CREDIT OPINION
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Update

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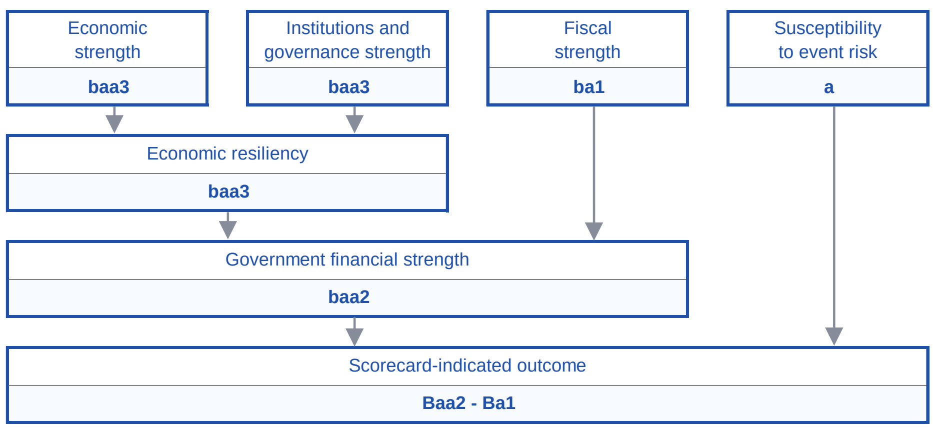
Government of Paraguay – Baa3 stable

Regular update

Summary

Paraguay's credit profile balances strong economic growth, improving institutions and limited external vulnerability, against a narrow revenue base relative to peers. In 2024, we expect the debt-to-GDP ratio to be 39%, well below regional peers and Baa-rated sovereigns and the interest-to-revenue ratio to be 11%, broadly in line with the median for regional and similarly rated peers. Main credit challenges include the economy's dependence on agriculture, which is exposed to climate shocks, and weak governance indicators.

Exhibit 1
Paraguay's credit profile is determined by four factors



Source: Moody's Ratings

Credit strengths

» Low government debt burden in absolute and relative terms

» Robust GDP growth and ongoing economic diversification

» Compliance with fiscal targets support stable debt burden

Credit challenges

» Agriculture-dependent economy subject to climate shocks

» Relatively low, albeit improving, government revenue collection compared to peers

» Relatively weak governance indicators

Rating outlook

The stable outlook reflects our expectations that the process of economic diversification and increasing resilience to shocks will continue, supported by Paraguay's effort to invest in critical infrastructure and attract more foreign direct investment, further integrating into export-oriented supply chains. Progress in these areas will mitigate risks related to Paraguay's exposure to volatility in commodity prices and climate shocks.

Ongoing implementation of the government's strategy to improve institutions and control of corruption such as approval of public procurement system and civil service reform will solidify improvements in institutional strength. We also expect the government will preserve Paraguay's fiscal strength and ongoing efforts to reduce the share of foreign currency debt in total government debt will reduce exposure to exchange rate risk, although, most of the government debt will likely remain in foreign currency for the foreseeable future.

Factors that could lead to an upgrade

We would upgrade Paraguay's sovereign rating if the government implementation of structural reforms continues to enhance the country's institutional and governance framework, and efforts to raise government revenues and reduce the share of foreign currency debt are likely to yield significant credit benefits, improving Paraguay's fiscal strength and overall credit quality. Successful efforts to increase private investment in the country's infrastructure and renewable energy sectors and reduce vulnerability to shocks would also contribute to a higher rating.

Factors that could lead to a downgrade

Negative pressure on the rating could emerge if efforts to modernize the economy and increase resiliency seem increasingly likely to fall short of our expectations, weighing on economic strength. A prolonged period of weaker private investment or economic growth would likely change our assessment of Paraguay's credit profile. Equally important, if efforts to maintain and improve Paraguay's fiscal strength prove insufficient, leading to higher debt and/or a rising interest burden, this would likely lead to a rating downgrade. The rating would also come under pressure if implementation of the structural reform agenda stalls and falls short of our expectations for the improvement in Paraguay's institutional strength.

Key indicators

Exhibit 2

Paraguay	2019	2020	2021	2022	2023	2024F	2025F	2026F
Real GDP (% change)	-0.4	-0.8	4.0	0.2	5.0	4.0	3.5	3.5
Inflation rate (% change average)	2.8	1.8	4.8	9.8	4.6	3.8	3.1	3.6
Gen. gov. financial balance/GDP (%)[1]	-2.9	-6.1	-3.6	-2.9	-4.2	-2.6	-1.9	-1.5
Gen. gov. primary balance/GDP (%)[1]	-2.0	-5.1	-2.5	-1.7	-2.5	-0.6	-0.1	0.4
Gen. gov. debt/GDP (%)[1]	24.2	35.2	34.6	37.7	38.3	39.2	39.7	39.7
Gen. gov. debt/revenues (%)[1]	170.0	260.5	252.7	268.4	275.3	268.3	272.2	274.1
Gen. gov. interest payment/revenues (%)[1]	5.8	7.9	8.0	8.8	11.9	13.5	12.1	12.8
Current account balance/GDP (%)	-0.6	1.8	-1.1	-7.1	-0.6	-3.9	-2.5	-2.2
External debt/CA receipts (%)[2]	108.7	149.2	131.3	123.7	108.8	107.8	107.8	106.5
External vulnerability indicator (EVI) [3][4]	45.4	41.2	31.3	36.0	33.8	50.4	51.9	54.1

[1] Central Government
[2] Current Account Receipts
[3] (Short-Term External Debt + Currently Maturing Long-Term External Debt + Total Nonresident Deposits Over One Year)/Official Foreign Exchange Reserves
[4] Excludes total nonresident deposits over one year

Source: Moody's Ratings

Detailed credit considerations

We set Paraguay's **economic strength** score at “baa3,” one notch above the initial score of “ba1,” to reflect expectation of stronger average growth, along with increased diversification of the economy. Paraguay’s relatively small economy and low wealth levels partially offset these factors.

Paraguay's nominal GDP of around $43 billion in 2023 and GDP per capita (on a purchasing power parity basis) of $15,869 in 2023 are both well below the Baa median of $309 billion and $34,782, respectively. Between 2010 and 2019, Paraguay's economy expanded at an average annual rate of 4.3% in real terms, above the average growth rates of 3.9% for the Baa median. Paraguay's economy contracted by only 0.8% in 2020, marking the least severe contraction among the Latin American economies, and recovered in 2021 with more than 4% growth. In 2022, Paraguay's economy grew minimally at 0.2% in real terms as severe drought conditions hampered the soy and grain production and hydropower sector. The economy rebounded in 2023, growing 5% and we expect continued robust economic growth of about 4% for 2024.

Although climate-related shocks and the agriculture sector's significant contribution to output have historically resulted in some economic volatility, the ongoing positive developments in economic diversification, particularly related to the government's efforts to increase the value-added of agricultural exports, light manufacturing and upgrade infrastructure through public investment, indicate a reduction in the volatility of economic output.

We set the score for **institutions and governance strength** at “baa3” to reflect Paraguay's improving institutional framework, and still somewhat weak governance indicators. Our assessment incorporates the Worldwide Governance Indicator scores for Paraguay (specifically, government effectiveness, rule of law and control of corruption), which are consistently at or below the 25th percentile of sovereigns that we rate and are weaker than the median for its Baa-rated peers.

Nevertheless, Paraguay’s institutional framework has improved with the passage of several laws, including the Fiscal Responsibility Law (FRL), the Law to Modernize the State’s Financial Administration, the Public-Private Partnership Law and the recently created superintendency of pensions. Other institutional reforms relate to the public procurement system, civil service, the social security system and further enhancements to the FRL. In addition, the government’s track record of sound fiscal management indicates a higher degree of government effectiveness than that suggested by the country’s governance indicators alone.

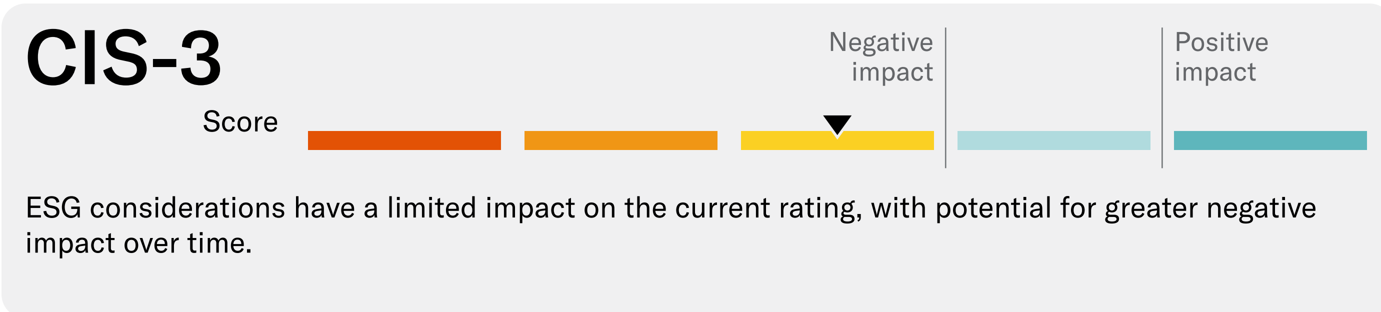
Our assessment of a “ba1” **fiscal strength** score reflects the country’s favorable debt metrics compared with those of its peers in the Baa category. Debt increased to 35% of GDP in 2020 from 24% in 2019 because of an increase in borrowing to finance the response to the coronavirus pandemic. Debt will increase slightly to just over 39% of GDP in 2024 and stabilize around that level through 2025. Despite this increase in debt, Paraguay's debt-to-GDP ratio of about 38% in 2023 remains below the median of 54% for Baa-rated sovereigns. Paraguay’s debt affordability, as measured by the ratio of interest payments to revenue has weakened over the past five years (2019-23), with interest payments at around 12% of revenue in 2023, up from 1.3% in 2012, slightly above the median for Baa-rated sovereigns of around 10% for 2023.

The **susceptibility to event risk** score is set at “a,” driven by our “a” score for political risk, which reflects our expectation that political events will not substantially affect the sovereign's credit metrics, leading to significant changes in economic policies, or impairing the government's willingness or ability to service debt. Our government liquidity risk score of “a” reflects a track record of narrow government deficits and low gross borrowing requirements. The banking sector risk score of “a” reflects the relatively small size of the banking sector, with banking sector assets at around 70% of GDP, and Paraguayan banks' persistently high liquidity ratios, loan loss reserves and capitalization ratios. Finally, our external vulnerability risk score of “a” reflects Paraguay’s low debt burden, adequate reserve buffer and flexible exchange rate. Despite the relatively high financial dollarization in Paraguay, we do not see significant vulnerability to external shocks due to borrowers natural hedge in foreign currency earnings.

ESG considerations

Paraguay's ESG credit impact score is CIS-3

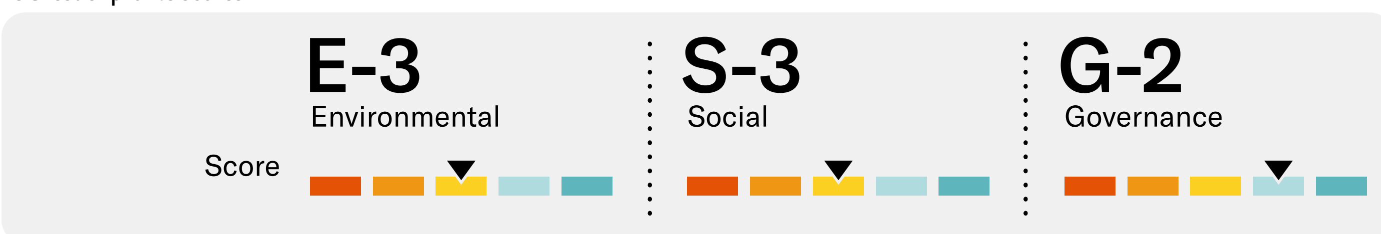
Exhibit 3
ESG credit impact score



Source: Moody's Ratings

Paraguay's ESG Credit Impact Score (**CIS-3**) reflects effective macroeconomic and fiscal policies, and moderately strong governance profile. Social risks are driven by shortcomings in education and labor productivity and some deficiency in access to basic services. Exposure to environmental risks is driven by climate shocks and reliance on agriculture. Strong fiscal metrics mitigate these risks.

Exhibit 4
ESG issuer profile scores



Source: Moody's Ratings

Environmental

Paraguay's exposure to environmental risks (**E-3** issuer profile score) reflects the recurrence of droughts and flooding, which impacts the agriculture sector and hydro-electric generation. Paraguay also benefits from its position as a producer and exporter of clean energy with limited reliance on hydrocarbon.

Social

Paraguay's exposure to social risks (**S-3** issuer profile score) reflects positive demographic trends and rising income levels, but relatively weak educational outcomes which weakens economic and labor force competitiveness.

Governance

The influence of governance on Paraguay's credit profile (**G-2** issuer profile score) reflects improving institutional and governance strength, moderate policy effectiveness, political stability, and a track record of sound macroeconomic and fiscal policies.

ESG Issuer Profile Scores and Credit Impact Scores for the rated entity/transaction are available on Moodys.com. In order to view the latest scores, please click here to go to the landing page for the entity/transaction on MDC and view the ESG Scores section.

All of these considerations are further discussed in the "Detailed credit considerations" section above. Our approach to ESG is explained in our report on how the scores depict varied and largely credit-negative impact of ESG factors and our cross-sector methodology General Principles for Assessing Environmental, Social and Governance Risks Methodology.

Recent developments

Last year's fiscal deficit of 2.6% of GDP was in line with the Fiscal Responsibility Law's convergence path

The fiscal deficit for 2024 closed at 2.6% of GDP, aligning with the convergence plan and the General National Budget Law (PGN) 2024. This result demonstrates the government's commitment to fiscal discipline and responsible financial management. Last year the government cleared payment arrears to the healthcare and infrastructure sector by the previous administration and outlined a new fiscal convergence path that began with the fiscal deficit of 4.1% of GDP for 2023 to converge in 2026 to the target deficit of 1.5% of GDP, in line with the FRL. We expect a fiscal deficit of 1.9% of GDP in 2025, close to the target.

Central bank reduces its annual inflation target to 3.5%

In December 2024 the Board of Directors at the Central Bank of Paraguay decided to reduce the inflation target to 3.5% from 4% and maintain the target range of +/- two percentage points. This decision is influenced by several key factors, including the positive trend of inflation within the inflation targeting framework, which has generally stayed below the set goals. A lower inflation target helps protect the purchasing power of the population, especially for low-income households.

On January 23, the Monetary Policy Committee of the Central Bank of Paraguay voted for the tenth consecutive month to maintain its monetary policy rate at 6%, keeping the easing cycle on hold. In its decision-making process, the central bank noted that month-over-month inflation increased 0.7% in December, while year-over-year inflation stood at 3.8%. Furthermore, in the latest central bank poll of economic participants from January, inflation expectations for the next 12 months and 24 months shifted down to the new target at 3.5%.

GDP growth in third quarter eases

Growth in the third quarter of 2024 came in at 3.4% year-over-year. When broken down by supply side sectors, the third-quarter result was supported by strong growth in the livestock, forestry, fishing, and mining (13.9%), and construction (5.5%) sectors while the hydropower (-9.4%) sector was the main laggard (see Exhibit 5). When analyzing from the demand side, internal demand grew 5.7% year-over-year, strong growth supported by the positive impacts of government consumption (8.5%) and gross fixed capital formation (7.7%, see Exhibit 6). The positive results enforce our expectation of 4% real GDP growth for 2024. Furthermore, the economic activity indicator (IMAEP) for the months of October and November, recorded inter-annual expansion of 5.1% and 7.5%, respectively. For 2025, we forecast 3.5% growth as economic activity moderates, in line with Paraguay's potential growth. However, there is still upside potential for medium-term growth performance once large FDI projects begin construction and operation.

Exhibit 5

On the supply side, growth eased in Q3 mostly due to the decline in the hydropower sector

Year-over-year Variation (%)

	III-23	IV-23	I-24	II-24	III-24
Total GDP	**4.1**	**5.2**	**4.5**	**5.0**	**3.4**
Agriculture	4.3	-5.6	1.1	2.5	2.9
Electricity and Water (with binational)	14.8	7.8	0.8	-8.6	-9.4
GDP (excluding Agriculture and Binational)	**3.5**	**6.1**	**5.6**	**7.0**	**4.8**
Livestock, Forestry, Fishing, and Mining	-1.3	11.6	4.9	5.4	13.9
Manufacturing	3.5	10.6	5.2	5.8	4.0
Construction	-1.8	-8.1	-2.2	4.7	5.5
Services	3.9	5.1	5.0	6.2	3.2
Product Taxes	6.1	7.0	13.5	11.8	9.6

Source: Banco Central del Paraguay

Exhibit 6

On the demand side, gross capital formation was a key driver of Q3 growth

Year-over-year Variation (%)

	III-23	IV-23	I-24	II-24	III-24
GDP	**4.1**	**5.2**	**4.5**	**5.0**	**3.4**
Total Consumption	3.5	2.7	4.8	6.3	4.7
Private Consumption	2.4	3.6	4.8	5.5	4.0
Government Consumption	10.0	-1.0	4.5	10.4	8.5
Gross Capital Formation	-17.5	-14.9	-0.2	8.2	9.8
Gross Fixed Capital Formation	-2.6	0.5	3.5	8.6	7.7
Exports	34.1	42.7	8.6	8.6	-5.2
Imports	16.6	18.3	5.9	13.3	-0.6

Source: Banco Central del Paraguay

Paraguay's beef export sector has reached new heights, with a record of over 407 million kilograms exported in 2024, generating revenues of about $1.8 billion. This achievement underscores the country's strong agricultural sector and its ability to meet international demand. Paraguay's tourism sector has also shown remarkable growth, generating more than $766 million in revenues in 2024. The country received over 2.2 million international visitors, reflecting a 22% increase compared to the previous year. This growth highlights Paraguay's potential as a tourist destination.

Despite the strong growth in those two sectors, Paraguay's current account deficit is expected to widen in 2024 as soybean and hydroelectric export revenue declined. We expect a current account deficit of 3.9% in 2024. Moving forward, the current account is expected to gradually narrow despite higher foreign direct investment in large-scale forestry and manufacturing projects potentially driving increased demand for imports.

Paraguay creates a National Unified Registry clarifying regulation in the real estate sector

On January 9, President Santiago Peña enacted the creation of the National Unified Registry (RUN), marking a significant step towards resolving real estate issues in Paraguay. This comprehensive reform aims to provide a definitive solution to the land problem, ensuring an effective and coordinated real estate regime. This initiative is an important step in improving institutional strength and is expected to enhance property rights and stimulate investment in the real estate sector.

Moody's rating methodology and scorecard factors: Paraguay – Baa3 stable

Factor / Sub-Factor	Metric	Indicator Year	Indicator	Initial Factor Score	Final Factor Score	Weights
Factor 1: Economic strength				**ba1**	**baa3**	**50%**
Growth dynamics	Average real GDP growth (%)	2019-2028F	2.6	baa3		25%
	MAD Volatility in Real GDP Growth (%)	2014-2023	1.3	baa3		10%
Scale of the economy	Nominal GDP ($ billion)	2023	43.1	ba3		30%
National income	GDP per capita (PPP, Intl$)	2023	15,869.1	baa3		35%
Adjustment to factor 1	*# notches*				1	max ±9
Factor 2: Institutions and governance strength				**baa3**	**baa3**	**50%**
Quality of institutions	Quality of legislative and executive institutions			ba		20%
	Strength of civil society and the judiciary			ba		20%
Policy effectiveness	Fiscal policy effectiveness			baa		30%
	Monetary and macroeconomic policy effectiveness			baa		30%
Specified adjustment	Government default history and track record of arrears				0	max -3
Other adjustment to factor 2	*# notches*				0	max ±3
F1 x F2: Economic resiliency				**baa3**	**baa3**	
Factor 3: Fiscal strength				**ba1**	**ba1**	
Debt burden	General government debt/GDP (%)	2023	38.3	a1		25%
	General government debt/revenue (%)	2023	275.3	ba2		25%
Debt affordability	General government interest payments/revenue (%)	2023	11.9	baa3		25%
	General government interest payments/GDP (%)	2023	1.7	aa3		25%
Specified adjustments	*Total of specified adjustment (# notches)*			-3	-3	max ±6
	Debt Trend - Historical Change in Debt Burden	2015-2023	21.5	0	0	
	Debt Trend - Expected Change in Debt Burden	2023-2025F	1.4	0	0	
	General Government Foreign Currency Debt/ GDP	2023	33.2	-3	-3	
	Other non-financial public sector debt/GDP	2023	4.2	0	0	
	Government Financial Assets including Sovereign Wealth Funds / GDP	2023	2.9	0	0	
Other adjustment to factor 3	*# notches*				0	max ±3
F1 x F2 x F3: Government financial strength				**baa2**	**baa2**	
Factor 4: Susceptibility to event risk				**a**	**a**	Min
Political risk				a		
	Domestic political risk and geopolitical risk			a		
Government liquidity risk				a	a	
	Ease of access to funding			a		
Specified adjustment	High refinancing risk				0	max -2
Banking sector risk				a	a	
	Risk of banking sector credit event (BSCE)	Latest available	ba2	ba1-ba2		
	Total domestic bank assets/GDP	2023	--	<80		
Adjustment to F4 BSR	*# notches*				0	max ±2
External vulnerability risk				a	a	
	External vulnerability risk			a		
Adjustment to F4 EVR	*# notches*				0	max ±2
Overall adjustment to F4	*# notches*				0	max -2
F1 x F2 x F3 x F4: Scorecard-indicated outcome				**Baa2 - Ba1**	**Baa2 - Ba1**	

Note: While information used to determine the grid mapping is mainly historical, our ratings incorporate expectations around future metrics and risk developments that may differ from the ones implied by the scorecard-indicated outcome. Thus, the rating process is deliberative and not mechanical, meaning that it depends on peer comparisons and should leave room for exceptional risk factors to be taken into account that may result in an assigned rating outside the scorecard-indicated outcome. For more information please see our Sovereign Ratings Methodology.

Footnotes: (1) Initial factor score: scorecard indicators combine with the automatic adjustments to produce an initial factor score for every rating factor, as detailed in Moody's Sovereign Ratings Methodology. **(2) Final factor score:** where additional analytical considerations exist, initial factor scores are augmented to produce a final factor score. Guidance on additional factors typically considered can be found in Moody's Sovereign Ratings Methodology; details on country-specific considerations are provided in Moody's research. **(3) Scorecard-indicated outcome:** Factor 1: Economic Strength, and Factor 2: Institutions and Governance Strength, combine with equal weight into a construct we designate as Economic Resiliency (ER). An aggregation function then combines ER and Factor 3: Fiscal Strength, following a non-linear pattern where Fiscal Strength has higher weight for countries with moderate ER and lower weight for countries with high or low ER. As a final step, Factor 4, a country's Susceptibility to Event Risk, is a constraint which can only lower the government financial strength as given by combining the first three factors. **(4) There are 20 ranking categories for quantitative sub-factors:** aaa, aa1, aa2, aa3, a1, a2, a3, baa1, baa2, baa3, ba1, ba2, ba3, b1, b2, b3, caa1, caa2, caa3, ca and 8 ranking categories for qualitative sub-factors: aaa, aa, a, baa, ba, b, caa, ca **(5) Indicator value:** if not explicitly stated otherwise, the indicator value corresponds to the latest available data.

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