

I. THE ECONOMIC ENVIRONMENT(1) Introduction

1. The Republic of Paraguay, with an area of 406,752 square kilometres and an estimated population of 4.9 million (1996), is a landlocked country located in South America; it is bounded by Argentina, Bolivia and Brazil. The Paraguay River divides the country in two parts: in the east lie grassy plains and wooded hills; in the west, a marshy plain bordering the river gives way to dry forest and thorny scrub. The climate is sub-tropical in the east and semi-arid in the far west. The capital, Asunción, with a population of some 502,000, is located on the western border with Argentina and is one of the country's two major river ports.

2. GDP per capita was estimated at some US\$1,933 in 1996, almost double the level of 1989 when an economic reform programme was launched (Table I.1). There have been relatively few social programmes in the past, but these are now being planned as income rises from exports of electricity from Itaipú, the world's largest hydroelectric scheme. The rate of population growth of some 2.8 per cent is one of the highest in Latin America and is falling only slowly: the fertility rate declined only slightly from 4.8 births per woman in 1980 to 4.7 in 1994, while life expectancy increased from about 66 in the 1970s to 68 by 1994. All children receive primary education, while 29 per cent are enrolled in secondary school, up from 20 per cent in the 1970s.

**Table I.1**  
**Economic developments, 1989-96**

	1989	1990	1991	1992	1993	1994	1995	1996
	(Average annual growth rate in per cent)							
Real GDP	5.8	3.1	2.5	1.8	4.1	3.1	4.7	1.3
Consumption	2.1	11.0	3.7	7.2	5.3	8.5	1.8	...
Gross domestic investment	10.1	9.2	8.6	-6.5	2.3	4.5	4.9	...
Exports of goods and services	8.0	19.6	7.4	-4.1	39.6	6.5	16.9	-5.7
Imports of goods and services	-14.2	66.7	14.5	4.1	31.6	26.7	11.4	-9.6
Inflation	...	44.1	11.8	17.8	20.4	18.3	10.5	8.2
Unemployment rate (%)	...	7.5	9.4	9.8	9.0	9.4	8.1	9.8
Memorandum:								
Population ('000)	4,089	4,219	4,334	4,453	4,575	4,670	4,828	4,955
GDP/capita (US\$ current prices)	1,006	1,253	1,443	1,448	1,495	1,672	1,858	1,933
School enrolment ratio (%)								
Primary	105.8	107.5	109.4	110.5	111.1	...	...	...
Secondary	29.2	30.1	30.4	33.8	...	...	...	...
Tertiary	7.9	8.2	...	...	10.1	...	...	...

... Not available.

Source: Banco Central del Paraguay (1997); Informe Económico, February; Banco Central del Paraguay (1996), Estadísticas Económicas, December.

3. Economic growth, as measured by real GDP, has been moderate but quite variable in recent years, and inflation has been brought under control. More recently, growth has been affected by an appreciating currency, expensive credit and the recessionary impact of the 1995 financial crisis, but some recovery is expected in 1997. Economic performance is highly vulnerable to trends in agricultural production and exports (cash crops), as well as shopping tourism, for which Paraguay is a regional

centre. Attempts to reduce the public sector deficit have had an initial negative effect on economic growth, but progress in public sector reform has been retarded by political considerations.

4. Recent increases in, and greater diversification of, foreign direct investment inflows appear to be linked to political and economic reforms, greater integration into the global economy, including through membership of the WTO and MERCOSUR, as well as a tradition of market openness and abundant cheap supplies of electrical energy, which favour Paraguay's long-term economic development.

(2) Recent Economic Developments

(i) Composition and growth of GDP and employment

5. In recent years Paraguay has experienced low to moderate rates of real GDP growth, generally below the peak level of 1989; the low of 1.3 per cent in 1996 was mainly due to the continued recessionary impact of the 1995 banking crisis, discussed in Chapter IV (Table I.1). The uneven GDP growth mainly reflects developments in the agricultural sector, linked to adverse climatic conditions, world commodity prices and credit supply. Other factors include: an increase in government spending in the run-up to the May 1994 presidential elections, followed by a period of fiscal and monetary austerity; the postponement or trimming of public investment projects in response to lower fiscal receipts and the need to support the banking sector in 1995/96; and a decline in private investment in 1995 because of political and financial uncertainty.

6. Forecasts indicate that growth is to recover to 3 per cent in 1997. This expansion is expected to be driven by a record soybean harvest, an increase in public and private investment, an expansive fiscal policy in the 1997 budget, recovery in domestic demand and higher growth in Argentina and Brazil, in particular. However, much depends on the movement of world prices for soybeans and the strength of the recovery in Argentina and Brazil.

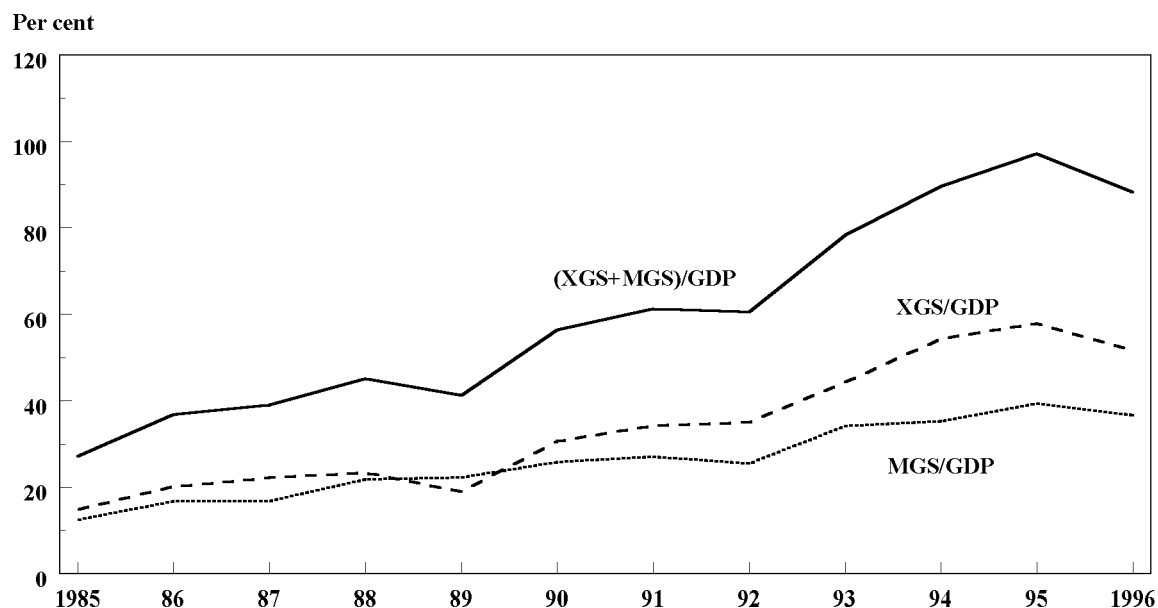
7. Since 1989, the share of trade in goods and non-factor services in GDP has more than doubled to reach 88 per cent in 1996 (Chart I.1). This development is explained by a substantial increase in the share of exports of goods and services in GDP after 1990 under the influence of the reform programme begun in 1989, as well as the progressive rise of the share of imports in GDP, mainly related to improved procedures for statistical reporting, customs valuation and registration.

8. Agriculture is by far the most important single sector in GDP, foreign exchange earnings, and employment, but its share varies with climatic conditions and world prices (Chapter IV). Between 1990 and 1995, the composition of GDP moved towards basic services (with the growth of electricity output from Itaipú), while the contribution of manufacturing declined steadily (Table I.2). In recent years most jobs were created in services, including construction, and in agriculture. From 1989 to 1996, real GDP per capita fluctuated in line with general economic activity, registering, on average, an annual growth of 0.5 per cent (Chart I.2) with absolute declines in 1990-92 and 1996. It has been estimated that 5 per cent annual GDP growth is the minimum necessary to lift a large part of the population out of poverty (Box I.1).<sup>1</sup>

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<sup>1</sup>Latin American Regional Reports - Southern Cone (1996). Estimates from a recent study by the FAO/IBR cited in *ABC Color*, (1996).

**Chart I.1**  
**Trade in goods and non-factor services, 1985-96**



Source: Banco Central del Paraguay (1996), Estadísticas Económicas, December.

**Table I.2**  
**Structure of the economy, 1990-96**

	1990	1991	1992	1993	1994	1995	1996 <sup>a</sup>
Share of main sectors in GDP (%)							
Agriculture	17.2	16.0	15.5	16.0	15.1	16.1	16.0
Livestock	7.5	7.8	7.8	7.7	7.6	7.5	7.6
Forestry	2.7	2.8	2.8	2.8	2.8	2.8	2.8
Manufacturing	16.1	15.9	15.6	15.3	15.1	14.8	14.3
Construction	5.2	5.2	5.4	5.3	5.4	5.3	5.4
Services	50.7	51.7	52.2	52.2	53.4	52.9	53.3
of which:							
Electricity	2.8	3.0	3.3	3.7	4.3	4.7	4.9
Commerce & finance	26.4	26.9	26.6	26.5	26.8	26.0	25.4
Government	4.5	4.5	4.8	4.8	5.0	5.1	5.5
Share of sectors in total employment (%)							
Agriculture	37.3	36.9	36.2	36.5	35.5	35.8	35.5
Manufacturing	12.8	12.7	12.5	12.3	12.2	12.0	11.5
Construction	6.5	6.2	7.1	7.4	8.0	8.5	9.1
Services	43.2	44.1	44.0	43.7	44.2	43.5	43.8

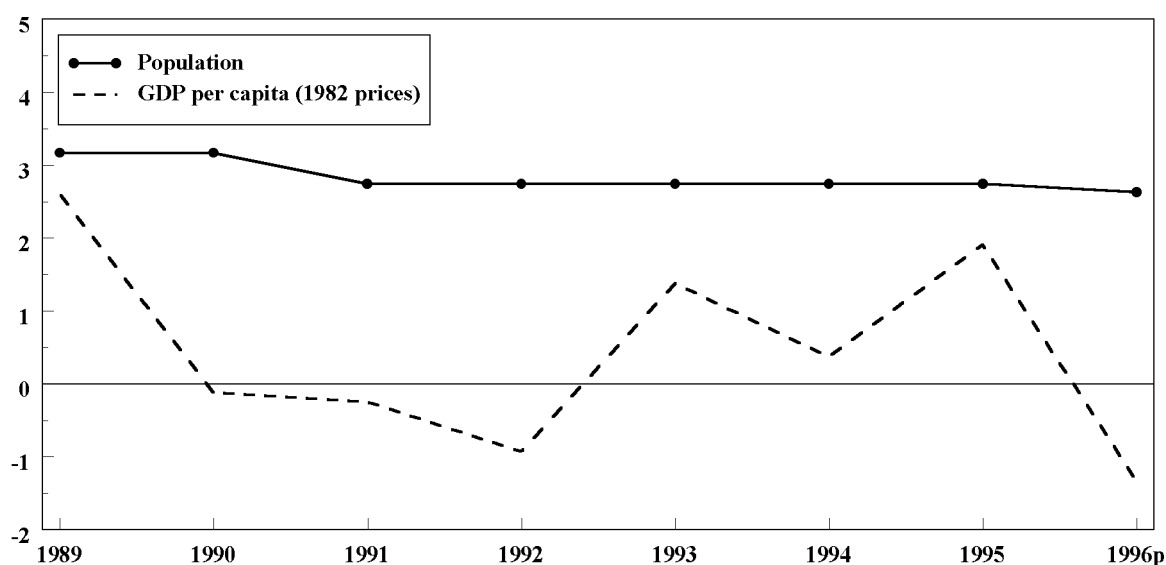
a Provisional.

Source: Banco Central del Paraguay (1997), Informe Económico, February; Banco Central del Paraguay (1996), Estadísticas Económicas, December.

## Chart I.2

### Developments in real per capita income and population growth, 1989-96

Per cent, annual growth rate



P Provisional.

Source: Banco Central del Paraguay (1996), Estadísticas Económicas, December.

#### Box I.1 Development challenges and action

Paraguay's future development and economic growth appear to depend on the timely elaboration of strategies and programmes addressing issues such as job-creation, informality, social welfare and rural poverty.

One of the most serious challenges facing the present and future governments is the creation of jobs to meet the increasing labour force. Argentina and Brazil have traditionally provided relief by absorbing Paraguay's excess labour. Although restrictive financial and monetary policies have assisted in the fight against inflation, they have had an initial adverse effect on economic activity and unemployment.

Business is concerned about the "unfair" distribution of taxes and fees, not recovered from the large informal sector, which includes the unregistered border trade (of a volume exceeding the GNP). According to a recent report of the Technical Secretariat for Planning, the informal sector in Paraguay employs 44 per cent of all urban workers (excluding domestic servants and public-sector workers), of which 54 per cent were in retail trade.

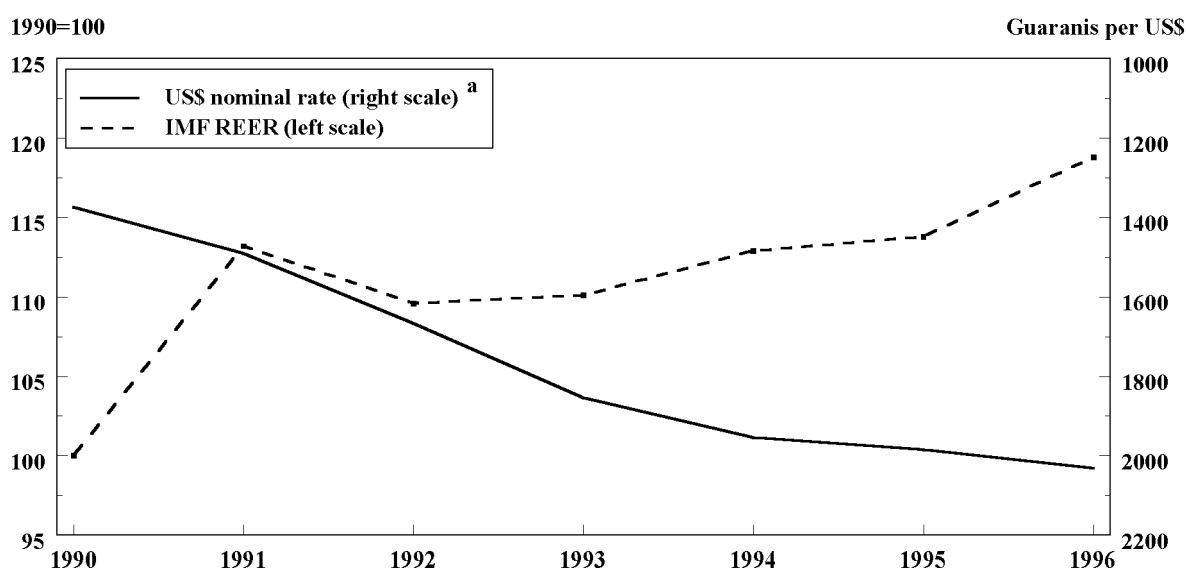
A recent report of the Secretariat for Social Action of the Office of the President, indicates that poverty is largely concentrated in rural areas. In 1994, public social spending was among the lowest in the region (as a percentage of GDP). The State social security organization (IPS) covers only 19 per cent of the population, 71 per cent of which live in Asunción. In October 1996, the first Plan for a Social (Human Resource) Development Strategy against poverty was announced.

9. To promote economic growth, a Plan for the Reactivation of the Economy is to be launched in 1997, financed with receipts from a bond issue. The plan is to include the deepening of economic reforms; the channelling of funds to the productive sector (mainly agro-industry); changes in the financial sector; infrastructure and construction-related investment; and support to small- and medium-size firms.<sup>2</sup>

(ii) Prices

10. Under the influence of the reform programme, inflation fell from a peak of 44 per cent in 1990 to 8 per cent in 1996, albeit with a surge to some 20 per cent in 1993 (Table I.1). Apart from the anti-inflationary effects of more stringent economic policies, this reduction in inflation also reflects the deflationary impact of the 1995 financial crisis, including weak consumer demand driven by credit shortage, extensive use of the emission of Treasury Bills and the real appreciation of the guaraní (Chart I.3). This process was also assisted by efforts to resist pressure to increase the minimum wage level.<sup>3</sup> Increases in public tariffs were also delayed, although this could have indirect inflationary effects by increasing the public sector deficit.

**Chart I.3**  
**Exchange rate developments, 1990-96**



a Period average.

Source: IMF, International Financial Statistics.

<sup>2</sup>*Última hora*, 20 January 1997.

<sup>3</sup>In 1994, 34 per cent of the economically active population in urban areas earned less than the minimum wage, one of the highest shares in Latin America.

11. For 1997, the inflation target is set at 8 per cent, but is not likely to be met because of price increases in January 1997 on basic public goods and services (water and electricity charges, petroleum products, public transport, cement); a widening fiscal deficit, generated by government spending in the pre-election year; and an increase of 10 per cent in the minimum wage.

(iii) Exchange rate developments

12. In February 1989, Paraguay replaced its multiple exchange rate régime with a single market-determined floating rate. Since the Central Bank of Paraguay has intervened to smooth out undesirable sharp fluctuations due to changes in market conditions and speculative capital inflows, but it does not interfere with underlying market trends.<sup>4</sup> No controls are imposed on foreign exchange transactions, which may be conducted through commercial banks and exchange houses; nevertheless, since January 1997, new legislation against money-laundering operations has introduced registration and screening requirements for amounts exceeding US\$10,000.<sup>5</sup>

13. Following the initial devaluation after the floating of the currency, strong capital inflows led to a virtually continuous appreciation of the real effective exchange rate (REER) between 1990 and 1996, with nominal depreciation against the U.S. dollar being less than the movement in the relative rates of inflation (Chart I.3). While this real appreciation assisted in controlling inflation, it has had a negative effect on the country's competitiveness; this trend is of particular concern for cotton exporters faced with declining sectoral productivity and cotton profitability.

14. Paraguay has been sensitive to exchange rate policy developments in Brazil, a major trade partner. For example, following the introduction of Brazil's *Plano Real* in 1994, Paraguay has benefited from the initial strengthening of the Brazilian currency against the United States dollar to increase its non-traditional exports of maize, beer, milk and clothing to the United States. Reportedly, the nominal depreciation of the *guaraní* at the end of 1996 was affected by Brazil's tightening of its foreign exchange allowance (reduced from the equivalent of US\$250 to US\$150) for shopping tourism, as well as Argentina's reduction of import duties on liquor, electronic goods and perfumes.<sup>6</sup>

15. A Reciprocal Payments and Credits Agreement governs payments among Latin American Integration Association (LAIA) partners (Chapter II); clearing takes place every four months.<sup>7</sup> In 1995, Paraguay's domestic regulations with respect to this Agreement were amended, to reduce the

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<sup>4</sup>*Banco Central del Paraguay* (1995), p.52; IMF (1996), p.377.

<sup>5</sup>Money-laundering was also made punishable with prison terms of up to ten years (Law 1015, 10 January 1997).

<sup>6</sup>EIU (1996a), p. 35.

<sup>7</sup>Under this Agreement, a multilateral clearing system is operated through accounts maintained among the central banks concerned. Recent amendments relate to the definition of "automatic payments" as well as residents' operations. In 1994, a dispute settlement mechanism was established to resolve disagreements between the central banks on issues related to the Agreement (LAIA Resolution 76, 28 September 1994). IMF (1996), p.377; WTO (1996b).

risk associated with guarantees provided by the Central Bank of Paraguay on operations covered by the Agreement.<sup>8</sup> Paraguay also maintains a reciprocal credit agreement with the Dominican Republic.

16. Since 1990, movements in the growth of Paraguay's international reserves have reflected mainly the willingness of economic agents to release their foreign currency holdings, royalty inflows from the hydroelectric power plants *Itaipú Binacional* and *Entidad Binacional Yacyretá* (discussed in Chapters III and IV) and the fact that interest earned on reserves held in overseas bank accounts is lower in real terms than domestic interest rates (Table I.3). In December 1996, reserves stood at about US\$1.1 billion, corresponding to more than two months of imports.<sup>9</sup>

**Table I.3**  
**Balance-of-payments, 1989-96**  
(US\$ million)

	1989	1990	1991	1992	1993	1994	1995	1996 <sup>a</sup>
Current account balance	256	-170	-332	-628	-412	-610	-475	-669
Merchandise trade balance <sup>b</sup>	164	-270	-758	-871	-932	-1,382	-1,507	-1,378
Exports of goods (f.o.b.) <sup>c</sup>	1,180	1,366	1,110	1,054	1,827	2,222	2,961	2,680
Imports of goods (f.o.b.)	1,016	1,636	1,868	1,925	2,759	3,603	4,468	4,059
Shipments	-131	-202	-251	-269	-329	-295	-407	-462
Other transportation	-27	-3	21	11	1	-26	-34	-24
Travel	52	25	366	338	412	540	795	612
Investment income	-63	-75	-57	-128	-90	-67	-72	-94
Other services	-29	-36	-63	-46	81	235	253	236
Current transfers	24	56	72	72	100	32	72	39
Binational entities	265	335	338	265	346	353	426	401
Capital and financial account balance	-20	62	151	-212	181	411	234	351
Direct investment <sup>d</sup>	13	70	84	137	119	164	157	225
Other capital	-33	-8	68	-349	62	247	77	126
Long-term capital	18	-140	-35	-126	6	68	89	-34
Public sector	59	-130	-30	-123	-2	71	87	-11
Private sector	-36	...	-4	0	4	1	...	1
Bank deposits	-6	-10	-1	-3	4	-4	1	-24
Short-term capital	-51	132	102	-223	56	179	-12	160
Errors and omissions	-91	327	481	493	317	527	289	207
Overall balance	145	220	299	-347	86	328	47	-111
Change in reserves (- Increase)	-145	-219	-299	347	-86	-328	-47	111

... Not available.

a Preliminary.

b Includes registered trade based on data DOT/IMF.

c Includes re-exports.

d Includes direct investment of binational entities.

Source: Banco Central del Paraguay (1997), Informe Económico, February.

<sup>8</sup>*Informe del Excelentísimo Señor Presidente Constitucional, Juan Carlos Wasmosy, al Honorable Congreso Nacional*, 1 July 1996, p.15. Reportedly, in the context of the 1995 financial crisis, the Central Bank of Paraguay was defrauded of US\$28 million through banking operations under this Agreement.

<sup>9</sup>*Banco Central del Paraguay* (1997).

(iv) Public finances

17. In 1991 the tax system was simplified by: replacing several small, difficult-to-collect taxes with a value-added tax and a selective consumption tax (Chapter III); introducing a single tax on small businesses, a uniform rate of earnings tax, an income tax on agriculture property, and changes in the sanctions system against late payments and tax evasion (Chapter IV).<sup>10</sup> Improvements in tax administration made since mid-1994 have led to a rapid increase in customs tax receipts. Further efforts, begun in February 1996, to reduce evasion of corporate income tax have focused on the major contributors in Asunción and the border region with Brazil.<sup>11</sup> In response to recommendations from the IMF in May 1996, the Government has also announced its intention to reduce public expenditure, and has increased the level of the selective consumption tax on beer and cigarettes as well as the basis for VAT valuation under the tourism régime in January 1997. Consideration was also given to introducing additional fiscal measures, including the elimination of the single tax on small businesses and the introduction of personal income tax.

18. In recent years, Paraguay has frequently run fiscal deficits. Government revenue is highly dependent on indirect taxation mainly in the form of foreign trade taxes and VAT, there being no personal income tax. Until recently, public spending has been dominated by current expenditure (78 per cent in 1996), with capital investment bearing the brunt of efforts to contain the overall deficit; however, from 1997 current expenditure is to be kept at a minimum level and priority is to be given to investment in infrastructure-related projects (see below). Savings through public sector reforms and more rigorous control of public finance have been delayed, partly for political considerations (Box I.2).<sup>12</sup>

19. In 1996 Paraguay registered a record fiscal deficit of about G141 billion (US\$70.5 million) because of increased expenditure to finance a wage rise for public sector workers; the bail-out of collapsed banks; lower receipts (partly due to the extension of Brazil's restrictions on foreign exchange allowance for tourist purchases) and delayed payments of royalties from the *Itaipú Binacional* (Chapter IV).

20. The 1997 Budget is intended to reactivate the economy through public works, and about a fifth of the financial resources are allocated to the Ministry of Public Works. However, current expenditure is limited to 40 per cent of total spending, an austerity measure adopted in June 1996. To finance the public deficit in 1997, a major increase in both foreign and domestic credit will be required, with potentially inflationary consequences; a US\$150 million two- to five-year issue of Treasury bonds was authorized.

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<sup>10</sup>World Bank (1994a), p.29.

<sup>11</sup>EIU (1996b), p.25.

<sup>12</sup>Reportedly, several unorthodox or fraudulent practices have been uncovered in recent years, causing the authorities concern about the possible impact on the country's economic performance and prospects, as well as its credibility vis-à-vis potential investors, trading partners or multilateral lending agencies. These have mainly related to rescue operations of the 1995 financial crisis, public procurement, the collection of import duties and port charges as well as speculative use of public funds.



**Box I.2 State reforms: Background and prospects**

Paraguay's public sector, small by Latin American standards in the 1970s, grew in the 1980s in the light of direct State involvement in large investment projects (e.g., the Itaipú hydroelectric power project, a mini-steel mill, a cement plant, a second international airport). These projects have had a major economic and social impact.

As part of the reform programme, Law 126/91, published on 9 January 1992, authorized the Executive to sell entirely or partly five State-owned companies, setting preferential treatment for nationals. In practice, little progress has been made in this area. Since 1992, no privatization case has been concluded except for LAP, the airline company, whose assets were fully sold to the private sector in 1996 only, and CAPASA, the alcohol firm, where the State still retains about one third of the shares. Privatization of the three other State companies (ACEPAR/steel, FLOMERES/merchant marine, and railway) has been delayed for several reasons including continuous pressure from trade union federations (including the public-sector confederation), legal challenges, problems with valuation of assets, or a lack of interest from potential buyers (Chapters II, III and IV).

Despite the lack of significant progress in implementing the initial programme and considerable difficulties in passing new legislation, the Government envisages further reductions in the degree of State involvement or de-monopolization in other areas, e.g., cement production, electricity production and distribution, sanitation, telecommunications, certain port services, social security, and banking. However, it seems unlikely that outstanding structural reforms will be carried out prior to the 1998 presidential elections.

**(v) Balance of payments**

21. In recent years Paraguay has experienced a series of current account deficits, financed by foreign borrowing as well as potentially volatile short-term capital inflows. Despite increasing inflows from royalty payments from *Itaipú Binacional*, the current account deficit has been increasing, driven by a widening merchandise trade deficit. This is related to Paraguay's heavy dependence on two primary export products (soybeans and cotton) whose prices have been in decline, as well as a steady increase in imports (Table I.3). However, the authorities expect the current account deficit to shrink by 4 per cent in 1997 as a result of reduced demand for imports and higher revenue from exports.

**(vi) External debt**

22. Between 1989 and 1993 Paraguay progressively reduced its external debt by clearing all its outstanding debt to Brazil through debt swaps (1989-1990) and by negotiating debt re-scheduling with creditor nations of the Paris Club on a case-by-case basis rather than signing a stand-by agreement with the IMF in 1992. Since 1994 total external debt has risen mainly due to borrowing from multilateral and bilateral lenders (Chapter II).

**(3) Developments in Merchandise Trade**

23. Following the trade liberalization efforts of the early 1990s (Chapter III) and the real appreciation of the currency, noted earlier, a growing merchandise trade deficit, particularly with MERCOSUR partners, has emerged. The rise in (largely unrecorded) re-exports of goods to neighbouring countries up to 1995, was balanced by negative developments in world commodity prices, and the cut back in receipts from shopping tourism, and there was also a major improvement in the recording of imports. The small decline in the deficit in 1996 is explained by a reduction in imports associated with the continuing domestic recession and the increase in value of soybean exports.

24. Trade statistics do not accurately reflect trade flows because of unregistered trade with Brazil and Argentina as well as the weaknesses of the domestic statistical service. Unregistered flows include imports and re-exports (of machinery, vehicles, spare parts, alcoholic beverages, perfumes, electronic goods, tobacco) mainly related to shopping tourism, as well as unauthorized trade in certain agricultural and forestry products (Chapters III and IV). Trade in re-exported goods is estimated at between US\$3 billion (estimates by the Chamber of Commerce of Ciudad del Este) and US\$12 billion (Brazilian Customs estimates).<sup>13</sup> Despite forecasts of a decline in shopping tourism operations as a result of MERCOSUR commitments, no such trend is yet apparent, probably because of the substantial differences in domestic indirect taxes.

(i) Composition of trade

25. Since 1989 Paraguay's reported merchandise trade structure has not changed significantly (Chart I.4). Domestic exports remain highly concentrated in certain commodities whose trade weight varies according to domestic output and developments in world prices; in this context, the share of soybeans and cotton in the total declined by more than 21 per cent between 1989 and 1995 (Chart I.4). In the same period, the share of food in total imports rose sharply, while the share of fuel in total imports declined.

(ii) Direction of trade

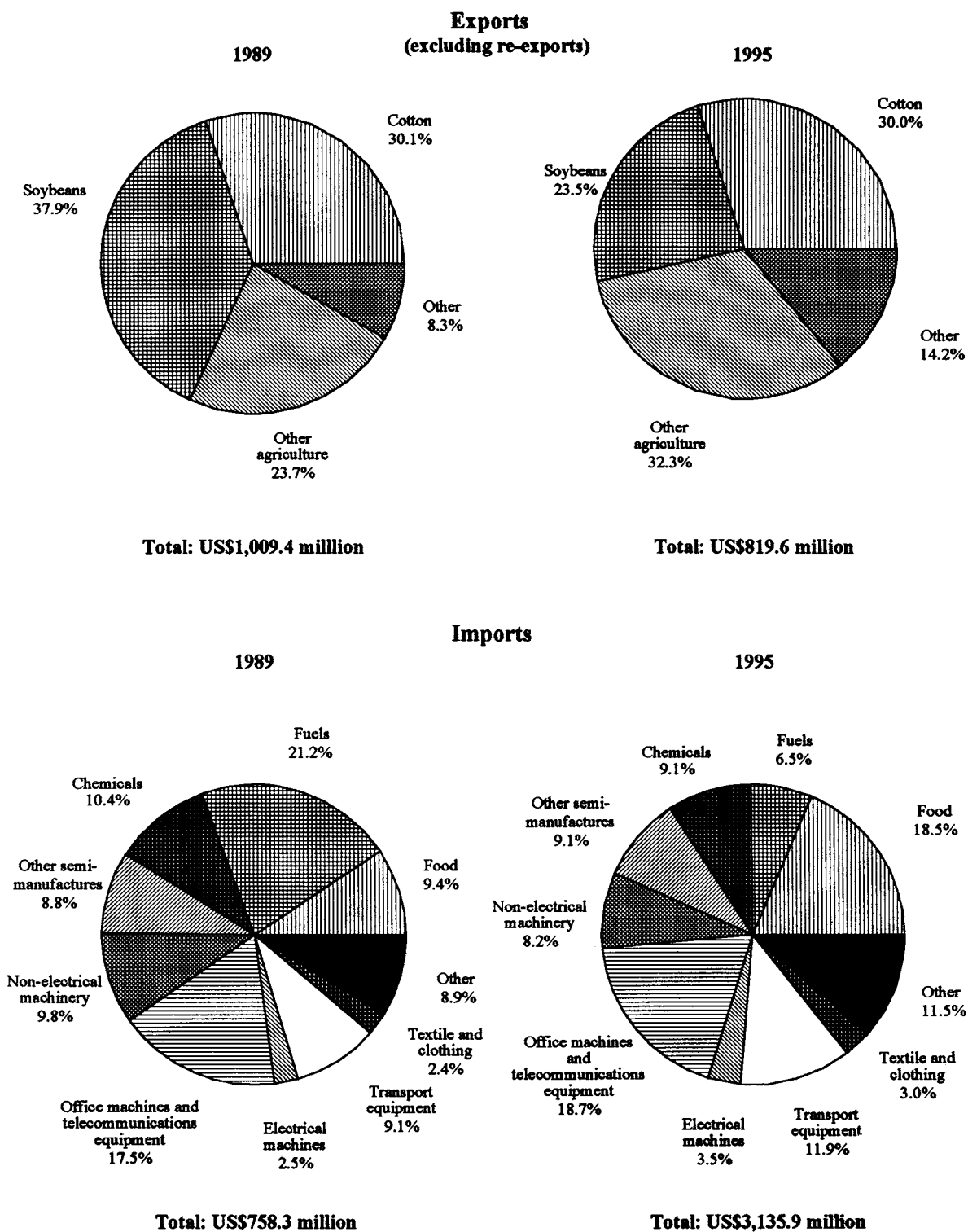
26. Regional trade has gained importance in the light of the implementation of regional trade liberalization commitments (Chapter II); in 1995 more than 43 per cent of Paraguay's imports came from other Latin American partners which were in turn the destination of about two thirds of its exports. Between 1991 and 1995 there was a 27 per cent increase in the share of total imports from the region and their value almost tripled to US\$1.3 billion; the larger part originated in MERCOSUR and other LAIA countries, mainly Chile (Chart I.5). The share of exports to the region relative to total exports rose by 38 per cent, mainly due to the rapid growth of exports to MERCOSUR partners.

27. Individually, Brazil is Paraguay's most important trading partner (Chart I.6). Under MERCOSUR, Argentina and Brazil have become even more important as suppliers and export markets (including for cotton). The European Union is a major export market for soybeans, but since 1989, its share in merchandise trade has dropped slightly. The share of imports from Asian countries (mainly China) has risen sharply in the same period.

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<sup>13</sup>EIU (1995c), p.42; EIU (1996b), p.26; World Bank (1994a), p.89.

**Chart I.4**  
**Merchandise trade by sector, 1989 and 1995**

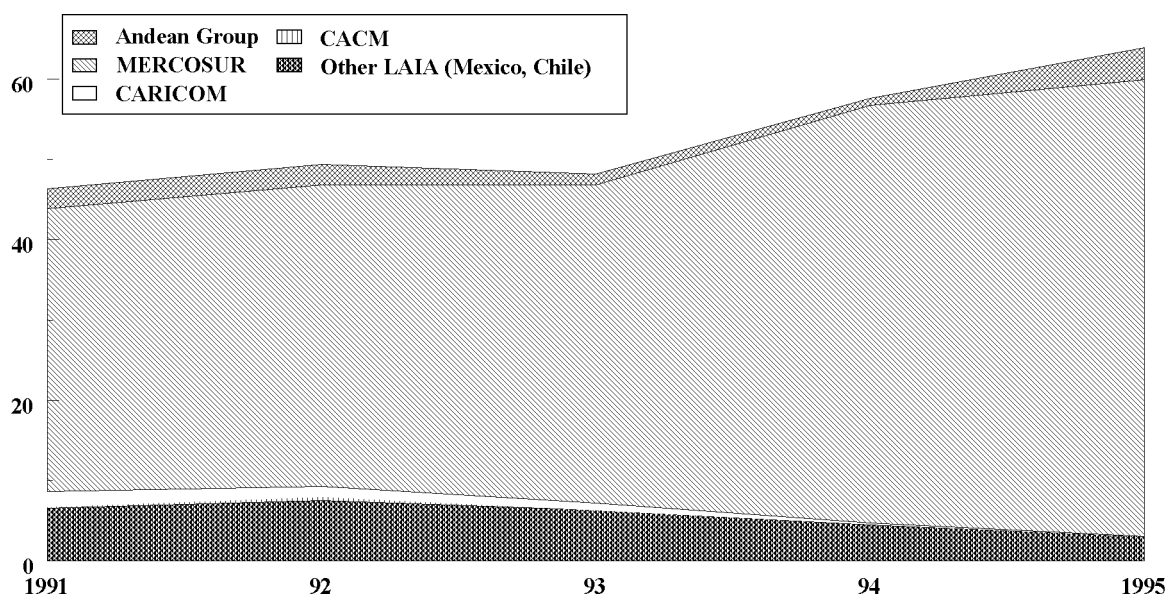


Source: UNSTAT Comtrade database.

**Chart I.5**  
**Paraguay's foreign trade with Latin America, 1991-95**

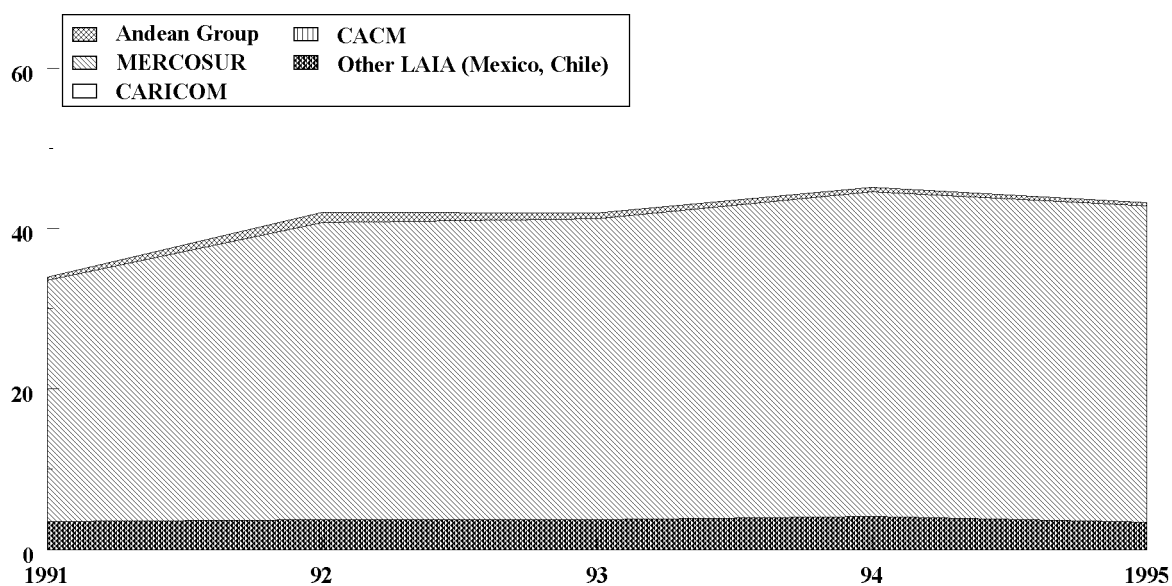
**a Exports**

Per cent of total exports



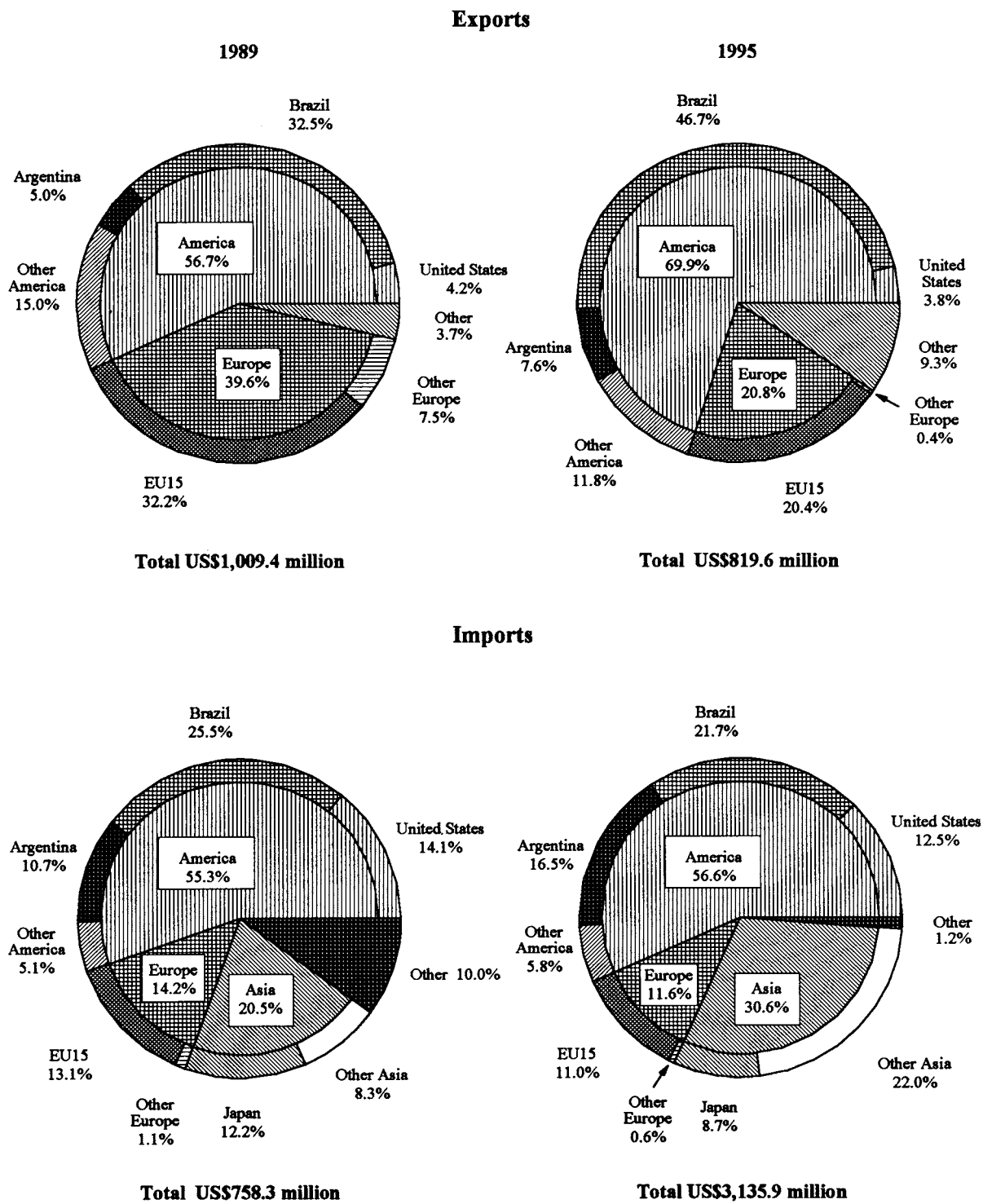
**b Imports**

Per cent of total imports



Source: UNSTAT Comtrade database.

**Chart I.6**  
**Merchandise trade by partner, 1989 and 1995**



**Source:** UNSTAT, Comtrade database.

28. Paraguay's overall merchandise trade deficit with other Latin American partners has progressively increased from about US\$276 million in 1992 to US\$909 million in 1995.<sup>14</sup> This was mainly due to rising recorded trade deficits with MERCOSUR partners and Chile. However, the recorded trade deficit does not take full account of unregistered re-exports related to shopping tourism; the authorities indicated that 22 per cent of registered imports are re-exported.

(4) Trends and Patterns in Foreign Investment

29. Following the 1989 reforms (including the introduction of investment incentives), the establishment of MERCOSUR, and the introduction of legislation on free-trade zones, foreign direct investment (FDI) has risen. According to balance-of-payments data, annual FDI inflows exceeded US\$200 million both in 1995 and 1996.

30. Recent FDI inflows have also become more diversified (Chart I.7). The sectoral pattern of inflows seems to have moved away from traditional industries (e.g., agro-industry) and spread to other sectors including services. Industrial investment and agricultural expansion were the main sectors for new FDI in 1996; these included investment in a US\$500 million cellulose plant, metal alloys and a natural gas pipeline (to fuel fertilizer and methanol plants).<sup>15</sup> In addition to new FDI inflows and re-investment of profits, loans from abroad have also increased (Chart I.8).

31. In recent years, foreign direct investment has originated mainly in the EU (France, Germany and the United Kingdom) and MERCOSUR countries, mainly Brazil (Chart I.7); in 1994 their shares corresponded to 37.5 per cent and 24.3 per cent of total inflows. Between 1992 and 1994 other major foreign investors included Switzerland and the United States.

32. Chinese Taipei is also an important investor in Paraguay. In 1996 several State-run firms from Chinese Taipei were planning to invest in Paraguay (steel, electricity) while 72 private companies from the same source were behind a US\$150 million industrial park to be operational by mid-1997. The park is expected to generate exports of US\$400 million a year, mainly destined for the MERCOSUR market.

33. In addition to low labour and energy costs, participation in an enlarged MERCOSUR market and plans for greater involvement of the private sector in certain public services are expected to make Paraguay more attractive to foreign investors. Problems related to poor infrastructure in areas such as telecommunications and transport are to be tackled with de-monopolization and increased public spending in public works, as discussed above. An improved legislative framework for assembly operations was expected to be approved by mid-1997.

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<sup>14</sup>UNSTAT, Comtrade database.

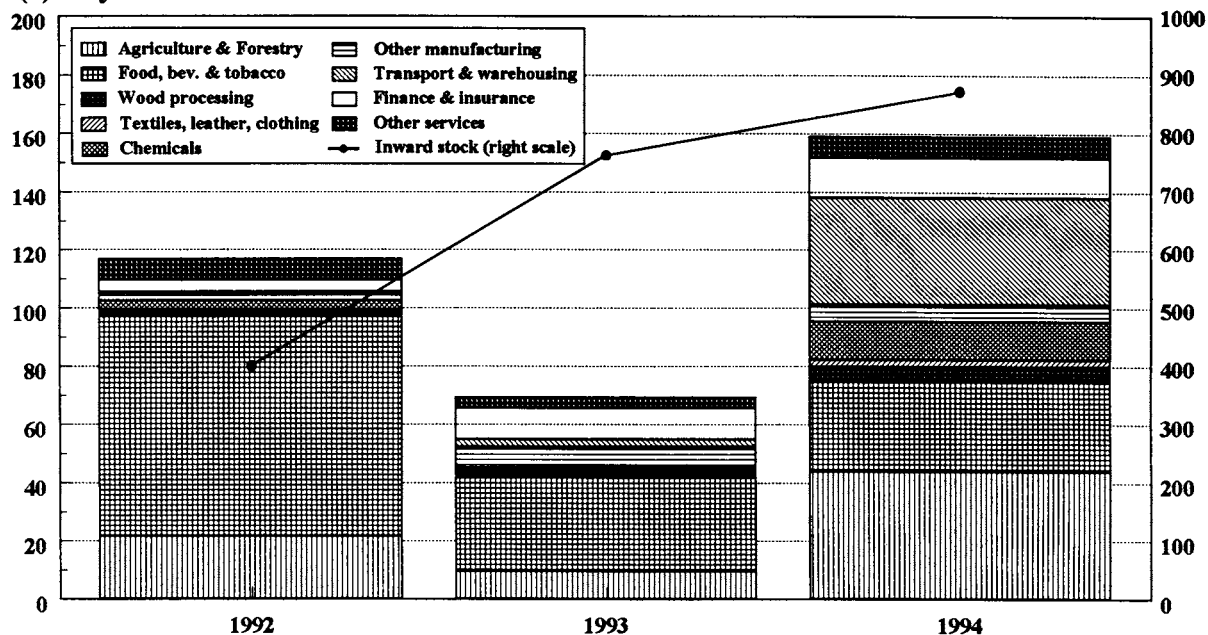
<sup>15</sup>EIU (1997), p. 31.

Chart I.7

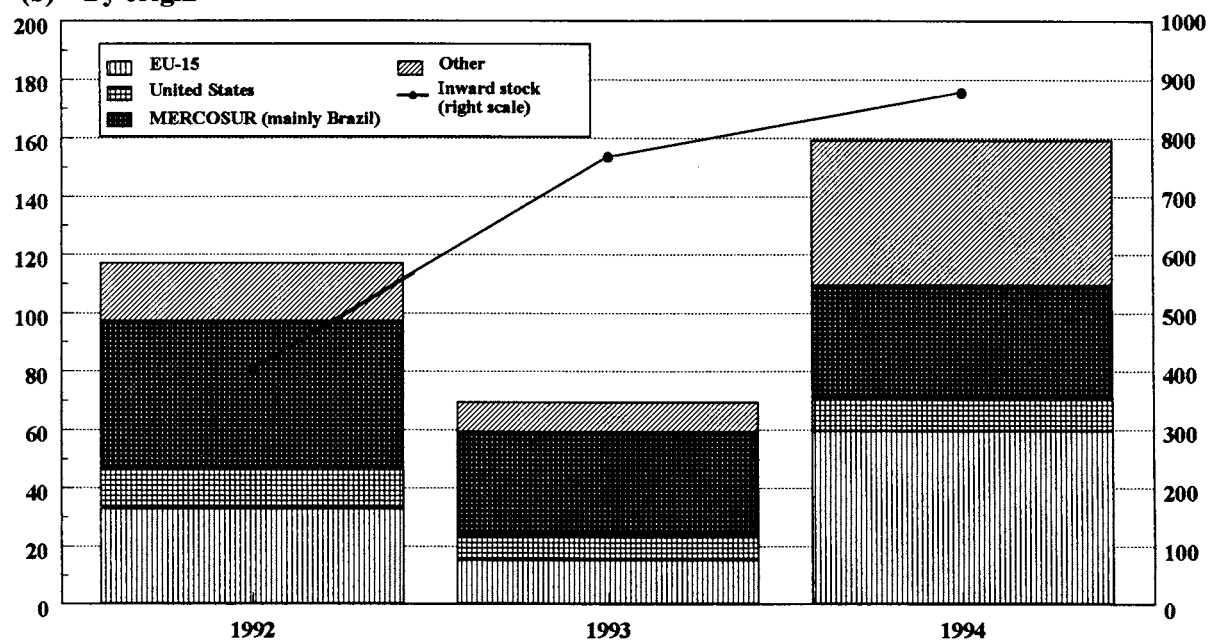
## Net inflows and inward stock of foreign direct investment, 1992-94

US\$ million

## (a) By sector



## (b) By origin

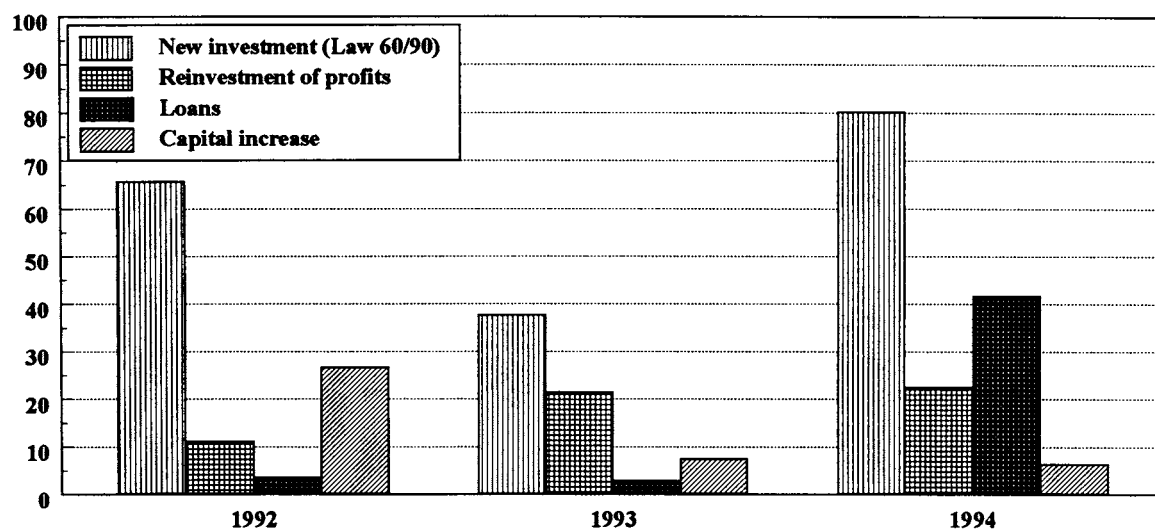


Note: Inward stock estimated by accumulating flows since 1970.

Source: Banco Central del Paraguay; UN (1995), World Investment Report.

**Chart I.8**  
**Types of net inflows of foreign direct investment, 1992-94**

(US\$ million)



**Source:** Banco Central del Paraguay.