



Highlights of Paraguay 2009 – 2010

1 2009 - Drought causes severe reduction in GDP

Drought has interrupted a cycle of economic expansion giving rise to negative expectations for the economic agents, suspension of significant investments and reductions in the levels of economic activity. Further aggravating the internal situation, the international crisis created additional pressure on foreign trade transactions, and also on internal consumption which was maintained only by means of an expansive and anti-cyclical fiscal policy applied by the Government.

Performance of the Economy

❖ Gross Domestic Product

The economy of Paraguay suffered a significant downturn in its previous growth dynamics until 2008, showing an actual 3.8% reduction in comparison with the 5.8% growth of 2008, the first fall after 6 years of consistent growth. The downturn represented a 5.5% decrease in per-capita GDP in constant US dollars down to USD 1,471, equivalent to USD 2,350 in current dollars. In order to compensate the fall in private expenditure the Ministry of Finance applied an anti-cyclical fiscal policy with a fiscal stimulus impact representing 3.9% of GDP, together with an increase in physical investment of 1.1% in terms of GDP. International reserves increased 34.8% in comparison with 2008, up to USD 3,860.7 million, equivalent to 24.2% of GDP.

❖ Performance by sectors

There was a 23.8% decrease in the agricultural sector, the main factor for the downturn in the overall economy, decreasing the sector's share in GDP by 4.2 percentage points to a 16% weight in GDP, in retreat to its average position during years 2000 and 2001. The soybean crop, driver of the sector, fell 39%, down to 4.15 million tons, due to a 1.8% decrease in the area sowed plus a steep 38% decrease in yields that barely reached 1,599 kilograms per hectare due to the drought during the first few months of 2009.

The sectors other than agriculture showed positive evolution for the seventh consecutive year, recording a 1.2% growth in 2009, which fell 3.5 percentage points short of their growth rate in 2008. The overall increase in these sectors was based on the good performance of services in general, with growth rates of 15.9% for government services, 11.5% for business services, 5% for each household and communications services and 8% for financial services. Ranching also contributed with a 4% growth while other significant sectors showed decreases at negative rates of 4% for commerce, 1.9% for manufacturing and 7.5% for transportation.

Finally, while construction suffered a strong slowdown, public investment continued growing for the third consecutive year, but with a modest 1% rate which fell ten percentage points below the 2008 growth rate.

❖ External sector

In accordance with estimates of the Central Bank of Paraguay (CBP) the country's exports during year 2009 amounted USD 5,770.5 million, which includes officially reported transactions, re-exports, under-reported transactions, sales of goods to bi-national entities, sales of electric power and other, representing a decrease of 25.75% on the exports of 2008. Likewise, officially registered and unregistered import's transactions decreased 23.9% in total, aggregating USD 6,806.1 million and resulted in a deficit of USD 1,035.6 million in the balance of trade, which however was 11.8% lower than the comparable deficit of 2008.

❖ Employment

The slowdown in the economic activities led to increase the unemployment rate to 9% in accordance with estimates developed by the PricewaterhouseCoopers Economy Club. The official minimum salary in force effective May 2009 is Guaranies (PYG) 1,408,864 equivalent to USD 284 at the average exchange rate of year 2009, PYG 4,967 to USD 1.

❖ The Financial System

In order to inject liquidity into the financial system to mitigate the effects of the international financial crisis, the CBP applied an expansive monetary policy during 2009, withdrawing US dollars from the market and lowering the reference interest rates. As a consequence, credits increased 31.8% in local currency and 17.7% in foreign currency, while deposits increased 44.7% in Guaranies and 25.8% in US dollars.

❖ Inflation and international interest rates

The serious fall in the economic activity was decisive for avoiding the transfer of the excess money in circulation to the price structure, which led to harness inflation at 1.9% below the CBP target floor for 2009. However, inflationary pressures came from the increase in the average exchange rate and from a 4.4% increase in food products due to the official protectionist policy, which precluded the free importation of fruit and vegetable products that recorded aggregate price increases of 20.8% in year 2009.

The average exchange rate of the US dollar measured in local currency was PYG 4,967, up 13.9% from the 2008 average, representing the nominal depreciation of the Guaraní in terms of the US dollar. In constant currency terms, the depreciation of the effective exchange rate was 7%, which is an indication that, in the average, the country has gained competitive capacity during year 2009.

2 Fiscal Aspects

The main changes in tax legislation applicable to years 2009 and 2010 are the following:

❖ Personal Income Tax (PIT)

This tax is in force as from January 1, 2010 after several postponements.

The tax is levied, among other, on income of Paraguayan source derived from activities generating personal income, and the designated taxpayers are individuals and Simple partnerships.

Draft legislation has been presented in Paraguayan Congress aimed at repealing the law or postponing it for another two years.

In the meantime, as long as the law is neither promulgated nor repealed, the tax would remain in force at the general tax rate of 10 %.

Both the individual and the Simple Company taxpayers will have a term of 30 working days for registration with the Tax authority and filing of Sworn Declaration reporting their incomes. In the case of individuals, the 30 days are counted as from the date their personal income exceeds 10 minimum salaries per month (aggregating about USD 34,000 per annum) and in the case of Simple Companies as from their date of constitution independently from the amount of their income.

The sworn declaration of incomes may be filed in custody with a Notary Public in a lacquer-sealed envelope, who must issue a custody statement for presentation to the Tax Administration.

Inception of the tax obligation is configured at the end of fiscal year that coincides with the calendar year. The cash basis is the method of recognition of results: cash received for income and cash paid for expenditure.

❖ Purchase and/or sale of real estate property within Paraguay

These transactions executed between foreign legal entities not structured in Paraguay or not having appointed a legal representative in Paraguay, will no longer require presentation to the intervening notary public of a Tax clearance certificate or communication confirming the non-taxpayer status of the intervening parties.

However, sales transactions will require presentation of the payment voucher of the applicable Business Income Tax (“BIT”) and the notary will be the designated withholding agent for the corresponding Value added tax (VAT).

❖ Communication of assignment for sale of company share or quota holdings

General Resolution No. 23/09 issued by the Tax Administration has specified the data to be reported by the taxpayers in their communication of such assignments in compliance with the respective legal regulations, as follows:

- a) nominal value of the shares or quotas
- b) market value of the transfer
- c) identification of the company owning the shares or quotas being assigned
- d) name and surname or company name of the buyer
- e) date of the sale transaction
- f) type and reference number of the instrument documenting the sale transaction.

Such communication by the taxpayer is the condition that will ensure that the assignment of the shares or quota holdings will not be subject to VAT.

❖ Bio-fuel – detailed rulings on incentives for their development in the country

Decree No. 3,667/09 issues rulings for incentives encouraging the production of bio-fuel in Paraguay, benefiting the sectors engaged in the production, marketing and importation of goods that will impact the offer and demand of bio-fuel produced locally.

This decree includes the following provisions:

In connection with the bio-fuel production process, the importation of the fixed assets required can be made under the benefits of Investment Law No. 60/90; raw materials can be included under the exception agreements of the Common MERCOSUR Tariff.

Further, the importation vehicles utilizing the “flex-fuel” technology, which can use indistinctly hydrated ethanol and pure gasoline or mixed with dehydrated ethanol, or a combination of both in any proportion including E 85 vehicles, will enjoy a 0% tariff in accordance with the Common MERCOSUR Nomenclature. In addition, Government entities or bodies must give preference to the acquisition of this type of vehicles.

In transactions of importation or sale of alcohol-fuel, pure (absolute) alcohol and bio-diesel fuel, VAT may be levied at the 10% rate applied on 20% of the custom value plus other taxes imposed on the transaction before clearance from customs.

In addition to the Ministry of Finance, other entities having tuition on these matters are the following:

- a) Ministry of Agriculture and Ranching
- b) Ministry of Industry and Commerce
- c) National Customs Authority

3 Prospects for year 2010

Based on the solid economic foundations leading to a relatively soft landing by the end of year 2009 and on the anti-cyclical fiscal policy in coordination with an expansive monetary policy, Paraguay has been able to overcome the obstacles generated by the drought and by the international financial crisis. During the last quarter of 2009 there were certain indications of increasing activity in the economy.

Regarding year 2010, investments in the range of USD 250 million are foreseen in the frame of the “Asunción 2011” project aimed at the construction of the trunk system for public transportation, the city’s waterfront avenue and the moving of public administration premises to buildings located in the ancient down-town area of the city along the new avenue. The Asunción 2011 project forms part of the city’s bicentennial celebration with funding provided by the Inter-American Development Bank, included within its five-year plan providing for disbursements in the range of USD 1 billion.

In addition, the current climate conditions are favoring the agricultural sector, as rainfall is accompanying the soybean production cycle with an increase in the yield expectancy of about 2,792 kilograms per hectare and an overall crop estimated at 7.48 million tons. These excellent prospects for the agricultural sector may lead to a GDP figure significantly above the level reached in 2009. The range of GDP growth is estimated at 9.0 percent in a base scenario, with a lower limit of 7.2% and a higher limit of 11.2%.

The increase in agricultural activity comes together with the recovery of the refinancing credits disbursed in 2009, benefiting the agents related to the sector, and possibly encouraging investments therein. On another hand, there is 35% increase expectancy for exports together with a level of inflow of family remittances from Paraguayan expatriates working abroad, similar to that of 2009.

Another significant factor is the possible improvement in the labor market, with an unemployment rate estimated at 7.5%, 1.3 percentage points down from the 2009 rate, with the consequent positive impact on household consumption, which however may generate greater inflationary pressure, that would increase compared to 2009, finishing the year at 5.5% within the CBP’s target.

Finally, given the current international and local conditions, it is estimated that the exchange rate of the US currency will keep stable, within a range estimated at PYG 4,527 to USD 1 in a base-scenario, with a lower limit of PYG/USD 4,765 and an upper limit of PYG/USD 4,645.



4 Principal Indicators of the Economy

(Certain 2009 indicators are preliminary And subject to variation)

	2010*	2009	2008	2007	2006	2005
GDP (in % of annual growth)	9.0	-3.8	5.8	6.8	4.3	2.9
GDP USD per capita	1,590	1,485	1,572	1,512	1,442	1,394
Consumers' price index (annual %)	5.5	1.9	7.5	6.0	12.5	9.9
Closing exchange rate (sellers)	4,685	4,620	4,960	4,900	5,210	6,140
Average exchange rate (annual buyers/sellers)	4,643	4,967	4,364	5,033	5,635	6,178
Variation in the average sellers rate (annual %)	1.4	-6.9	1.2	-6.0	-15.1	-1.9
Variation in the average buyers rate (annual %)	-6.5	13.8	-13.3	-10.7	-8.8	3.3
Population (in thousands)	6,388	6,275	6,164	6,055	5,946	5,899
Population growth (annual %)	1.8	1.8	1.8	1.8	0.8	1.9
Unemployment % (both overt and covert)	7.58	8.8	7.2	8.5	11.1	9.4
Exports (% of GDP)	24.4	21.2	26.5	23.0	19.9	22.1
Imports (% of GDP)	48.3	43.4	50.4	45.3	48.5	41.1
Surplus/Deficit (+/-) of public sector (in guaranis)	-421	61	1,831	448	264	374
Surplus/Deficit (+/-) of public sector (% of GDP)	-0.5	0.1	2.5	0.7	0.5	0.8
Foreign debt (% of GDP)	14.2	14.9	13.2	18.0	24.0	30.4

(In millions of USD)

Gross domestic product	18,149	14,972	16,872	12,222	9,276	7,473
Surplus/Deficit of public sector (+/-)	-91	12	419	89	47	61
Exports (FOB)	4,434	3,167	4,663	2,817	1,843	1,655
Re-exports	4,534	2,551	3,248	2,772	2,431	1,607
Imports (FOB)	8,771	6,497	8,506	5,539	4,502	3,703
Balance of trade -deficit	-4,337	-3,330	-4,043	-2,721	-2,659	-1,418
Foreign debt	2,572	2,237	2,234	2,205	2,230	2,271

* Projected figures for year.

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