

# Development Challenges in Guatemala

Arnoldo López

## Medium-Term Economic and Social Trends

In recent years Guatemala has maintained its economic stability, while political uncertainty has represented the main source of risk. In the last five years the country's GDP displayed average annual growth rate of 3.6%, a rate well above the average in Latin America and the Caribbean (1.3%). Growth has decelerated since 2016 (3.1%), however, registering 2.8% in 2017. This moderation has been influenced by lower-than-expected public expenditure and a deceleration in investment in an environment of political uncertainty.

Investment has been low. Private investment has exhibited a downward trend in recent years, reaching only 11.1% of GDP in 2017. A similar pattern is observed in public investment, which represented 1.2% of GDP.

Other macroeconomic indicators are generally favorable. With respect to prices, annual inflation has remained within the target range set by the Central Bank (3%-5%) since 2012. From 2012 to 2017 inflation averaged 3.8% per annum. The exchange rate has experienced a slight tendency towards appreciation, influenced by an increase in remittances (10.9% of GDP in 2017) and savings in oil-related expenditures due to lower international prices. As a result, the exchange rate has appreciated 6% compared to 2012. Remittances also contribute to offsetting the commercial deficit, which results in a current account surplus of 2.1% of GDP in 2017. The monetary policy rate remains accommodative at 2.75% in a scenario of moderate growth, inflation within the target range and stable inflation expectations.

Economic stability and moderate GDP, however, have yet to produce major improvements in labor conditions and poverty. An estimated 70% of the economically active population works in the informal sector, a situation coexisting with a low unemployment rate of 3.2% in 2017 (2.7% in 2016). Poverty remains high, at 59.3% of the total population, with a 23.4% rate of extreme poverty (2014). The incidence of poverty is even more acute among indigenous and rural populations, at 79.2% and 76.1%, respectively.

## Medium-Term Economic and Social Outlook

GDP growth is expected to increase moderately towards 4.0% in the medium term, supported by a recovery in public expenditure and an improvement in the global economy that would support demand for domestic goods. For 2018 and the medium term, inflation is expected to remain stable and within the Central Bank's range of 3%-5%. Stability in revenues and expenditures would result in moderate public deficits that would keep the debt-to-GDP ratio under control. In this scenario of economic inertia, however, social conditions can improve only very slowly.

## Risk Factors

The economic scenario faces several risks. On the external front, the possibility of more protectionist global trade policies around the world could limit the country's exports, and a change in US migration policy could reduce remittances and generate pressures on the social safety net. An abrupt increase in international oil prices, moreover, would increase imports and reduce disposable income. On the internal front, a prolonged period of political uncertainty could further reduce already low levels of investment and slow down the implementation of political reforms.

## **Development Challenges**

GDP growth has not been robust enough to increase GDP per capita<sup>1</sup> and labor income, or reduce the level of informality. In addition, growth has been unevenly distributed, as high levels of poverty and disparities between rural and urban areas remain.

These disparities mainly derive from gaps in i) access to health and education services, ii) infrastructure, and iii) opportunities to generate income. The country's development is further constrained by its institutional and fiscal frameworks, as well as ethnic and gender inequality. In addition, low public revenues represent a limitation for the provision of public goods and services that could support economic and social development. Finally, greater transparency and efficiency are needed in public programs.

## **Conclusion**

Current challenges notwithstanding, Guatemala has in place several important elements for accelerating development. First, the country has consolidated a sound macroeconomic framework, with stable economic growth, inflation under control, and low levels of fiscal deficit and public debt in relation to GDP (24%). Second, there is social support and commitment from the Public Prosecutor's Office to reduce corruption and apply the law. Third, legal changes are underway to strengthen institutions and the rule of law, such as reforms to the electoral system, government procurement, and the justice system.

---

<sup>1</sup> In the last five years, total population grew on average at a rate of 2.4% per annum.