

I. ECONOMIC ENVIRONMENT

(1) OVERVIEW

1. El Salvador's real GDP grew at an average annual rate of 3.1 per cent in the period 2003-2008 - below the average for Latin America in the same period, but slightly faster than in the years covered by the previous Review. Growth accelerated in 2006 and 2007, notably as a result of a strong surge in domestic demand; but it then slowed sharply from the second half of 2008 onwards in the wake of the international crisis, which also resulted in lower levels of investment, exports and remittances from Salvadoran workers abroad, and a drop in gross private capital formation of some 5 per cent for 2008 as a whole.

2. As El Salvador is a dollarized economy, it cannot conduct an autonomous monetary policy; so fiscal policy plays a key role. The fiscal deficit narrowed steadily between 2003 and 2007, before expanding in the first few months of 2009 to give a central government deficit of 1 per cent of GDP in June 2009, as a result of lower income and higher spending. The NFPS (non-financial public sector) deficit stood at 1.3 per cent of GDP in June 2009.

3. The current account deficit grew steadily from 2005 onwards, fuelled mainly by faltering merchandise trade, to reach 7.6 per cent of GDP in 2008. The deficit has been offset by the high level of current transfers, chiefly consisting of remittances from Salvadorans living abroad, which were equivalent to 17.1 per cent of GDP in 2008; and it has been financed by capital inflows, principally in the form of foreign direct investment (FDI), government bond issues and loans. El Salvador has also negotiated loans from the World Bank and the Inter-American Development Bank (IDB) totalling US\$950 million. In September 2009, the International Monetary Fund (IMF) and the Salvadoran authorities reached preliminary agreement on a new economic programme, which could be underpinned by a three-year stand-by arrangement (SBA) for US\$800 million. This new programme replaces the 15-month precautionary SBA approved in January 2009.

4. Trade in goods and services represented 73.6 per cent of El Salvador's GDP in 2008, the country's leading partners for trade in goods (including the maquila industry) being the United States of America and the other members of the Central American Common Market (CACM). Manufactures remain the major export category, although the share of textiles and clothing shrank during the period under review, while share of commodities grew. Manufactures still also account for the largest share of imports. The traditional deficit in the balance of trade in services has widened since 2003 and was equivalent to 2.6 per cent of GDP in 2008.

(2) MACROECONOMIC TRENDS

(i) Structure and development of the economy

5. The sector composition of the Salvadoran economy changed during the period under review, largely reflecting the favourable international economic setting prevailing until mid-2008, and the various sectors' accommodation to this. For example, the share of agriculture in GDP increased from 8.3 per cent in 2003 to 12.2 per cent in 2008, mainly thanks to the rising trend in agricultural product prices, while the manufacturing sector, including the maquila industry, saw its GDP share at current prices shrink from 22.5 per cent to 20.1 per cent over the same period. Services accounted for 61.5 per cent of GDP in 2008, with commerce, restaurants and hotels (20.1 per cent of GDP in 2008) followed by transport (9 per cent) as the leading subsectors.

6. Real GDP expanded at an average annual rate of 3.1 per cent in 2003-2008 - below the Latin American average for the period, but slightly faster than the 2.8 per cent reported in the previous

Review for 1996-2001 (Table I.1). Growth gathered pace in 2006 and 2007, driven mainly by burgeoning domestic demand; but from the second half of 2008 onwards, the expansion was impacted by the international crisis, and gross private capital formation for 2008 was down by over 5 per cent.

7. Results for the first half of 2009 reveal a contraction in economic activity, reflecting the slump in external demand and smaller remittances. Goods exports were down by 16.5 per cent in nominal terms in the first quarter, and there was a particularly sharp decline in maquila exports, which fell by 22.8 per cent year-on-year.¹

Table I.1
Basic economic indicators, 2003-2009

	2003	2004	2005	2006	2007	2008	2009 I	2009 II
I. Gross Domestic Product (GDP)								
Current GDP (US\$ million)	15,047	15,798	17,070	18,654	20,373	22,115	5,521	5,468
Current GDP per capita (US\$)	2,504	2,621	2,822	3,071	3,341	3,611		
Gross disposable national income (US\$ million) ^a	16,738	17,895	19,526	21,595	23,546	25,410		
Net current transfers from abroad (US\$ million)	2,114	2,555	3,035	3,472	3,750	3,832		
Gross disposable national income per capita (US\$)	2,786	2,969	3,228	3,555	3,861	4,149		
Real GDP, rate of growth (%)	2.3	1.9	3.1	4.2	4.7	2.5	-1.8	-2.4
Domestic demand	3.3	2.7	3.1	6.9	5.9	2.7		
Final consumption expenditure	1.9	2.9	3.9	5.6	6.4	4.2		
Private consumption	2.1	3.0	4.0	5.9	6.8	4.3		
Public administrations	-0.3	1.1	1.8	2.8	1.1	1.8		
Gross capital formation	7.8	-3.9	2.5	6.8	6.4	-5.3		
Gross fixed capital formation	2.5	-5.0	2.1	11.1	6.4	-5.3		
Private	4.1	2.6	-0.8	12.7	7.7	-6.5		
Public	-4.9	-43.2	27.9	-0.4	-4.1	5.0		
Exports of goods and services	4.7	5.7	1.4	10.1	4.6	5.5		
Aggregate supply	3.3	2.7	3.1	6.9	5.9	3.4		
Imports of goods and services	4.8	4.1	3.1	11.2	7.9	4.7		
II. Sectoral breakdown (% of current GDP)^b								
Agriculture	8.3	8.9	9.7	10.1	11.2	12.2	12.0	12.4
Mining	0.5	0.4	0.3	0.3	0.3	0.4	0.4	0.4
Manufactures	22.5	22.1	21.1	20.6	20.3	20.1	20.0	20.2
Electricity, gas and water	2.0	1.8	1.8	1.9	1.8	1.9	2.0	2.0
Construction	4.7	4.2	4.2	4.2	4.0	3.9	4.4	4.0
Commerce, restaurants and hotels	19.4	19.8	20.0	19.8	20.0	20.1	20.2	20.0
Transport, storage and telecommunications	8.9	9.2	9.1	9.3	9.2	9.0	8.9	8.9
Financial services	4.3	4.5	4.5	4.5	4.5	4.4	4.4	4.4
Real estate	4.2	4.2	4.2	4.1	4.1	4.0	4.2	4.1
Housing	7.6	7.5	7.5	7.1	6.8	6.5	6.2	6.4
Community, social and personal services	7.4	7.7	7.4	7.3	7.2	7.2	7.4	7.4
Public services	6.9	6.6	6.5	6.6	6.4	6.4	6.7	6.7
III. Breakdown by expenditure (% of current GDP)								
Total consumption	98.9	101.0	102.0	103.3	105.3	107.5		
Private	89.0	91.4	92.4	93.7	96.1	98.4		
Public	9.9	9.6	9.6	9.6	9.2	9.2		
Gross fixed capital formation	16.7	15.7	15.3	16.1	16.1	15.0		
Private	13.4	13.8	13.0	13.9	14.1	12.8		
Public	3.3	1.9	2.3	2.2	2.0	2.1		
Changes in equity capital	0.3	0.5	0.4	0.0	0.0	0.0		
Exports of goods and services	27.1	27.8	26.6	27.8	27.2	25.6		
Imports of goods and services	43.0	45.1	44.3	47.2	48.5	48.1		

¹ Central Reserve Bank of El Salvador (BCR, 2009a).

	2003	2004	2005	2006	2007	2008	2009 I	2009 II
Gross national saving	12.3	12.2	12.4	12.5	10.3	7.4		
IV. Memorandum items								
Population (million) ^c	6.0	6.0	6.0	6.1	6.1	6.1		
Terms of trade (1980 = 100)	107.7	116.6	116.5	109.1	103.0	n.a.		
Net international reserves (US\$ million)	1,906	1,888	1,829	1,907	2,198	2,541	2,783	

n.a. Not available.

a Gross domestic product, less property income from abroad, plus net current transfers.

b Excluding imputed bank service charges, customs duties and value-added tax, which explain the difference with a figure of 100 per cent.

c Ministry of the Economy. Directorate-General of Statistics and Censuses (DIGESTYC). *Estimaciones y Proyecciones de Población, 1950-2050*.

2009 I GDP data through first quarter.

2009 II GDP data through second quarter.

Source: Central Reserve Bank of El Salvador.

8. GDP per capita at current prices increased from about US\$2,504 in 2003 to US\$3,611 in 2008. Net transfers, particularly from the United States, remain a crucial source of financing for domestic private expenditure; and, as a result, gross disposable income per capita is higher than per capita GDP. In 2008, gross disposable income per capita, at US\$4,149, was 14.9 per cent above per capita GDP.

9. Expenditure on GDP in El Salvador is still dominated by consumption, which in 2008 represented 107 per cent of total output, with private consumption absorbing 98 per cent. Despite this high proportion, the national saving rate remained relatively stable until 2006, before a sharply higher consumption in 2007 and 2008 lowered the savings rate to 7.4 per cent in the latter year. Private investment represented 12.8 per cent of GDP in 2008, compared to 13.4 per cent in 2003.

10. Exports of goods and services maintained a relatively constant GDP share between 2003 and 2008, while the corresponding imports expanded to nearly 50 per cent of GDP in 2008, reflecting the high level of domestic demand in the Salvadoran economy.

11. The economically active population grew from 2.52 million in 2003 to 2.75 million in 2007, (the last year for which data are available), representing annual growth of 1.8 per cent, which is slower than the rate of expansion of GDP. The unemployment rate reported for that year was 6.3 per cent. The informal sector is very important in the Salvadoran economy, providing 48.6 per cent of total employment (Multi-Purpose Household Survey, 2008) and playing a major role in poverty reduction.²

12. Although development indicators continued to improve during the review period, World Bank data show that 37 per cent of the population was still living in poverty in 2007.³ According to the authorities, the equivalent figure in 2009 was 34.6 per cent.

(ii) Fiscal policy

13. The Ministry of Finance is responsible for fiscal policy in El Salvador, setting budgetary policy applicable to the non-financial public sector (NFPS), pursuant to the Organic Law on State Financial Management. Fiscal policy and annual budgets during the review period were formulated in conformity with the public debt programme specified in the 2004-2009 Strategic Plan, which set the

² Ministry of the Economy, DIGESTYC (2004).

³ World Bank (2009b).

following targets: NFPS medium and long-term borrowing not to exceed 40 per cent of GDP as an average for the five-year period; NFPS debt service to be paid on time; and the debt service indicator to be kept below 30 per cent of current income, and brought below 20 per cent by the end of the period.⁴

14. The following guidelines have been set for fiscal policy in 2009: keep the NFPS fiscal deficit at appropriate levels, although without a specific target; endeavour to generate a current account surplus for the NFPS to ensure that government financing is used exclusively for investment; increase tax revenue without raising tax rates, mainly by combating contraband and tax evasion; target public investment on priority areas; and maintain borrowing levels in accordance with best international practices and the country's ability to pay.⁵

15. Central government income is still a relatively small proportion of GDP, despite expanding from 13.2 per cent in 2003 to 14.7 per cent in 2008 (Table I.2). This slight increase is explained mainly by additional tax revenue obtained in the framework of the fight against tax evasion and smuggling. Public expenditure accounted for 15.3 per cent of GDP in 2008. The central government fiscal balance strengthened between 2003 and 2007, as the deficit decreased steadily from 2.7 per cent of GDP in 2003 to 0.2 per cent in the latter year, before expanding slightly to 0.6 per cent of GDP in 2008. The NFPS deficit has fluctuated between 0.2 per cent and 2.1 per cent of GDP in the period 2003-2008, and was 1.1 per cent of GDP in 2008.

16. The fiscal situation worsened sharply in the first six months of 2009, as the Central Government recorded a deficit of US\$213.4 million (1.0 per cent of year's GDP), following the surplus of US\$111.4 million achieved in the same period a year earlier. This was the result of a substantial drop in income, mainly tax revenue, and higher expenditure, particularly current spending (payroll, goods and services, interest and current transfers). Of these transfers, 52 per cent went to government bodies, while the remainder was channelled to the private sector, largely in the form of subsidies on transport, electric power and liquefied gas. Debt service as of August 2009 (US\$1,063.9 million) represented 4.8 per cent of estimated GDP for the year, consisting of principal repayments of US\$706.8 million and interest of US\$357.1 million.⁶

Table I.2
Central government finances, 2003-2009
(% of GDP)

	2003	2004	2005	2006	2007	2008	2009 ^a
Income	13.2	13.3	13.5	14.4	14.6	14.7	6.9
Current income	12.7	13.0	13.2	14.2	14.3	14.4	6.8
Taxes	11.5	11.5	12.5	13.3	13.4	13.0	6.4
Income tax	3.3	3.4	3.9	4.2	4.6	4.5	2.7
VAT	6.1	6.0	6.5	7.0	6.8	6.6	2.8
Consumption tax	0.4	0.5	0.6	0.5	0.5	0.4	0.2
Property taxes and other taxes	0.1	0.1	0.1	0.1	0.1	0.1	0.0
Customs duties	1.2	1.1	1.1	1.1	1.0	0.8	0.3
Non-tax and other income	1.2	1.4	0.7	0.8	0.8	0.7	0.4
Income from capital and grants	0.4	0.3	0.3	0.2	0.3	0.2	0.1
Expenditure	15.9	14.4	14.6	14.8	14.8	15.3	7.9
Current expenses	12.1	12.2	12.1	12.3	12.3	12.6	6.6
Payroll	4.9	4.7	4.5	4.5	4.4	4.4	2.3
Goods and services	2.1	2.3	2.4	2.1	2.2	2.3	1.1
Interest	1.9	2.0	2.2	2.4	2.4	2.3	1.2
Transfers	3.2	3.2	3.0	3.3	3.3	3.5	1.9

⁴ Ministry of Finance, Directorate-General of Investment and Public Credit (2004).

⁵ Ministry of Finance, Directorate-General of the Budget (2008).

⁶ BCR (2009b).

	2003	2004	2005	2006	2007	2008	2009 ^a
Capital expenditure	3.8	2.3	2.6	2.7	2.6	2.7	1.3
Central government balance	-2.7	-1.1	-1.0	-0.4	-0.2	-0.6	-1.0
NFPS balance	-2.1	-0.6	-1.0	-1.1	-0.2	-1.0	-1.3
Total public debt (US\$ million)	7,103.2	7,282.6	7,703.7	8,359.2	8,638.7	9,707.6	10,339.0
Total public debt (% GDP)	47.2	46.1	45.1	44.8	42.7	43.9	47.3
NFPS debt (% GDP)	40.3	40.5	39.7	39.7	36.6	35.8	38.1

a First six months as a percentage of annual GDP. Preliminary figures.

Source: Central Reserve Bank of El Salvador.

17. In June 2009, the Government announced an 18-month global plan to cope with the crisis, worth approximately US\$587 million, representing 17 per cent of total public expenditure. According to the authorities, this has since had to be refocused to cope with the damage caused by torrential rainfall in November 2009 and the resulting national disaster situation.

18. During the period under review, revenue from income tax and the property transfer and services tax increased from 3.3 per cent and 6.1 per cent of GDP, respectively in 2003, to 4.5 per cent and 6.6 per cent in 2008. In contrast, customs revenue decreased from 1.2 per cent to 0.8 per cent of GDP. Customs duties represented less than 2 per cent of merchandise imports in 2008 - below the 3.2 per cent reported in 2001, for example.

19. The prudential limit of 40 per cent of GDP for NFPS debt, imposed in 2004, has been complied with since 2005, while the total public debt dropped from 47.2 per cent of GDP in 2003 to 43.9 per cent in 2008, before rising again in 2009. The total public debt stood at US\$10,339.2 million in June 2009, of which US\$8,280.0 million corresponded to the NFPS. In late 2008, a US\$950 million increase in external borrowing was approved to restructure the debt and promote social development, the corresponding funds being secured through loans from the World Bank and the IDB (see below).

(iii) Monetary and exchange-rate policies

20. Although responsibility for the conduct of monetary policy lies with the Central Reserve Bank of El Salvador, El Salvador cannot conduct an independent monetary policy because it is a dollarized economy. The United States dollar has been the currency of legal tender since 1 January 2001, when the Law on Monetary Integration entered into force (Decree No. 2001 of 22 December 2000).⁷ This legislation fixed the exchange rate between the colón and the dollar at 8.75 - the rate that had been in force during the previous seven years. The dollar is also the unit of account used by the financial system. The Law on Monetary Integration eliminated three of the main central bank functions: monetary policy management, lender of last resort to the banking system, and currency issuance. It also authorized the central bank to fulfil other functions, such as managing liquidity reserves and supplying dollars to the economy.⁸

21. The authorities consider that the monetary integration process has been implemented successfully, and that it has helped consolidate the country's macroeconomic stability and strengthen its financial system. The benefits identified include loans with lower interest rates and longer

⁷ The Law on Monetary Integration can be viewed at: <http://www.bcr.gob.sv/uploaded/content/category/1016779392.pdf>.

⁸ BCR (2009e).

maturities, elimination of exchange-rate risk, and protection of the value of savings, wages and purchasing power.⁹

22. Interest rates have stayed low for most of the period under review, which mainly reflects the benefits of dollarization on El Salvador's perceived country-risk, since exchange-rate risk is eliminated. Interest rates on loans with maturities of up to one year fluctuated between 6.3 per cent and 7.9 per cent as an annual average between 2003 and 2008, with spreads (the difference between the borrowing and lending rates) below 4 per cent (Table I.3). Nonetheless, both interest rates and spreads in El Salvador have risen since mid-2008, as a result of the global financial crisis, even though rates in the United States have come down. This is partly the result of higher perceived risk, but mainly reflects the situation on the credit market, where the supply of credit has dwindled. This, in turn, reflects the drop in remittances and consequently smaller volume of deposits in the financial system, as shown by lower levels of near-money in 2009. Real borrowing rates have been negative for most of the period under review, but they turned positive again in 2008.

23. Since the introduction of the Law on Monetary Integration, the central bank has had little power to influence the price level. Inflation was held at levels below 5 per cent for most of the review period, but started to rise in the wake of higher international food and raw materials prices. The absence of an independent monetary policy means that external shocks are transmitted more immediately to the domestic price level. Average cumulative inflation for 2008 amounted to 5.5 per cent, having peaked at 9.9 per cent in August; the latter reflected increases in 2008 of about 18 per cent in the price of food and beverages and almost 12 per cent in the transport sector, which includes the price of regular gasoline. Inflation began to ease in the first few months of 2009, in response to weaker raw materials prices and a slowdown in demand growth.

Table I.3
Monetary and price indicators, 2003-2009

Indicator	2003	2004	2005	2006	2007	2008	2009 ^a
Consumer price index (variation %, end of period)	2.8	5.4	4.3	4.9	4.9	5.5	0.2
M1 (variation %)	1.2	12.5	7.4	15.2	16.5	1.6	-0.3
M2 (variation %)	0.3	3.0	2.6	11.9	17.6	0.1	-0.2
Near-money (variation %)	0.2	0.9	1.4	11.1	17.9	-0.2	-0.2
Loans to the private sector (variation %)	7.0	5.6	7.7	10.9	7.1	4.4	-2.7
Real effective exchange rate index (global, base 2009)	-0.7	-0.2	-0.2	-1.4	0.8	-2.0	-2.9
180-day deposit rate (% p.a.)	3.4	3.3	3.4	4.4	4.7	4.2	4.8
Rate on loans of up to one year (% p.a.)	6.6	6.3	6.9	7.5	7.8	7.9	9.5
Spread	3.2	3.0	3.5	3.1	3.4	3.7	4.8

a Figures at July (CPI in June).

Source: Central Reserve Bank and IMF International Financial Statistics, March 2009.

24. The real exchange rate has experienced relatively small variations during the review period; and the IMF views the rate as consistent with the country's economic fundamentals. The real exchange rate depreciated between early 2007 and early 2008, owing to the weakness of the United States dollar in relation to the currencies used by El Salvador's main trading partners, and this offset the increase in domestic inflation.¹⁰

25. El Salvador does not impose any controls on foreign currency transactions.

⁹ BCR online information. Viewed at: <http://www.bcr.gob.sv/?cat=1053&name=Reseña%20Histórica&lang=es>.

¹⁰ IMF (2009b).

(iv) Balance of payments

26. El Salvador ran a current account deficit continuously between 2003 and 2008, which ranged between US\$702 million and US\$1,682 million (Table I.4). The gap grew steadily from 2005 onwards, to reach a level of 7.6 per cent of GDP in 2008. The merchandise trade balance has recorded a growing deficit since 2005, amounting to US\$4,394 million or 19.9 per cent of GDP in 2008. This is explained by the fact that imports have outpaced exports: the former were 65 per cent higher in 2008 than in 2003, while exports grew by just 46 per cent over the same period. The balance of trade in services has also been in deficit throughout the period under review.

27. Nonetheless, the size of the current account deficit has been mitigated by the high level of current transfers, mainly in the form of remittances from Salvadorans living abroad - particularly in the United States and Spain. Foreign remittances totalled US\$3,788 million in 2008, equivalent to 17.1 per cent of GDP¹¹, compared to US\$2,105 million (14 per cent of GDP) in 2003. The international economic crisis has had repercussions on employment levels in industrialized countries, which has meant that Salvadorans living in the United States are sending less money home; in the first half of 2009, remittances dropped by 10.3 per cent compared to the same period a year earlier, shrinking from US\$1,938.5 million to US\$1,739.7 million. The smaller volume of transfers has had a major impact on final consumption, particularly in 2009.

Table I.4
Balance of payments, 2003-2009
(US\$ million)

	2003	2004	2005	2006	2007	2008	2009 ^a
I. Current account	-702	-642	-610	-783	-1,221	-1,682	-114
Trade in goods	-2,287	-2,661	-2,938	-3,533	-4,105	-4,394	-1,226
Exports f.o.b. ^b	3,153	3,339	3,447	3,759	4,039	4,611	1,955
Imports f.o.b. ^b	5,439	6,000	6,385	7,291	8,144	9,004	3,181
Services	-107	-79	-128	-192	-291	-584	-303
Receipts	949	951	946	1,015	1,130	1,041	399
Payments	1,055	1,030	1,074	1,207	1,420	1,625	702
Investment income	-423	-458	-579	-531	-576	-536	-356
Receipts	140	144	175	234	287	223	88
Payments	564	602	754	765	863	759	444
Current transfers (net)	2,114	2,555	3,035	3,472	3,75	3,832	1,770
Private remittances	2,105	2,548	3,017	3,471	3,695	3,788	1,740
Public transfers and other	9	7	18	1	55	44	31
II. Capital and financial account	846	276	929	1,094	400	1,380	-6
Capital account	113	100	94	97	151	80	50
Financial account	733	175	836	997	250	1,300	-56
Direct investment	123	366	398	268	1,408	719	51
Portfolio investment	189	57	105	777	-196	138	277
Other investments	737	-300	274	24	-682	777	-148
III. Errors and omissions	-144	352	-360	-423	783	216	120
IV. Overall balance	-144	352	-360	-423	783	216	120
V. Financing							
Free reserves (variation)	144	-352	360	423	-783	-216	-120
Memorandum							
Current account deficit (percentage of GDP)	4.7	4.1	3.6	4.2	6.0	7.6	n.a.
Total external debt (US\$ million)	8,602.9	8,869.8	9,419.8	10,259.2	9,808.4	10,691.1	10,143.7
Net international reserves (US\$ million)	1,905.8	1,888.3	1,829.4	1,907.2	2,197.5	2,540.9	2,782.9

n.a. Not available.

a June 2009.

b Includes the maquila industry.

Source: Central Bank of El Salvador.

¹¹ BCR (2009d).

28. El Salvador's total external debt expanded from US\$8,602.9 million in 2003 to US\$10,691.1 million in 2008, while net international reserves (foreign assets) rose from US\$1,905.8 million in December 2003 to US\$2,782.9 million in June 2009 - to some extent reflecting the higher external debt. Reserves are invested conservatively; and, at the end of the second quarter, the duration for investment in United States dollars was 0.18 years. Just over 77 per cent of investments are held with sovereign issuers, such as the United States Treasury, other agencies of the United States and Germany, and supranational organizations such as the Bank for International Settlements (BIS), the World Bank and others. About 87 per cent of the securities held are tradable on secondary markets, while the remaining 13 per cent consist of time deposits with maturities of up to one week. This is consistent with the risk profile specified in the investment policy and the range of assets in which the portfolios are invested.¹²

29. El Salvador has negotiated loans with the World Bank and the IDB totalling US\$950 million.¹³ In January 2009, the IMF approved a precautionary 15-month SBA for El Salvador amounting to roughly US\$800 million (SDR 513.9) to support the country's economic strategy in coping with the adverse effects of the international financial crisis. The Salvadoran authorities stated that they had no intention of using the funds and the programme supported by the IMF was a precautionary measure forming part of a global strategy to bolster the country's defences against the crisis. The programme's key objective is to help provide liquidity to the country's economy. The authorities believe that the agreement approved in January has achieved its main objective of helping El Salvador cope with the financial crisis and maintain stability in the macroeconomic and financial sectors, as well as boosting investor confidence. In September 2009, the IMF and the Salvadoran authorities reached preliminary agreement for a new economic programme that could be supported by a precautionary three-year SBA also for a total of SDR 513.9 million. The new programme replaces the 15-month SBA approved in January 2009.¹⁴

(3) MERCHANDISE TRADE AND INVESTMENT FLOWS

30. The composition and geographic distribution of El Salvador's merchandise trade is shown in Annexes AI.1 to AI.6. Complete data are only available since 2005.

31. The country's merchandise trade grew significantly during the period under review. Exports (including maquila exports) expanded from US\$3,418 million in 2005 to US\$4,549 million in 2008, while imports (including maquila-related) grew from US\$6,690 million in 2005 to US\$9,754 million in 2008, i.e. an average annual growth of 13.4 per cent. Imports greatly outweighed exports in value terms throughout the period under review, thereby generating a trade deficit of US\$5,295 million in 2008, excluding maquila activity.

(i) Composition of trade

32. Tables AI.1 to AI.4 show the composition of trade during the period under review. The structure of El Salvador's exports suffered a number of alterations during that period, with the textiles and clothing shares both shrinking. Manufactures remain the main export category and, maquila activities included, accounted for over 73.7 per cent of total exports in 2008. Within this category, textile products and their manufactures are the leading export item, accounting for 41.3 per cent of the total in 2008 - albeit considerably below the 52.7 per cent recorded in 2005. Chemicals and plastics accounted for 10.9 per cent of exports in 2008, compared to 7.1 per cent in 2005.

¹² BCR online information (2009). Viewed at: <http://www.bcr.gob.sv/>.

¹³ IMF Press Release No. 09/10, 16 January 2009, and IMF (2009). Viewed at: <http://www.imf.org/>.

¹⁴ IMF Press Release No. 09/322, 24 September 2009. Viewed at: <http://www.imf.org/>.

33. Commodities slightly increased their share of total exports during the period, food products being the leading category in that sector. These, along with beverages, alcoholic liquids and vinegar, tobacco and manufactured tobacco substitutes, accounted for 19.9 per cent of total foreign sales in 2008, compared to 17.2 per cent in 2005. Coffee remains the leading individual commodity export, accounting for 5.7 per cent of total exports in 2008.

34. Manufactured goods remain the leading category on the import side, representing 63 per cent of total foreign purchases in 2008, albeit a smaller share than previously. Machinery, transport equipment and chemical products account for a large share of manufactured imports (Table AI.4). Commodity imports increased substantially during the review period, mainly owing to larger fuel purchases.

(ii) Geographic distribution of trade

35. El Salvador's main export markets are the other members of the CACM and the United States (Table AI.5). Within the Central American region, Guatemala was the leading destination in 2008, absorbing roughly 13.6 per cent of El Salvador's exports, above the 11.5 per cent recorded in 2003. The United States provided a market for 48.1 per cent of the country's exports in 2008, while other major trading partners, Honduras and Nicaragua, absorbed 13 per cent and 5.5 per cent respectively. A further 7 per cent of Salvadoran exports in 2008 went to Europe, mainly Germany and Spain.

36. The United States is El Salvador's main supplier country, providing 34.4 per cent of all imports in 2008. Mexico was the next most important, supplying 9 per cent of the total, followed by Guatemala with 8.5 per cent. The Central American region as a whole accounted for 17 per cent of El Salvador's total imports (Table AI.6), while the European Union provided 6.9 per cent, led by Germany and Spain, with 1.6 per cent and 1 per cent, respectively.

(iii) Trade in services

37. El Salvador's balance of trade in services is traditionally in deficit, and the gap has been growing since 2004 to reach a level of US\$584 million in 2008, equivalent to 2.6 per cent of GDP. Most service categories run trade deficits, the largest of which are in transport and insurance, while travel and communications are the key exceptions generating surpluses (Table I.5).

Table I.5
Trade in services, 2003-2009
(US\$ million)

Description	2003	2004	2005	2006	2007	2008 ^a	2009 ^b
Balance	-106.8	-79	-128	-191.5	-290.5	-584.0	-303.2
Revenue	948.5	951.2	945.7	1,015.0	1,129.7	1,041.0	398.7
Transport	330.1	342.5	344.6	352.3	367	351.2	133.1
Travel	383.1	314.3	360.8	381.6	482.3	424.5	154.5
Communications	122.9	139.3	122.7	135.7	162.1	153.7	62.8
Construction	10	18.6	24.1	45.4	22.9	33.1	9.5
Insurance	31.4	34.8	32.4	34.7	37.1	29.6	16.5
Financial sector	2.8	9.7	7.1	3.4	4.1	1.4	0.2
Information services	0.4	0.4	0	0.7	0	1.0	0.0
Royalties	0.2	0.1	2.4	0.5	0.4	1.4	0.2
Personal, cultural and recreational services	0	0.2	0	0	0	0.0	0.0
Government services	42.3	51	30.3	38.8	38	26.4	14.9
Other services	25.3	40.3	21.2	21.9	15.8	18.8	7.0
Expenditure	1,055.3	1,030	1,073.6	1,206.5	1,420.2	1,625.1	701.9
Transport	477.1	504.5	520.2	589.4	730.3	948.5	432.4
Travel	229.6	167.9	206.0	224.1	278.7	240.7	83.4
Communications	36.9	34	25.2	25.5	30.8	44.8	9.8
Construction	6.3	6.5	12.7	8.5	8	13.6	2.8

Description	2003	2004	2005	2006	2007	2008 ^a	2009 ^b
Insurance	106.4	108.4	101.7	128.4	148.4	189.5	94.8
Financial	19.7	28.5	13	9.3	9.8	12.0	3.5
Information services	3.1	6.1	2.9	3.9	7.5	4.9	1.4
Royalties	22.2	17.8	30.4	27.3	24.1	33.7	13.8
Personal, cultural and recreational services	1.2	1.5	1.6	1.3	1.9	1.0	0.2
Government services	15.6	24	21.8	26.4	28	35.9	12.8
Other services	137.2	130.7	138.2	162.3	152.8	100.4	47.1

a Preliminary figures.

b At June 2009.

Source: Central Reserve Bank of El Salvador.

(iv) Foreign direct investment

38. The volume of foreign investment in El Salvador reached a level of US\$6,701.4 million in late 2008, of which US\$1,858 million was channelled to the financial sector, mainly representing foreign takeovers of local banks, along with US\$917 million to the telecommunications sector and US\$879 million to the electricity sector (Table I.6). Other sectors receiving substantial FDI inflows include manufacturing, maquila and commerce.

Table I.6
Balance of foreign direct investment by receiving economic sector, 2003-2009
(US\$ million)

	2003	2004	2005	2006	2007	2008 ^a	2009 ^{a,b}
Industry	496.1	536.9	853.5	870.2	891.6	919.7	926.0
Commerce	239.2	278.3	305	356.3	397.3	411.9	426.9
Construction	12.4	12.4	12.4	12.4	12.3	12.3	12.3
Communications	411.3	746	793.8	793.9	860.6	917.4	927.9
Electricity	848.2	800.2	800.2	847.6	847.6	879.5	879.5
Agriculture and fisheries	46.8	68.6	67.1	67.7	69.6	69.6	69.6
Mining and quarrying	0	0	1.5	29.5	37.8	42.5	43.0
Financial	161.1	148.1	250.4	321.9	1,489.4	1,858.9	1,902.5
Maquila	263.3	294.7	298.9	298.5	399.1	425.4	488.9
Other services	110.9	110.8	125.2	137.1	177.2	184.2	192.4
Subtotal	2,589.2	2,996.1	3,508.1	3,735.0	5,182.5	5,721.5	5,869.2
Loans between FDI firms	686.2	659.4	658.4	672.8	733.8	979.9	865.7
Total	3,275.4	3,655.5	4,166.5	4,407.8	5,916.2	6,701.4	6,734.9

a Preliminary figures.

b At June 2009.

Source: Central Reserve Bank of El Salvador, on the basis of surveys of private-sector firms and the balance sheets of banks in the financial system.

39. The United States was the leading foreign investor in this period, with investments totalling almost US\$2 billion. Other major investors were Panama and Mexico (Table I.7).

Table I.7
Balance of foreign direct investment by country of origin, 2003-2009
(US\$ million)

Country	2003	2004	2005	2006	2007	2008	2009 ^{a,b}
United States	1,031.7	1,026.7	1,358.9	1,371.8	1,870.9	1,999.8	2,013.6
Panama	100.1	102.5	144.5	212.3	1,053.5	1,374	1,443.8
Mexico	83.6	614.7	647.8	655	714.4	722.0	723.8
British Virgin Islands	29.2	56.2	356.2	355.9	356.6	361.8	361.9
Spain	161.4	195	195.2	195.3	205.4	205.9	205.9

Country	2003	2004	2005	2006	2007	2008	2009 ^{a,b}
Canada	46.6	56	130.3	145.3	153.6	162.4	163.0
Costa Rica	68.7	68.8	67.4	70.1	104.2	111.2	111.2
Guatemala	57.8	60.1	70.4	93.4	96.3	102.4	103.3
Germany	84.8	84.9	89.4	92.2	93.6	98.6	98.6
Bahamas	66.4	67.8	68.6	74.9	75.2	75.2	75.2
Italy	26.6	26.6	26.6	74	74	105.9	105.9
Chinese Taipei	56.7	57.3	58.6	58.3	58.3	59.0	61.4
Singapore	32.2	32.5	36.5	37.3	45	45.0	91.8
Netherlands	39.1	39.1	55	56.3	42	43.3	47.5
Nicaragua	20	20.4	21.3	27.8	35.5	45.5	45.5
Republic of Korea	22.9	23.5	26	22	30	25.1	25.5
Honduras	19.4	21	21.6	21.8	22	22.5	22.3
Japan	14.2	14.2	14.2	14.2	18.7	17.5	16.3
Switzerland	11.7	15.6	16.8	16.8	16.8	18.5	18.5
Aruba	15	15	15	15	15	15	15.0
Brazil	0	0	0	4.3	13.7	22.7	22.7
Bermuda	11.2	11.8	12.3	13.3	13.3	13.3	13.3
United Kingdom	6.4	7.4	8.2	9.7	12.7	13.1	13.4
France	214.7	5.8	5.8	6	4.5	4.5	11.7
Israel	5.7	2.3	1	1.5	2.5	2.5	2.5
Peru	22.3	22.3	22.3	22.3	1.8	1.8	1.8
Chile	0.2	0.7	0.3	24.8	0.8	0.7	0.7
Ecuador	9.0	9.0	9.0	9.0	0.0	0.0	0.0
Venezuela	309.5	309.5	0.0	0.0	0.0	0.0	0.0
Other	22.4	29.6	29.6	34.4	52.2	52.2	52.7
Loans between FDI firms	686.2	659.4	658.4	672.8	733.8	979.9	865.7
Total	3,275.4	3,655.5	4,166.5	4,407.8	5,916.2	6,701.4	6,734.9

a Preliminary figures.

b At June 2009.

Source: Central Reserve Bank of El Salvador, on the basis of surveys of private-sector firms and the balance sheets of banks in the financial system.

(4) OUTLOOK

40. Economic results in 2009 and 2010 will be affected by the world recession, with export growth likely to suffer from the contraction of demand in El Salvador's main export markets such as the United States. There will also be a significant effect on remittances, which have been shrinking as unemployment in the United States has spread. Remittances represented over 17 per cent of GDP in 2008 and finance much of private consumption.

41. The IMF is forecasting GDP growth of -2.5 per cent for 2009 and just 0.5 per cent in 2010, with inflation at 1.8 per cent and 2.4 per cent in those two years.¹⁵ This stands in contrast to more optimistic projections made late last year, when the Fund predicted 2.6 per cent growth in 2009, albeit with inflation higher at 6 per cent.¹⁶ It also envisaged a public-sector deficit on the order of 2.2 per cent of GDP, and a balance of payments current account deficit equivalent to 5.4 per cent of GDP - levels that will probably be surpassed as the overall economic outlook has worsened.

¹⁵ IMF online information. Viewed at: <http://www.imf.org/external/country/SLV/index.htm>.

¹⁶ IMF (2009b).