	-0.7	-1.1	-1.3	-0.9	-0.5	-0.2	0.1	0.3
Primary balance excl. royalties and grants 3/	-3.2	-6.3	-5.8	-4.3	-5.8	-6.1	-5.6	-4.9	-4.4	-4.0	-3.6
Output gap for GDP excl. agriculture and energy	0.1	-0.3	2.3	3.5	2.1	-0.2	-0.8	-0.4	0.0	0.0	0.0
Structural primary balance excl. royalties and grants 3/	-3.2	-6.2	-6.3	-5.1	-6.3	-6.1	-5.4	-4.9	-4.4	-4.0	-3.6
Fiscal Impulse	1.1	3.0	0.1	-1.2	1.2	-0.2	-0.7	-0.5	-0.4	-0.5	-0.4
Central government gross debt	9.9	12.6	13.6	16.2	19.1	20.9	21.8	23.0	23.9	24.9	25.5
Nominal GDP (in billions of Guaranies)	105,203	108,832	125,152	137,798	146,566	158,409	169,324	181,792	195,336	210,827	228,171

Sources: Ministry of Finance; Central Bank of Paraguay; and IMF staff estimates and projections.

1/ Includes mainly use of government deposits at the Central Bank.

2/ Captures the discrepancy between above-the-line calculations and financial accounts.

3/ In percent of potential non-agricultural non-energy GDP.

Table 3. Paraguay Operations of the Consolidated Public Sector 1/
(In percent of GDP)

	2011	2012	2013	2014	Est.		Projections				
					2015	2016	2017	2018	2019	2020	2021
Revenue	23.3	23.6	22.1	22.8	22.0	21.8	22.0	22.0	22.1	22.1	22.1
Tax revenue	12.6	12.8	12.3	12.7	12.4	12.2	12.5	12.6	12.8	12.9	13.0
Nontax revenue and grants 2/	9.3	10.4	9.1	9.6	9.6	9.6	9.6	9.5	9.4	9.3	9.2
Public enterprises operating surplus	1.4	0.5	0.7	0.4	0.0	0.0	-0.1	-0.1	-0.1	-0.1	-0.1
Expenditure	21.3	25.3	23.5	23.5	24.4	24.4	24.6	24.4	24.5	24.5	24.4
Expense	18.2	21.6	20.3	20.5	21.0	21.0	21.3	21.4	21.5	21.5	21.4
Wages and salaries	9.4	12.0	11.7	11.3	11.5	11.3	11.3	11.3	11.2	11.1	11.0
Goods and services	2.7	2.7	2.1	2.7	2.8	2.8	2.8	2.8	2.8	2.9	2.9
Interest payments	0.7	0.6	0.8	0.8	1.0	1.2	1.6	1.9	2.2	2.5	2.6
Transfers 3/	4.5	5.2	5.0	5.0	5.1	5.1	5.0	4.8	4.7	4.5	4.4
Current transfers	3.4	4.1	4.1	4.2	4.3	4.3	4.3	4.2	4.1	4.0	3.8
Capital transfers	1.1	1.1	0.9	0.8	0.9	0.8	0.7	0.6	0.6	0.6	0.6
Other expense	1.0	1.1	0.7	0.7	0.5	0.5	0.5	0.5	0.5	0.5	0.5
Gross operating balance	5.0	2.1	1.8	2.2	1.0	0.8	0.7	0.6	0.6	0.6	0.7
Net acquisition of nonfinancial assets 4/	3.1	3.7	3.2	3.0	3.4	3.4	3.3	3.1	3.0	3.0	3.0
Net lending/borrowing (overall balance)	1.9	-1.6	-1.4	-0.7	-2.5	-2.6	-2.6	-2.4	-2.4	-2.3	-2.2
Net financial transactions	-1.9	1.6	1.4	0.7	2.5	2.6	2.6	2.4	2.4	2.3	2.2
Net acquisition of financial assets	0.5	0.6	0.9	0.7	-0.1	0.5	0.5	0.5	0.5	0.5	0.5
Net incurrence of liabilities	-1.4	2.2	2.3	1.4	2.4	3.1	3.2	3.0	2.9	2.9	2.8
External	-0.3	-0.1	1.7	3.1	1.6	3.4	0.7	0.7	0.5	0.4	0.4
Disbursements	0.6	0.8	2.4	3.8	2.2	4.1	1.3	1.3	1.0	1.0	0.9
Amortizations	-0.9	-0.9	-0.7	-0.6	-0.6	-0.7	-0.6	-0.6	-0.5	-0.5	-0.5
Domestic	-1.4	2.1	0.4	-1.9	0.7	-0.3	2.5	2.3	2.5	2.4	2.4
Domestic debt	-0.4	0.7	0.7	0.5	0.1	-0.4	1.2	1.6	1.8	1.9	1.8
Disbursements	0.0	1.0	0.9	0.8	0.4	0.3	1.9	2.4	2.7	3.4	1.8
Amortizations	-0.5	-0.3	-0.1	-0.3	-0.3	-0.7	-0.7	-0.7	-0.9	-1.5	0.0
Deposits	-1.6	1.2	-1.2	-2.7	-0.1	-0.5	0.6	-0.1	-0.1	-0.3	-0.3
Quasifiscal deficit financing 5/	0.6	0.2	0.9	0.4	0.7	0.6	0.7	0.7	0.8	0.8	0.9
Net change in domestic arrears	0.3	0.2	0.2	0.2	0.1	0.0	0.0	0.0	0.0	0.0	0.0
Memorandum items:											
Primary balance	2.6	-1.0	-0.7	0.1	-1.4	-1.4	-1.0	-0.5	-0.2	0.1	0.4
Public sector debt (excl. central bank bills)	13.0	16.2	17.0	20.2	23.8	26.5	27.2	28.1	28.8	29.5	29.9
Domestic public debt	1.9	5.3	5.4	5.8	5.8	5.1	6.0	7.3	8.6	10.0	11.0
Foreign public debt	11.1	10.9	11.6	14.5	18.0	21.4	21.2	20.8	20.2	19.6	18.9

Sources: Ministry of Finance; and IMF staff estimates and projections.

1/ Includes the nonfinancial public sector and the central bank.

The GFSM 2001 presentation is an approximation based on the reallocation of certain revenue and expenditure categories within the GFSM 1986 template (reported on a cash basis).

2/ Includes social contributions and grants.

3/ Includes social benefits, grants, and capital transfers.

4/ Includes capital formation.

5/ Corresponds to net losses of central bank capital which are not automatically compensated by the government.

Table 4. Paraguay: Balance of Payments
(In millions of U.S. dollars)

	2011	2012	2013	2014	Est.	Projections					
					2015	2016	2017	2018	2019	2020	2021
Current account	110	-501	478	-127	-512	-363	-322	-273	-243	-245	-184
Trade balance	855	572	1,663	1,026	906	1,017	877	976	1,081	1,188	1,328
Exports	12,634	11,654	13,605	13,105	11,189	10,614	11,156	11,841	12,536	13,196	13,873
Electricity	2,257	2,232	2,237	2,180	2,069	2,090	2,168	2,222	2,278	2,347	2,418
Other registered	5,509	5,052	7,220	7,456	6,351	6,032	6,501	7,007	7,526	8,012	8,518
<i>Of which: Beef</i>	754	827	1,059	1,431	1,246	993	1,003	1,063	1,127	1,200	1,278
<i>Of which: Soy</i>	2,295	1,624	2,790	2,425	1,766	1,723	1,835	1,960	2,087	2,233	2,378
Unregistered	4,867	4,371	4,149	3,469	2,769	2,492	2,487	2,611	2,731	2,837	2,936
Imports	-11,779	-11,083	-11,942	-12,079	-10,283	-9,597	-10,279	-10,865	-11,455	-12,008	-12,544
Registered	-11,549	-10,756	-11,302	-11,305	-9,496	-8,855	-9,487	-10,029	-10,575	-11,085	-11,580
<i>Of which: Fuel products</i>	-1,507	-1,647	-1,735	-1,696	-907	-550	-679	-780	-877	-958	-1,023
Unregistered	-230	-326	-640	-774	-787	-742	-792	-835	-880	-922	-964
Services (net)	-181	-170	-219	-222	-229	-294	-302	-303	-305	-298	-289
Transport	-309	-296	-276	-311	-311	-322	-337	-350	-364	-369	-375
Travel	67	58	30	33	-8	-52	-54	-53	-53	-52	-51
Other	62	68	27	56	89	80	90	100	111	123	137
Factor income	-1,278	-1,661	-1,685	-1,537	-1,853	-1,915	-1,762	-1,845	-1,954	-2,095	-2,207
Transfers	714	759	720	606	664	829	864	899	935	959	984
Capital and financial account	467	922	90	1,706	235	394	215	402	408	463	519
Capital transfers	40	51	61	141	119	113	118	124	131	139	148
Direct investment	557	480	72	346	358	430	516	568	602	641	679
Portfolio investment	100	500	500	1,300	292	0	0	0	0	0	0
<i>Of which: government</i>	0	0	500	1,000	292	600	0	0	0	0	0
Other investment	-230	-108	-543	-81	-534	-150	-419	-290	-325	-317	-307
<i>Of which: government</i>	-59	-30	13	-11	113	330	201	202	153	154	155
Errors and omissions	206	-446	469	-448	-285	0	0	0	0	0	0
Overall balance	783	-25	1,036	1,131	-562	31	-106	129	164	218	336
Net international reserves (increase -)	-783	25	-1,036	-1,131	562	-31	106	-129	-164	-218	-335
Gross reserves	-784	25	-1,036	-1,131	562	-31	106	-129	-164	-218	-336
Reserve liabilities	1	0	0	0	0	0	0	0	0	0	0
Exceptional financing	0	0	0	0	0	0	0	0	0	0	0
Memorandum items:											
Current account in percent of GDP	0.4	-2.0	1.7	-0.4	-1.8	-1.4	-1.2	-0.9	-0.8	-0.7	-0.5
Gross reserves (in millions of U.S. dollars)	4,984	4,994	5,871	6,891	6,329	6,360	6,254	6,383	6,547	6,765	7,101
In months of imports of GNFS	5.0	4.6	5.3	7.3	7.1	6.7	6.2	6.0	5.9	5.9	5.9
External public debt in percent of GDP 1/	11.1	10.9	11.6	14.5	18.0	21.4	21.2	20.8	20.2	19.6	18.9
Debt service in percent of exports GNFS	10.4	11.2	9.0	9.7	11.1	12.3	12.4	12.4	12.4	12.5	12.4
Export volume (percent change) 2/	19.8	0.6	-9.6	29.9	5.4	-2.8	3.5	4.6	5.2	5.3	5.4
Import volume (percent change) 2/	32.8	27.9	-11.0	10.9	9.0	-1.3	1.5	3.2	3.3	3.4	3.6
Terms of trade (percent change) 2/	14.3	-10.2	11.4	9.8	-2.8	1.7	-2.5	-1.2	-1.3	-1.2	-0.9

Sources: Central Bank of Paraguay; and IMF staff estimates and projections.

1/ Based on average exchange rate valuation of GDP.

2/ Excludes unregistered trade and imports destined for re-export.

Table 5. Paraguay: Summary Accounts of the Central Bank
(In billions of Guaranies; eop; valued at constant exchange rate)

	2011	2012	2013	2014	2015
Currency issue	7,324	8,606	9,744	10,615	10,920
Growth	11.6	17.5	13.2	8.9	2.9
Net international reserves	23,011	23,067	27,125	31,934	27,511
In millions of U.S. dollars	4,971	4,983	5,859	6,898	5,943
Net domestic assets	-15,687	-14,461	-17,381	-21,319	-17,110
Net nonfinancial public sector	-3,263	-1,354	-5,837	-8,282	-6,564
Net credit to the central government	-3,756	-1,342	-5,837	-8,282	-6,564
Net credit to the rest of NFPS	493	-12	-1	-1	-1
Net credit to the banking system	-11,382	-11,792	-14,926	-16,961	-16,121
Reserve requirements	-6,115	-6,539	-7,605	-9,096	-9,615
Free reserves	-2,577	-2,685	-1,207	-2,036	-2,292
Monetary control instruments 1/	-4,111	-3,665	-7,473	-6,918	-5,349
Other	1,421	1,097	1,361	1,090	1,135
Other assets and liabilities (net)	-1,042	-1,315	3,382	3,924	5,575
Capital and reserves	1,298	1,557	5,387	6,218	2,897
Other assets net 2/	-2,340	-2,872	-2,005	-2,294	2,678
Memorandum Items:					
Total stock of IRMs outstanding 1/	4,155	3,601	7,614	6,873	5,307
Quasifiscal balance	661	261	1,123	542	994
In percent of GDP	0.6	0.2	0.9	0.4	0.7
Cost of monetary policy operations	433	400	534	592	583
In percent of GDP	0.4	0.4	0.4	0.4	0.4

Sources: Central Bank of Paraguay; and IMF staff estimates and projections.

1/ Includes overnight-deposit facility and central bank bills (LRM). A fraction of LRM is held by non-bank institutions.

2/ Includes LRM held by the non-banking sector.

Table 6. Paraguay: Summary Accounts of the Financial System 1/

	2011	2012	2013	2014	2015	Projections					
						2016	2017	2018	2019	2020	2021
I. Central Bank											
Net international reserves	23,011	23,067	27,125	31,934	27,511	27,668	27,175	27,773	28,535	29,543	31,092
In millions of U.S. dollars	4,971	4,983	5,859	6,898	5,943	5,977	5,870	5,999	6,164	6,382	6,716
Net domestic assets	-15,687	-14,461	-17,381	-21,319	-17,110	-16,412	-15,532	-15,701	-16,013	-16,525	-17,538
Credit to public sector, net	-3,263	-1,354	-5,837	-8,282	-6,564	-6,209	-4,873	-4,304	-3,731	-3,564	-3,395
Credit to banking system, net 2/	-7,271	-8,127	-7,452	-10,042	-10,772	-9,618	-8,668	-8,689	-8,713	-8,726	-8,806
Credit	1,421	1,097	1,361	1,090	1,135	1,135	1,135	1,135	1,135	1,135	1,135
Deposits	8,692	9,224	8,813	11,132	11,907	10,753	9,803	9,825	9,848	9,861	9,941
Central bank securities	-4,155	-3,601	-7,614	-6,873	-5,307	-7,522	-10,470	-12,668	-15,178	-17,705	-20,959
Other	-998	-1,379	3,522	3,879	6,051	6,936	8,479	9,960	11,609	13,470	15,621
Currency issue	7,324	8,606	9,744	10,615	10,920	11,255	11,643	12,072	12,521	13,018	13,553
II. Monetary Survey											
Net foreign assets	22,574	22,533	25,147	29,517	25,621	25,858	25,927	26,544	27,323	28,383	29,992
In millions of U.S. dollars	4,876	4,868	5,432	6,376	5,534	5,586	5,601	5,734	5,902	6,131	6,479
Net domestic assets	25,156	31,695	39,319	44,795	52,103	56,687	61,460	65,427	69,789	72,457	74,373
Credit to the public sector	-6,560	-4,856	-9,327	-12,278	-11,203	-10,841	-9,500	-8,925	-8,347	-8,169	-7,988
Credit to the private sector	41,337	47,878	57,168	68,539	74,600	78,059	82,107	86,347	90,667	94,369	98,135
Other	-9,620	-11,326	-8,522	-11,466	-11,294	-10,532	-11,147	-11,994	-12,532	-13,743	-15,773
Broad liquidity (M3)	45,205	51,464	60,706	69,487	72,190	76,875	81,579	86,243	90,800	94,502	97,927
Foreign currency deposits	14,338	16,893	20,286	25,358	26,386	28,233	30,068	31,872	33,625	34,584	35,362
Money and quasi-money (M2)	30,867	34,571	40,420	44,129	45,804	48,642	51,511	54,371	57,175	59,918	62,564
Quasi-money	14,729	16,813	20,340	22,411	23,121	24,740	26,348	27,929	29,465	30,938	32,330
Money (M1)	16,138	17,758	20,080	21,718	22,683	23,902	25,163	26,442	27,710	28,980	30,234
(Annual percent change)											
M0 (Currency issued)	11.6	17.5	13.2	8.9	2.9	3.1	3.4	3.7	3.7	4.0	4.1
Credit to the private sector	25.6	15.8	19.4	19.9	8.8	4.6	5.2	5.2	5.0	4.1	4.0
M1	9.1	10.0	13.1	8.2	4.4	5.4	5.3	5.1	4.8	4.6	4.3
M2	16.8	12.0	16.9	9.2	3.8	6.2	5.9	5.6	5.2	4.8	4.4
M3	16.8	13.8	18.0	14.5	3.9	6.5	6.1	5.7	5.3	4.1	3.6
Of which: Foreign currency deposits	16.9	17.8	20.1	25.0	4.1	7.0	6.5	6.0	5.5	2.9	2.3
Memorandum items:											
Ratio of foreign currency deposits to M3 (percent)	31.7	32.8	33.4	36.5	36.6	36.7	36.9	37.0	37.0	36.6	36.1
Ratio of foreign currency deposits to total private sector deposits (percent)	34.2	35.3	35.4	38.2	38.1	38.2	38.4	38.6	38.4	38.1	37.6
Sources: Central Bank of Paraguay; and IMF staff estimates and projections.											
1/ Includes banks, finance companies, and the 20 largest cooperatives.											
2/ Excludes LRM held by the banking sector.											

Table 7. Paraguay: Indicators of External Vulnerability
(In percent of GDP, unless otherwise indicated)

	2010	2011	2012	2013	2014	2015
Monetary and financial indicators						
Broad money (M3), percentage change 1/	20.0	16.8	13.8	18.0	14.5	3.9
Credit to the private sector, real (percent change) 1/	28.7	19.7	11.4	15.1	15.1	5.6
Share of nonperforming loans in total loans (percent)	1.3	1.7	2.1	2.0	1.8	2.5
Average domestic bank lending rate, real	21.5	6.0	11.0	11.6	7.6	11.2
Central Bank bill yield, real	0.8	-0.8	1.8	3.1	0.9	20.5
Central bank foreign short-term liabilities (millions of U.S. dollars)	0.0	0.0	0.0	0.0	0.0	1.4
External indicators						
Merchandise exports (percentage change)	35.1	20.7	-7.8	16.7	-3.7	-14.6
Merchandise imports (percentage change)	44.7	22.9	-5.9	7.8	1.1	-14.9
Merchandise terms of trade (percentage change)	8.3	14.3	-10.2	11.4	9.8	-2.8
Real effective exchange rate (percentage change)	3.7	2.2	9.3	-3.0	8.5	-6.0
Current account balance (percent of GDP)	-0.3	0.4	-2.0	1.7	-0.4	-1.8
Capital and financial account (percent of GDP)	1.0	1.9	3.7	0.3	5.5	0.8
Net foreign direct investment (percent of GDP)	1.1	2.2	1.9	0.2	1.1	1.3
Other net investment (percent of GDP)	-0.3	-0.9	-0.4	-1.9	-0.3	-1.9
External public debt (percent of GDP) 2/	13.2	11.1	10.9	11.6	14.5	18.0
Total external debt (percent of GDP)	78.8	62.2	65.3	55.4	56.5	62.6
Excluding debt of binational companies	20.6	17.1	21.1	19.8	24.9	30.0
Debt service (in percent of exports GNFS)	12.7	10.4	11.2	9.0	9.7	11.1
International reserves (in millions of U.S. dollars)	4,165	4,971	4,983	5,860	6,899	5,944.3
In months of imports of GNFS	3.9	5.0	4.6	5.3	7.3	7.1
Ratio to short-term external debt 3/	2.4	2.7	2.8	3.2	3.8	3.4
Ratio to foreign currency deposits in domestic banks	1.5	1.5	1.3	1.3	1.3	4.2

Sources: Central Bank of Paraguay; and IMF staff estimates.

1/ Foreign-currency components are valued at the accounting exchange rate.

2/ Based on end-of-period exchange rate conversion of U.S. dollar-denominated debt.

3/ Private and public external debt with a residual maturity of one year or less.

Table 8. Paraguay: Financial Soundness Indicators

	2013	2014	2015	2015 Feb	2016 Feb
<i>(in percent)</i>					
Basic indicators					
Capital adequacy					
Regulatory capital/risk-weighted assets	14.6	15.2	16.2	17.0	n.a.
Tier 1 capital/risk-weighted assets	11.1	11.2	11.3	11.1	n.a.
NPLs net of provisions/equity	3.7	3.9	6.3	4.3	n.a.
Asset quality					
NPLs/total loans	2.0	1.8	2.5	2.0	2.9
Provisions/NPLs	135.7	135.0	116.5	123.2	106.4
<i>(in percent of total loans)</i>					
Sectoral distribution of credit					
Agriculture	24.7	24.1	24.4	24.1	24.4
Livestock	11.2	10.5	10.0	10.3	10.0
Industry	10.9	10.4	10.0	10.0	10.0
Wholesale	14.0	14.8	15.5	15.0	15.0
Retail	8.2	8.6	8.4	8.6	7.8
Services	8.5	8.5	9.4	8.9	9.2
Consumption	15.4	14.7	13.3	15.3	13.7
Export credit	0.4	1.2	1.2	1.4	1.2
Financial sector	6.8	7.3	7.8	6.3	8.7
<i>(in percent)</i>					
Profitability					
Return on assets	2.4	2.4	2.3	2.6	1.9
Return on equity	29.4	28.3	27.8	25.3	18.0
Net interest income/operating margin	74.7	74.7	74.4	76.0	78.8
Admin. expenses/operating margin	54.3	52.8	48.9	51.2	49.7
Liquidity					
Liquid assets/total assets	38.3	34.0	23.4	34.3	n.a.
Liquid assets/sight deposits	80.3	72.2	52.3	72.7	n.a.
Market risk					
FX position/equity	10.7	8.7	9.3	5.6	n.a.
Recommended indicators					
Capital/assets	9.7	10.0	9.7	10.0	9.9
Personnel expenses/admin. expenses	44.6	45.3	45.7	46.6	45.7
Public deposits/total loans					
FX loans/total loans	47.2	49.5	50.9	49.5	n.a.
FX liabilities/total liabilities	46.7	50.5	55.3	49.6	n.a.

Sources: Central Bank of Paraguay; IMF, *Financial Soundness Indicators*; and Haver Analytics.

Table 9. Paraguay: Medium-Term Outlook
(In percent of GDP, unless otherwise indicated)

	2014	2015	Projections					
			2016	2017	2018	2019	2020	2021
National accounts and prices								
Real GDP growth (in percent)	4.7	3.0	2.9	3.2	3.5	3.7	3.9	4.0
Gross domestic investment	16.2	16.5	16.0	16.1	15.8	15.9	15.9	16.0
Gross domestic savings	15.8	14.7	14.7	14.9	14.9	15.1	15.2	15.5
Consumer prices (end of period; in percent)	4.2	3.1	4.5	4.5	4.5	4.5	4.5	4.5
Public finances								
Central government primary balance	-0.7	-1.1	-1.3	-0.9	-0.5	-0.2	0.1	0.3
Central government net lending/borrowing	-1.1	-1.7	-2.1	-2.0	-1.8	-1.8	-1.7	-1.5
Central government debt	16.2	19.1	20.9	21.8	23.0	23.9	24.9	25.5
Public sector debt	20.2	23.8	26.5	27.2	28.1	28.8	29.5	29.9
External sector								
Terms of trade (annual percent change)	9.8	-2.8	1.7	-2.5	-1.2	-1.3	-1.2	-0.9
Current account	-0.4	-1.8	-1.4	-1.2	-0.9	-0.8	-0.7	-0.5
Foreign direct investment	1.1	1.3	1.6	1.8	1.9	1.9	1.9	1.9
Gross international reserves (in US\$ billion)	6.9	6.3	6.4	6.3	6.4	6.5	6.8	7.1

Sources: Central Bank of Paraguay; Ministry of Finance; and IMF staff estimates and projections.

Annex I. Implementation of Past Fund Policy Advice

The authorities have taken on board several of the policy recommendations from the 2014 Article IV consultation.

- Directors commended authorities' efforts in increasing tax collection and recommended that these should be extended to achieve lasting improvements in public services. *Authorities have moved ahead with base broadening measures, such as the extension of the VAT to cooperatives, and made good progress in strengthening institutional frameworks at the tax revenue authority (SET). With technical support from the IMF, SET undertook significant organizational improvements and advanced in the elaboration of new audit and enforcement strategies. SET has also made important progress in enhancing taxpayers' registries and in implementing online collection through bank and other similar entities.*
- On fiscal policy, directors noted that over time, a stronger budget process will be essential to support fiscal discipline. They also highlighted that a prudent medium-term fiscal plan should also incorporate some buffer against adverse shocks, given the high volatility of Paraguay's economic environment. *There are signs of increased effectiveness of the fiscal responsibility law, even if the short track record of compliance is mixed. The draft 2016 budget submitted to congress complied with the numerical targets of the law. While the final approved version still respected the deficit ceiling, modifications introduced by congress altered the composition of spending. Over the medium-term, authorities' plans fully conform to the numerical targets.*
- On monetary and exchange rate policy, directors recommended efforts focused on further enhancing the effectiveness of the inflation targeting regime. *During the course of 2015, the interest rate corridor around the monetary policy rate (MPR) has been narrowed in an effort to establish the policy rate as the main anchor. At the same time, the monetary authority has increased issuance of monetary regulation instruments (IRMs), used for repos, and reduced the rejection rate of bids in order to steer the overnight rate above the floor of the corridor towards the MPR.*
- On financial sector policy, directors argued that the revision of central bank and banking laws is essential to put risk-based regulation and supervision on a robust legal basis. *A draft banking law has been presented officially to congress, and is currently under review. This legislation would grant additional powers to the BCP and facilitate the move towards risk-based supervision. The authorities indicated that passage was a priority and expressed optimism that congressional approval could happen this year.*

The authorities have also maintained their commitment to transparency in the discussions with staff, by consenting to the publication of the mission's concluding statement and arranging a press conference that typically generates comprehensive media coverage of the mission's main findings and policy recommendations.

	Paraguay	Overall Assessment
Foreign asset and liability position	<p>Background. Paraguay's net international investment position (NIIP) has hovered around -40 percent of GDP over the last 5 years. The negative FDI position reflects large inflows of capital in the agriculture sector and in the businesses related to the maquila. More recently the construction sector was another repository of FDI. Paraguay also has a negative net asset position related to loans mostly due to large projects financed by multinationals and more recently to bond issuance by the government on international markets.</p> <p>Assessment. Gross external debt has grown in the last couple of years (from about 55 percent to about 59 percent of GDP), as a result of the multilateral loans and bonds component of the net asset position. Nevertheless, the external debt position remains sustainable under a range of adverse shocks (Figure A1 and Table A1, Annex III).</p>	<p><i>The external position and the exchange rate are broadly consistent with medium-term fundamentals. The external debt position does not raise concerns of sustainability.</i></p>
Current account	<p>Background. Paraguay's current account has been in surplus over the past 20 years averaging 0.4 percent of GDP. In the past couple of years, the balance has turned to negative, mainly as a result of low agriculture commodity prices. The current account is projected to remain in deficit over the medium term, mainly as commodity prices are not expected to recover and fuel import prices will increase starting in 2017. While national savings have remained relatively stable as a share of GDP, investment has decreased in the last 2 years, as a result of low prospects in the commodity production sectors.</p> <p>Assessment. The current account is estimated to have reached -1.8 percent of GDP in 2015, the largest imbalance since 2012. The country has gone through a significant adjustment, in line with worsening the external fundamentals. The current account is projected to remain in negative balance moving towards -0.5 percent in the medium term below its' 20-year average current account balance (0.4 percent) mainly as a result of permanently lower commodity export prices and reverting import prices.</p>	
Real exchange rate and competitiveness	<p>Background. Paraguay's real effective exchange rate (REER) is highly correlated with commodity prices. Amidst lower commodity export prices and a consequent negative terms-of-trade shock, the REER has depreciated by 5 percent during 2015, primarily reflecting nominal depreciation. Inflation has remained tame during 2015, with the only exception of December as import prices remained low.</p> <p>Assessment. The EBA approach delivered inconclusive and mixed results on the equilibrium REER. Staff sees the rate moving in line with fundamentals, with an adjustment smoothed by BCP interventions.</p>	
Capital and financial accounts	<p>Background. The CA deficit is financed by FDI and external loans, with a multilateral playing an important role. Lately, the government has more frequently tapped the international markets with a placement of two bonds in 2015 and a placement of USD 600 million this year.</p> <p>Assessment. Paraguay has a fully open capital and financial account but financial markets are not deep or developed, yet. Despite adverse conditions in the region, Paraguay has enjoyed a stable flow of FDI. Vulnerabilities arising from linkages with international financial markets in the region are very limited, with foreign asset holding below 1 percent of total financial system assets.</p>	
FX intervention and reserves level	<p>Background. During Fall 2015, in addition to regular sales of government dollar receipts, the BCP has enacted a series of discretionary interventions and as a result reserves dropped by over USD 500 million.</p> <p>Assessment. Reserves remain ample at 7 months of imports and above the Fund metrics for a small open economy. A flexible exchange rate is the first line of defense against external shocks. Staff has recommended to continue with a rules-based approach for the regular dollar sales and to limit discretionary interventions to exceptional situations of disorderly market conditions.</p>	

Table 1. Paraguay: External Debt Sustainability Framework, 2010–21
(In percent of GDP, unless otherwise indicated)

	Actual					Projections								Debt-stabilizing non-interest current account 6/ -1.0
	2010	2011	2012	2013	2014	2015	2016	2017	2018	2019	2020	2021		
Baseline: External debt	78.8	62.2	65.3	55.2	54.9	59.2	64.9	62.2	58.8	55.2	51.7	48.4		
Change in external debt	-18.6	-16.6	3.1	-10.1	-0.3	4.4	5.7	-2.7	-3.4	-3.6	-3.5	-3.3		
Identified external debt-creating flows (4+8+9)	-20.8	-17.1	2.3	-12.1	-3.6	-0.7	-1.4	-2.0	-2.3	-2.4	-2.4	-2.3		
Current account deficit, excluding interest payments	-3.2	-3.1	-0.5	-3.6	-1.5	-0.3	-1.1	-1.6	-2.0	-2.3	-2.5	-2.6		
Deficit in balance of goods and services	-4.0	-2.7	-1.6	-5.0	-2.6	-2.3	-2.7	-2.1	-2.3	-2.5	-2.5	-2.4		
Exports	55.5	53.2	50.5	49.9	45.3	42.9	42.7	43.1	43.3	43.4	43.1	42.8		
Imports	51.5	50.5	48.8	44.9	42.7	40.7	40.0	41.0	41.0	40.9	40.7	40.4		
Net non-debt creating capital inflows (negative)	-1.1	-0.8	-1.0	-0.6	-0.6	-0.7	-0.9	-1.0	-1.1	-1.1	-1.0	-1.0		
Automatic debt dynamics 1/	-16.5	-13.2	3.8	-7.9	-1.5	0.3	0.6	0.6	0.8	1.0	1.1	1.4		
Contribution from nominal interest rate	3.5	2.7	2.6	1.9	1.9	2.1	2.4	2.6	2.8	3.0	3.1	3.3		
Contribution from real GDP growth	-10.1	-2.7	0.8	-7.8	-2.4	-1.8	-1.8	-2.0	-2.1	-2.0	-2.0	-1.9		
Contribution from price and exchange rate changes 2/	-9.8	-13.1	0.5	-2.1	-1.0	...	...	...	...	...	...	...
Residual, incl. change in gross foreign assets (2-3) 3/	2.2	0.4	0.8	2.0	3.3	5.1	7.1	-0.7	-1.1	-1.2	-1.1	-1.0		
External debt-to-exports ratio (in percent)	141.9	116.8	129.4	110.6	121.0	137.9	152.1	144.5	135.7	127.1	119.8	113.0		
Gross external financing need (in billions of US dollars) 4/ in percent of GDP	0.8 3.9	0.6 2.4	1.3 5.1	0.3 0.9	0.9 2.9	1.2 4.4	1.1 4.0	1.0 3.7	1.0 3.3	0.9 3.0	0.9 2.9	1.0 2.7		
Scenario with key variables at their historical averages 5/						59.2	49.2	37.9	27.6	18.2	9.7	2.7	-1.5	
Key Macroeconomic Assumptions Underlying Baseline						Historical Average	Standard Deviation							
Nominal GDP (US dollars)	20.0	25.1	24.6	29.0	30.9			28.1	26.8	27.9	29.4	31.0	32.9	34.8
Real GDP growth (in percent)	13.1	4.3	-1.2	14.0	4.7	5.0	5.6	3.0	2.9	3.2	3.5	3.7	3.9	3.9
GDP deflator in US dollars (change in percent)	11.3	20.0	-0.8	3.3	1.8	9.7	11.6	-11.7	-7.2	0.9	1.8	1.8	1.9	1.9
Nominal external interest rate (in percent)	4.5	4.3	4.1	3.5	3.6	5.0	1.6	3.5	3.8	4.2	4.8	5.4	6.0	6.7
Growth of exports (US dollar terms, in percent)	33.6	20.0	-7.1	16.5	-3.2	13.6	17.1	-13.9	-5.1	5.0	6.0	5.8	5.1	5.1
Growth of imports (US dollar terms, in percent)	44.2	22.7	-5.3	8.3	1.4	16.7	21.4	-13.5	-6.1	6.8	5.5	5.3	5.3	5.3
Current account balance, excluding interest payments	3.2	3.1	0.5	3.6	1.5	6.3	4.9	0.3	1.1	1.6	2.0	2.3	2.5	2.6
Net non-debt creating capital inflows	1.1	0.8	1.0	0.6	0.6	0.6	0.5	0.7	0.9	1.0	1.1	1.0	1.0	1.0

1/ Derived as $[r - g - r(1+g) + ea(1+r)]/(1+g+r+gr)$ times previous period debt stock, with r = nominal effective interest rate on external debt; g = change in domestic GDP deflator in US dollar terms, e = real GDP growth rate,

e = nominal appreciation (increase in dollar value of domestic currency), and a = share of domestic-currency denominated debt in total external debt.

2/ The contribution from price and exchange rate changes is defined as $[-r(1+g) + ea(1+r)]/(1+g+r+gr)$ times previous period debt stock. r increases with an appreciating domestic currency ($e > 0$) and rising inflation (based on GDP deflator).

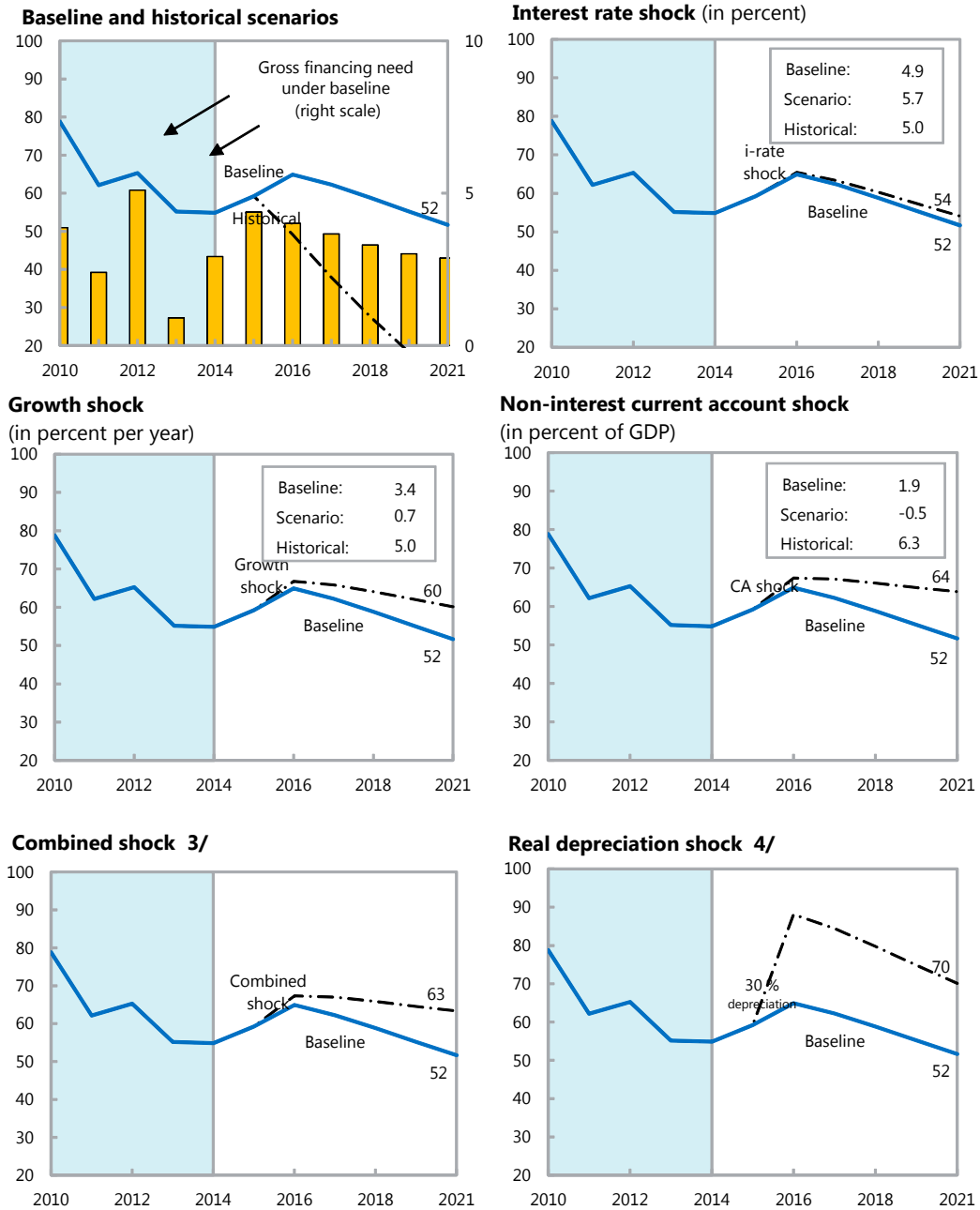
3/ For projection, line includes the impact of price and exchange rate changes.

4/ Defined as current account deficit, plus amortization on medium- and long-term debt, plus short-term debt at end of previous period.

5/ The key variables include real GDP growth; nominal interest rate; dollar deflator growth; and both non-interest current account and non-debt inflows in percent of GDP.

6/ Long-run, constant balance that stabilizes the debt ratio assuming that key variables (real GDP growth, nominal interest rate, dollar deflator growth, and non-debt inflows in percent of GDP) remain at their levels of the last projection year.

Figure 1. Paraguay: External Debt Sustainability: Bound Tests 1/ 2/
(External debt in percent of GDP)



Sources: International Monetary Fund, Country desk data, and staff estimates.
 1/ Shaded areas represent actual data. Individual shocks are permanent one-half standard deviation shocks. Figures in the boxes represent average projections for the respective variables in the baseline and scenario being presented. Ten-year historical average for the variable is also shown.
 2/ For historical scenarios, the historical averages are calculated over the ten-year period, and the information is used to project debt dynamics five years ahead.
 3/ Permanent 1/4 standard deviation shocks applied to real interest rate, growth rate, and current account balance.
 4/ One-time real depreciation of 30 percent occurs in 2010.

Annex IV. Public Debt Sustainability Analysis

Table 1. Paraguay: Public Sector DSA – Baseline Scenario

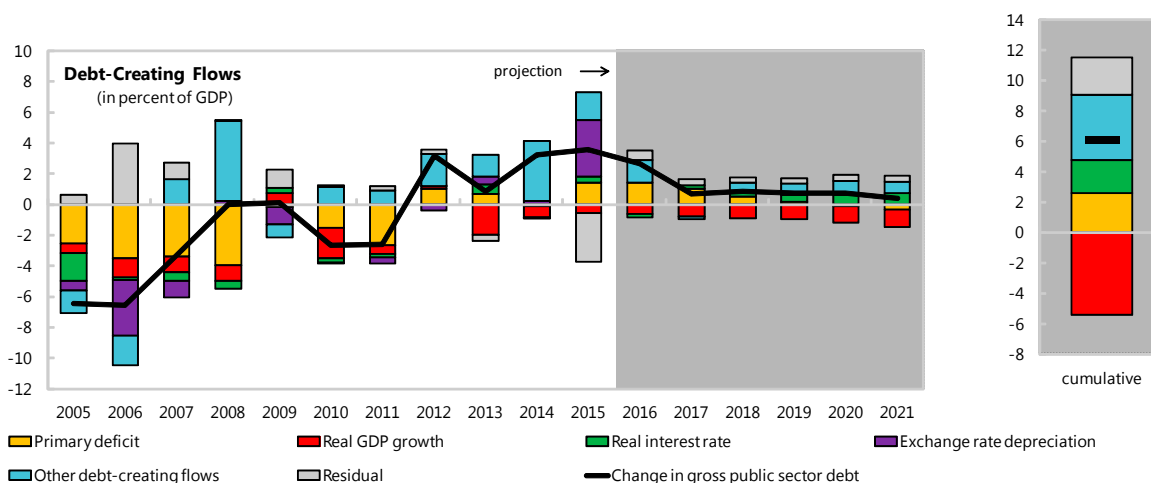
(In percent of GDP unless otherwise indicated)

Debt, Economic and Market Indicators ^{1/}

	Actual			Projections						As of April 05, 2016		
	2005-2013	2014	2015	2016	2017	2018	2019	2020	2021	Sovereign Spreads	Foreign	Local
Nominal gross public debt	18.4	20.2	23.8	26.5	27.2	28.1	28.8	29.5	29.9	EMBIG (bp)		331
Public gross financing needs	0.9	1.7	3.4	3.6	3.2	2.6	2.6	3.0	3.3	5Y CDS (bp)		...
Real GDP growth (in percent)	5.0	4.7	3.0	2.9	3.2	3.5	3.7	3.9	4.0	Ratings	Moody's	Ba1
Inflation (GDP deflator, in percent)	6.1	5.1	3.3	5.0	3.5	3.7	3.6	3.9	4.0		S&Ps	BB
Nominal GDP growth (in percent)	11.4	10.1	6.4	8.1	6.9	7.4	7.5	7.9	8.2		Fitch	BB
Effective interest rate (in percent) ^{2/}	5.3	5.3	5.5	4.4	4.4	5.0	5.7	6.3	7.0			BB

Contribution to Changes in Public Debt

	Actual			Projections						cumulative	debt-stabilizing primary balance ^{8/}
	2005-2013	2014	2015	2016	2017	2018	2019	2020	2021		
Change in gross public sector debt	-1.9	3.2	3.6	2.7	0.7	0.9	0.7	0.7	0.4	6.1	
Identified debt-creating flows	-2.7	3.3	6.8	2.1	0.3	0.5	0.4	0.3	0.0	3.6	
Primary deficit	-1.8	-0.1	1.4	1.4	1.0	0.5	0.2	-0.1	-0.4	2.6	
Primary (noninterest) revenue and grants	21.3	22.8	22.0	21.8	22.0	22.0	22.1	22.1	22.1	132.1	
Primary (noninterest) expenditure	19.5	22.7	23.4	23.1	23.0	22.5	22.2	22.0	21.8	134.7	
Automatic debt dynamics ^{3/}	-1.9	-0.5	3.5	-0.8	-0.6	-0.6	-0.5	-0.4	-0.3	-3.3	
Interest rate/growth differential ^{4/}	-1.1	-0.7	-0.2	-0.8	-0.6	-0.6	-0.5	-0.4	-0.3	-3.3	
Of which: real interest rate	-0.3	0.0	0.4	-0.2	0.2	0.3	0.5	0.6	0.8	2.2	
Of which: real GDP growth	-0.8	-0.7	-0.6	-0.6	-0.8	-0.9	-1.0	-1.0	-1.1	-5.4	
Exchange rate depreciation ^{5/}	-0.7	0.3	3.7	...	...	...	...	...	...	...
Other identified debt-creating flows	0.9	3.9	1.8	1.5	-0.1	0.6	0.7	0.9	0.7	4.3	
NFPS asset accumulation ^{6/}	0.9	3.9	1.8	1.5	-0.1	0.6	0.7	0.9	0.7	4.3	
Residual ^{7/}	0.8	-0.1	-3.2	0.6	0.4	0.3	0.3	0.4	0.4	2.5	



Source: Fund staff estimates and projections.

1/ Public sector is defined as consolidated public sector. It includes the non-financial public sector and the central bank. The stock of public debt excludes central bank bills.

2/ Defined as interest payments divided by debt stock (excluding guarantees) at the end of previous year.

3/ Derived as $[(r - \pi(1+g) - g + ae(1+r))/(1+g+\pi+g\pi)]$ times previous period debt ratio, with r = interest rate; π = growth rate of GDP deflator; g = real GDP growth rate;

a = share of foreign-currency denominated debt; and e = nominal exchange rate depreciation (measured by increase in local currency value of U.S. dollar).

4/ The real interest rate contribution is derived from the numerator in footnote 3 as $r - \pi(1+g)$ and the real growth contribution as $-g$.

5/ The exchange rate contribution is derived from the numerator in footnote 3 as $ae(1+r)$.

6/ Includes social security surplus, accumulation of deposits from the sovereign bond issuance in 2014, and financing of the national development bank.

7/ Includes asset changes and interest revenues (if any). For projections, it includes the impacts of exchange rate changes.

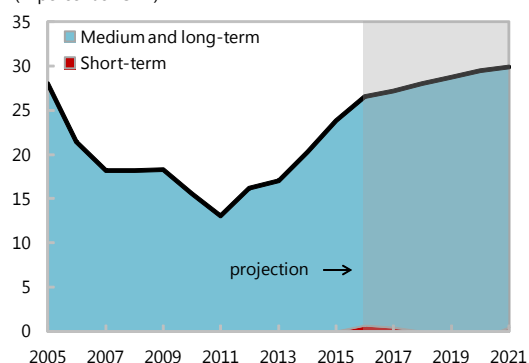
8/ Assumes that key variables (real GDP growth, real interest rate, and other identified debt-creating flows) remain at the level of the last projection year.

Table. 2. Paraguay: Public DSA – Composition of the Public Debt and Alternative Scenarios

Composition of Public Debt

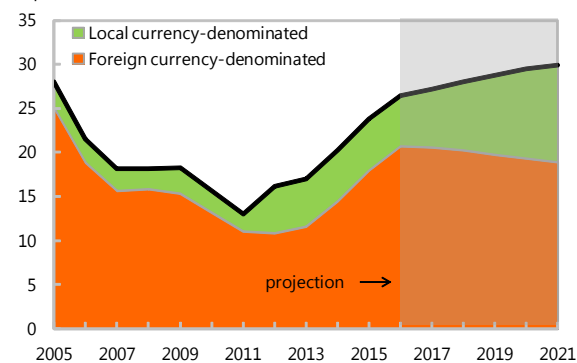
By Maturity

(in percent of GDP)



By Currency

(in percent of GDP)



Alternative Scenarios

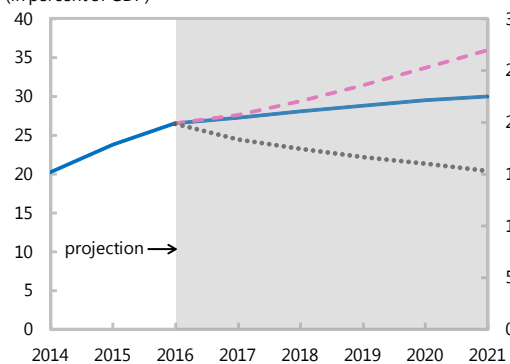
— Baseline

..... Historical

- - - Constant Primary Balance

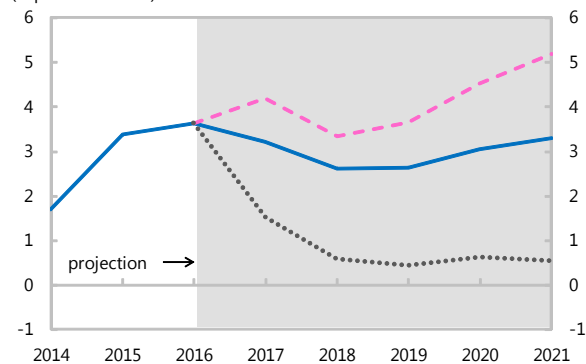
Gross Nominal Public Debt

(in percent of GDP)



Public Gross Financing Needs

(in percent of GDP)



Underlying Assumptions

(in percent)

	2016	2017	2018	2019	2020	2021
Baseline Scenario						
Real GDP growth	2.9	3.2	3.5	3.7	3.9	4.0
Inflation	5.0	3.5	3.7	3.6	3.9	4.0
Primary Balance	-1.4	-1.0	-0.5	-0.2	0.1	0.4
Effective interest rate	4.4	4.4	5.0	5.7	6.3	7.0
Constant Primary Balance Scenario						
Real GDP growth	2.9	3.2	3.5	3.7	3.9	4.0
Inflation	5.0	3.5	3.7	3.6	3.9	4.0
Primary Balance	-1.4	-1.4	-1.4	-1.4	-1.4	-1.4
Effective interest rate	4.4	4.4	5.2	5.9	6.6	7.2
Historical Scenario						
Real GDP growth	2.9	5.1	5.1	5.1	5.1	5.1
Inflation	5.0	3.5	3.7	3.6	3.9	4.0
Primary Balance	-1.4	1.2	1.2	1.2	1.2	1.2
Effective interest rate	4.4	4.4	4.8	5.1	5.3	5.6

Source: Fund staff estimates and projections.

Annex V. Spillovers from Brazil¹

To assess the effect of a shock to growth in Brazil on growth in Paraguay, a set of Vector Autoregressions (VARs) have been estimated. The main finding is that when Brazil GDP falls by 1 percentage point, on average, this is associated with a fall in Paraguay's GDP by about ½ to ¾ percentage points; however these estimates are often imprecise and the confidence intervals may include zero.

A standard VAR model is used to identify the dynamic response of Paraguay's GDP to a shock to growth in Brazil. We estimate several models with three sets of variables: global, regional and domestic. The global variables include the VIX volatility index, the 10-year U.S. Treasury bond yield, world price of soy, and the Paraguay-specific commodity terms of trade index (as in Gruss (2014) and WHD REO (2014)). The key regional variable is, of course, Brazil GDP. The domestic variables are Paraguay GDP and the real effective exchange rate for Paraguay. The model is estimated using quarterly data from 1994Q1 to 2015Q3, with two lags, and all variables are expressed in quarter-on-quarter growth (seasonally adjusted for GDP), except for the VIX and the U.S. interest rate, which are expressed in levels. Global variables are ordered first, followed by Brazil GDP, and then domestic variables, so that VIX, the U.S. interest rate and Brazil GDP do not respond to changes in Paraguay's conditions.² In addition, a different specification in which the VIX and the U.S. interest rate are exogenous was also run and is reported at the bottom of Table 1, producing similar results.

Table 1. VAR Model Results

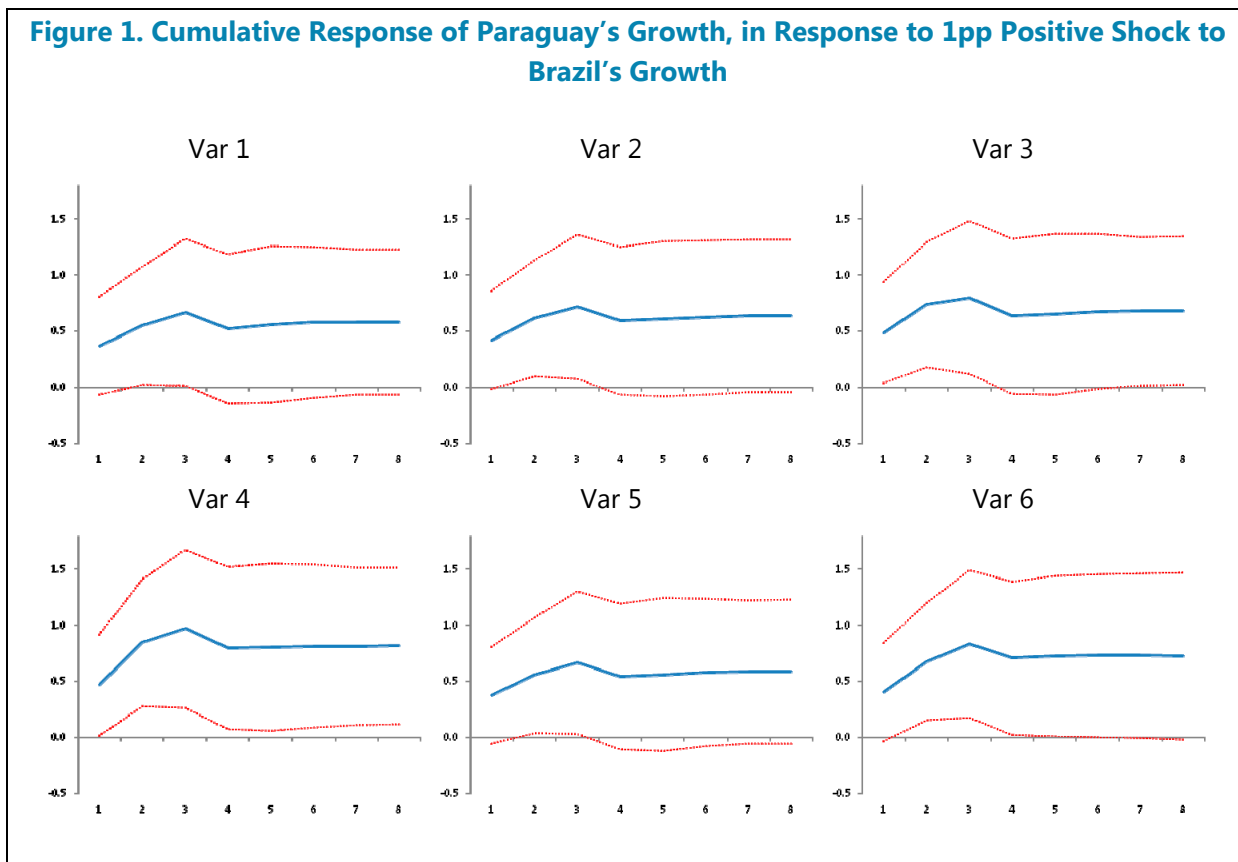
Model variables, ordered	Response of PRY GDP to 1pp rise in BRA GDP:		
	At quarter of largest cumulative effect	8 quarters after BRA shock	4 quarters after BRA shock
Var 1: VIX, US interest rate, Soy prices, BRA GDP, PRY GDP, REER	0.58	0.51	0.45
Var 2: VIX, Soy prices, BRA GDP, PRY GDP, REER	0.61	0.54	0.51
Var 3: US interest rate, Soy prices, BRA GDP, PRY GDP, REER	0.68	0.58	0.54
Var 4: US interest rate, Commodity TOT, Brazil GDP, PRY GDP, REER	0.78	0.66	0.64
Var 5: VIX, US interest rate, Soy prices, Brazil GDP, PRY GDP	0.59	0.52	0.48
Var 6: VIX, Commodity TOT, BRA GDP, PRY GDP, REER	0.68	0.59	0.58
Soy prices, BRA GDP, PRY GDP, REER; Exogen: VIX, US interest rate	0.77	0.69	0.69

Source: IMF staff calculations.

¹ Prepared by Natalija Novta (WHD).

² The general approach is similar to the one taken in 2015 selected issues paper for Paraguay, as well as the 2012 Regional Economic Outlook for the Western Hemisphere.

While a shock to Brazil’s GDP³ can have a sizeable effect on Paraguay, this effect is often not statistically different from zero. In other words, the effect is imprecisely estimated, and the confidence intervals for the cumulative effect after 4 quarters range from no effect to well over 1 percentage point (Figure 1). To a large extent this is due to the fact that economic growth in Paraguay is very volatile, given the prominence of agriculture and electricity sectors which are dependent on the weather. The current crisis in Brazil has had an impact on Paraguay, mainly through diminished activity in border towns and smaller re-exports. However, other sectors of Paraguay’s economy are still relatively resilient even as Brazil nears 8 quarters of negative growth.



³ The shock shown in Figure 1 is a positive shock to Brazil’s GDP. The x-axis shows quarters after the shock hits Brazil, and y axis shows the cumulative change in Paraguay’s growth in response the shock in Brazil’s growth.

References

Gruss, B. (2014) "After the Boom-Commodity Prices and Economic Growth in Latin America and the Caribbean" IMF Working Paper 14/154. (Washington: International Monetary Fund).

International Monetary Fund (2012) "Spillovers from Large Neighbors in Latin America" Chapter 4 in *Regional Economic Outlook: Western Hemisphere*, Washington, April.



PARAGUAY

STAFF REPORT FOR THE 2016 ARTICLE IV CONSULTATION— INFORMATIONAL ANNEX

April 14, 2016

Prepared By

The Western Hemisphere Department
(In consultation with other departments)

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FUND RELATIONS

(As of March 31, 2016)

Article VIII

Membership Status: Joined: December 28, 1945

General Resources Account:	SDR Million	% Quota
Quota	201.40	100.00
IMF's Holdings of Currency (Holdings Rate)	154.55	76.74
Reserve Tranche Position	46.85	23.26

SDR Department:	SDR Million	% Allocation
Net cumulative allocation	95.19	100.00
Holdings	95.68	100.51

Outstanding Purchases and Loans: None

Latest Financial Arrangements:

Type	Date of Arrangement	Expiration Date	Amount Approved (SDR Million)	Amount Drawn (SDR Million)
Stand-By	May 31, 2006	Aug 31, 2008	30.00	0.00
Stand-By	Dec 15, 2003	Nov 30, 2005	50.00	0.00

Projected Payments to Fund^{1/}

(SDR Million; based on existing use of resources and present holdings of SDRs):

	Forthcoming			
	2015	2016	2017	2018
Principal				
Charges/Interest	0.00	0.00	0.00	0.00
Total	0.00	0.00	0.00	0.00

^{1/} When a member has overdue financial obligations outstanding for more than three months, the amount of such arrears will be shown in this section.

Exchange Arrangement: The currency of Paraguay is the Paraguayan guaraní. The exchange arrangement of the guaraní is floating, and the exchange rate is determined by supply and demand. The objective of the Central Bank of Paraguay (BCP) under Article 3 of Organic Law No. 489/95 is to preserve and safeguard the stability of the currency and promote the efficiency and stability of the financial system. Article 50 establishes that foreign currency trading by the BCP aims to smooth seasonal fluctuations in supply and demand and offset erratic capital flows and speculative movements that could disrupt the market or the exchange rate. Article 47 establishes that the exchange rate is determined by market forces. The BCP publishes information on its foreign exchange interventions on its website. The BCP intervenes occasionally in the market to smooth the

effects of undue fluctuation. The BCP, as the government's financial agent, receives U.S. dollars from the government flowing from the royalties and compensation paid by the binational hydroelectric entities and exchanges them for *guaranies* at the request of the government for the purpose of public expenditures. The BCP implemented effective July 1, 2013, a program of preannounced sales of the U.S. dollars it purchases from the government. The new program is more transparent, better communicated, and more consistent with an inflation-targeting regime. This program indicates in advance the nature, frequency, and size of the BCP's foreign exchange transactions to avoid influencing market expectations of the exchange rate. Paraguay has accepted the obligations of Article VIII, Sections 2(a), 3, and 4 of the Fund's Articles of Agreement. Its exchange system is free of restrictions on the making of payments and transfers for current international transactions.

Article IV Consultation: The Executive Board concluded the 2014 Article IV consultation in February 2015.

Technical Assistance 2010–16:

DPT	Purpose	Date of Delivery
FAD	Debt Management	February 2010
MCM	First Issuance Sovereign Bond	March 2010
STA	Monetary and Financial Statistics	April 2010
MCM	Banking Supervision	April 2010
STA	National Accounts	August 2010
MCM and WB	FSAP/FSSA	November 2010
FAD	Tax and Customs Administration	December 2010
FAD	Public-Private Partnerships	February 2011
STA	National Accounts Statistics	March–April 2011
FAD	Medium-Term Macro-Fiscal Framework and Public Investment Management	March–April 2011
MCM	Monetary Policy, Central Bank Operations, and Accounting	April 2011
FAD	Public Transport Subsidies	June–July 2011
MCM	Financial Soundness Indicators and Financial Oversight	November 2011
FAD	Improve Fiscal Projections and Financial Planning	December 2011
FAD	Modernization of the Customs Administration	December 2011
FAD	Debt and Cash Management	March 2012
FAD	Tax Policy	March 2012
MCM	Monetary Policy, Central Bank Operations, and Accounting	April 2012
FAD	Tax and Custom Administration	December 2012
FAD	Debt and Public Investment Management	May 2013
MCM/LEG	Launch of the AML/CFT	June 2013
MCM	Inflation Targeting and Central Bank Operations	August 2013

PARAGUAY

FAD	Revenue Administration	September 2013
FAD	Tax Administration	December 2013
STA	ROSC	February 2014
FAD	Tax and Customs Administration	Apr, May, Jul, Sep
MCM	Bank Supervision and Regulation	July 2014
MCM	Monetary and FX Policy	July 2014
LEG	Anti Money Laundering Activities	May, Jun, Sep 2014
FAD	Public Financial Management	July 2014
STA	Producer Price Index Statistics	August 2014
STA	Balance of Payments and IIP Statistics	September 2014
MCM	Central Bank Monetary and Foreign Exchange Operations	October 2014
MCM	Insurance Supervision	December 2014
FAD	Budget Preparation and Execution	December 2014
LEG	Anti Money Laundering Activities	February 2015
STA	Government Financial Statistics Mission	March 2015
MCM	Risk-Based Bank Supervision	April 2015
LEG	Anti Money Laundering Activities	April 2015
FAD	Customs Administration	May 2015
MCM	Bank Stress testing	May 2015
FAD	Tax Revenue Administration	July 2015
MCM	Risk-Based Bank Supervision	August 2015
LEG	Anti Money Laundering Activities	September 2015
MCM	Risk-Based Bank Supervision	November 2015
LEG	Anti Money Laundering Activities	December 2015
MCM	Foreign Exchange Operations	February 2016
FAD	Tax Revenue Administration	March 2016
FAD	Fiscal Responsibility Law	March 2016
LEG	Anti Money Laundering Activities	March/April 2016

Safeguards Assessment: Under the Fund's safeguards assessment policy, the BCP was subject to a full safeguard assessment in respect to the arrangement approved on May 31, 2006. A safeguards assessment of the BCP was completed in October 2006. The report stated that while the BCP has made some progress in strengthening the safeguards framework since the 2003 safeguards assessment, vulnerabilities remain in certain areas such as financial reporting and program data reporting to the Fund.

Resident Representative: Mr. Alejandro Santos has been the regional resident representative since December 2014. He is based in Lima, Peru.

RELATIONS WITH THE WORLD BANK UNDER JMAP

Meeting of teams. The IMF and World Bank Paraguay teams met in January 2016 to exchange views on economic developments and the macroeconomic outlook in Paraguay, and discuss ongoing work and work plans for the year ahead. The IMF mission also met with the World Bank's representative in Asuncion during the Article IV mission. This section summarizes key themes of the discussions.

The outlook for Paraguay is challenging given the regional context and will require policies to consolidate macroeconomic stability and address structural problems. Paraguay enjoyed strong growth over the period 2003–14 and achieved significant progress in poverty reduction.

Nevertheless, important barriers to development persist, including large infrastructure gaps, limited capacity to execute public investment projects, and deep-rooted institutional weaknesses. The challenge ahead is to advance the structural reform agenda, without jeopardizing the sound macroeconomic position attained over the past decade.

In this context, the following reform areas have been identified as macro-critical:

- *Fiscal and public financial management framework.* The fiscal responsibility law provides a suitable anchor for fiscal sustainability, but there is scope to adopt measures to improve budgetary processes and strengthen legal and institutional aspects of the fiscal framework. Potential fiscal risks, including from private sector participation in infrastructure investment, need to be addressed proactively.
- *Tax revenue administration.* Strengthening tax administration and enforcement is necessary to mobilize revenues while enhancing the efficiency and equity of the system. This includes measures to strengthen sanctions against evasion, reducing exemptions, and exploring the possibilities to broaden the tax base.
- *Infrastructure.* Improvements in public infrastructure, including transport, electricity, and water and sanitation are crucial to support economic development and increase potential growth. Boosting the pro-poor delivery of public goods and services, including in education and health, will contribute to poverty reduction and shared prosperity.
- *Financial system.* The new banking and central bank laws should provide a robust legal basis for risk-based regulation and supervision. There is still a need to strengthen the prudential oversight of the cooperative sector and foster cooperation among the different regulatory authorities.

The division of labor between the teams would be along the following lines:

- *Tax revenue administration, fiscal responsibility law, and government finance statistics.* The Fund will continue to support the authorities' efforts to improve the tax system and increase revenue collection through technical assistance (TA). It is also envisaged that a technical assistance mission on strengthening the legal and institutional framework for the fiscal responsibility law will take place in

the spring of 2016. The Fund will also provide technical assistance to cement Paraguay's transition to the GFSM 2001 standards for its fiscal accounts, including further support to fully move towards accrual accounting.

- *Financial system.* The Fund will continue to provide TA on the implementation of risk-based bank supervision and regulation and stands ready to assist in the implementation of the new banking laws. The Fund will also provide follow-up support on stress testing of the insurance sector and on developing monitoring tools to reduce contagion risk between the banking and insurance sectors.
- *Foreign Exchange operations.* The Fund will provide technical assistance to the BCP on foreign exchange operations, including on steps to strengthen a rules-based approach to foreign exchange interventions.
- *Paraguay Job Diagnostic:* The Bank will undertake a comprehensive multi-sector job diagnostic analysis to identify challenges for expanding and improving employment opportunities in Paraguay.
- *State-owned enterprises and PPPs.* The Bank will continue to provide TA to support the government's efforts to improve corporate governance, eliminate payment arrears, and technical oversight of SOEs and strengthen the PPP institutional framework. In addition, The Bank will support the authorities' efforts to assess fiscal risks and contingent liabilities from SOEs.
- *Governance and Business Climate.* The Bank will continue its support to the government's efforts to strengthen institutional capacity, improve governance and transparency for a more efficient management of public resource. The Bank will support the authorities' efforts to boost competitiveness, through the promotion of a better investment and business climate.

Work programs. The table below lists the teams' work programs for the year ahead.

Work Programs of The World Bank and IMF Teams			
Title	Products	Provisional Timing of Missions	Expected Delivery Date
<i>Bank Work Program</i>			
	Programmatic TA on strengthening Governance		June 2016
	Programmatic TA on Finance and Markets		June 2016
	Programmatic TA on Improved Territorial Development.		June 2016
	TA for WTO Trade Facilitation Agreement		June 2016
	Programmatic TA on Fiscal equity and efficiency, and macro resilience		December 2016
	TA on Improving investment climate		December 2016
	TA on Institutional strengthening for the implementation of the PPP program		December 2016
	TA on strengthening Agriculture Risk Management System		December 2016
	Programmatic TA on poverty Jobs Diagnostic Analysis		June 2017
<i>Fund Work Program</i>			
	Article IV Consultation	February 2016	April 2016 (Board Date)
	TA on Risk-based Bank Supervision & Regulation	November 2015	
	TA on Anti Money Laundering Activities	December 2015	
	TA on Foreign Exchange operations	February 2016	
	TA on Tax Revenue Administration	Spring 2016	
	TA on Fiscal Responsibility Law	March 2016	
	TA on Anti Money Laundering Activities	April 2016	
	TA on Government Finance Statistics	April 2016	
	TA on Insurance Supervision: Follow-up on Stress Testing and Contagion Risk	April 2016	

RELATIONS WITH THE INTER-AMERICAN DEVELOPMENT BANK

Meeting of teams. The IMF and IADB Paraguay teams met in November 2015 to exchange views on economic developments in Paraguay, and discuss ongoing work and work plans for the year ahead. The IMF mission also met with IADB staff based in Asuncion.

The IADB's Board of Executive Directors approved in 2014 the Country Strategy with Paraguay (2014–2018). Sovereign-guaranteed lending under the program is expected to reach approximately US\$1 billion. Under the Strategy, the national authorities and the Bank identified the following priority sectors in which the IDB Group would focus both its financial and non-financial products and services: (i) transportation and connectivity; (ii) water and sanitation; (iii) energy; (iv) productive development; (v) financial sector; and (vi) public management. Furthermore, the Bank will support the social sector through two channels: (i) with specific interventions in each of the priority sectors, in support of the objective of reducing extreme poverty; and (ii) through a crosscutting element in the form of interventions to support the investment of FONACIDE resources, primarily targeting education and health.

As of November 30, 2015, the Bank's active portfolio in Paraguay included loans for the financing of 21 projects. The lending portfolio amounts to US\$850 million, of which US\$447 million are pending disbursement. Disbursements in 2015 are expected to total US\$41 million. The current portfolio includes lending to support the Government in the following sectors: transportation (51 percent), energy (10 percent), social sector (2 percent), financial sector (8 percent), education (4 percent), agriculture (3 percent) and others (22 percent). The portfolio additionally includes 6 projects pending legislative ratification, amounting to US\$395 million, and one project pending signature which amounts to US\$20 million. Additionally, the portfolio includes 18 loans to the private sector for US\$98 million, mostly in the financial sector.

Financial Relations with the Inter-American Development Bank¹

(In millions of U.S. dollars)

Loan Transactions

	2006	2007	2008	2009	2010	2011	2012	2013	2014	2015
Disbursement	67.2	67.8	85.6	91.3	240.3	91.4	102.8	142.4	81.4	41.0
Amortization	66.7	88.1	94.3	91.3	96.2	94.5	91	83.9	97.7	132.4
Net Loan Flows	0.5	-20.3	-8.7	0	144.1	-3.1	11.8	58.5	-16.3	-91.4

Source: Inter-American Development Bank

¹/Only loans with sovereign guarantee are considered.

STATISTICAL ISSUES

(As of April 2016)

Assessment of Data Adequacy for Surveillance

General: Data provision to the Fund has some shortcomings, but is broadly adequate for surveillance. Paraguay has made significant improvements in the compilation and dissemination of macroeconomic statistics, but some shortcomings persist. In February 2014, a Data ROSC mission conducted an assessment of data quality based on the new 2012 DQAF for six datasets (national accounts, CPI, PPI, GFS, monetary, and balance of payments and IIP statistics). The mission also assessed Paraguay's macroeconomic statistics against the GDDS and, at the request of the authorities, against the SDDS; the authorities' response to the report and the mission's recommendations were published on the Fund's website on August 18, 2014. The country is a GDDS participant.

National Accounts. National accounts estimates, broadly consistent with the guidelines of the *1993 SNA*, were released in 2005. A program for changing the outdated base year (1994=100) and implementing relevant *2008 SNA* recommendations is under development. The production boundary is broadly in line with the *1993 SNA* and recently included the two binational hydroelectric enterprises following the *2008 SNA*. Nonetheless, there are no independent estimates of the non-observed economy after 1997, and mineral exploration and own-account production are mostly excluded. Source data for nonfinancial services, household consumption, and changes in inventories are insufficient. Currently, the major deviations from concepts and definitions established in the *1993 SNA* involve: investment in in-house development of software; investment in mineral exploration; investment in military expenses in fixed assets; the estimation of output broken down by market, nonmarket, and own final use components; the inclusion of work-in-progress in forestry and livestock production; and the partial inclusion of the non-observed economy in the national accounts. Annual GDP meets GDDS recommendations, and QNA meets DSSD timeliness requirements (90 days)

Labor market. Since the introduction of a regular household survey in 1998, the coverage and quality of employment and unemployment statistics have improved significantly. Since 2010, data are released on a quarterly basis, although the latter covers the Asunción area only. The last available observation for the quarterly series is the fourth quarter of 2015.

Price statistics. Both the consumer (CPI) and producer price indices (PPI) are reported on a regular and timely basis. Since January 2008, the Central Bank of Paraguay (BCP) has been using a CPI index based on the 2005–06 household budget survey. The geographic coverage of the CPI is limited to Greater Asunción (the capital and metropolitan area), and expenditure weights are representative of the consumption patterns of urban households. The PPI has a base weight period of June 2010 and its basket (185 items) is representative of current national output; electricity, water, and gas are not covered.

The data ROSC mission found that the resources are insufficient for real sector statistics and constrain further development, particularly the full adoption of the 1993 SNA. The authorities have been trying to address these resource shortcomings in the context of the recent compilation of a new CPI and the production of QNA series.

Government finance statistics. The government finance statistics (GFS) used for internal purposes and for reporting to WHD are broadly consistent with the recommendations of the *Government Finance Statistics Manual 2001* (GFSM 2001). In early 2015, the Ministry of Finance introduced GFSM 2001 classifications and presentation for monthly budgetary central government statistics, which are published regularly on the Ministry's website. The asset position of the social security system is available on a daily basis. Statistics on the central administration include data of the Postal Service Directorate (a nonfinancial public corporation) and the statistics of the nonfinancial public sector include data of financial public corporations—four employer social insurance schemes. These social insurance schemes are treated as financial corporations in the monetary and financial accounts. Data on medium- and long-term external debt are reliable and available on a monthly basis. Deficiencies remain in recording short-term supplier and commercial credit of the public sector. The latest available data for general government and its subsectors in the 2014 GFS Yearbook are for 2013. However, since 1994 no outstanding debt data and no breakdowns for expenditure by function have been provided for publication in the GFS Yearbook. Monthly and quarterly data are not reported for publication in IFS.

Balance of payments. The classification of the balance of payments and the international investment position (IIP) follows the recommendations of the fifth edition of the *Balance of Payments Manual* (BPM5). Quarterly data on balance of payments and the IIP are available from 2001 onwards, and are reported to STA for publication in the IFS. Improvements have been made in the quality of the external sector statistics, especially in the coverage of foreign direct investment and in the recording of external debt transactions but some deficiencies remain. An STA mission on External Sector Statistics assisted the BCP in September 2014 in implementing recommendations of the ROSC mission. One of the main recommendations of the mission, submit quarterly balance of payments and IIP data on a *BPM6* basis, has not been implemented yet.

Monetary and financial statistics. Paraguay reports monetary data for the central bank and other depository corporations (ODCs) using the standardized report forms (SRFs). An integrated monetary database meeting the data needs of the BCP, STA, and WHD is in operation. Coverage of the ODC survey is complete, including data on credit cooperatives. The Superintendence of Banks reports 11 of the 12 core and 7 of the 13 encouraged financial soundness indicators for deposit takers to STA on a monthly basis.