Financial Stability Report

First Half 2014

BANCO CENTRAL
DE LA REPÚBLICA ARGENTINA

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Preface

Pursuant to the latest amendment of its Charter, the Central Bank's mandate and objectives were enlarged. Section 3° provides that the purpose of "the Bank is to promote —within the Framework of its powers and the policies set by the National Government— monetary and financial stability, employment, and economic development with social equality".

Financial stability, one of the express objectives of the new mandate, is a critical condition to ensure the financial system contribution towards economic and social development. As widely shown throughout history and ratified by the latest international crisis, there are serious negative externalities which result from an ill-functioning process of financial intermediation. Hence, the protection of financial stability by Central Banks has once more come to the fore.

A transparent communication (public-oriented) strategy has been designed with a view to promoting financial stability and complementing regulatory and supervisory powers. In this sense, the ***Financial Stability Report*** *(****FSR****) gives a comprehensive assessment of the development of financial system conditions. The* ***FSR*** *combines several channels of information on the subject gathered by the Central Bank in a single publication. In addition, the Central Bank discloses —between* ***BEF*** *half-yearly publications— a monthly* ***Report on Banks*** *so as to keep the public informed of the latest developments of the financial system. The Central Bank mainly resorts to these publications to disclose its outlook for the financial sector.*

Buenos Aires, June 17, 2014

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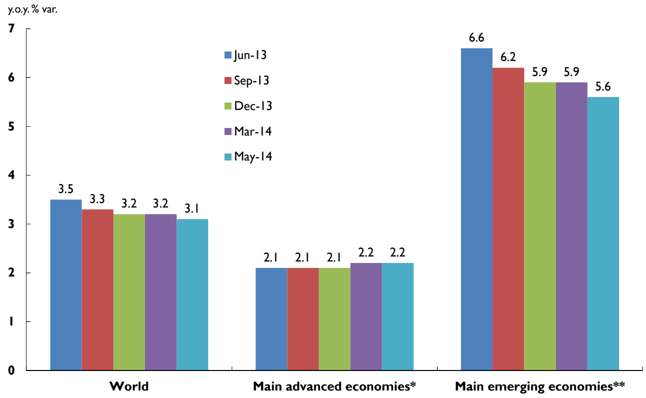
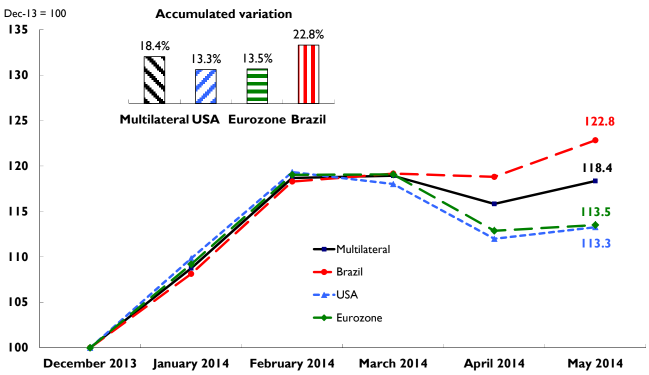


Source: FocusEconomics

*G-7 **Brazil, Russia, India and China

Chart 2

Multilateral and Selected Partners Real Exchange Rate Evolution



Source: BCRA and Bloomberg

After the deceleration of the first quarter of 2014, the economic activity worldwide would have regained some momentum mainly due to the recent performance of advanced economies. These countries have continued to apply expansionary monetary policies, even though with mixed trends (while the United States has started to lessen the stimuli since early 2014, in Europe the ECB has recently announced several measures), combined with restrictive fiscal policies. Despite some improvements on the margin, the labor market still shows signs of weakness in some of these nations and the trend of the private sector to deleverage still remains, which limits the future evolution of consumption and investment.

The economic performance of emerging countries that are more dependent on capital flows was still impacted by external contraction and, especially, by the effects of expectations about a future change in the US monetary policy bias. These economies experienced pressures on the values of their currencies and on their domestic prices to which they responded with a tightening of their monetary policies through interest rate increases. In turn, developing nations that are less dependent on international capital flows implemented additional stimulus policies. Thus, the macroeconomic performance of emerging countries was increasingly mixed.

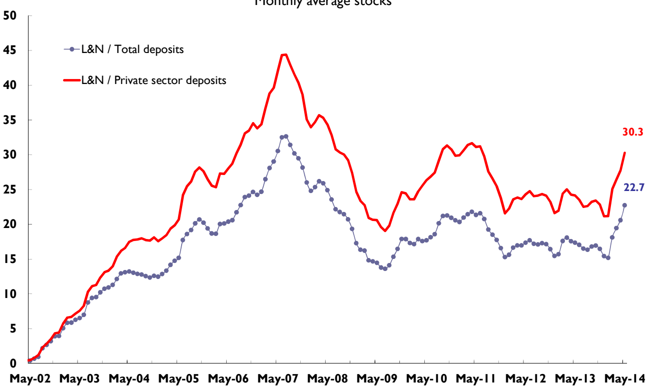
At international level, there are still factors of uncertainty. The main reasons for concern are, on the one hand, the potential bias change in the US monetary policy and, on the other, the effect of the measures announced by the European Central Bank (ECB). There is also concern for the deceleration observed in some global growth engines, such as China, as well as for the difficulties of Europe to regain momentum and the geopolitical tensions resulting from the conflict between Ukraine and Russia. Vis-à-vis this context, caution prevails in the financial markets.

On the domestic front, the reduction of external demand for Argentine products —especially from Brazil— added to a weakening trend in domestic consumption and investment, reflected in a slowdown of the economic activity so far in 2014. On the supply side, the industrial sector and the construction business were particularly hit, even though this was partially offset by the improvement of agricultural production and the sustained growth of services. This evolution occurred in a context of relative stability in the main labor market indicators which, added to the effective

Chart 3

LEBAC, NOBAC and Deposits

Monthly average stocks

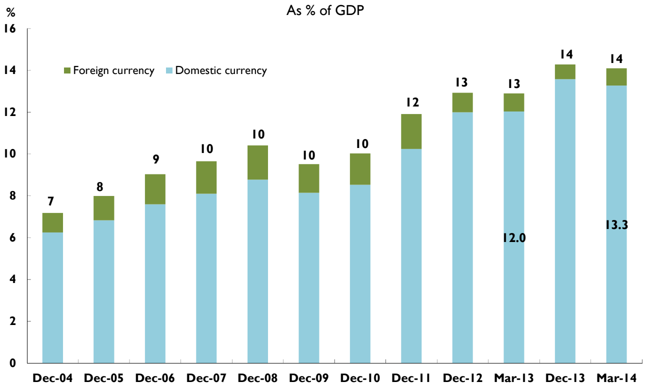


Source: BCRA

Chart 4

Credit to Private Sector

As % of GDP



Note: Estimated data based on the new National Accounts series (base year: 2004).
Source: BCRA and INDEC

implementation of the wage increases signed in this year's collective bargaining agreements, might help household consumption to recover in the next few months. In addition, the income improvement of sectors linked to farming production and the sustainability of policies tending to support the income of the most vulnerable sectors of the population, together with the recent adjustments of pension benefits and family allowances, will also contribute positively to this outlook.

Within a less favorable international context, the exchange rate depreciated in January 2014 and helped improve the external competitiveness of our economy. In addition, a decision was made to increase the interest rates of the Central Bank's bills (LEBACs), thus boosting saving in domestic currency and also increasing liquidity absorption through such instruments. In this sense, during the first five months of the current year, the Central Bank sterilized $58.4 billion through the bonds it issues and through repo transactions; despite this, the stock of LEBACs and NOBACs relative to deposits stood below the historical levels.

The Central Bank has also reintroduced limits to banks' net global position in foreign currency, so that they reduce their exposure to currency risk and increase the supply of foreign currency, therefore contributing to lessen pressures on the foreign exchange market. As a result of these measures, which were in line with BCRA's objective of monetary and financial stability, and added to the higher seasonal currency settlement by exporters, the monetary authority became once again a net purchaser in the foreign exchange market. By the end of May, international reserves totaled US$28.54 billion —with an increase of US$1.53 billion in April and May; therefore, from January to May, net purchases by the Central Bank amounted to US$3.74 billion, against US$731 million in the same period of 2013.

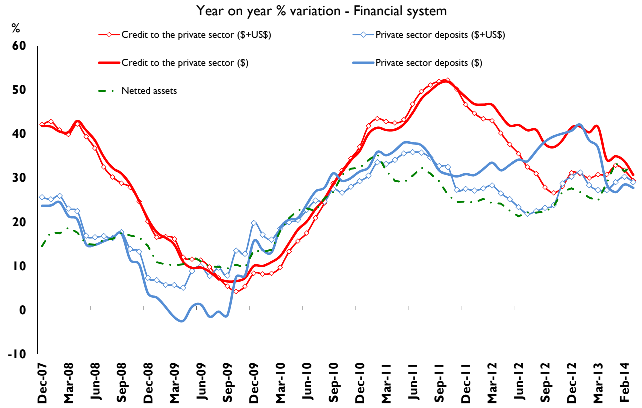
A positive bias was observed in the first months of 2014 in the prices of the Argentine financial assets of high liquidity in the domestic markets, even though they experienced a more marked volatility at the beginning of the year. This evolution was due to both context-related factors in the international markets and domestic factors, which include the performance of the exchange rate and the agreements reached with Repsol and the Paris Club, among others. The recent rejection by the US Supreme Court to the appeal submitted by Argentina about the litigation with sovereign bondholders that did not agree to the restructurings offered by the country opens a new scenario for the next months.

Within this international and domestic context, by late 2013 and early 2014, the financial intermediation activity continued to expand in Argentina, even though at a more moderate pace. Thus, bank loans to the private sector went up at a 29.4% year-on-year (y.o.y.) rate as of March 2014, mainly driven by the lines in pesos.

Chart 5

Financial Intermediation

Year on year % variation - Financial system



Source: BCRA

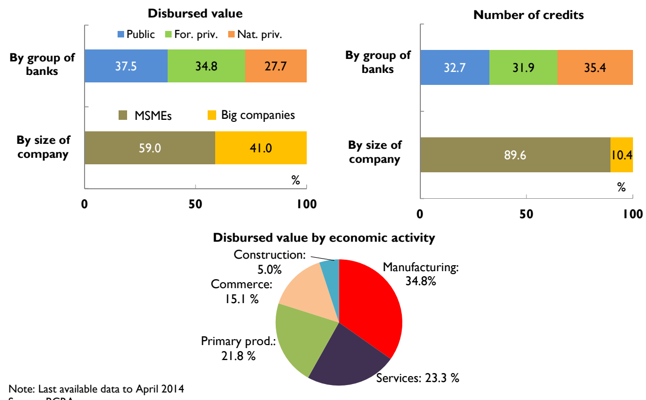
In the first months of 2014, the increase of financing to the private sector was mainly explained by loans to companies, which went up nearly 31% y.o.y. in March. The Central Bank continued promoting the instruments devoted to finance investment through the Credit Line for Productive Investment (LCIP) and the Bicentennial Productive Financing Program (PFPB). Regarding the former, loans were awarded for $58.1 billion in its first three tranches, with a total disbursement so far of $56.77 billion, mainly to micro, small and medium-sized enterprises (MiPyMEs). With reference to the tranche corresponding to the first half of 2014, with preliminary information as of April, it has been observed that approximately 41% of the aggregate target for the period has been already fulfilled.

With a view to stimulating lending to households under more favorable conditions, within a context of high liquidity and solvency at the financial institutions, the Central Bank has recently implemented a set of measures under the framework of its new Charter and subject to the powers granted by it. In this sense, limits were established to the interest rates on personal and pledge-backed loans. These interest rates cannot exceed the product between the "benchmark interest rate" (simple average of LEBACs cut-off rates, with a term not exceeding 90 days) and a multiplication factor ranging from 1.25 to 2, depending on the type of loan and the classification of the bank granting it. With this regulatory change, the BCRA widens direct and indirect regulation on lending to natural persons.

Chart 6

Credit Line for Productive Investment

First three tranches accumulated disburses - Share % in total

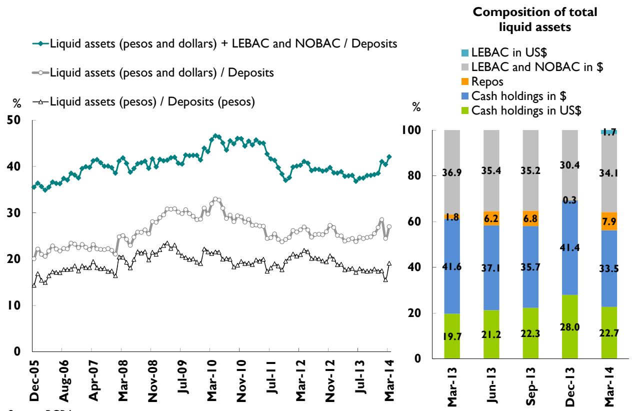


Note: Last available data to April 2014
Source: BCRA

On the other hand, financial institutions and non-financial credit card issuers are required to request BCRA's authorization to apply increases to their charges and commission fees for basic financial products and services. Likewise, the information about Total Financial Cost of all loans to be provided by the entities has been improved and clarified; in addition, requirements of registration and information disclosure were established for legal persons accessing to bank lending and offering loans to individuals, such as mutual, cooperatives and non-financial issuers of credit or charge cards, among others.

Chart 7

Financial System Liquidity



Source: BCRA

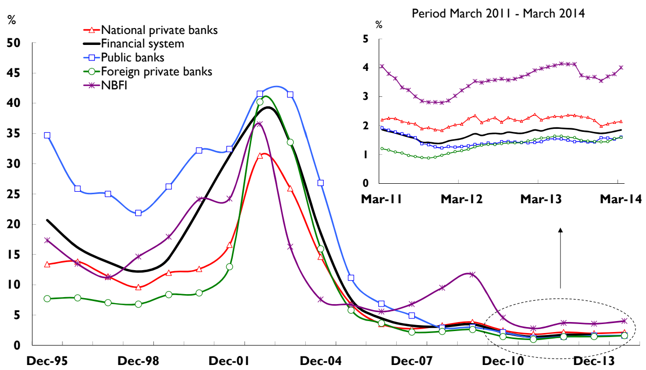
Public and private sectors' deposits grew 28% y.o.y. by the end of the first quarter of 2014, above the change observed one year ago. This evolution was mainly due to private sector's deposits in pesos, which went up 27.8% y.o.y.; in this context, deposits related to saving by the population —time deposits— have exhibited the best relative performance (35.5% y.o.y.).

Since late 2013, within a framework of moderate exposure levels and significant coverage in terms of liquidity and capital positions, the map of risks faced by the financial system has experienced some changes. Regarding credit, due to the decreased momentum in intermediation activities, the banks have slightly reduced private sector's financing weight in their assets. In turn, despite the slight increase of recent months, the delinquency ratio of the portfolio still stands at a historically low level. Likewise, loan loss provisions still exceed the non-performing portfolio. The low aggregate indebtedness levels of companies and households significantly help sustain the payment capacity of these sectors, even though the evolution of income and cost of the new financing will be monitored closely in the next months. In this sense, the collective bargaining agreements and the public transfers have contributed to increase households' resources.

Chart 8

Private Sector Non-performing Financing

Non-performing portfolio / Total financing (%)



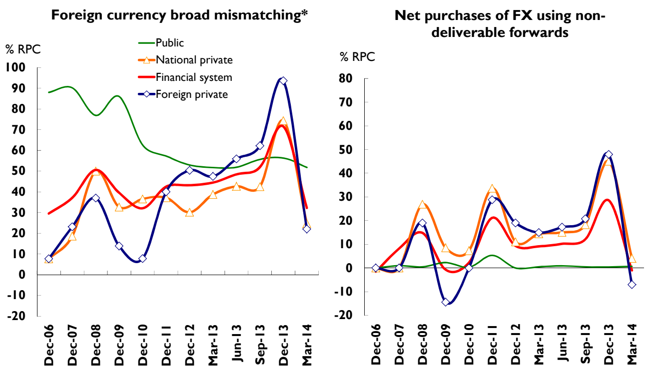
Source: BCRA

With reference to liquidity risk, the financial system has broadened coverage indicators in recent months and there have been some slight changes in exposure ratios. For example, within aggregate funding, the sources of shorter relative term have become marginally more important, even though the concentration of deposits has also lessened. Regarding the domestic regulatory system and on the basis of the commitments undertaken within the framework of the G20, the Central Bank has been working to introduce two liquidity quantitative ratios that financial entities will be required to comply with, in agreement with the international regulatory standards developed by the Basel Committee on Banking Supervision (known as "Basel III"). On the one hand, in line with the schedule already defined at international level, the BCRA has made progress in the plan for the development and implementation of the so-called Liquidity Coverage Ratio (LCR). On the other, the Central Bank continues to participate in the debate around the design of the Net Stable Funding Ratio, which is still at a stage of preliminary analysis, under the framework of multilateral forums (see Box 3).

In terms of its macroprudential role, and taking into account the potential impact that an active currency mismatching accumulated by the group of entities might have on the financial stability and on the macroeconomic variables, the Central Bank has driven some regulatory changes. In early 2014, it reestablished the limits to positive net global position in foreign currency and restricted the banks' positive futures net global position in foreign currency. The new regulations have allowed keeping a limited currency risk for the banking sector and simultaneously lessened volatility in the foreign exchange market.

Chart 9

Foreign Currency Mismatching by Group of Banks

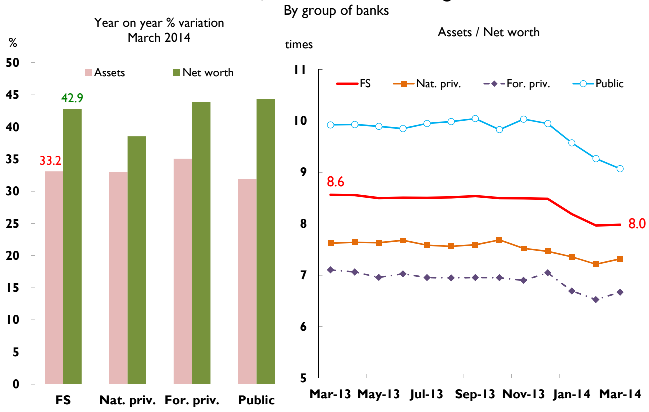


*Note: (Assets - Liabilities + Net purchases of FX using non-deliverable forwards) / RPC
Source: BCRA

From a systemic perspective, the interest rate increase established in late 2013 and early 2014 has had a reduced impact on the financial margins of this sector. This was in line with a reduction in interest rate risk exposure if compared to the situation observed in early 2013, mainly explained by a drop in the duration of assets net of liabilities in domestic currency of the banking book. In line with the current international standard, as from last year, the interest rate risk is no longer part of the minimum capital requirements for financial entities (Pillar I) and started to be framed within the Supervisory Review Process (Pillar II). The Superintendence of Financial and Foreign Exchange Institutions (SEFyC) is in charge of assessing banks' exposure to this risk and may deal with the cases it deems as appropriate through a request for capital increase, a reduction of exposure, or both.

Chart 10

Assets, Net Worth and Leverage
By group of banks



Source: BCRA

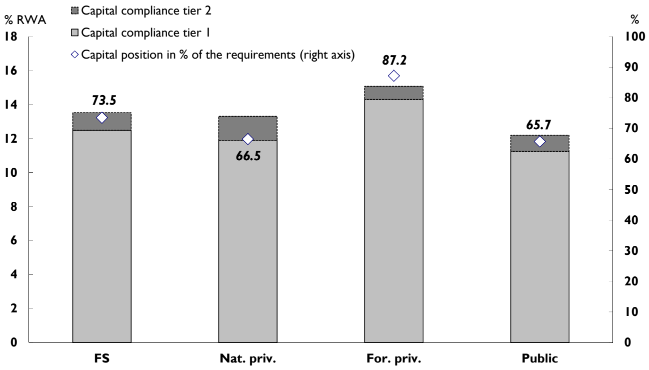
The risk that fluctuations in the prices of financial assets may significantly impact on the financial system balance sheet continued to be moderate, mainly due to a reduced level of exposure to this factor; the main traded instruments accounted for only 3.5% of the financial system netted assets by the end of the first quarter of 2014. In the first months of the current year, a higher volatility of sovereign bonds' prices and the increasing relevance of instruments in foreign currency valued at market prices in the aggregate assets accounted for a slight increase in the net worth exposure of banks to market risk. In the next few months, there will be a new scenario for the evolution of sovereign bond prices as from the decision of the US Supreme Court with respect to the litigation with the Argentine sovereign debt bondholders that did not agree to the 2005 and 2010 debt restructuring processes.

In the framework of the evaluation and monitoring of systemic risk, the Central Bank is paying special attention to the evolution of financial entities with a higher potential impact on the aggregate performance of the system. In this sense, in line with the implementation

Chart 11

Capital Compliance and Excess of the Requirement (Position)

March 2014



Source: BCRA

of recommendations by Basel III, BCRA has recently prepared and released the guidelines required to identify systemically-important local banks and will continue making progress in this matter (see Box 4).

Lastly, it is worth mentioning that the set of exposures to the main risks inherent in this activity finds an important safeguard in the sector's capital position. As a result, solvency indicators remained high and a new reduction of aggregate leverage of the financial system was observed in recent months. In particular, the regulatory capital compliance accounted for 13.3% of total risk-weighted assets in March 2014. Book profits largely accounted for the positive momentum of capital buffers.

For the next few months, the domestic financial system is expected to exhibit a limited risk exposure, with sizable solvency and liquidity levels. This evolution would be strengthened by a higher momentum of lending to companies and households within a context of rebuilding of the domestic economic activity and also by the effect of the active policies adopted by the Central Bank.

I. International Context

Summary

The recovery of the economic activity and of global trade transactions started by mid-2013 would have continued so far in 2014, after a temporary slowdown during the first quarter. This performance was mainly due to developed countries since emerging economies expanded at a relatively stable pace. As a result, the gap between the growth rates of both groups of countries narrowed.

In general, the main advanced nations kept their expansionary monetary policies even though with different perspectives depending on each specific case. Thus, while in the US the Federal Reserve (FED) has gradually limited the stimulus related to the financial assets purchase program, the European Central Bank (ECB) deepened the expansionary bias of its measures in early June in order to boost the economic performance of the region and prevent a deflationary outlook. At the same time, the maintenance of fiscal adjustment policies –though less stringent as from 2014–, the persistence of weak labor markets –especially in some economies– and the long and slow process of the private sector's debt reduction continued limiting the evolution of aggregate demand of this group of countries.

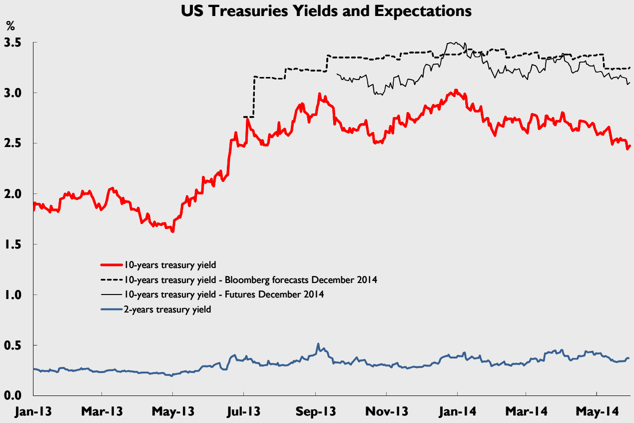
In turn, developing economies continued to exhibit a more heterogeneous performance. Some countries deepened the implementation of additional fiscal and monetary stimuli. On the opposite front, other countries increased the benchmark interest rate within a context of currency depreciation and, in some a cases, increasing inflationary pressures. These countries sought to respond to the rising costs of foreign financing given their dependence on international capital flows.

The weak global economic performance and the US dollar appreciation largely accounted for the year-on-year (y.o.y.) drop of the leading commodity prices at global level, except for energy price which was driven by geopolitical conflicts. In the first tranche of 2014 and at a more specific level, the soundness of demand, the limited stocks and the unfavorable weather conditions led to a rise in the prices of the main grains (soybean, corn and wheat).

Caution prevailed in financial markets, with investors especially focused on the future actions of the FED –and uncertainty about the effective speed of policy reversal and its potential impact on the recovery of advanced economies–, on the geopolitical conflicts and on the growth rate of large emerging economies. More recently, this scenario was also impacted by the doubts over the effects of the ECB's announcements about capital flows and the evolution of the US dollar/euro exchange rate. The higher volatility observed in January and February lessened later on, thus allowing for improvements in the stock market indexes of the main developed economies and some contraction of their long-term sovereign debt yields. The assets of emerging economies have also exhibited a positive trend in recent months, accumulating an expansion in stock market indexes and a reduction of sovereign spreads so far in 2014.

Chart I.1

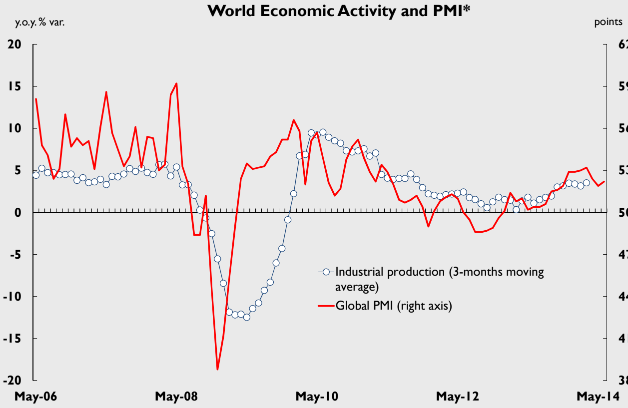
US Treasuries Yields and Expectations



Source: Bloomberg

Chart I.2

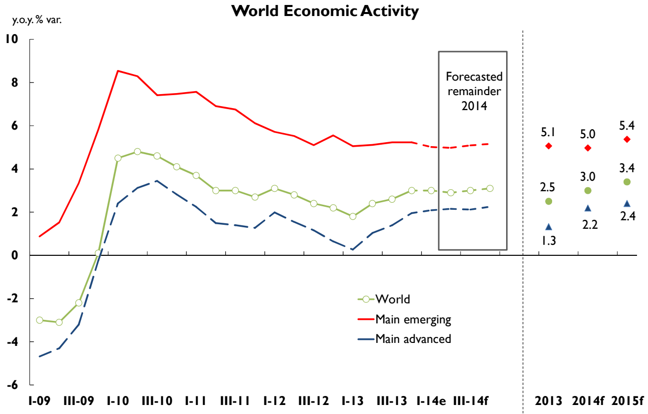
World Economic Activity and PMI*



*Purchasing Managers Index
Source: BCRA based on Bloomberg and Netherlands Bureau for Economic Policy Analysis

Chart I.3

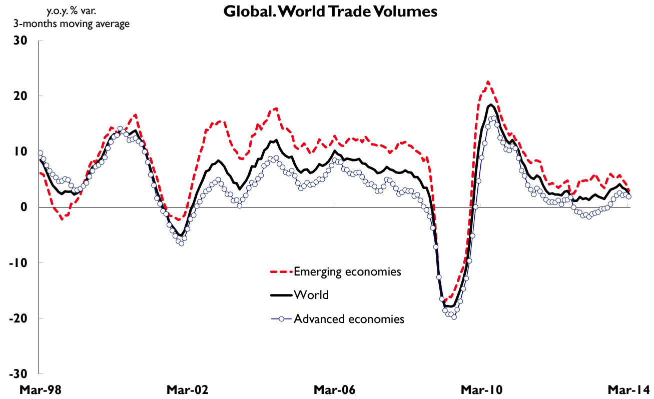
World Economic Activity



Source: BCRA from FocusEconomics and IMF data e: Estimated f: Forecasted

Chart I.4

Global. World Trade Volumes



Source: Netherlands Bureau for Economic Policy Analysis and World Trade Organization

International context

Despite the slow recovery of the still-weak advanced nations, the expansion pace of global activity would have gained momentum after the temporary slowdown of the first quarter of 2014

The global activity recovery started by mid-2013 would have temporarily lost momentum at the beginning of 2014 (see Chart I.2), but the year-on-year (y.o.y.) growth pace has stabilized in recent months. This performance is expected to continue in the following months, thus accumulating a 3% expansion during 2014, standing above the figure recorded in 2013 (2.5%; see Chart I.3).

Trade volumes worldwide followed the performance observed in the global economic activity (see Chart I.4). The partial indicators of the international transactions during the second quarter indicate an improvement in the volumes traded in advanced countries and a stable path in the case of emerging nations.

The economic activity of the developed countries all together recorded a 1.3% hike in 2013 while, after recovering from the loss of momentum seen in the first quarter of the current year, it would close 2014 with a rise of approximately 2.2%.

The reduced activity level in the US during the first quarter of 2014, mainly impacted by the extremely cold weather conditions, the drop in foreign demand and the adverse effect of the stocks cycle, matched the moderate increase of GDP in 2013 (1.9%). Nevertheless, the unemployment rate continued going down, and widespread improvements have been observed in the partial indicators of the economic activity in recent months.

In December 2013 the formal announcement was made of the beginning of the gradual reduction in the assets purchase pace within the non-conventional stimulus program (tapering) as from early 2014. Specialized experts estimate that the US Federal Reserve (FED) will continue reducing gradually the assets purchase pace and that the program will come to an end by the last quarter of this year (see Box 1). On the other hand, investors have started to focus on potential changes in the short-term interest rates and anticipate that the upward cycle would only start in 2015.

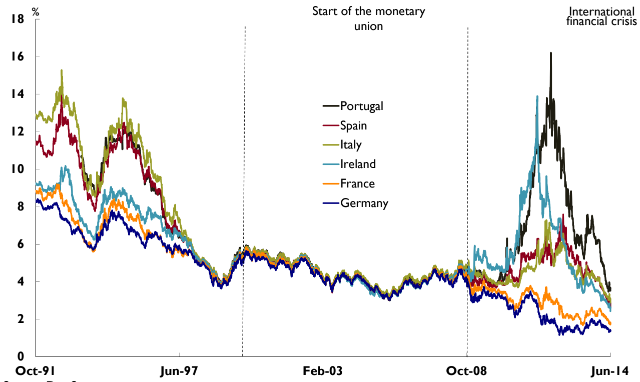
In terms of the fiscal policy, progress was made in the reduction of the financial deficit while temporary agreements were reached at Congress to suspend until

March 2015 the debt ceiling. Likewise, the normal execution of the federal budget was authorized, thus overcoming the partial governmental paralysis recorded last year.

The Euro Zone continued to be immersed in its slow recovery process, even though an expansion of the activity was evident in the last quarters for most of the bloc countries. Nevertheless, some of them have yet failed to reach the pre-crisis GDP level. So, after a 0.4% reduction of GDP in 2013 for the whole region, a rise close to 1% is estimated for the current year. Although the regional improvement has been limited, the most vulnerable countries of the region faced a more favorable international financial context with reduced tensions over the sustainability problems of the monetary union and abundant capital inflows (see Chart I.5). However, within a context of deeply deteriorated labor markets and excessively low inflation rates, ECB's authorities announced in June a series of measures[1].

Chart I.5

Eurozone. Selected Economies. 10-years Bonds Yield

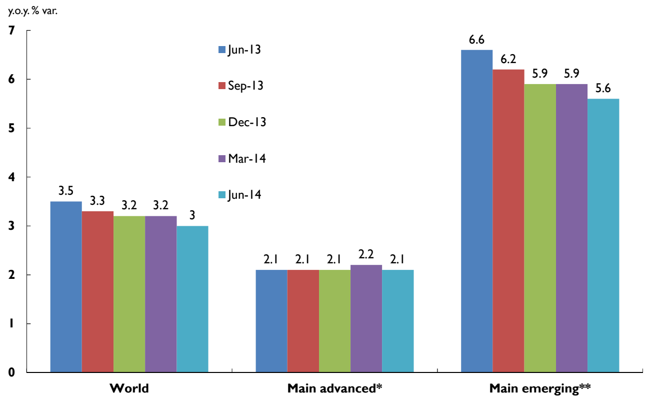


Source: DataStream

On the one hand, the ECB announced cuts to the benchmark interest rate (for the main refinancing operations and marginal lending facility) while the rate related to the deposit facility was negative. On the other hand, the ECB decided to keep the refinancing operations at a fixed cost and full allocation at least until the end of 2016; in addition, the sterilization operations of liquidity injections related to the Securities Markets Program were suspended; in turn, 4-year refinancing operations (TLTRO) at a fixed rate tied to the improvement of bank lending to the non-financial private sector were launched. Finally, the ECB has announced that progress has been made to be ready, if appropriate, to make purchases of instruments related to assets-backed securities (ABS).

Chart I.6

Evolution of 2014 Growth Forecasts



Source: FocusEconomics

*G-7 **Brazil, Russia, India and China

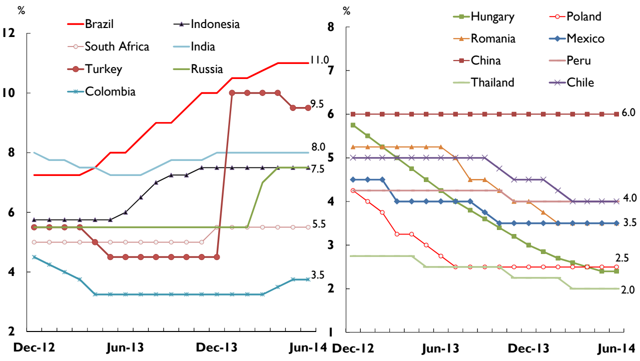
In Japan, the economic activity gained momentum, underpinned by extraordinary stimulus measures that would last for several years. Thus, after a 1.6% rise in the activity level in 2013, a remarkable growth was recorded in the first quarter of 2014 (3% in y.o.y. terms). However, the tax increases decided as from April weakened household spending and affected the activity level as shown by several leading indicators.

The ensemble of the main emerging economies grew approximately 5% in 2013, and a similar expansion is estimated for 2014, after successive downward revisions to the forecasts (see Chart I.6). Within a framework of more stringent external financial conditions since the end of the first half of 2013, there was a greater heterogeneity in the economic performance and the economic policy responses among developing countries. The economies that are more

[1] After reporting in successive monetary policy meetings the possibility of implementing new stimuli.

Chart I.7

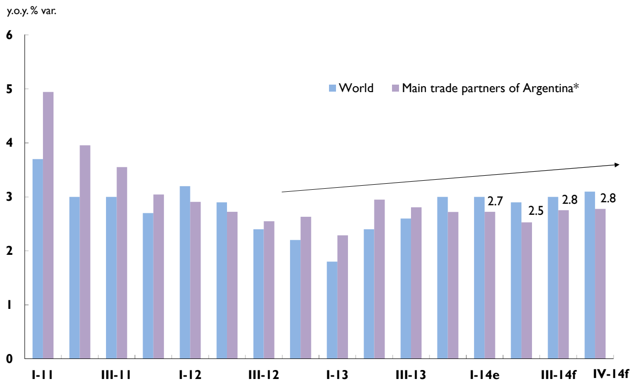
Selected Emerging Economies. Reference Interest Rate



Source: Datastream

Chart I.8

Economic Growth



*Weighted by their share in Argentine exports, which together reach 80% of total.

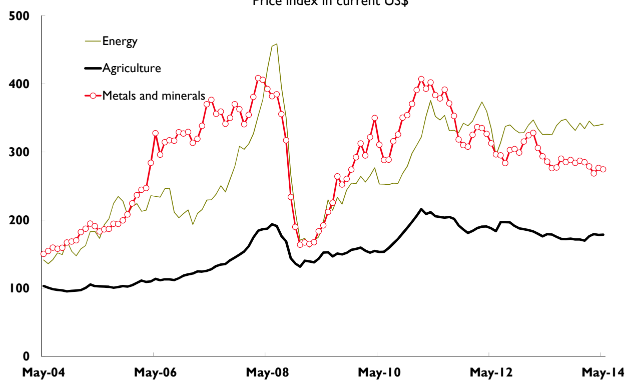
Source: BCRA from FocusEconomics and Central Banks of Brazil

e: Estimated f:

Chart I.9

Commodities Prices

Price index in current US$



Source: World Bank

dependent on external capital flows increased their benchmark interest rates so as to mitigate the pressures on their currencies and on their domestic prices. In the opposite direction, some countries (such as Hungary, Romania and, more recently, Mexico) implemented new cuts to their benchmark interest rates (see Chart I.7).

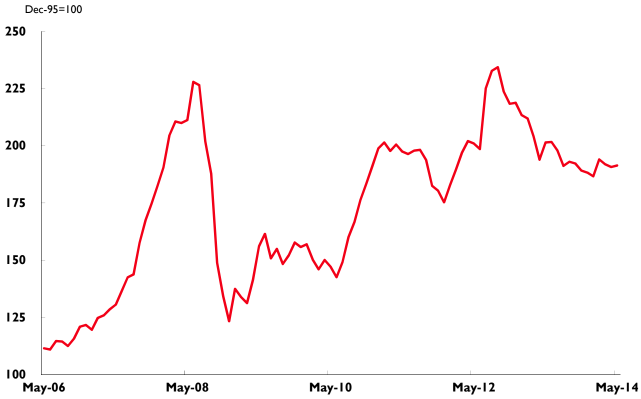
The growth rate of Argentina's main trading partners continued to stand below the global average, especially among emerging partners (see Chart I.8). Brazil continued exhibiting a weak economic performance after a moderate expansion of 2.3% in 2013. Despite this, since the inflation rate stood above the target value for monetary policy, the Central Bank of Brazil ordered successive increases in the SELIC target rate as from May 2013, which is currently standing at 11%.

Meanwhile, the Chinese economy slowed down once again in the first quarter of 2014 (7.4% y.o.y.), after growing 7.7% in 2013. Within this context, the government announced new stimulus measures for different sectors. As a result, some leading indicators of the economic activity, such as the industrial Purchase Management Index (PMI), would signal an incipient improvement of the growth rate during the second quarter of the current year. Nevertheless, the structural reforms devoted to increase the weight of the domestic market forces on the economy and a larger financial liberalization might contribute to reduce the momentum of the activity level in the following quarters. For example, the lower incidence of subsidized financing through public companies and the increase of interest rates, among other factors, would act in the opposite direction relative to the positive effects of the wage recovery within a relatively robust labor market.

Within a context of US dollar appreciation, international commodity prices continued exhibiting a downward performance similar to that of 2013 (see Chart I.9). However, a breakdown analysis shows that the prices of the main grains (soybean, corn and wheat) went up sharply at the beginning of 2014, even though they still stood below the levels observed a year ago. Among other factors, this performance resulted from the sound global demand, the limited stock levels and the downward revision of supply estimates due to adverse weather conditions. Meanwhile, the fragile performance of global economic activity added downward pressures to the prices of industrial commodities, even though energy price remained relative stable in year-on-year terms since the geopolitical conflicts in the Middle East and –more recently– the tensions between Russia and Ukraine and the advanced nations with a higher weight globally have impacted in the opposite direction.

Chart I.10

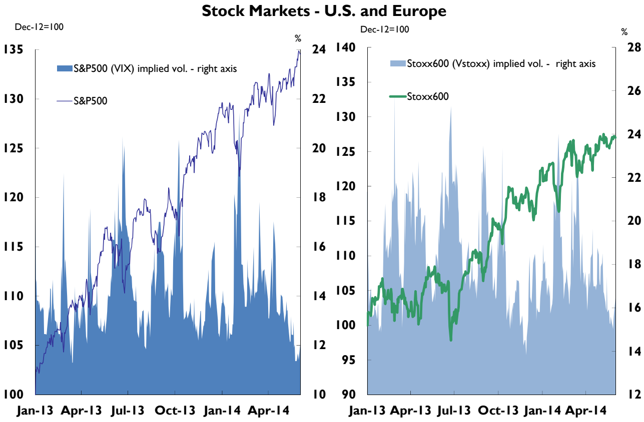
Commodities Price Index



Source: BCRA

Chart I.11

Stock Markets - U.S. and Europe



Source: Bloomberg

Within this context, the Commodity Price Index (IPMP) – that follows the evolution of the international prices of the most relevant commodities for Argentina's exports– continued exhibiting year-on-year drops, as it had occurred in 2013 (-9% y.o.y. in the first five months of 2014; see Chart I.10).

The expectations regarding the stimuli by the Fed, the situation of emerging economies and the geopolitical factors gave rise to a context of heightened caution in early 2014

The first months of 2014 were characterized by a heightened caution in international financial markets after ending 2013 with remarkable price improvements, even though with some episodes of higher volatility. In this sense, the expectations regarding the measures to be adopted by the US Fed continued playing a key role. This, as well as other factors, such as the uncertainties over the economic situation in Europe and over the growth pace of large emerging nations, added up to the fear created by the tensions between Ukraine and Russia, given their potential geopolitical effects at global level.

In Europe, the conditions of financial markets in general and the debt level of vulnerable economies in particular continued improving. While Ireland –which, by end 2013, was the first country of the region to put an end to the foreign aid program– returned to the markets at the beginning of the year, Portugal and Greece also issued medium and long term debt instruments voluntarily in the markets for the first time since the 2010-2011 crisis. As regards the progress towards a banking union scheme in Europe, a comprehensive assessment of the financial system has been launched, including both stress tests and an analysis of the financial entities' assets quality and the risks of the financial system in general. The results of this assessment will be available before the European Central Bank (ECB) takes over its new functions within the framework of the Single Supervisory Mechanism[2] next November. Despite these improvements, there are still risks related to the evolution of macroeconomic fundamentals, especially in recent months about the possibility that there might be a more severe low inflation period than originally anticipated, which led the ECB to announce new measures in June.

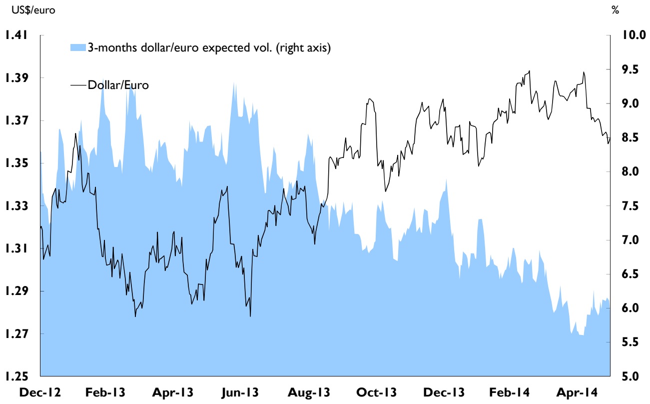
Thus, after closing 2013 with a strong expansion, the main stock market indexes of developed nations have accumulated more limited profits so far in 2014. For

[2] On the other hand, there were improvements on a new agreement on the Single Resolution Mechanism (SRM) for banks in trouble and the Single Resolution Fund (SRF) to give support such mechanism.

example, for both S&P500 (US) and Euro Stoxx 600 (Europe), the accumulated stock so far this year[3] is close to 4% measured in US dollars, even though it deteriorated between late January and early February and recovered later on (see Chart I.11). Thus, 2014 performance is moderate against the profits recorded in 2013 (in a range between 20% and 30%). In terms of expected volatility, relatively high levels were observed in the US during the first two months of 2014. In the case of Europe, additional episodes of high volatility were observed in March, which were partly explained by tensions between Russia and Ukraine. However, in both cases, by the end of May, the expected volatility stood below the figures of 2013, and so far in 2014, the average values have stood at relatively low levels in historical terms.

Chart I.12

Dollar/Euro and Expected Volatility

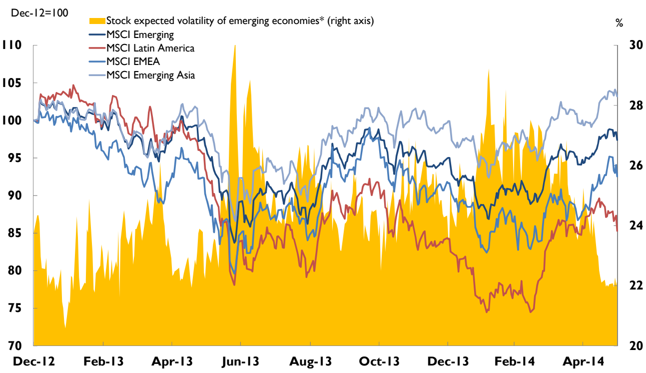


Source: Bloomberg

On the other hand, the long-term sovereign debt yields of the main developed countries tended to reduce during the first months of the year, offsetting in part the marked widening accumulated in 2013. For example, after going up 130 basis points (bp) in 2013, the US 10-year Treasury bond contracted in the current year, going from a level closed to 3% by the end of 2013 to less than 2.5% by late May 2014. Within this context, a contraction of the levels expected by the end of this year was observed, even though a widening of long-term yields[4] is expected for the rest of 2014 (see Chart I.1). In the case of Germany's long-term sovereign debt yields, a drop of nearly 60 bp in the 10-year segment was seen so far in 2014, virtually reversing the rises accumulated throughout 2013.

Chart I.13

Emerging Economies Stock Markets and Expected Volatility



*Average implied volatility of call options of the main stocks that make up the MSCI Emerging.
Source: BCRA based on Bloomberg

The US dollar has tended to appreciate against the other main currencies of developed economies so far in 2014. With expectations over a gradual moderation in the Fed's highly expansionary policy and the potential implementation of new stimulus measures in the Euro Zone (after the announcements made in June), the US dollar accumulated in the first five months of the year an appreciation of 1% against the euro, after depreciating 4% in 2013 (see Chart I.12). Nevertheless, this result did not evidence a sustained trend in the first months of the year. The US dollar/euro exchange rate went up during a good part of the period; it stood around USD/€1.40 in early May (a level unseen since the end of 2011) and then fell sharply during the rest of the month. In turn, the US dollar had a mixed performance against the main currencies. Against the yen, the US dollar has weakened over 3% in 2014, after appreciating over 20% in 2013

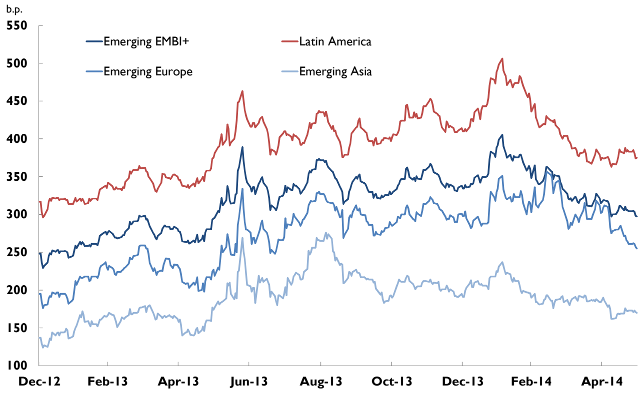
[3] Until late May.
[4] By year end, the expectations for the yields of US 10-year Treasuries stand within a range of 3.1-3.25% according to Bloomberg and Treasuries futures.

(as a result of the expansionary policies of the Bank of Japan).

With reference to emerging economies assets, according to the Morgan Stanley Capital International (MSCI) Index, in aggregate, stocks have expanded 2.5% measured in US dollars so far in 2014. This result came after the drop observed in January and part of February (within a context of increasing volatility) and tended to recover as from the second fortnight of March to late May. This marks a stark contrast with the negative bias seen in 2013, when the MSCI EM recorded a 5% drop (see Chary I.13). In regional terms, the improvements in the stock markets' prices measured in US dollars were more marked in 2014 for emerging Asia (with expansions over 3%) than for EMEA[5] –the group that was hardest hit by the conflicts between Russia and Ukraine –with an expansion of 1% in US dollars.

Chart I.14

Emerging Economies - Sovereign Risk Spreads (EMBI+)



Source: Bloomberg

As regards the sovereign debt risk differentials of emerging nations, they have contracted so far in 2014 despite the reduction observed in the yields of long-term Treasuries. In fact, the EMBI+ overspread contracted more than 35 bp in the first months of this year, after widening 85 bp in 2013 (see Chart I.14). In the case of Latin America, the spread movements of EMBI+ were similar to those of the aggregate of both 2013 and so far in 2014. Within this framework, the amount of gross debt issues traded in international markets by emerging economies' agents –both governments and the private sector– evidenced a 6% y.o.y. drop in aggregate from January to May 2014 (see Chart I.15).

This evolution results from the reduced flow of corporate debt issues, since the transactions by governments were on the rise against the same period of 2013[6]. Finally, in terms of portfolio flows, while in early 2014 the outflow of funds specializing in emerging countries' assets (debt and stocks) still persisted, this performance started to lessen in March and then reversed in April and May, when net inflows were recorded. However, so far in 2014, net outflows have accumulated, both for funds specializing in emerging economies' stocks and for those specializing in debt instruments.

In early 2014, emerging countries' currencies were highly volatile and then stabilized after the first two months of the year. This initial performance was due to several factors, including doubts over China's growth pace, the intensified tensions in Ukraine and the ongoing

[5] Emerging Europe, Middle East and Africa.

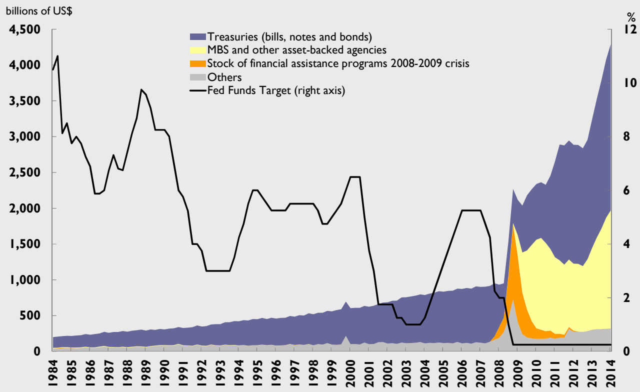
[6] The amount of sovereign debt issues went up 30% between January and May against the same period of 2013, while the corporate sector transactions (whose amount accounted for almost three fourths of the total in January-May) exhibited a 14% y.o.y. drop.

Box 1 / Expectations about the Evolution of the US Monetary Policy

After the US Federal Reserve (Fed) formally announced the beginning of a reduction in the purchase pace of financial instruments by late 2013, the markets started to focus their attention on short-term interest rates. Currently, a cycle of gradual increases in the Fed Funds target interest rate is expected for the second half of 2015. The implementation of this policy, together with the management of the assets portfolio held by the Fed and their impact on the yield of long-term Treasuries, are highly relevant for the evolution of both financial markets in general and the instruments of emerging economies in particular, with potential implications at macroeconomic level

Chart B.1.1

Federal Reserve Assets and Target Fed Funds Rate



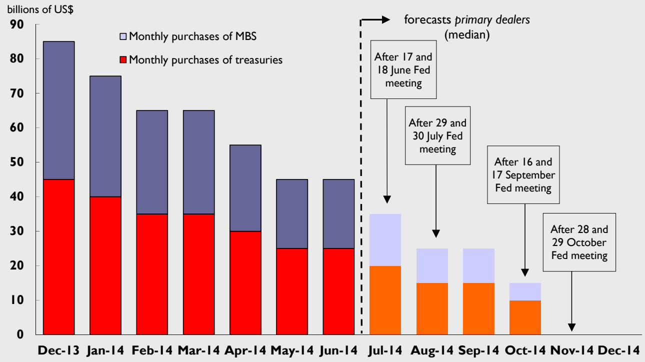
Source: Federal Reserve

As from the peak of the 2008-2009 financial crisis, the US Federal Reserve has implemented a series of stimulus measures, such as maintaining the interest rate at minimum levels and announcing the future evolution of such rates (known as forward guidance). This involved the implementation of unconventional measures such as the purchase of financial instruments to influence market conditions, resulting in a strong growth of Fed's assets and a change in its composition[7] (see Chart B.1.1). The purchase of assets included several rounds of quantitative easing which, in its latest version (announced in September 2012 and extended by end of that year) encompassed long-term Treasuries and mortgage-backed securities (MBS).

Within a context of gradual improvement of the US economic conditions, the possibility of progressively removing the current stimulus measures gained ground since the first half of 2013. Therefore, the expectations about the future measures to be adopted by the Fed became especially relevant in terms of the evolution of the international financial markets, including the assets of emerging economies.

Chart B.1.2

Evolution of Federal Reserve's Monthly Asset Purchases



Source: Federal Reserve and Primary Dealers survey of the Federal Reserve of NY (April 2014 survey, last available)

By late 2013, and after an initial period of uncertainty, the Fed announced the beginning of the asset purchase reduction (tapering) as from January. So far, there have been four cutback rounds in the monthly purchase of assets, from US$ 85 billion by late 2013 down to US$ 45 billion per month since May[8]. Even though the Fed has not committed to follow a specific path for its tapering process, the purchase of assets is expected to continue contracting –provided there are no negative surprises in the evolution of the US economy– after the successive meetings of the FOMC (Federal Open Market Committee) (see Chart B.1.2)[9].

Consequently, the forecasts of the primary dealers collected in the survey made by the New York Federal Reserve, as well as other studies performed among

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[7] Another important course of action in the 2008-2010 period resulted from different programs related to financial entities (banks, money market funds, primary dealers) or to some sectors of the market (commercial paper of companies, securitized assets). This was accompanied by the aid provided to specific financial entities (banks, AIG, etc.) during the peak of the financial crisis. More recently, in 2011 and 2012, short-term Treasuries were sold to purchase long-term Treasuries (dubbed "Operation Twist").

[8] While up to last December, long-term Treasuries for US$ 45 billion and MBS for US$ 40 billion were purchased, as from May, these figures have gone down to US$ 25 billion in Treasuries and US$ 20 billion in MBS.

[9] In the remaining months of 2014, monetary policy meetings will be held in June, July, September, October and December.

market participants[10], anticipate that the current purchase program would come to an end in the last months of the year. Later on, the Fed would continue influencing the conditions of the financial markets (long-term Treasuries yields, mortgage market conditions, etc.) based on how it manages the significant –and still growing– portfolio asset holdings and their related flows.

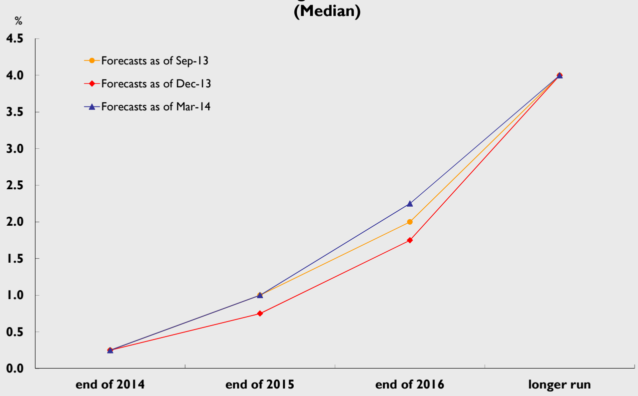
With the tapering process already in progress, investors started to follow closely the future cycle of increases in short-term interest rates. This occurs in a context of debate around how an effective increase in the interest rates will be implemented –in operating terms– considering the remarkable rise in the size of the Fed's balance sheet and the excess of liquidity in the financial system[11].

In this sense, the monetary policy meeting held in March has been especially relevant since it introduced several measures. For example, the application of the forward guidance scheme has acquired a more qualitative bias. The guidance, which used to include explicit mentions of unemployment levels (over 6.5%) and 1-to-2-year inflation expectations (not exceeding 50 basis points [bp] above the long-term target of 2%), now encompasses a pattern of decisions including the follow-up of a wide set of indicators without undertaking specific targets: labor market data, inflationary pressure and expectations on inflation and on financial markets evolution.

In turn, at the monetary policy meeting held in March, forecasts of the FOMC's members were presented. These data revealed that, even though most of its members continued estimating that the increases of the Fed Funds target interest rate would start in 2015 (as already anticipated by previous forecasts), in general the expectations tended to estimate higher targets for short-term rates by the end of 2015 and 2016 than originally expected (see Chart B.1.3). Added to this, there were comments by Janet Yellen, in her first meeting as Fed Chair, about the timing to begin with the cycle of interest rate rises, which were interpreted as a signal that the process would start earlier than expected in 2015[12]. Nevertheless, the initial effect of these surprises has moderated more recently, at the same time that the Fed continued to emphasize that, under the current conditions, the monetary stimuli are still required, the cycle to normalize the monetary conditions will be gradual, once it has started, and short-term interest rates will be kept for a while at levels below those deemed as normal in the long-term.

Chart B.1.3

Fed Funds Target - FOMC Forecasts (Median)



Source: Federal Reserve.

Both the surveys among the financial sector's agents and the futures markets anticipate that short-term interest rates are expected to go up during the second half of 2015. Then, for example, surveys made by Bloomberg reveal that, by September 2015, the Fed Funds target interest rate is expected to stand 0.50%, against its current range of 0-0.25% (see Chart B.1.4). In turn, according to the forecasts collected, primary dealers[13], on average, believe that the first increase of the rates will occur in the third quarter of 2015, closing the year at around 0.75%[14]. In turn, in the futures market, Fed Funds contracts maturing by late 2015 are being traded at a level above 0.5% (while until early May, they were traded at 0.75%). It is worth highlighting that all these measurements are below the median of 1% of the FOMC participants by the end of 2015.

As regards medium term forecasts, primary dealers anticipate that the Fed Funds target will stand at 2% by the end of 2016, above 3% by late 2017 and at 3.75% by mid-2018. This implies a progressive movement towards the 4% target expected by FOMC members for the long-term (a level close to the average observed in the last 30 years[15]).

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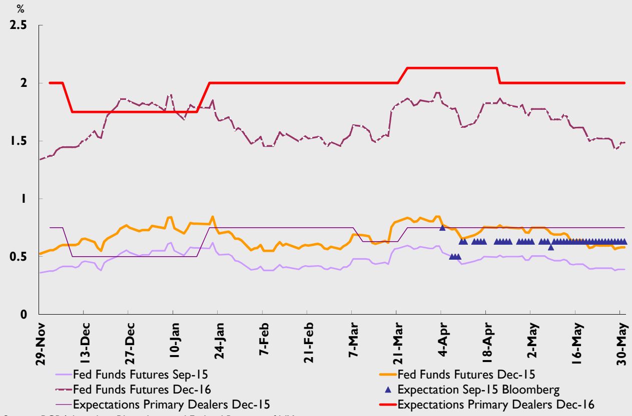
[10] For instance, the surveys made by specialized information platforms such as Bloomberg or Reuters.
[11] For instance, within an advance planning, the NY Fed is performing an exercise related to the overnight reverse repos line at a fixed rate with a wide range of counterparties. This exercise aims at improving the capacity to act on short-term rates within a context of a marked increase in the Fed's balance sheet.
[12] Yellen stated that short-term interest rates might start to go up six months after the end of the current asset purchase program.
[13] Based on April 2014 survey, with expectations as per year half.
[14] For the same period, in the previous survey (March), over half of the contributors expected the yields of the 10-year Treasuries to be within a range of 3.5-4.5%.
[15] In the same period, the average yield of the 10-year Treasuries exceeded 5.5% (above the 4.5% of the 10 years before the peak of the 2008-2009 international financial crisis). In turn, the forecasts of the US Congressional Budget Office (CBO) assume that, in the 2014-2024 period, the yields of the 10-year Treasuries will go up from a

Chart B.1.4

Expectation of *Fed Funds* Target and Rates Futures



Source: BCRA based on Bloomberg and Federal Reserve of NY

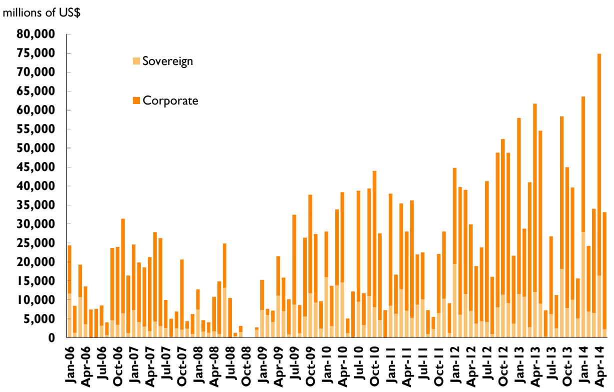
As evidenced by the episodes of turbulence observed in 2013[16], whenever expectations are adjusted (for instance, with sudden revisions to the tapering pace or to the expected increase of short-term interest rates), the changes involved in portfolio allocations at global level would affect the financial markets in general. Likewise, the way in which the long-term Treasuries yields accompany the path towards a scenario of higher short-term interest rates becomes especially relevant. In this sense, the behavior of the yield curve slope depends in part on the measures adopted by the Fed for its long-term Treasuries portfolio. The effect on the US yield curve is particularly relevant for emerging nations because of the implications on its assets –after the remarkable jump of this type of assets in recent years–, on capital flows and on the macroeconomic conditions of emerging countries.

level close to 3% in 2014 to 5% in 2018, with rises between 50 and 60 bp per year between 2014 and 2017.

[16] See Box "Emerging Economies' Assets and Volatility in International Markets", Financial Stability Report, second half of 2013.

Chart I.15

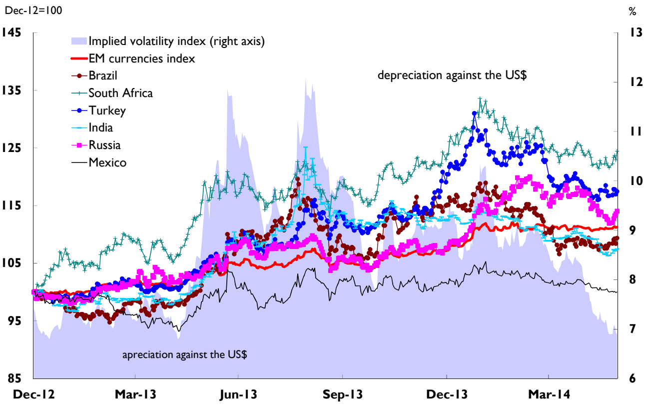
Emerging Economies. International Markets Debt Issuance



Source: BCRA based on Bloomberg

Chart I.16

EM Exchange Rates and Volatility



Source: BCRA from Bloomberg data

outflows of funds specializing in emerging nations' stocks and debt instruments. Vis-à-vis a more volatile context, several countries had to resort to specific measures to face the situation, including increases in their benchmark interest rates (for instance, Turkey and South Africa) and interventions in the foreign exchange markets. Consequently, emerging economies' currencies have accumulated, on average, a depreciation of nearly 4% against the US dollar so far in 2014, after weakening more than 7% in 2013 (see Chart I.16).

At regional level, in 2014, Latin American currencies depreciated 7% on average against the US dollar. However, this performance was not the same for the entire region. For example, the Brazilian real appreciated 5% against the US dollar in the first months of 2014, reversing in part the 15% depreciation recorded in 2013. The appreciation of the Brazilian real occurred within a context of improvements in the balance of payments and continuous increases of the SELIC target rate by the Central Bank of Brazil up to the meeting held in April[17]. At the same time, the monetary authority continued intervening in the foreign exchange market systematically, even though reducing its positions on the margin. In turn, EMEA currencies, adversely affected by the tensions between Russia and Ukraine[18], have accumulated a depreciation of over 6% against the US dollar so far in 2014. Finally, Emerging Asia currencies have appreciated against the US dollar, even though it is worth stating that the Chinese currency depreciated against the dollar.

Even though the heightened caution observed in international markets at the beginning of 2014 has faded away in relative terms in recent months, several factors are still followed up closely. Especially relevant will be the evolution of the US economy and the response by the Fed in terms of the gradual removal of the stimulus measures implemented in recent years, which were of an extraordinary nature. In turn, in Europe, the economic situation and, in particular, the effect of the monetary stimulus announced in June by the ECB (with potential measures that might be added in the future) will continue to be especially followed up. In this case, another factor to be monitored is the result of the comprehensive evaluation of the financial systems and the ongoing progress towards a banking union. Lastly,

[17] In the meeting held in May, the SELIC target remained unchanged at 11%.

[18] The Russian ruble depreciated almost 6% against the US dollar while the Ukrainian currency accumulates a depreciation of over 40% so far this year. In the case of Russia, outflows of capitals intensified (while funds of the Russian financial system would have returned from Europe to Russia more recently). In turn, the Central Bank increased the interest rate and intervened in the foreign exchange market to stabilize the value of the ruble.

changes in the stimulus policies of developed countries might have an impact on the evolution of developing economies and their assets and financial markets, with potential policy responses by these nations. Additionally, the risk associated to geopolitical matters –intensification of the conflict between Russia and Ukraine and the situation in Iraq– cannot be disregarded, as a result of which there might be new episodes of volatility in 2014.

II. Local Context

Summary

Following the performance observed since mid-2013, the economic activity weakened so far in 2014. This evolution mirrored the ongoing decrease of external demand —mainly from Brazil— and a reduced boost from domestic spending (consumption and investment). The production of goods was adversely impacted by a weakened activity in manufacturing and the construction business, which was offset in part by the increase observed in agricultural production. In turn, services were on the rise, even though they decelerated on the margin. In the first part of 2014, the main indicators of the labor market showed signs of a relative stability. The unemployment rate stood at 7.1% of the labor force (PEA) from January to March 2014, down 0.8 p.p. against the level recorded one year ago.

The exports of goods fell in the first months of 2014 due to the weak performance of Argentina's main trading partners. In turn, imports also lost ground in the same period, even though to a lesser extent. The trade result also experienced a year-on-year decline, even though it continued to be positive and was the main support of the current account.

Since early 2014, the monthly increase pace of retail prices has slowed down markedly, as a consequence of the monetary and exchange policy, and the price agreement policies, among other factors, within a context of a reduced economic activity.

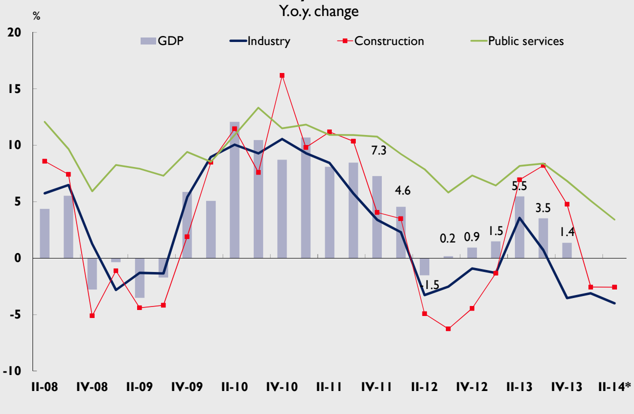
At the beginning of 2014, and within a less favorable international context, the exchange rate depreciated and helped improve the external competitiveness. In addition, a decision was made to increase the interest rates in the auctions of the Central Bank's bills (LEBACs), thus boosting saving in domestic currency, given the higher return of deposits in pesos. At the same time, there was an increase in liquidity absorption through such instruments, even though their stock relative to deposits stood below the historical levels. The BCRA has also reintroduced limits to the banks' net global position in foreign currency, so that they increase the supply of foreign currency and contribute to lessen pressures on the foreign exchange market. As a result of these measures, which were in line with BCRA's objective of monetary and financial stability, the year-on-year expansion of monetary aggregates tended to moderate.

Consumption is likely to recover as soon as the wage increases resulting from the collective bargaining agreements become effective, provided the labor market conditions remain stable. In turn, the income improvement of sectors related to farming activity, together with the policies devoted to support the income of the most vulnerable sectors, including the recent increases in pension and retirement benefits and family allowances, would also contribute to consumption recovery.

Prices of financial assets kept a positive bias in the domestic markets in the first months of 2014, despite the increasing volatility observed in January and February. This was due to both international and local factors (the agreements with Repsol and the Paris Club, among others). Sovereign bonds exhibited a mixed performance. In mid-June, the US Supreme Court rejected the petition for a writ of certiorari filed by the Republic of Argentina in the litigation with the debt bondholders that did not agree to the debt restructurings already offered by the country, which would lead to a new scenario for the evolution of prices of domestic financial assets in the short term.

Chart II.1

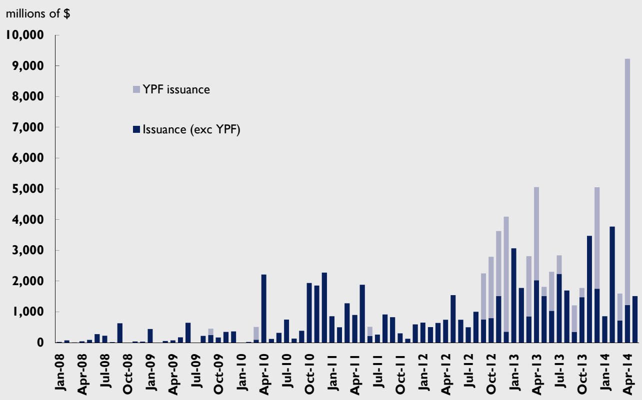
Activity Indicators
Y.o.y. change



Source: INDEC

Chart II.2

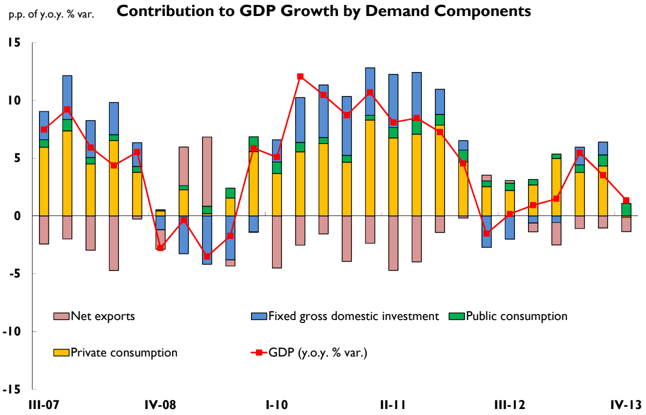
Private Sector Financing - Corporate Bonds



Source: BCRA based on IAMC, CNV and BCBA

Chart II.3

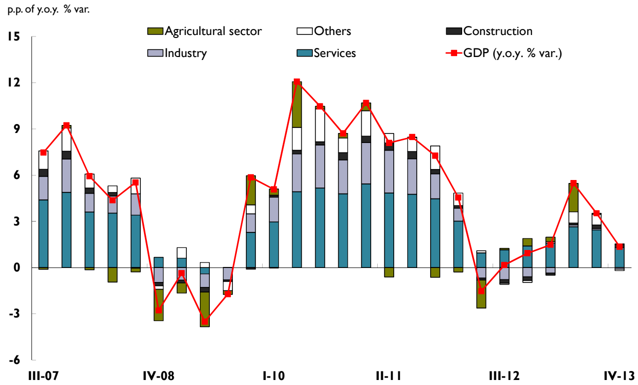
Contribution to GDP Growth by Demand Components



Source: INDEC

Chart II.4

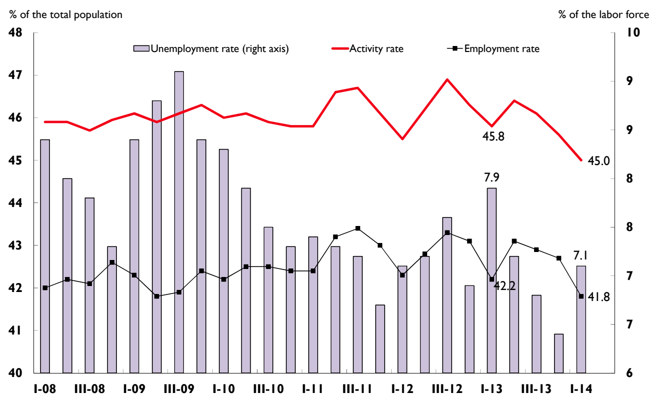
Contribution to GDP Growth by Economic Sector



Source: INDEC

Chart II.5

Key Labour Market Indicators



Source: INDEC

II.1 Macroeconomic context

So far in 2014, the economic activity has continued the deceleration process started in mid-2013

GDP expanded 3% in 2013, thus exceeding the 0.9%[19] growth recorded in 2012. However, during the second half of 2013, the growth pace of goods and services production slowed down against the figures recorded in the first half of that year. This weakened expansion was mainly related to the performance of private consumption, added to the negative contribution by net exports (see Chart II.3). In turn, investment recovered some momentum, even though it still stands below the levels of 2011. Thus, capital expenses increased 3% throughout 2013, and their ratio relative to GDP stood at 20.9%. On the supply side, the slowdown of the economic expansion pace between June and December 2013 was mainly due to a lower contribution to growth by the farming and services sectors and to the absence of contribution by manufacturing. On the other hand, the construction business reversed the trend observed in the first half of the year and grew around 5% year-on-year (y.o.y.) on average (see Chart II.4).

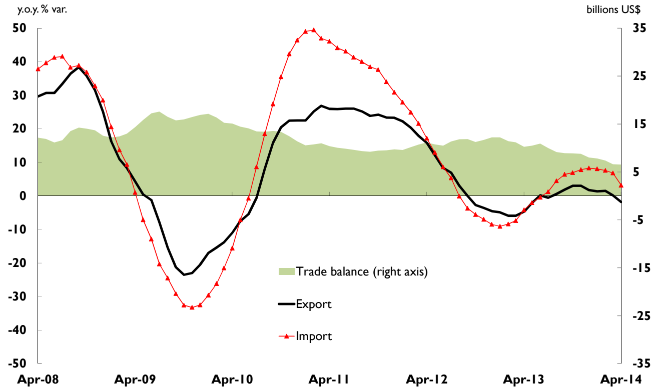
So far in 2014, the economic activity deepened the trend observed since mid-2013, adversely impacted by the ongoing decline of external demand and the weakening of domestic spending, in terms of both consumption and investment. At sectoral level, the production of goods contracted as a result of the weak performance of manufacturing and the construction business (see Chart II.1). According to the Monthly Industrial Indicator (EMI), manufacturing went down 3.4% y.o.y. from January to April 2014 while, according to the Summarized Construction Activity Indicator (ISAC), this sector fell 2.6% y.o.y. in the same period. On the other hand, services were on the rise and increased at a 4.6% y.o.y. rate in the first four months of the current year, mainly driven by trade, transportation and communications. In addition, agricultural activity would have gone up as well, given the estimated rise close to 3.5% in the 2013/14 cycle harvest —mainly due to a higher production of soybean and wheat.

The main indicators of the labor market remained relatively sound during the first quarter of 2014. According to the Permanent Household Survey (EPH), for the 31 agglomerations under study, unemployment stood at 7.1% of the labor force (PEA) from January to March, down 0.8 percentage points (p.p.) against the first

[19] Recently, INDEC released the preliminary data of National Accounts with an updating of the year used as calculation base, as a result of which 1993 was replaced by 2004.

Chart II.6

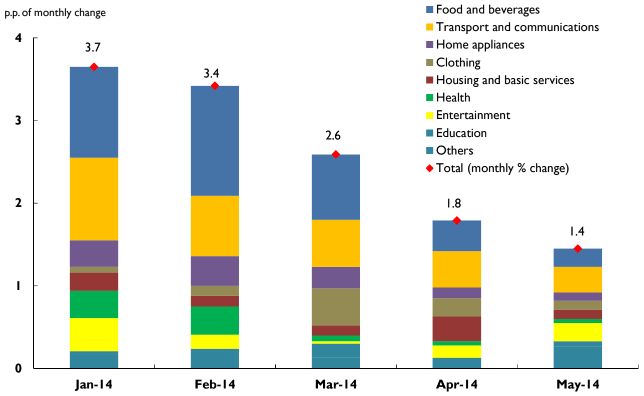
Export, Import and Trade Balance
(12-months moving average)



Source: INDEC

Chart II.7

National Urban Consumer Price Index (IPCNu)



Source: INDEC

quarter of 2013. In turn, the labor force accounted for 45% of the population, while the employment rate stood at 41.8%, going down in both cases if compared to the figures recorded one year ago, but still standing at high levels (see Chart II.5).

Regarding foreign trade, exports have accumulated a 10.3% y.o.y. drop in the first four months of 2014, mainly due to a reduction in volumes shipped. The contraction of industrial manufactures mirrored the decline in transportation material shipments —mainly to Brazil— and the drop in the price of commodity exports, as a consequence of the reduced sales of wheat and corn. This performance was offset in part by the increase in the sales of agriculture and livestock manufactures —driven by the soybean sector— and of fuels.

On the other hand, imports fell close to 5% y.o.y. from January to April, due to a reduction in the volumes purchased. All import uses fell in year-on-year terms, except for fuels and lubricants, and capital goods. Imports and exports all together resulted in a trade surplus of US$1.05 billion in the aggregate up to April, down US$1.45 billion against the figure recorded in the same period of 2013 (see Chart II.6).

According to the new National Urban Consumer Price Index (IPCNu [Urban CPI])[20], the monthly hike of retail prices decelerated so far in 2014[21]. Thus, according to this indicator, from January to May 2014, the consumption basket cost went up 13.5%. This rise was mainly due to the price evolution of food products and beverages, as well as of transportation and communications (see Chart II.7).

It is worth mentioning that, as of this date, most collective bargaining agreements have closed their wage adjustment negotiations corresponding to the current year. In general terms, wage increases stood at around 30%, thus exceeding the adjustments applied in 2012 and 2013. In this sense, it is estimated that the remunerations for the economy, which grew 33% y.o.y. last April, will experience a higher growth pace in the short term (see Chart II.8).

As a result, an improvement in domestic spending may be expected for the next few months based on the rebound in household consumption, driven by the enforcement of the wage increases agreed upon and the

[20] As from February, INDEC has released a new retail price index, called IPCNu (Urban CPI), which has national coverage and considers a new consumption basket updated according to the result of the latest National Survey of Family Spending of 2012/13. For further details about the methodology of the indicator, see Box "National Urban Consumer Price Index (IPCNu [Urban CPI])" in the Macroeconomic and Monetary Policy Report of February 2014.

[21] It must be considered that the government has implemented the "Precios Cuidados" Plan at national level, which consists in flexible price administration, on the basis of which reference prices are established for a set of goods.

maintenance of income transfer policies to the most vulnerable sectors, as well as the improvement in the income of farming-related sectors. This evolution will play a key role to sustain labor market conditions.

II.2 Monetary context

The Central Bank has implemented a set of measures intended to balance the foreign exchange market and promote saving in domestic currency

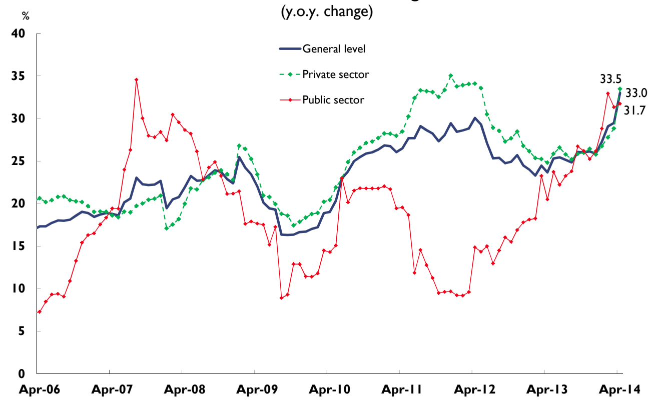
In January 2014, within a context where many emerging countries faced pressures on their domestic currencies, the exchange rate depreciated and allowed for improving the external competitiveness (see Chart II.9). In addition, natural persons residing in the country were allowed to access the formation of freely-available external assets, subject to some specific parameters[22].

In line with its policy to favor saving in domestic currency, and according to its mandate of preserving monetary and financial stability, the Central Bank decided to increase LEBACs interest rates at predetermined rates. As a result, LEBACs with shorter terms stood at levels of 28.7% and 28.9%, from late February to March, and the interest rate on the instrument with longer terms stood at 30.3%[23]. Likewise, after several months, instruments at variable rate were issued, resulting in a positive spread on Private Bank BADLAR, which stood at 1.3 p.p. in February and at 0.8 p.p. so far in May. As from April, the Central Bank decided to adjust LEBACs interest rates within a context where the variables of monetary and exchange markets tended to stabilize, accumulating a 2 p.p. decline by the end of May.

Likewise, in order to promote that private sector savings in dollars be kept at banks, in January the Central Bank started to auction LEBACs denominated in US dollars. The new instruments can be purchased by financial entities based on the time deposits in dollars of the private sector held by institutions as from January 27, 2014. These deposits have higher interest rates than those prevailing in the market since, in order to underwrite these LEBACs in dollars, the Central Bank has established a maximum spread relative to that of time deposits. This measure has supplemented another adopted in December 2013, when the Central Bank started to auction LEBACs in pesos payable at the

Chart II.8

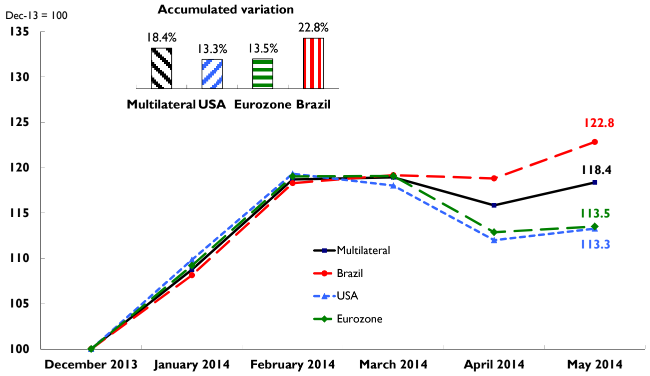
Evolution of Nominal Wages
(y.o.y. change)



Source: INDEC

Chart II.9

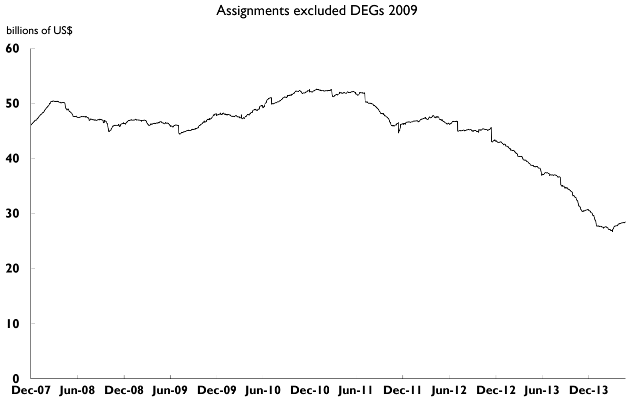
Multilateral and Selected Partners Real Exchange Rate Evolution



Source: BCRA and Bloomberg

Chart II.10

BCRA International Reserves
Assignments excluded DEGs 2009

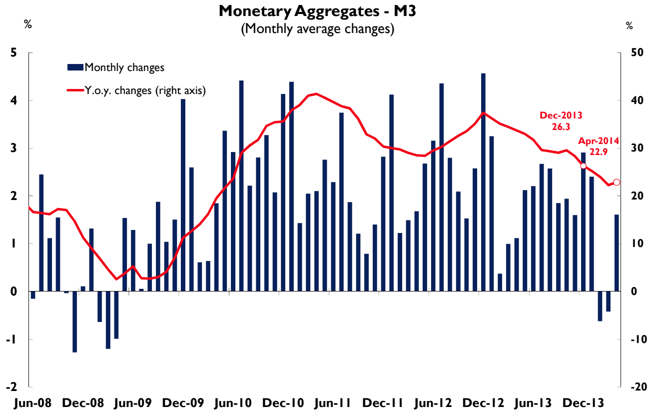


Source: BCRA

[22] Communication "A" 5526. On a supplementary basis, AFIP determined that any persons making these purchases must make a 20% early payment of the income tax and the tax on personal assets if they decide to withdraw the currencies in cash, while the tax is 0% if the currencies are deposited in an account for at least one year.
[23] In recent months, LEBACs with longer terms were issued, and in some instruments the terms exceeded one year.

Chart II.11

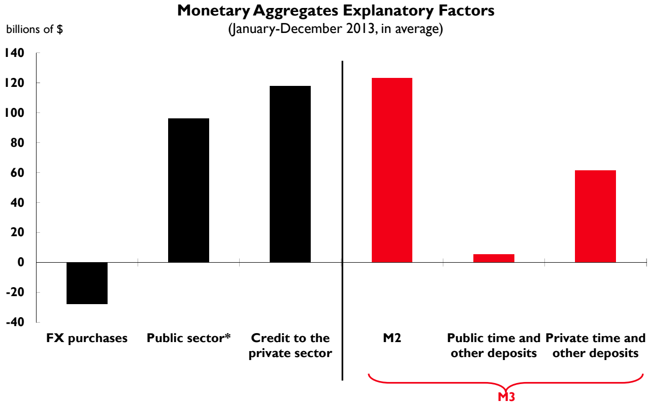
Monetary Aggregates - M3
(Monthly average changes)



Note: M3 includes cash held by public and the total amount of deposits in pesos. Source: BCRA

Chart II.12

Monetary Aggregates Explanatory Factors
(January-December 2013, in average)



*Includes public sector operations with effect on the monetary base and public sector loans.
Source: BCRA

benchmark exchange rate between the Argentine peso and the US dollar so as to regularize export settlement and increase the net supply of foreign currencies. These bills may be underwritten only by exporters of the grain and oil sectors.

In turn, these measures were accompanied by macroprudential measures. In this sense, in early February 2014, the net global position in foreign currency was limited to the lower of 30% of the banks' own liquid resources or the Adjusted Stockholders' Equity (RPC)[24]. As a result, the financial institutions had to reduce the stocks of their accounts in dollars with the BCRA and increase their supply of foreign currency, thereby lessening the pressure on the foreign exchange market.

As a result of all the measures adopted, the level of international reserves stabilized by the end of January around US$28 billion and the Central Bank was once again a net purchaser of currency in the foreign exchange market (see Chart II.10). By the end of May, within a context of higher foreign currency settlement by exporters, international reserves totaled US$28.54 billion. Thus, net purchases in the first five months of 2014 reached US$3.74 billion, against US$731 million recorded in the same period of 2013.

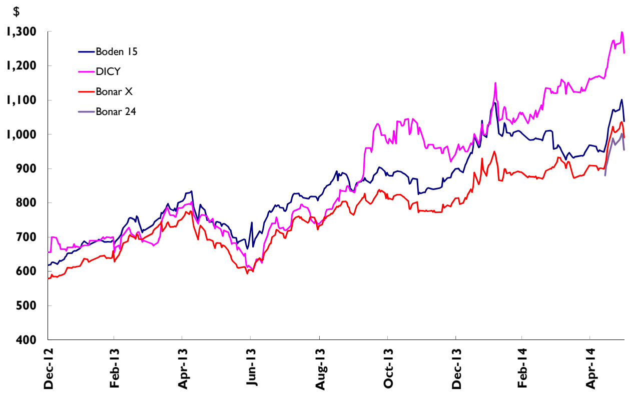
In this context, the expansion pace of monetary aggregates in pesos slowed down as from the sterilization policy established by the Central Bank. The expansion pace of the broadest monetary aggregate in pesos, M3[25], which recorded a 26.3% y.o.y. growth in December 2013, continued to moderate, reaching in April a 22.9% y.o.y. change (see Chart II.11).

Throughout 2013, within the framework of the policies implemented by BCRA, loans to the private sector continued to be the main growth engine of monetary aggregates (see Chart II.12). In this sense, policies devoted to stimulating credit for productive purposes, through the Bicentennial Productive Financing Program (PFPB) and the Credit Line for Productive Investment (LCIP), allowed for sustaining a high expansion pace of loans in pesos to the private sector, in particular those of longer terms and intended for micro, small and medium-sized enterprises (MiPyMEs). Due to its positive impact, the Central Bank established a new quota for LCIP, especially devoted to providing financing to MiPyMEs. In this fourth implementation stage, which will cover the first half of 2014, the financial institutions subject to the regulation must provide loans to the private sector for at

[24] See Communication "A" 5536.
[25] It includes cash held by the public, settlement checks in pesos and deposits in pesos.

Chart II.13

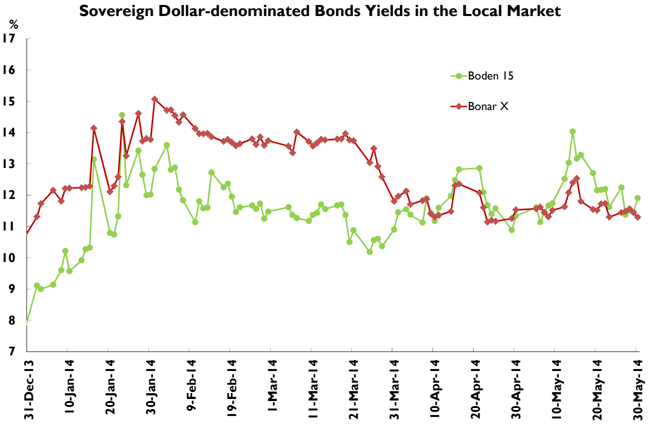
Most Liquid Sovereign Dollar-denominated Bond Prices



Source: BCBA and MAE. Prices in pesos (more liquidity operations).

Chart II.14

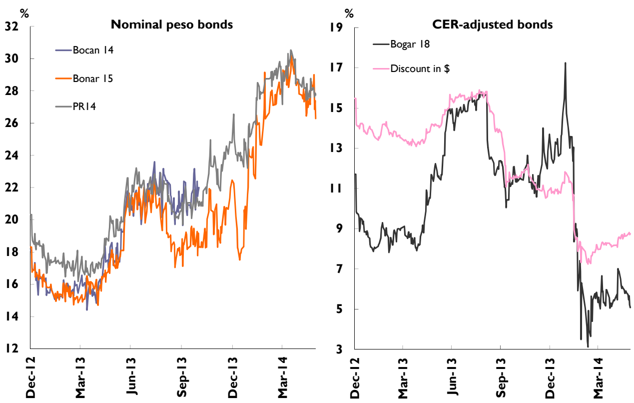
Sovereign Dollar-denominated Bonds Yields in the Local Market



Source: BCRA based on BCBA data

Chart II.15

Peso-denominated Bonds Yields



Source: BCBA and MAE

least 5% of their deposits in pesos as of November 2013. Likewise, in order to maintain a sound financing flow for working capital and preserve the payment chain of commercial lines, the Central Bank ordered that, in March, up to 10% of the quota for the first half of 2014 could be applied to the discount of deferred payment checks of MiPyMEs, and up to an additional 10% during April, May and June 2014, (totaling 40% of the quota).

II.3 Capital markets

Argentine financial assets exhibited a rather favorable performance (with some exceptions) from January to May 2014, even though subject to a higher volatility at the beginning of the year. This evolution was related to international context and also to idiosyncratic factors. The latter include the litigation with the sovereign debt bondholders which did not agree to the successive debt restructurings of 2005 and 2010. In this sense, by mid-June, the US Supreme Court rejected the appeal filed by Argentina to the ruling by Judge Griesa, thus opening a new scenario for the evolution of Argentine financial assets.

Sovereign bonds exhibited a mixed performance at domestic level, with improvements in the most liquid dollar-denominated instruments

After the widespread rises recorded by the end of last year, the prices in domestic currency of sovereign dollar-denominated bonds (the transactions with the highest liquidity in the Argentine market) continued to be on the rise in the first months of 2014. This evolution is largely due to the increases recorded in early 2014, in line with the performance of the $/US$ exchange rate; later on, the evolution was mixed until May, when a new and clear upward bias in prices became evident (see Chart II.13). For example, for the two most liquid instruments, Boden 15 and Bonar X, an expansion between 15%-22% was observed between January and May in their prices expressed in pesos. In terms of their yields in dollars, taking into account domestically-traded transactions in foreign currency[26], these same instruments accumulate an increase between 60 and 420 bp so far this year (see Chart II.14).

Regarding sovereign peso-denominated bonds, so far in 2014, some of them lost the price increases they recorded in 2013. Among the CER-adjusted instruments in pesos, the positive bias in prices has deepened, within the framework of the launching of the IPCNu

[26] Based on data provided by the Buenos Aires Stock Exchange (BCBA). These transactions in foreign currency have a lower liquidity than transactions in pesos.

index (Urban CPI) at the beginning of the year. However, the nominal peso-denominated instruments, among which those with a coupon following the Private Bank BADLAR have stood out, exhibited declines in their prices within a context of increases in their benchmark interest rates. Thus, while the yields of CER-adjusted bonds with higher liquidity have lost over 500 bp on average so far in 2014, the yields of nominal peso-denominated instruments widened more than 300 bp until late May (see Chart II.15).

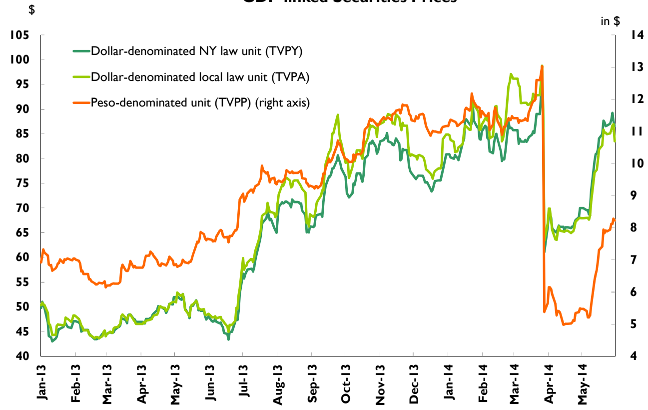
In turn, the prices of GDP-linked units have exhibited a volatile performance in recent months. After showing a remarkable upward trend in the second half of last year and the first two months of the current year, prices went down sharply in March, once 2013 GDP growth data were released[27] (see Chart II.16). Later on, these prices rebounded partially until late May.

After a downward revision in 2013, Argentina's debt sovereign risk spreads have shown a fluctuating performance in recent months, with an initial widening, some cuts in February and April and a renewed upward trend in the second fortnight of May. Thus, the Argentina EMBI+ spread, calculated on the basis of prices in foreign markets where bonds subject to international legislation are traded, went up 25 bp from late 2013 to late May 2014 (see Chart II.17). In the same period, Latin America EMBI+ spread shrank 35 bp. This performance is mainly due to factors such as the evolution of the litigation with the holdouts for the Argentine sovereign debt who did not agree to the restructuring processes offered by Argentina, the agreement reached with Repsol regarding the compensation for YPF[28] expropriation, and with the Paris Club regarding the scheme to definitely cancel our liabilities with such institution.

In the first months of 2014, the stock of BCRA instruments was on the rise, with interest rate increases supported in the auctions

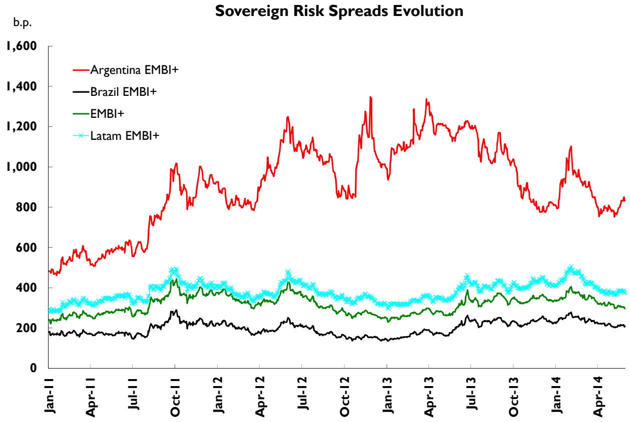
After having grown 26% in 2013, the stock of bills and notes of the Central Bank went up at a more marked pace (64%) in the first five months of the year. Despite this expansion, it is worth mentioning that the stock of these instruments measured in terms of deposits reached 22.7%, thus standing below the historical levels. The stock rise was accompanied by a context of increases in the rates auctioned in the primary market (see Chart II.18): in January, they went up 1,000 bp, and then they retreated partially by mid-April. In recent months, notes

Chart II.16
GDP-linked Securities Prices



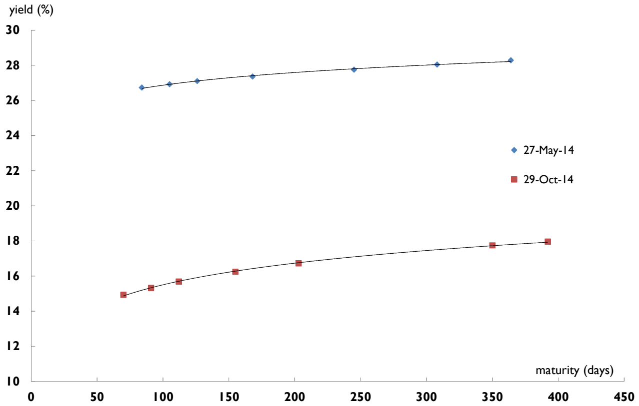
Source: Bloomberg based on domestic brokers

Chart II.17
Sovereign Risk Spreads Evolution



Source: Bloomberg

Chart II.18
LEBAC Auctions



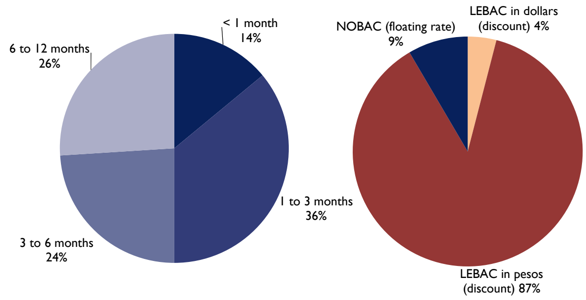
Source: BCRA

27 This figure would anticipate that 2013 growth would not have been sufficient to trigger the payment of the coupon by the end of the year.
28 As a result of the agreement with Repsol, the company received sovereign bonds (see Chapter 3) which were quickly sold in the market.

Chart II.19

LEBAC and NOBAC Stock Composition

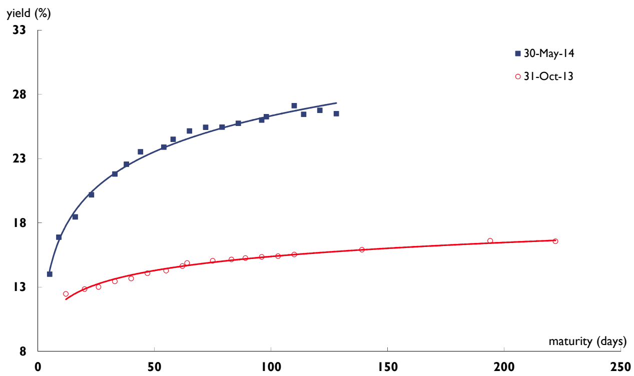
Outstanding stock by type of interest rate and maturity as of end of May14



Source: BCRA. Does not include lebacs in pesos liquidated by reference exchange rate.

Chart II.20

LEBAC Secondary Market



Source: BCRA based on MAE

were issued once again, as a result of which their share rose up to a level of nearly 9% of the outstanding stock (see Chart II.19). In turn, by the end of January, the Central Bank started to auction dollar-denominated domestic bills to be underwritten by financial entities taking time deposits in such currency (Communication "A" 5527)[29]. Lastly, the average term (weighted by amount) of the issues in pesos has remained almost unchanged since the end of 2013 and stood at a level close to a residual term of 180 days. With reference to the stock, the average term of the outstanding bills in pesos stood close to 130 days –residual term- (by the end of last year, it was standing at 135 days).

In the secondary market, the yields required on the bills have widened, in line with the increases of the interest rates of auctions as from late January (see Chart II.20). For the notes, even though their trading increased slightly in the first months of the year, transactions continued to be occasional, and this makes the comparison at different times more difficult.

The amount traded in fixed income instruments continued to be on the rise during the first four months of the year

The traded amounts in fixed income instruments in domestic markets (BCRA instruments and sovereign bonds) recorded a sizable increase from January to May 2014, and reached a daily average of $5.5 billion. This implies a 45% rise against the average amount of the previous five months and a year-on-year rise of almost 60% (see Chart II.21). Transactions with BCRA instruments accounted for a large part of the increase, especially in March and April, when their share reached almost 70% of the total[30]. The amount traded in sovereign bonds also went up since early 2014, reaching over $3.5 billion in terms of daily average. Bonds in dollars (especially Boden 15, followed by Bonar X) recorded the highest traded volume among sovereign bonds, with a higher weight than in the previous five months. In turn, the volume traded of bonds in pesos expanded during this period, led by instruments such as Discount, Bogar 18 and Bocon PR13.

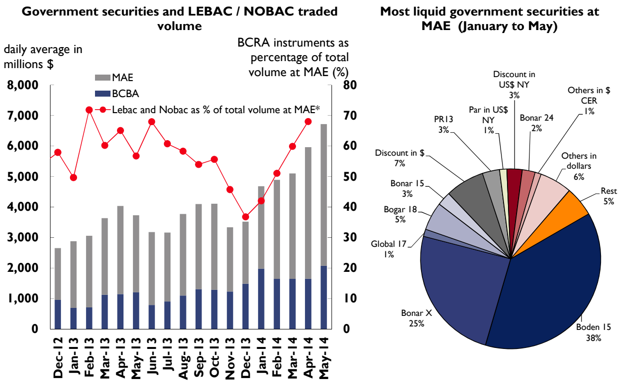
Financing to the private sector continues to be on the rise through market instruments, with a strong incidence of specific operations

[29] Likewise, in December, peso-denominated domestic bills settled according to the benchmark exchange rate started to be issued (Communication "A" 5502). These bills are excluded from the analysis made herein due to their special characteristics: they may be underwritten by the grain and oil sectors, their auction mechanism is different from the weekly scheme in force for the rest and early repurchases may be performed (to render them more liquid) by BCRA as from day 91 after their underwriting.

[30] Transactions with BCRA instruments in the secondary market went up between January and May this year, reaching a daily average of over $2.1 billion (up 60% against previous months), with a peak of $2.9 billion during April.

Chart II.21

Fixed Income Instruments - Traded Volume

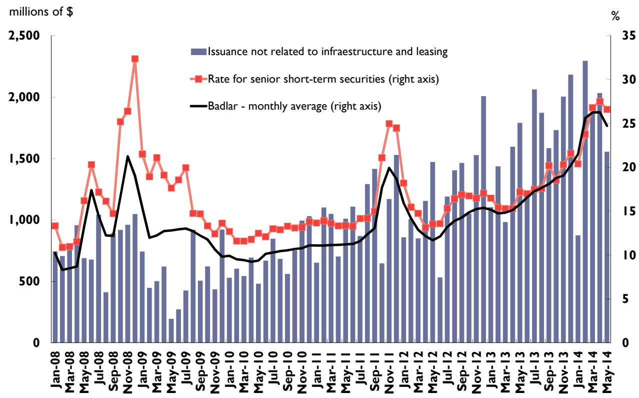


(*)May data not available.
Source: MAE and BCBA

Note: Bonar 24 began operating in May.

Chart II.22

Issuance of Instruments by Financial Trusts and Financing Rates



Source: BCRA based on CNV, BCBA and BCRA

Gross financing flow to the private sector and for infrastructure and housing projects through capital market instruments grew markedly in 2013, accumulating a volume over $71.7 billion, against $38 billion in 2012. However, this amount was largely impacted by a significant securitization transaction related to housing programs (Pro.Cre.Ar) and by the issues of YPF bonds (including two issues abroad during the third quarter). Leaving aside the infrastructure and housing trusts and YPF transactions, financing through markets amounted to about $44.5 billion in 2013. The growth of the financial sector's corporate bonds (67% y.o.y.) stood out, together with financing through financial trusts unrelated to infrastructure and housing (it grew 35% in 2013).

More recently, in the first months of 2014, the financing volume through the market (excluding infrastructure and housing) continued to go up. Thus, from January to May, it amounted to over $27 billion, up 10% against the figure recorded in the last five months of 2013 and up 20% against the same period of that year, even though this evolution is due to the influence of specific transactions involving high amounts.

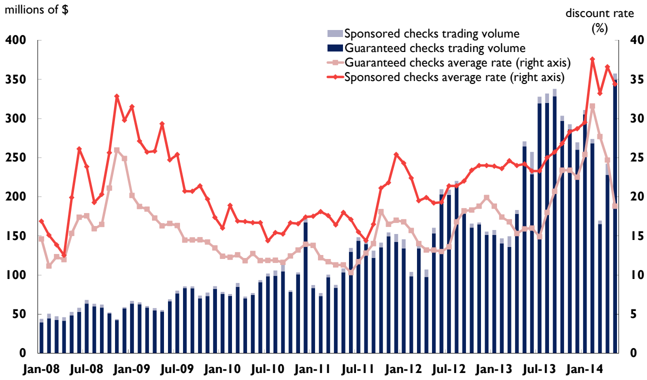
Financing through corporate bonds (ON) amounted to nearly $17 billion in the first months of the year (see Chart II.2), recording a sizable growth if compared to that of the previous five months ($13.2 billion) and also against the same period of 2013 ($14.6 billion). The size of this flow was directly related to YPF transaction abroad at the beginning of April for US$1 billion (see Box 2). Excluding YPF transactions, a contraction of 8% in the financing amount was observed in the first five months of the year against the previous five months, and of 13% in year-on-year terms.

From January to May, transactions of corporate bonds in domestic currency prevailed in terms of volume, while there were only three issues of dollar-linked bonds. In the transactions in pesos, an extension in the term of the instruments issues was observed, even though for a higher cost, in line with the increase of the Private Bank BADLAR.

Likewise, in the same period (January-May), financing through financial trusts (excluding infrastructure and housing) went down almost 9%, even though they went up 23% against the same period of 2013 (see Chart II.22). Particularly in January, when the interest rates went up, there was a sharp decline of transactions, with amounts standing at minimum levels, not seen for the last 18 months. From February onwards, cutoff rates followed the upward pattern of the Private Bank BADLAR, even

Chart II.23

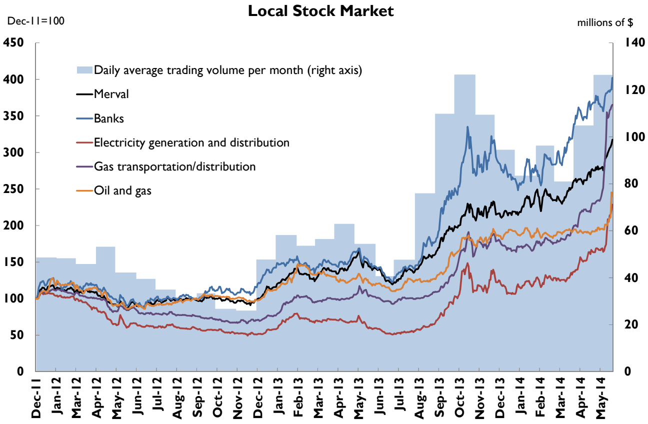
Trading of Deferred Payment Checks



Source: BCRA based on IAMC

Chart II.24

Local Stock Market



Source: BCRA based on BCBA

though a slight decline started to be observed in the yields required.

Regarding deferred payment checks traded at the Buenos Aires Stock Exchange, the traded volume contracted 12% in the first months of 2014 against the previous five months, even though there was a 49% y.o.y. increase (see Chart II.23). In turn, the average term of the guaranteed check segment shortened to the lowest level in almost three years but then started to extend at least in part. Discount interest rates charged experienced a sharp increase in January and February (they reached maximum peaks in the segment of guaranteed and sponsored checks since this operation started in 2013), and as from March and more sharply as from May, the guaranteed check segment (where more transactions are recorded) started to decline.

The stock market deepened its upward trend in the first months of the current year

The Merval Index ended last year with a strong expansion (89% in pesos and 42% in dollars, converted using the wholesale exchange rate). This upward bias prevailed in the first months of the year, and new historical peaks were reached. Thus, measured in domestic currency, the index recorded a 43% profit from January to May 2014 (see Chart II.24). At sectoral level, the expansion of stocks of companies related to electricity and gas distribution, with hikes of over 100% in the January-May period was highly remarkable. The stock related to the financial sector also went up sizably, with increases in a range of 55%-75% for stocks that are part of the Merval. In turn, other sectors, such as oil companies and iron & steel enterprises, recorded more limited increases in the price of their stocks, around 20%-25%, while those related to food and beverage companies went up 4% on average.

In turn, the volume of transactions with stocks went down slightly in the first five months of the year. The traded volumes fell from a daily average of $103 million in the last five months of 2013 down to $98 million in early 2014, even though they still stand above the levels observed one year ago[31].

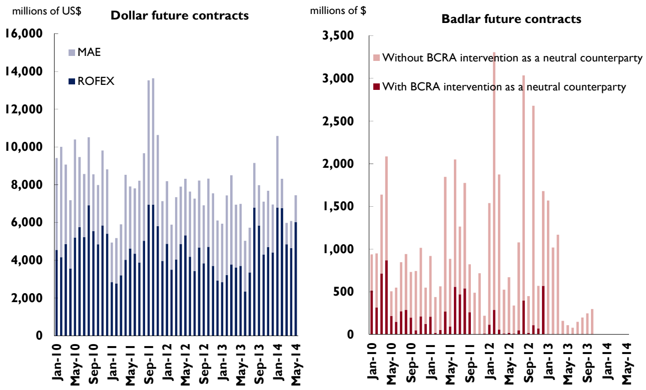
The transactions in the forward exchange rate markets went up in the first two months of the year and dropped later on

After recording an annual decline in the transactions during 2013, the amounts traded in exchange rate derivatives went up in the first two months of the year,

[31] In the same period of 2013, the traded average amounted to $57 million.

Chart II.25

Financial Derivatives Trading Volume



Source: ROFEX, MAE and BCRA

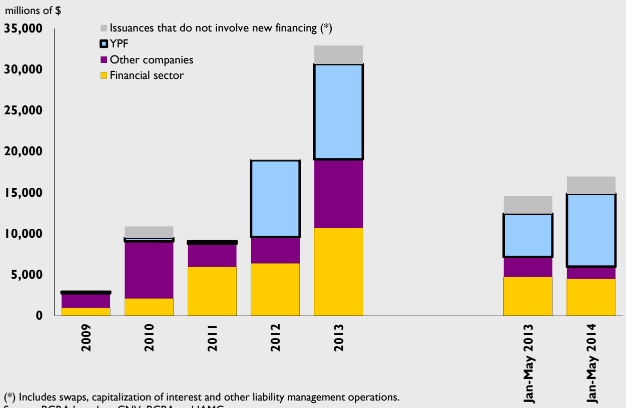
within a more volatile foreign exchange context. Later on, with more marginal changes in the exchange rate wholesale price and the implementation of regulatory limits to the net forward position in foreign currency of the financial entities[32], a sharp contraction in the amounts traded was observed in March and April (see Chart II.25). More recently, the amounts started to go up again. In turn, after increasing in January, the implicit rates in the dollar futures trading contracts with short-term maturity went down as from February. Regarding BADLAR futures, there have been no transactions since October last year.

[32] Communication “A” 5536.

Box 2 / Corporate Bonds of Argentine Companies

Financing to domestic companies through the issue of corporate bonds (ONs) has grown since 2012. A significant part of this evolution has resulted from YPF transactions –within the framework of the investment plan submitted by the oil company— with sizable transactions both in the domestic market and, more recently, also in foreign markets. Also remarkable is the momentum observed in the funding through market instruments by the financial sector (banks, non-banking financial institutions, financial groups, credit card closed systems, etc.), with transactions made largely in pesos even though, so far in 2014, the amounts issued by this sector reveals a slight year-on-year reduction. The total stock of corporate bonds, with two thirds denominated in foreign currency (whether payable in foreign currency or in pesos) has shown an upward trend, but it still accounts for less than 5% of GDP

Chart B.2.1
Gross Flow of Bond Issuance - Last 5 years



(*) Includes swaps, capitalization of interest and other liability management operations.
Source: BCRA based on CNV, BCBA and IAMC.

Even though financing in Argentina is mainly related to the banking system, capital market instruments play a supplementary role, allowing companies to diversify their funding[33]. In this sense, with reference to the period after the peak of the 2008-2009 international financial crisis, as from 2012, a strong increase of ONs gross[34] issues has been observed, and they have gained share in the amount of total transactions in the primary market against other instruments such as financial trusts (linked to lending for consumption and for infrastructure and housing projects) and the deferred payment checks (which is a segment essentially made up by small and medium-sized enterprises (SMEs)).

As already mentioned, this evolution has been largely influenced by the new financing to YPF (see Chart B.2.1), based on the 2013-2017 investment program submitted by the state-owned oil company. Thus, after making sizable transactions in the domestic market in the last part of 2012 and the first half of 2013 (both in pesos and dollar-linked), the transactions in dollars in the international markets performed at the end of 2013 and in early 2014 stand out[35]. Regardless of YPF transactions, the annual flow of corporate bond issues implying genuine financing[36] virtually doubled in 2013, to $19 billion against $9 billion on average in the previous three years. However, so far in 2014 (from January to May), these flows contracted 16% in year-on-year terms.

As from 2012, ONs issues started to concentrate mainly in two sectors. The oil & gas industry accounted for around a half of the amounts issued in 2012 and 2013 and for 66% in 2014, largely due to the transactions made by YPF. In turn, the financial sector –including banks, non-banking financial institutions regulated by BCRA and other agents, such as financial groups and credit card closed systems— accounted for almost one third of total flows in 2012 and 2013, while in the first four months of 2014, their weight fell to 26%. However, so far in 2014, the sector has accounted for nearly 75% of the aggregate amount issued if we exclude YPF issues and the transactions related to liabilities refinancing. Even though in 2013 there were transactions for sizable amounts in sectors such as food and beverage, and agriculture and livestock, the presence of the remaining sectors has become negligible so far this year.

[33] Bank lending to the non-financial private sector accounted for around 14% of GDP in March 2014 (see Chapter 4). In the same period, the stock of debt or equivalent instruments amounted to 3% of GDP in the case of the corporate bonds (ONs), 0.5% for traditional trusts and 1.5% for infrastructure-related financial trusts. Regarding shares of stock, the stock market capitalization was equivalent to almost 10% of GDP for domestic companies, even though the issues of stocks instruments have been marginal in recent years.

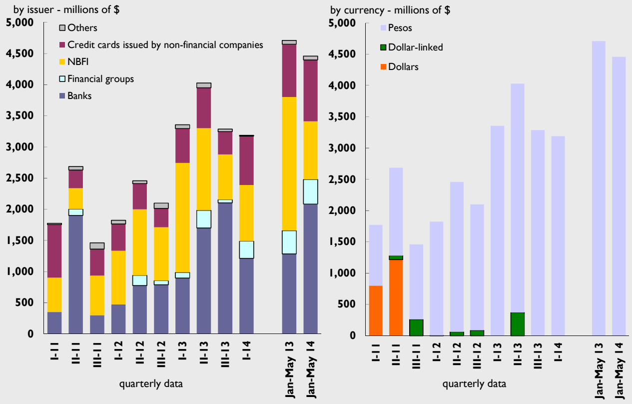
[34] Without netting for maturities occurred in that same period.

[35] In recent months, YPF made three issues in international markets, and the most recent one in April 2014, because of its magnitude, should be especially underlined. This transaction resulted in US$1 billion through a 10-year instrument with a yield at the time of the issue of 8.75%.

[36] That is to say, excluding transactions related to liabilities management, such as swaps and interest capitalization through the issuance of new bonds. In 2014, a specific transaction of this type corresponding to a company of the oil & gas sector stands out.

Chart B.2.2

Flow of Debt Issuance - Financial Sector

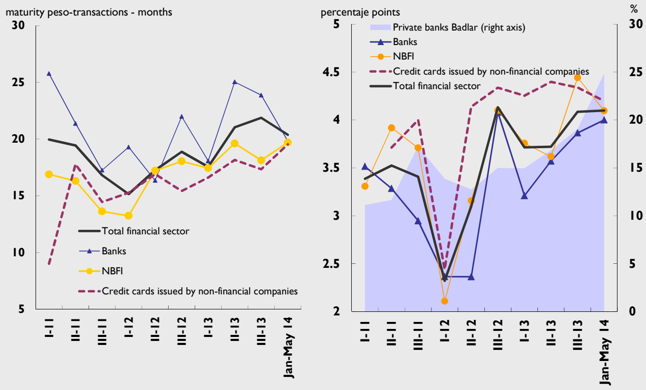


Source: BCRA based on CNV, BCBA and IAMC.

With reference to the evolution of the financial sector issues (see Chart B.2.2), from January to May, corporate bond transactions were recorded for nearly \$4.5 billion pesos, down 7% against the previous five months and 5% in year-on-year terms. In this period, the transactions performed by banks (47% of the total amount), credit card closed systems (22%) and non-banking financial institutions (21%)[37] stood out remarkably. Regarding the financing conditions, all these transactions were made in domestic currency, and largely at a variable rate, so far in 2014.

Chart B.2.3

Financial Sector Bond Issuance - Maturity and Margin over Badlar

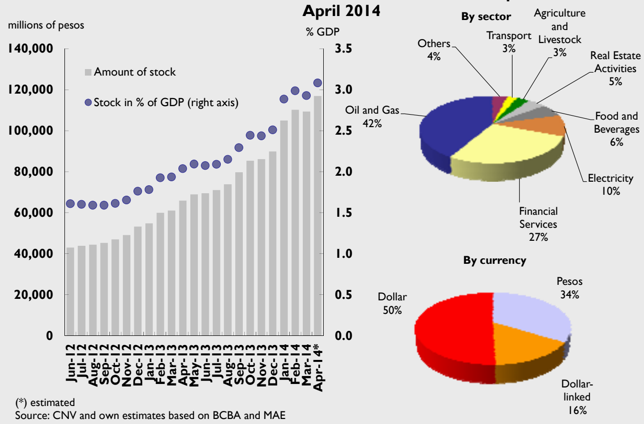


Data by quarter except 2014. Weighted average margin for operations in pesos between 18 and 24 months.
Source: BCRA based on CNV, BCBA and IAMC.

The new financing through the financial sector's ONs concentrated in the segment ranging from 18 to 24 months (80%) so far in 2014, even though there were also transaction for up to 60 months. As a result, for the aggregate of the sector, the average weighted term for the issues has stood slightly above 20 months, i.e. down almost one and a half months relative to the last four-month period of 2013[38], after showing an upward trend during a good part of the 2012-2013 period. Lastly, the financing cost for the sector went up in line with the evolution of the Private Bank BADLAR, with a margin standing on average slightly above 4% for the aggregate of issues between 18 and 24 months, and with no significant differences among the segments of the sector, despite the fact that banks usually issue at a lower cost than the other segments (see Chart B.2.3).

Chart B.2.4

Stock of Bond Issuance: Evolution and Estimated Composition at April 2014



(*) estimated
Source: CNV and own estimates based on BCBA and MAE

In terms of the outstanding stock, between late 2013 and April 2014, total corporate bonds went up 30% to a level close to \$117 billion, equivalent to around 3% of GDP (see Chart B.2.4). This increase was due to both the presence of new issues for sizable amounts and the effect of the exchange rate evolution. Regarding the former, it is estimated that over 40% of the stock is related to the oil & gas sector (YPF's debt alone accounts for 30% of the total stock). Regarding the latter, it is estimated that out of the stock as of April, two thirds are debt in foreign currency (half of the total would be payable in foreign currency, and 16% would be debt in dollars payable in pesos, under a format known as dollar-linked), while the remaining third is in pesos.

Looking into the future, financing through ONs is expected to continue having a positive momentum, even though the evolution of amounts in particular would still show a volatile pattern on a monthly basis. This is due to the existence of agents of varied magnitude and different business models, including both those with a higher weight of market instruments in their total funding and others with better flexibility to take advantage of

[37] Additionally, 9% corresponds to financial groups and a marginal portion to other issuers of the sector (leasing companies, non-banking firms dealing with personal loans, brokerage firms, fiduciaries, etc.).

[38] This is mainly due to bank transactions (in general with large and sizable transactions), while in other segments (non-banking financial institutions and credit card closed systems), the average weighted term of issue went up so far this year.

windows for opportunities to diversify their financing[39]. On the other hand, while interest rates in international markets stand at historically low levels, there are incentives for companies with income in foreign currency to finance themselves abroad, with transactions for higher volumes than those observed at domestic level. In the medium term, the implementation of the new law on capital markets[40] is expected to contribute to the corporate bonds market through the incorporation of new companies.

[39] For example, in the specific case of the financial system and considering the entities regulated by BCRA, while for the aggregate of banks ONs account for less than 2% of the total funding (net worth plus netted liabilities, for the non-banking financial institutions, this weight exceeds 20%.
[40] See Box "New Law on Capital Markets and regulation" in the Financial Stability Report of the second half of 2013.

III. Debtors Performance

Summary

The corporate sector is the main debtor of the financial system, and to March 2014, it covered approximately half the portfolio of lending to the non-financial sector. In this context, taking into account a dissimilar evolution in the activity of the different productive sectors, a slight increase was recorded in the aggregate levels of corporate indebtedness. Thus, corporate leverage totaled 21.4% of GDP by the end of 2013 —latest information available—, up 2 p.p. against the value recorded by the end of 2012. Mainly due to the effect of the peso-dollar nominal exchange rate increase throughout 2013, foreign financing was behind almost two thirds of the increase of total indebtedness.

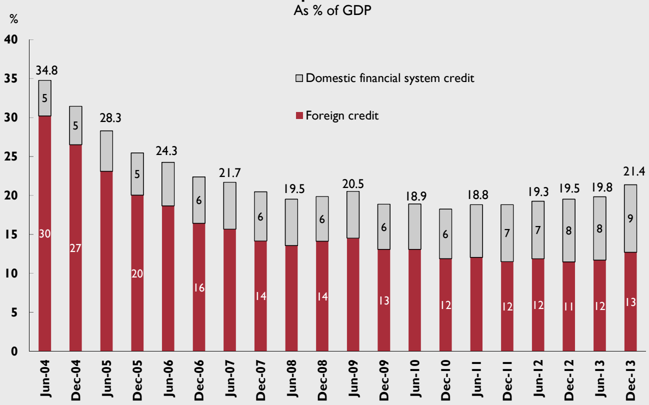
The low levels of indebtedness still prevailing in the sector, compared to both the country's own history and international values, contribute to preserving its financial position and repayment capacity. In this sense, the improvement of external competitiveness and the policy measures applied in order to recover household consumption should be especially emphasized, in addition to the measures intended to secure the monetary and financial stability conditions the BCRA has been implementing to this date.

The estimated household indebtedness in terms of total wage mass —net of contributions to the social security system— remained unchanged in the last twelve months, accounting for 23.6% as of March 2014. This occurred in a context of nominal income recomposition, hand in hand with the wage collective bargaining agreements and the increasing public transfers to lower income sectors. This performance has contributed to sustaining households' payment capacity.

As regards public finance, in the first months of 2014, the year-on-year expansion pace of tax collection speeded up, with a remarkable contribution of taxes directly associated to the exchange rate, and at the same time, it was possible to maintain the contribution of taxes related to domestic demand. The primary spending of the non-financial national public sector kept on growing at rates higher than revenue growth rates, leading to a lower primary result. In turn, the national public debt held by the private sector stood at significantly low levels, accounting for only 9.8% of GDP to September 2013, out of which 7.5 percentage points (p.p.) corresponded to liabilities expressed in foreign currency.

Chart III.1

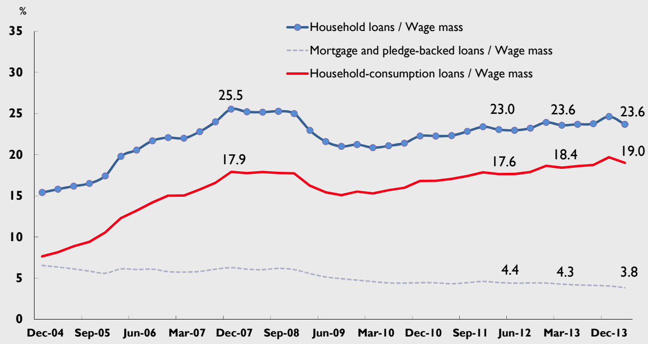
Corporate Debt
As % of GDP



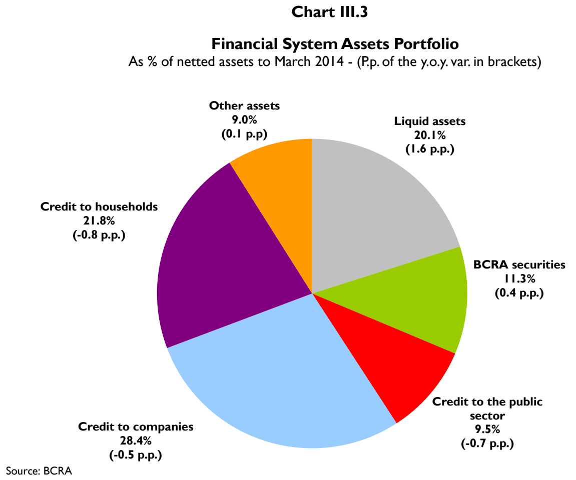
Note: Data subject to subsequent changes.
Source: INDEC and BCRA

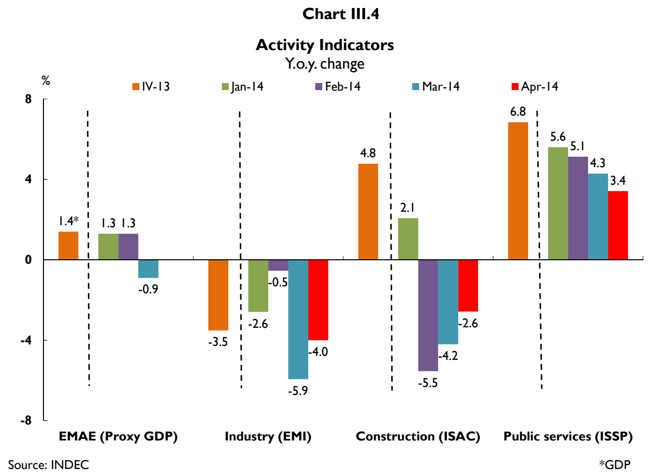
Chart III.2

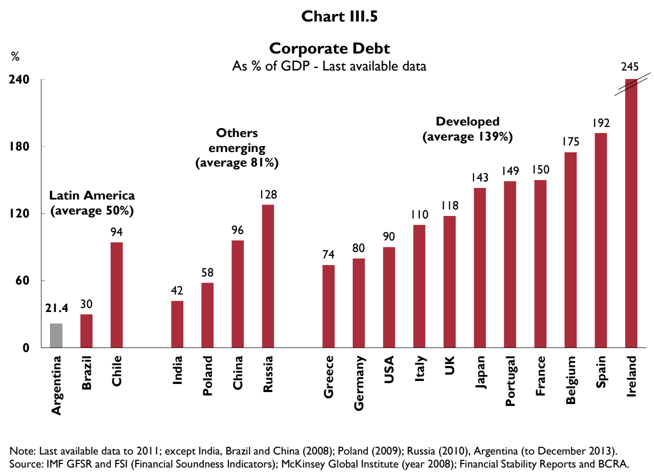
Household Debt
As % of formal wage mass net of contributions



Note: Loans to households include financial system financing, financial trusts for consumption loans as underlyng assets (credit cards and personal loans), collateralized loans (mortgage and pledge-backed) and the stock of non-bank credit cards. Data subject to subsequent changes.
Source: BCRA, INDEC and CNV







III.1 Financial System Debtors

Companies and households, in such order, continue to be the main debtors of the financial system, even though the relative weight of lending to these sectors in assets contracted at the beginning of 2014

At present, almost half of credit lent by the ensemble of financial entities to the non-financial sector corresponds to loans to companies. Thus, in aggregate terms, the corporate sector is the main debtor of the financial system (with a gross exposure equivalent almost to one third of its total netted assets as of March 2014).The household sector follows in order of relevance, and it accounts for approximately 22% of the total netted assets of the system (a little over one third of its total financing portfolio).

At the beginning of 2014, the growth of lending to the private sector contracted for both companies and households (see Chapter IV); as a result, the weighting of these exposures went down marginally relative to the total netted assets of the financial system (see Chart III.3). On the other side, in recent months, the share in such total of liquid assets and BCRA's security holdings kept on going up.

III.2 Corporate Sector

In recent months, there has been a dissimilar evolution in the activity of the different sectors, in a context of a slight increase of indebtedness levels

GDP kept a rising trend in year-on-year terms during the first quarter of 2014, mainly driven by the growth of services, despite the decline recorded in the production of goods (see Chart III.4). The industrial activity kept on going downwards, following the trend started in the second half of 2013, whereas the construction business contracted at the beginning of this year. The farming sector continued to grow, driven by agricultural production, with a moderate expansion pace due to the performance of the livestock sector and dairy production. In turn, the production of services increased again, even though it experienced the impact of the reduced manufacturing of goods, especially those related to commercial and transportation segments.

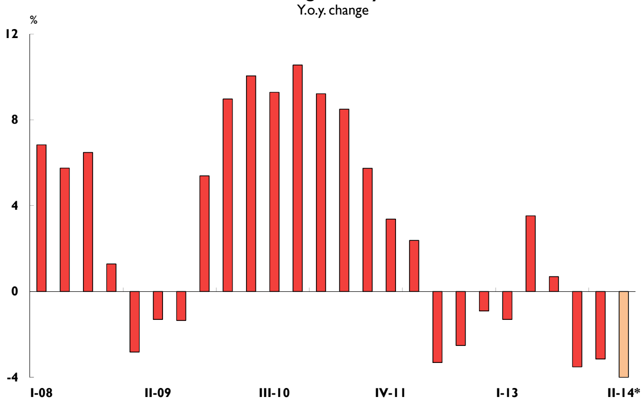
Against this backdrop, the estimated level of indebtedness of companies in aggregate terms reached 21.4% of GDP by the end of 2013[41] —latest data available—, up 2 p.p. against the value recorded by the

[41] In all indicators used throughout this Report, the new 2004-based GDP series is used.

Chart III.6

Manufacturing Monthly Estimator

Y.o.y. change



Source: INDEC

*data to Apr-14

end of 2012 (see Chart III.1). It must be pointed out that the leverage of the local corporate sector stands significantly below the values observed in other economies (see Chart III.5).

As regards aggregate indebtedness of local corporations, 60% of such debt is explained by financing from abroad. Within this segment of financing, approximately 60% constitutes commercial debt, whereas 25% would be given by companies of the same group. In aggregate, financing from abroad in terms of GDP accounted for almost two thirds of the increase in total indebtedness of the corporate sector recorded in 2013, which mainly reflects the effect of the peso-dollar nominal exchange rate increase.

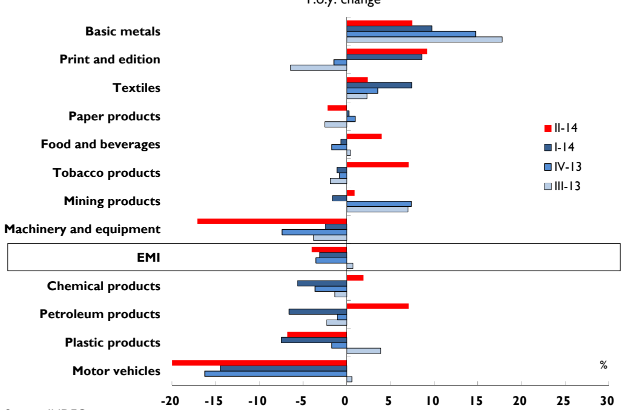
On the other hand, as to resources obtained in the domestic financial system, those taken by industry and services still prevail, with an increasing share of micro, small and medium-sized enterprises (MiPyMES) as a result of the public policies promoted by the Central Bank.

In the months to come, the evolution of the financial situation and repayment capacity of the corporate sector will be conditioned to the performance of their revenues and of the cost of indebtedness. In this regard, the context of improvement in external competitiveness and the policy measures aimed at recovering households' consumption must be weighted, as well as the measures intended to secure the monetary and financial stability conditions encouraged by the BCRA at the beginning of the year, added to the context of active policies developed by the Central Bank to favor the companies' access to credit lines for longer terms and at lower interest rates (see Chapter IV).

Chart III.7

Industry - Sectoral Evolution

Y.o.y. change



Source: INDEC

Productive Sectors

Industry

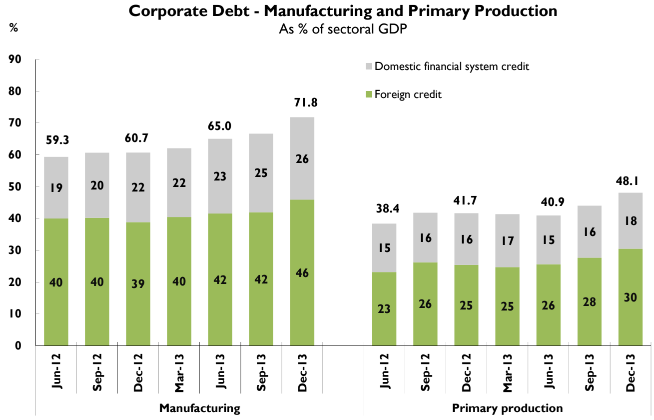
Industrial companies have continued to perform weakly in recent months, in a context of gradual increase in their levels of indebtedness

The manufacturing industry has not shown any signs of recovery so far in 2014 (see Chart III.6). Sectors mostly dependent on external demand, such as the automotive sector, continued to follow a downward trend, thus affecting other related industries (rubber and plastics and metal mechanics, among others). Besides, a decline was observed in the activity of the oil refining sector, and in the production of construction inputs and of some chemical products. Basic metals, textile products and segments related to publishing and printing exhibited a

Chart III.8

Corporate Debt - Manufacturing and Primary Production

As % of sectoral GDP



Note: Data subject to subsequent changes.
Source: BCRA and INDEC

Table III.1

Grain Production - Major Crops

	2011-12 thousands tns	2012-13* thousands tns (e)	2013-14* thousands tns (p)	% Change 2013-14 vs. 2012-13	Diff. in thousands of tns 2013-14 vs. 2012-13
Cereals	**46,219**	**50,996**	**50,588**	**-0.8**	**-408**
Corn	21,200	32,100	31,100	-3.1	-1,000
Wheat	14,500	8,000	9,200	15.0	1,200
Others	10,519	10,896	10,288	-5.6	-608
Oilseeds	**44,306**	**53,621**	**57,035**	**6.4**	**3,414**
Soybean	40,100	49,300	54,000	9.5	4,700
Others	4,206	4,321	3,035	-29.8	-1,286
Rest	**1,070**	**639**	**1,414**	**121.4**	**776**
Total	**91,595**	**105,256**	**109,038**	**3.6**	**3,782**

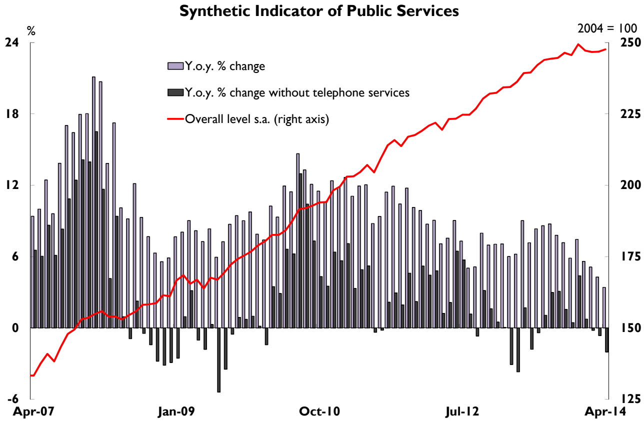
e: Estimated p: Proyected

*Includes the methodological change in the estimate of corn

Source: MAGyP

Chart III.9

Synthetic Indicator of Public Services



Source: INDEC

good performance, even though it was not enough to offset the contraction in the remaining sectors (see Chart III.7). Thus, the level of use of installed capacity (UCI) of the industry as a whole posted a drop during the first half of the year.

In turn, the estimated leverage of this sector's companies would have stood slightly above 70% of the sectoral GDP by the end of 2013 (see Chart III.8), and would have posted a year-on-year growth relatively more significant in the segment of financing from non-residents, which accounts for around 64% of the total[42].

Agricultural Sector

Activity in the agricultural chain broke a new record, favoring agricultural production, with a more extended use of domestic and external credit resources

The agricultural activity kept on expanding in the first months of the year. The present harvest (2013/2014), which is estimated to stand at around 109 million tons, will break a new grain production record with a rise close to 3.5% against the 2012/13 campaign (see Table III.1). This increase will be especially boosted by soybean, with a production that will reach 54 million tons, up 9.5% against the previous cycle, thanks to a combined rise of sown area and yields. The wheat harvest would recover this year after the discouraging performance of the previous cycle, hand-in-hand with the increase of the area planted with wheat.

In turn, the activity of the livestock sector considerably moderated its growth pace throughout the year. Bovine slaughtering posted a drop close to 3% y.o.y. in the first quarter of 2014, after growing approximately 10% y.o.y. in 2013. Poultry slaughtering also recorded drops from January to March, whereas dairy production recorded a further fall.

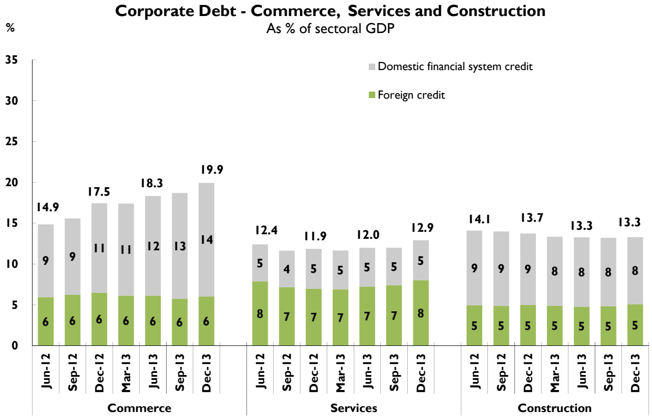
In general, the companies that are part of the primary sector of economy continue expanding their activity. Against this backdrop, sectoral indebtedness reached 48.1% of GDP by the end of 2013 (see Chart III.8), increasing throughout the year. Two thirds of total credit resources come from abroad[43], in a context of considerable capacity for generation of foreign currency by these companies.

[42] It must be stated that the most of the external indebtedness of this sector derives from lines associated to commercial activity —obligations related to import and export activities. The rest corresponds to financial lines —financial loans and debt securities, among others.
[43] Most part of external financing of the primary sector (originated in oil and mining sectors) is mostly made up by financial debt —financial loans and debt securities, among others.

Chart III.10

Corporate Debt - Commerce, Services and Construction

As % of sectoral GDP

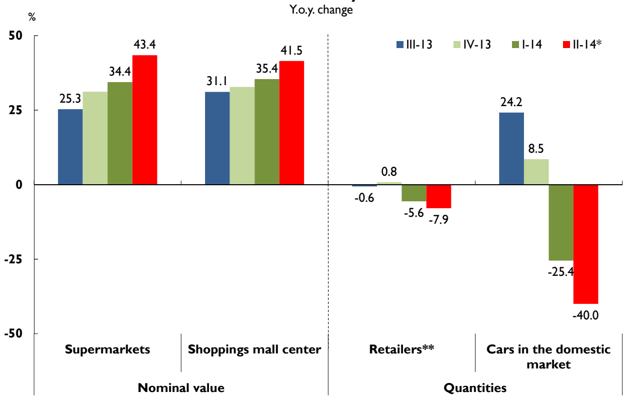


Note: Data subject to subsequent changes.
Source: BCRA and INDEC

Chart III.11

Commercial Activity Indicators

Y.o.y. change



Source: INDEC, CAME and ADEFA

*data to Apr-14 **relieved by CAME. More than 400 stores

Services

The services sector increased its activity pace, with low levels of indebtedness

Public services consumption continued exhibiting a positive trend during 2014, even though its growth rate moderated relative to the previous year (see Chart III.9). According to the Summarized Public Services Indicator (ISSP), telephone items led the increases, and they posted the highest contribution to the year-on-year rise of this index.

The other segments of this sector showed a dissimilar performance throughout the year. Electricity demand kept on increasing during the first four months of 2014, whereas the number of cars going past toll booths contracted and the number of passengers carried by urban transportation services remained practically unchanged. Cargo transportation contracted remarkably in the first months of 2014, a performance that is mostly explained by the evolution of primary product exports —which might be reversed after the higher sales of the summer crop as from the second quarter of the year.

The leverage of service companies rose almost 1 p.p. year-on-year, totaling 12.9% as of December 2013 (see Chart III.10). Thus, it continues to stand among the productive sectors with lowest indebtedness levels.

Commercial Sector

Heterogeneous performance in the activity of commercial companies, with an increasing —but still low— leverage

Commercial activity would have moderated its pace so far in 2014, in line with the performance of the production of goods. According to partial indicators, a significant contraction was observed in the volumes sold of durable goods, including motor vehicles —which decreased 32.3% y.o.y. in the first five months of 2014—, motorbikes, bicycles, home appliances and electronic items. In turn, the amounts billed in the main supermarket chains and in shopping malls showed some acceleration on the margin, rising around 36% y.o.y. between January and April (see Chart III.11).

The estimated aggregate indebtedness of this sector recorded an annual increase of almost 2.5 p.p., up to 19.9% of GDP by the end of 2013 (see Chart III.10). This level continues to be low if compared to other productive segments, and two thirds of the funds come from the domestic financial system.

Construction sector

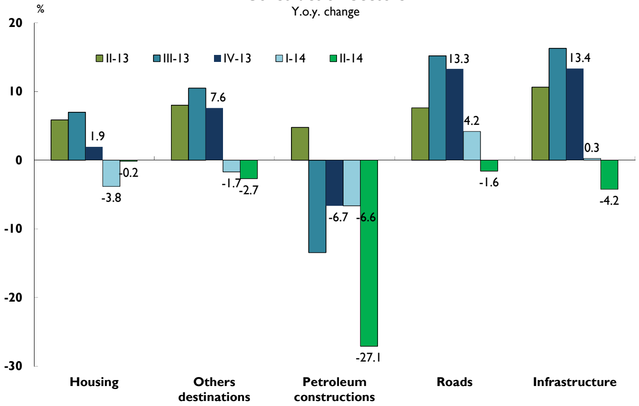
Reduced activity of construction companies, with low internal and external indebtedness levels

The construction sector lost momentum and started to show negative rates at the beginning of 2014. The contraction derived mainly from private works, in particular works intended for housing, against a backdrop in which public construction lost ground if compared to the previous year (see Chart III.12). Oil-related construction decreased their level of activity as well, even though they were partially affected by the statistical effect of a high year-on-year basis for comparison.

This context of lesser activity in construction companies was accompanied by a slightly decreasing level of aggregate sectoral indebtedness on an annual basis, accounting for 13.3% of GDP by the end of 2013 (see Chart III.10). It must be stated that less than 40% of the total corresponds to external funds.

Chart III.12

Construction Sectors



Source: INDEC

III.3 Households

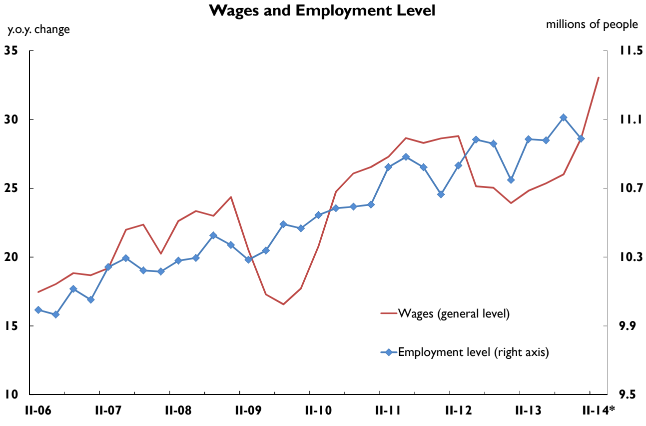
In a context of recovery of this sector's nominal income, in the last twelve months the aggregate indebtedness of households[44] in wage mass terms remained unchanged

Nominal income of households increased again during the first months of 2014, within a context of a labor market that stood relatively stable —despite the weakened economic activity pace— and upon the ongoing public policies aimed at supporting lower-income sectors.

According to data from the Household Permanent Survey (EPH) for the first quarter of 2014, the unemployment rate[45] went down again relative to the values recorded in 2013 and stood at 7.1% of the labor force (PEA). Labor share stood at historically high levels, 45% of population, down 0.8 p.p. against the value recorded one year ago. This occurred in a context where the employment rate fell 0.4 p.p. against the first quarter of 2013, down to 41.8%, thus showing that job creation last year was lower than population growth. The quality of employment marginally worsened during the

Chart III.13

Wages and Employment Level



Source: INDEC

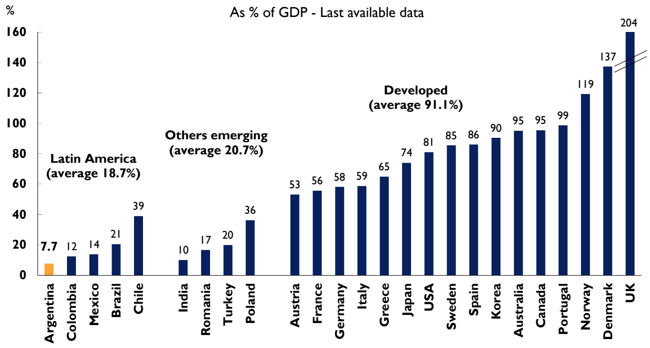
*data to Apr-14

[44] Household indebtedness includes the financing to individuals for consumption granted by the financial system, financial trusts with underlying assets of which are credits for consumption (credit cards and personal loans) and collateralized loans to families (mortgages and pledges) and the stock of loans of non-banking credit cards.
[45] In the 31 urban agglomerations surveyed.

Chart III.14

Household Debt

As % of GDP - Last available data

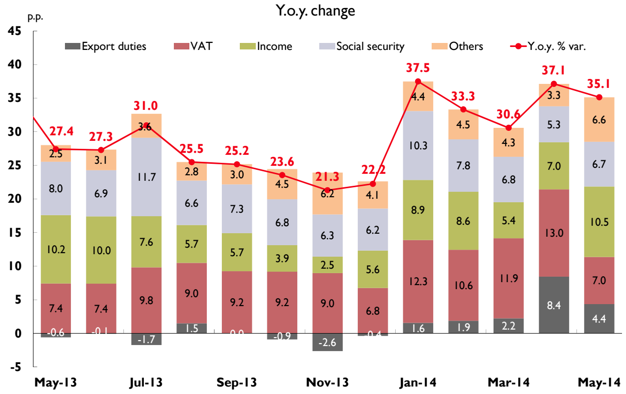


Note 1: Last available data to 2013, except India (2008); Mexico (2009); Colombia, Chile and Japan (2010); Spain (2012) and Argentina (March-14). Data from Argentina is subject to future changes.
Note 2: In the case of Argentina, it includes bank debt, financial trusts for consumption loans as underlyng assets (credit cards and personal loans) and real collateral loans (mortgages and pledge-backed) and the stock of non-bank credit cards.
Source: FMI, McKinsey Global Institute (year 2008), Financial Stability Reports and BCRA

Chart III.15

Contribution to Growth of National Tax Revenue

Y.o.y. change



Source: BCRA from Treasury Secretariat data

same period, since the under-employment rate went up 0.1 p.p., standing at 8.1% of PEA (see Chart III.13).

The nominal increase rate of the average wage income of economy sped up during the first four-month period of the year. According to the Wages Index of INDEC, total average remunerations went up 33.0% y.o.y. in April against 25.9% y.o.y. in December 2013. This increase, combined with the employment level, allowed for sustaining the wage mass —which in 2013 accounted for 51.4% of GDP— at historically high levels.

As long as the wage increases agreed under the latest wage collective bargaining came into effect, the income of households strengthened, whereas the wage-earning staffing might increase during the second quarter[46]. Thus, the mass of labor income would grow, resulting in an improvement of consumption by households in the next few months.

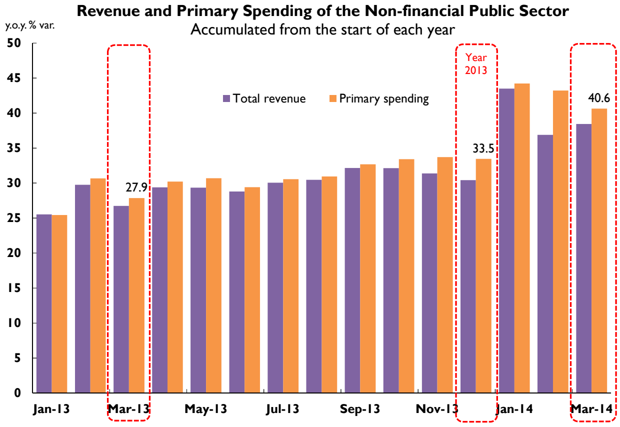
In turn, public policies kept on consolidating the income of the most vulnerable households throughout 2014. The main measures taken include the increase of retirement and pension benefits, upon application of the Social Security Mobility Act. Besides, in February, a Program to Support the Students of Argentina (PROG.R.ES.AR.) was created to provide a universal economic aid of $600 per month to young people from 18 to 24 years old, so that they start or complete their studies. Finally, effective as from June, an increase was established for the amount of family allowances between 20% and 40%. In the case of the Universal Child Allowance for Social Protection (AUH), the increase reached 40%. As a whole, the measure regarding family allowances will entail, according to official estimates, an additional fiscal cost of around $15 billion per year.

Despite showing a slight increase by the end of 2013, the aggregate indebtedness of households reached 23.6% of the annual total wage mass[47] in March 2014 (see Chart III.2), similar to the level recorded one year ago. This relative level of debt is significantly below the values observed in other emerging and developed economies (see Chart III.14). It must be stated that as a result of macroprudential policies timely implemented by the BCRA, the households' indebtedness is almost completely made up by credit lines in pesos, unlike the situation in the past. Thus, any potential change in the peso-dollar exchange rate does not affect the ratio of

[46] According to Manpower Employment Expectations Survey corresponding to the second quarter of 2014, the net employment expectation (number of surveyed businessmen expecting an increase in staffing net of those expecting a reduction) stood at 10 points against the 6 points obtained in the report for the previous quarter.
[47] Considering the wage mass coming from registered and non-registered workers, net of contributions to social security. The latest information published by INDEC is used, taking into account the change of year base to 2004.

Chart III.16

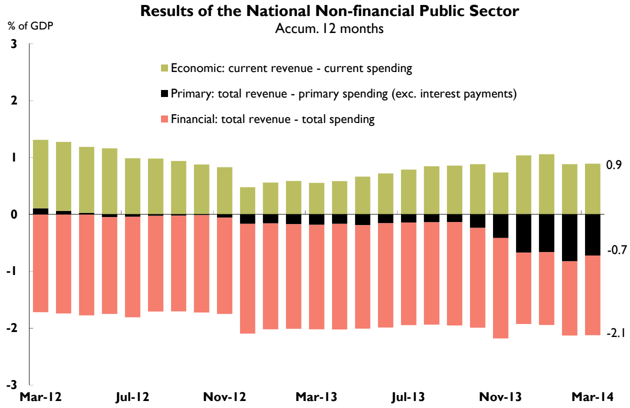
Revenue and Primary Spending of the Non-financial Public Sector
Accumulated from the start of each year



Source: BCRA from Treasury Secretariat data

Chart III.17

Results of the National Non-financial Public Sector
Accum. 12 months



Source: BCRA from Treasury Secretariat and INDEC data

households' indebtedness relative to the wage bill (since the latter is denominated in domestic currency).

In year-on-year terms, a change was observed in the composition of indebtedness, with an increasing weighting of debt from consumption lines —personal loans and credit cards— (up to a little more than 80% of the total), and a decrease of debt originated in collateralized loan lines —pledge-backed loans and mortgages. The low levels of aggregate indebtedness contribute to sustaining limited values in the average burden of debt services of the household sector, allowing them to face any changes in macroeconomic and financial conditions such as those mentioned in Chapter II of this Report —including the evolution of activity level and interest rates.

III.4 Public Sector

In the first months of 2014, spending of the non-financial public sector (NFPS) grew at a higher pace than revenue, whereas the national public debt with the private sector stood at very low levels in terms of GDP

In the first part of 2014, national tax collection accelerated its expansion pace (35% y.o.y.), basically driven by tax associated with the exchange rate, at the same time that the contribution of taxes related to domestic market was maintained[48] (see Chart III.15)[49]. In turn, spending of the non-financial national public sector (NFPS) grew so far this year at a pace of 6 p.p., exceeding the growth pace of revenue (see Chart III.16). Social security benefits continued to be the segment contributing the most to the year-on-year rise of primary spending, followed by current transfers to the private sector[50].

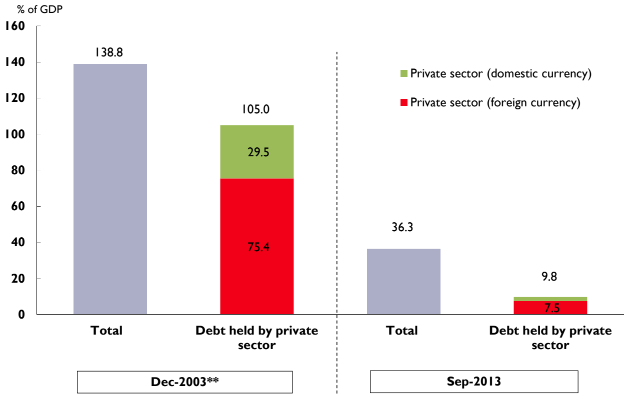
The higher social security spending was due to the increase of benefit amounts and the higher number of beneficiaries[51]. In turn, the increase of transfers to the private sector was due to higher transfers for family allowances—including the universal child allowance for

[48] In May, the government announced a new facilities plan for payment and protection of employment for obligations due until March 31, regarding tax, customs and social security matters.
[49] For further detail on the evolution of public sector finances, see the Macroeconomic and Monetary Policy Report, February 2014.
[50] By the end of March, the government established partial reductions of subsidies and increases of rates for the services of natural gas supply through networks, water and sewage.
[51] After the increases granted under the Social Security Mobility Act in March and September 2013 (15.18% and 14.41%, respectively), in March 2014 an 11.31% increase was established for benefits. Recently, the Argentine Executive Branch announced that a bill of law will be submitted to extend the Social Security Inclusion Plan to 470,000 prospective new beneficiaries, who were excluded since they had not enough years of proven contributions, with an estimated fiscal cost of around $12 billion (0.3% of GDP, estimated for 2014).

social protection (AUH)[52]— and subsidies for energy and passenger transportation services. Thus, social security benefits and current transfers to the private sector are expected to continue to drive primary spending in the next few months, added to the expenditures corresponding to the implementation of PROG.R.ES.AR., a plan intended to provide universal economic aid for low-income young people to start or complete their studies.

Chart III.18

Public National Debt*



*Excludes *holdouts*; **Ratio calculated using data from 1993 based nominal GDP.
Source: BCRA from Treasury Secretariat and INDEC data

Against this backdrop, the financial deficit of the NFPS in the last twelve months stood around 2.1% of GDP, whereas the primary negative result deepened in year-on-year terms (see Chart III.17).

In the first part of 2014, the National Treasury (NT) continued to mainly cover part of its financing needs through financial investments and loans from other non-financial public entities. Besides, the BCRA provided the NT with financing through Temporary Advances.

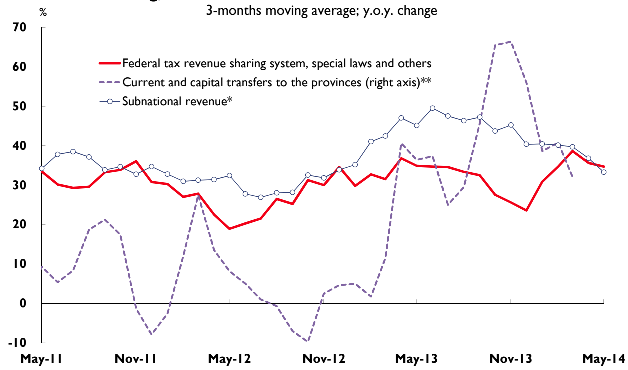
In turn, the NT issued debt in the domestic financial market, in two tranches, for approximately $10 billion, with a new bond called BONAR $ 2017[53].

The use of financing within the public sector allowed to keep at significantly low levels the risk of public debt refinancing based on the reduced balance of obligations to the private sector that, as at September 2013, accounted for only 9.8% of GDP (see Chart III.18). In particular, the debt with private holders denominated in foreign currency stood at 7.5% of GDP by the end of the third quarter of 2013.

Chart III.19

Sharing, Transfers to Provinces and Subnational Collection

3-months moving average; y.o.y. change



*Estimate based on available information.
**From Apr-09 provides for the distribution of resources Federal Solidarity Fund (Decree No. 206/2009).
Source: BCRA based on Treasury Secretariat and provincial governments data

Among the policies for management of national public debt, we should highlight that in January 2014 the swap took place of BONAR and of promissory notes $ 2014 for new securities with maturity in 2019, payable at BADLAR plus 250 basis points, thus allowing to significantly reduce the financial needs for the first quarter of 2014.

In addition, at the end of February, the Argentine government and the company Repsol signed the agreement for compensation for the expropriation of 51% of YPF shares, established by Law No. 26,741. In this context, the Spanish company accepted as compensation, for all and any concepts, a payment of US$5 billion in public debt securities under Argentine

[52] After the adjustment of wage ranges for collection of benefits and the increases granted during 2013, as from June 2014, the government established a new rise for family allowance amounts, up to 40% in the case of AUH, and for lower-income beneficiaries, and it also amended, as from June and October, the related wage tables.
[53] This security is fully amortized upon maturity, with a 3-year term, with quarterly interest determined at private BADLAR plus 200 basis points.

legislation[54]. The Argentine Congress ratified the agreement upon enactment of Law No. 26,932.

By the end of May, the Argentine government and the Secretariat of the Paris Club reached an agreement on the conditions for restructuring the debt of Argentina to the countries of such group. The debt of US$9.7 billion as of April 30, 2014, including default and penalty interest, will be paid under a flexible scheme between 5 to 7 years. An initial payment was established as principal for US$650 million in July 2014, and the next payment of principal for US$500 million in May 2015. The annual interest rate agreed is 3% for due balances during the first 5 years. A minimum payment was established to be made by Argentina every year. Besides, a criterion was defined for additional payments in case of an increase of investments from member countries of the official organization.

Table III.2

Dollar Linked Debt Placements of the Subnational Juridictions

(Jan-13 to May-14)

Date	Juridiction	Market	Amount in million (currency of origin)	Term (years)	Annual rate of return
Mar-13	CABA	domestic	100.0	5.0	4.0%
May-13	CABA	domestic	216.0	6.0	4.0%
May-13	Mendoza	domestic	94.6	3.0	3.0%
Jun-13	Neuquén	domestic	131.4	3.0	3.0%
Jul-13	Entre Ríos	domestic	89.0	3.0	4.8%
Aug-13	Prov. de Buenos Aires	domestic	200.0	1.5	4.2%
Oct-13	Neuquén	domestic	198.6	5.0	3.9%
Oct-13	Chubut	domestic	220.0	5.8	4.0%
Oct-13	Mendoza	domestic	55.4	5.0	2.8%
Dec-13	Mendoza	domestic	69.9	5.0	2.8%
Dec-13	CABA	domestic	113.2	6.0	2.0%
Dec-13	Entre Ríos	domestic	63.9	3.0	2.3%
Total 2013			**1,552.0**		
Jan-14	CABA	domestic	146.8	6.0	2.0%
May-14	CABA	domestic	100.0	2.0	4.8%
Total Jan-May 2014			**246.8**		

Source: BCRA from Provinces data.

According to the latest information available, the set of subnational jurisdictions would have recorded an improvement in primary and financial results during 2013, mainly after the significant increase of tax revenue, both of national origin —federal tax revenue sharing, special laws and other automatic distribution funds— as well as originated in the provinces. So far in 2014, tax revenue of national origin received by the provinces recorded a higher expansion pace than in the second half of 2013, in line with the evolution of federal tax collection. In turn, budget transfers to subnational jurisdictions continued showing significant year-on-year rises during the first months of the year. This increase of transfers from the National government was reinforced by the momentum of tax revenue in the provinces (see Chart III.19).

As regards subnational financing, under the Federal Program of Debt Reduction of Argentine Provinces, an extension was established for the refinancing scheme of provincial debts to the National government with 17 provinces[55]. In addition, the subnational public debt stock was reduced upon appropriation of $10 billion of Advances of the National Treasury (ATN) to the provinces. These measures are intended to improve the provinces' debt positioning.

In recent months, only the City of Buenos Aires kept on issuing bonds in the domestic market, with instruments

[54] Resolution No. 26/2014 of the Secretariat of Finance authorized issues and placements for a higher nominal value as a whole: US$1.25 billion of Discount Bonds, US$800 million of BONAR X, US$400 million of BODEN 15, US$3.55 billion of BONAR 2024 and US$150 million of a National Treasury Bill as guarantee for Banco de la Nación Argentina in order to be used as a counter-guarantee of the joint and several guarantee to be granted by such Bank to REPSOL S.A. for the 3 first interest services of BONAR 2024.

[55] The extension was provided of the grace period for principal and interest of their debts up to June 30, which implies that jurisdictions will stop paying around $4 billion for services expiring in the first half of the year. Resolutions No. 36/2013 and No. 108/2014 of the Ministry of Economy and Public Finances.

whose payments of services are made in pesos according to the US dollar price[56] (dollar-linked bonds; see Table III.2).

[56] In May 2014, an issue stood out, since it was an instrument similar to the structure of what is usually considered a bond, consisting of a dollar-linked bill of the Treasury of the Province of Neuquén for US$24.7 million, with a 30-month term, with quarterly coupon payments contemplating an interest rate of 2.89% and partial amortizations as from 2016.

IV. Financial Sector

Summary

In the second half of 2013 and in early 2014, the financial intermediation activity with the private sector continued to be on the rise, despite a more moderate pace on the margin. Total bank loans to companies and households grew at a 29.4% year-on-year (y.o.y.) rate, in nominal terms, as of March 2014, mainly driven by the credit lines in pesos, which expanded 30.7% y.o.y. All credit segments in pesos recorded a positive performance in year-on-year terms.

In the first months of 2014, the growth pace of financing in pesos to the private sector was mainly led by loans to companies, which went up 30.9% y.o.y. in March, slightly above the expansion recorded by loans to households (28.2% y.o.y.). The Central Bank of Argentina continued to promote investment through the Credit Line for Productive Investment (LCIP) and the Bicentennial Productive Financing Program (PFPB). In the case of the LCIP, which provides access to companies for a longer term and at lower interest rates, as from its implementation to early 2014, an increasing relevance was given to loans for micro, small and medium-sized enterprises (MiPyMEs), reaching $58.1 billion in its first three tranches —second half of 2012, and first and second halves of 2013—, with an effective total disbursement of $56.77 billion. Regarding the tranche corresponding to the first half of 2014, based on preliminary information as of April, around 41% of the aggregate target for the period has already been fulfilled. With a view to keeping a steady financing flow of working capital and preserving the companies' payment process, the BCRA ordered that up to 10% of 2014 first half quota can be applied in March to discounted deferred payment checks to MiPyMEs and up to an additional 10% in April, May and June 2014 (up to 40% of the quota).

Total deposits (from the public and private sectors) went up 28% y.o.y. by the end of the first quarter of 2014, standing above the change observed one year ago. This performance was mainly due to deposits in pesos from the private sector, which expanded 27.8% y.o.y.; in turn, time deposits were the most dynamic component of this segment (35.5% y.o.y.), mainly driven by their increasing returns.

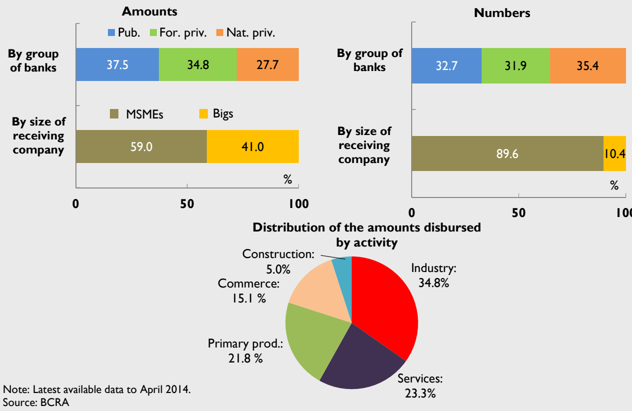
The financial system's leverage contracted in the first months of 2014, against the figures recorded by the end of 2013 and also in year-on-year terms. In March, netted assets of the ensemble of financial entities was eight times the net worth, 0.6 times less than a year ago. This evolution was driven by a relatively higher growth of net worth against the aggregate assets of the system. The financial system regulatory capital compliance totaled 13.3% of total risk-weighted assets in March 2014, and more than 90% was accounted for by Tier 1 capital compliance —the top-quality capital in terms of loss absorption.

The financial system ended 2013 with a 3.4% return on assets (ROA), with an increase of assets of 0.5 percentage points (p.p.) against 2012 year-end. At the beginning of 2014, financial entities recorded higher profitability levels, as a result of the balance sheet components related to exchange rate evolution. Thus, in the aggregate of the last 12 months up to March 2014, ROA stood at 4.3% (up 1.4 p.p. against the same period of 2013).

Chart IV.1

Credit Line for Productive Investment

Accumulated disbursements in the first three tranches - Share % in total

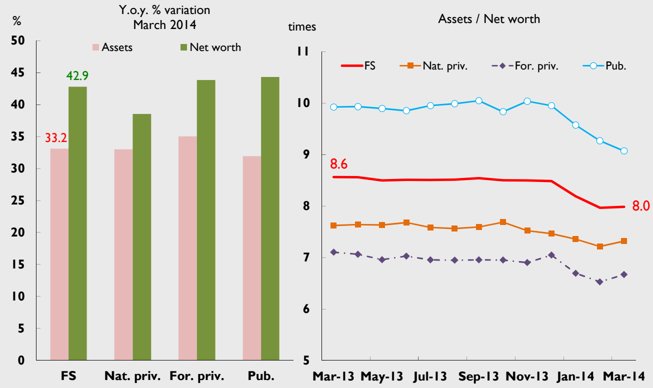


Note: Latest available data to April 2014.
Source: BCRA

Chart IV.2

Assets, Net Worth and Leverage

By group of banks

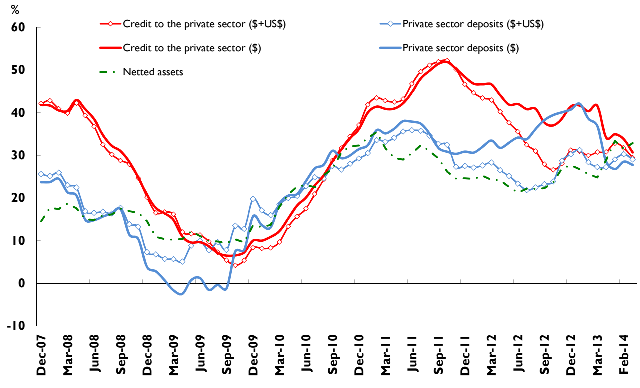


Source: BCRA

Chart IV.3

Financial Intermediation

Y.o.y. % change - Financial system



Source: BCRA

Table IV.1

Balance Sheet

Financial system

	As % of netted assets						Stock change*
					Change in p.p.		
	Dec-12	Mar-13	Dec-13	Mar-14	Dec-13 vs. Dec-12	Mar-14 vs. Mar-13	Last 12 months (%) Mar-14
Assets	100	100	100	100			
Liquid assets	21	19	20	20	-0.4	1.3	45
BCRA securities	9	11	9	11	-0.3	0.2	38
Total credit to the public sector	10	10	10	10	-0.4	-0.9	24
Total credit to the private sector	51	52	52	50	0.7	-2.5	29
Credit in $ to the private sector	47	49	49	47	1.9	-1.9	31
Credit in US$ to the private sector*	4	4	3	3	-1.2	-0.6	-28
Other assets	9	7	10	9	0.4	2.0	32
Liabilities + Net worth	100	100	100	100			
Public sector deposits	21	21	20	20	-0.9	-1.7	25
Private sector deposits	56	57	55	54	-0.7	-2.9	29
Outs. bonds, sub. debt and foreign lines of credits	2	2	2	3	0.2	0.5	70
Other liabilities	10	8	11	11	0.6	3.3	53
Net worth	11	12	12	12	0.8	0.6	43

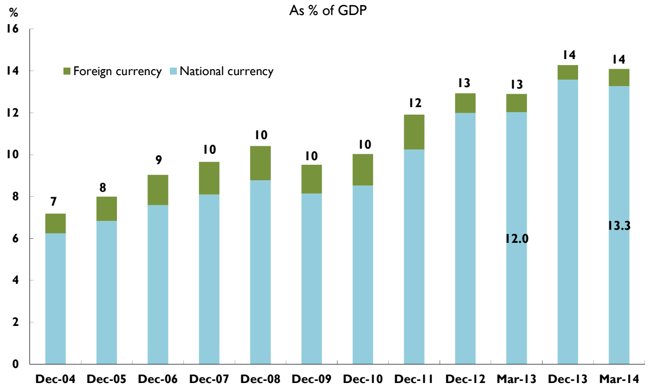
*Variations in currency of origin

Source: BCRA

Chart IV.4

Credit to Private Sector

As % of GDP



Note: estimated data from the new GDP series with base year 2004.
Source: BCRA and INDEC

IV.1 Financial Institutions[57]

IV.1.1 *Activity*

In 2013 and early 2014, the financial intermediation activity with the private sector continued to expand

Throughout 2013 and in early 2014, the financial intermediation levels with the private sector were on the rise, even though there was a slight deceleration on the margin (see Chart IV.3). Total lending to the private sector (in both domestic and foreign currency) grew 29.4% year-on-year (y.o.y.) by the end of the first quarter of 2014, while total deposits of this segment went up 29% y.o.y.

Netted assets[58] of the financial system expanded 28.9% y.o.y. in the aggregate of 2013, up 1.2 percentage points (p.p.) against the change observed in the same period of the year before. This upward trend continued in early 2014, with a rise of 32.9% y.o.y. in March 2014 (30.2%a. −annualized− by the end of the first quarter of the current year). Among the components making up the assets of the ensemble of banks, loans in pesos to companies and households exhibited the most remarkable relative year-on-year momentum in 2013, increasing their relative weight in total netted assets and accounting for 49% in December (see Table IV.1). In turn, lending in foreign currency lost share in the netted assets. As a result, by the end of 2013, total loans to the private sector accounted for 52% of the assets, exceeding the value observed by the end of 2012. In early 2014, due in part to seasonal factors, the growth pace of loans to the private sector lost ground slightly, reducing their share in the total stock of assets.

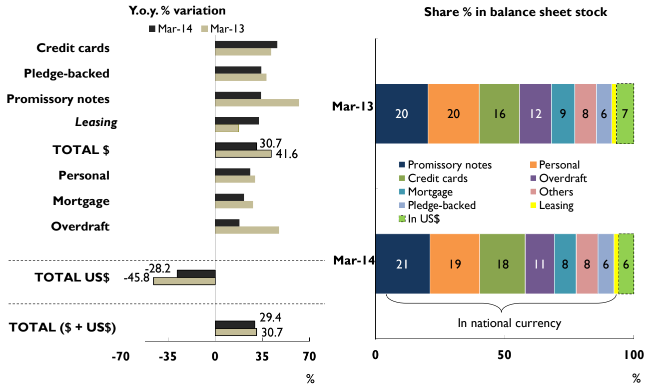
Lending to companies and households was once again driven by credit lines in pesos, which increased their share in terms of GDP

Bank loans continued to deepen in the economy. In March 2014, total lending to the private sector relative to GDP went up 1.2 p.p. against the same period of 2013 to a ratio of 14.1%[59]. This momentum was driven by the loans in pesos to households and companies, which accounted for 13.3% of GDP by the end of the first quarter, standing above the level reached one year ago (see Chart IV.4).

[57] The analysis of this section includes only the financial institutions regulated and supervised by the BCRA (Law No. 21,526).
[58] Assets are expressed net of accounting duplications from repo, forward and spot transactions to be settled.
[59] Data estimated on the basis of the new GDP series with base year 2004.

Chart IV.5

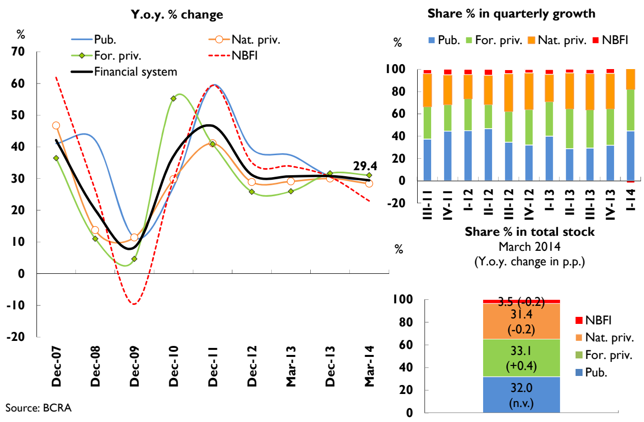
Credit to Private Sector in Currency of Origin



Note: Total includes balance sheet stock, including accrued interest and CER adjustment.
Source: BCRA

Chart IV.6

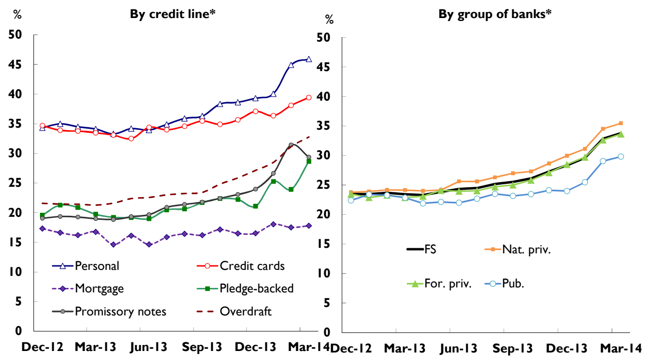
Credit to Private Sector by Group of Financial Entities



Source: BCRA

Chart IV.7

Lending Interest Rates in Pesos Operated Private Sector



*Average weighted by amount operated.
Source: BCRA

Following the trend observed in recent years, throughout 2013 and in early 2014, total credit expansion to the private sector was mainly accounted for by the segment in domestic currency. As a result, credit lines in pesos grew 30.7% y.o.y. in March 2014, standing slightly below the change recorded by the end of 2013 (34.1% y.o.y.) and also below the value observed one year ago (41.6% y.o.y.). All financing lines in domestic currency recorded a positive performance in this period, while credit cards, pledge-backed loans, documents and leasing were the lines with the highest relative y.o.y. expansion (see Chart IV.5). In turn, loans in foreign currency went down 28.2% y.o.y.[60] in March 2014, and their share in total lending to the private sector lost 1 p.p. against the same month of 2013 and accounted for only 6% of the total.

Within a framework where all groups of financial entities expanded their lending to the private sector, loans granted by public banks were the most dynamic in the first quarter of 2014

In early 2014, the ensemble of financial entities recorded year-on-year increases in their lending to the private sector, while a more moderate performance was observed on the margin. Foreign private banks and public banks recorded the highest relative year-on-year growth in March 2014, up 31.1% y.o.y. and 29.6% y.o.y., respectively. In particular, according to data corresponding to the first quarter of 2014, the loans granted by the public banks were the most dynamic in this period, contributing nearly 45% to the quarterly expansion of bank lending to companies and households (see Chart IV.6).

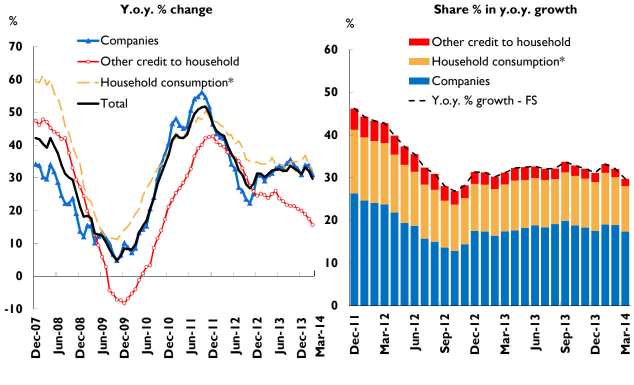
In 2013 and early 2014, the lending interest rates in pesos on the different credit lines for the private sector continued to go up moderately (see Chart IV.7). Particularly, the interest rates on overdrafts and personal loans recorded the highest relative year-on-year rises. Even though this performance was observed in the ensemble of banks, it is worth mentioning that the lending interest rates offered by the public banks stood below the average of the financial system in general. At the beginning of the second quarter of 2014, a decrease was observed in interest rates in pesos of all groups of banks and for most credit lines.

In the first months of 2014, the expansion pace of loans to companies surpassed that of loans to households

[60] Change observed in the currency of origin.

Chart IV.8

Total Credit to Private Sector by Type of Debtor



*Includes personal loans and financing through credit cards issued to families.
Source: BCRA

In line with the trend observed in 2013, the expansion pace of lending to the private sector was mainly accounted for by loans to companies at the beginning of 2014. They grew 30.9% y.o.y. in March this year, in line with the value recorded one year ago and slightly above the figure corresponding to lending to households (see Chart IV.8). As a result, loans to companies accounted for over 58% of the year-on-year increase of total financing to the private sector, thus increasing their share in total lending to up 56.6% (see Chart IV.9). This performance was mainly driven by foreign private banks and public banks, which increased the proportion of loans to companies within their total portfolios.

Loans to commercial and industrial companies were the most dynamic throughout 2013 and so far in 2014 and grew 42.7% y.o.y. and 33.8% y.o.y., respectively, in March 2014 (53.3%a. and 33.7%a. in the second half of 2013). As a result, the share of lending granted to both sectors went up in the total stock of credits given to companies, accounting for over 55% all together (see Chart IV.10). In turn, the loans granted for primary production exhibited a remarkable momentum in the first quarter of 2014 —they expanded 38.2%a. in this period—, accounting for almost 48% of the quarterly growth of total loans to companies.

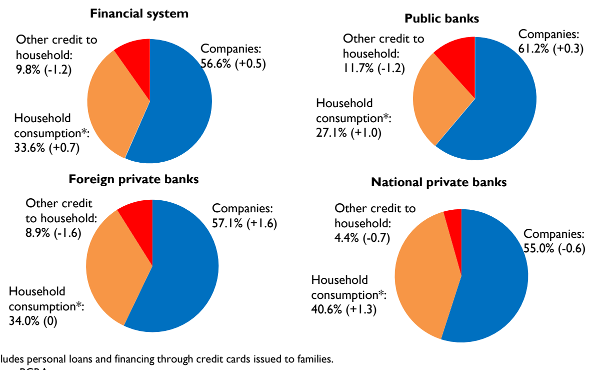
The expansion of bank loans to companies was driven by the different credit policies implemented by the BCRA, especially the lending provided to small and medium-sized enterprises

Chart IV.9

Total Credit to the Private Sector by Group of Banks

Share % in total stock - March 2014

(Y.o.y. change in p.p.)

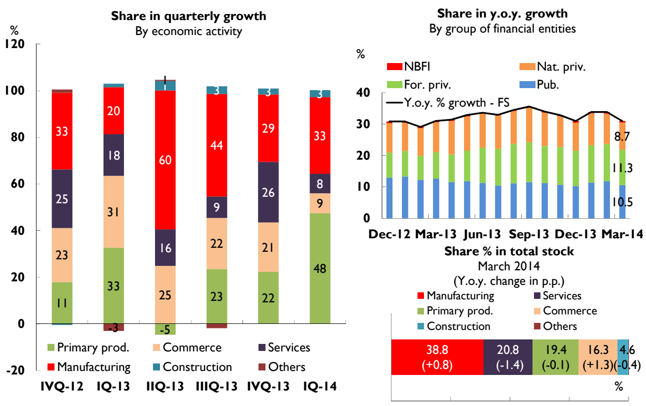


*Includes personal loans and financing through credit cards issued to families.
Source: BCRA

The evolution of financing to companies was driven in part by the different credit policies adopted by the Central Bank and aimed at promoting loans for productive investments. Within the framework of the "Credit Line for Productive Investment (LCIP)", which allows companies to access financing lines with longer terms and at lower interest rates, as from its implementation by mid-2012 and up to April 2014, through the first three tranches, loans were provided for around $58.1 billion, with a total effective disbursement of $56.77 billion. In particular, in 2013, credits for $35.39 billion in gross terms were granted to several companies, accounting for more than a half of the year-on-year increase of total lending to enterprises. It must be underlined that out of the total disbursement made in the first three tranches of LCIP, 59% was allocated to micro, small and medium-sized enterprises (MiPyMEs) (see Chart IV.1). In turn, 37.5% of the total disbursement was granted by public banks, followed by foreign private banks, with 34.8%. Taking into account the different productive sectors, loans to industry, to service providers and to primary production companies

Chart IV.10

Credit to Companies



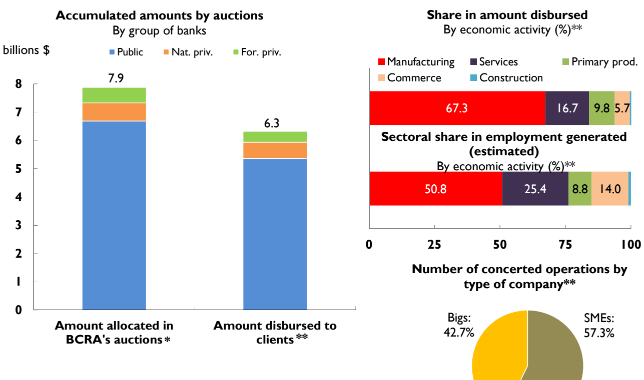
Source: BCRA

recorded the highest share in the total amount disbursed through LCIP.

With a view to continue deepening the positive effects of this tool, in June and December 2013, the BCRA renewed the quotas for the second half of 2013[61] and the first half of 2014[62]. Specifically, the entire quota corresponding to this last tranche —which would amount to approximately $23 billion— must be entirely allocated to MiPyMEs[63], allowing, as an exception, that half of the quota may be channeled through mortgages for individuals[64] and for large companies having specific productive projects[65]. In addition, as from mid-April 2014, other financing devoted to facilitate foreign trade transactions[66] may also be channeled through LCIP. This change adds up to the provision established by the end of February[67], pursuant to which a proportion of the quota corresponding to the fourth tranche of LCIP may be applied to the discount of deferred payment checks to MiPyMEs during March and April. Regarding the current tranche, with preliminary information as of April, approximately 41% of the target added for the period has been complied with.

Chart IV.11

Bicentenary Productive Financing Program



*Includes the 27 auctions.
**Amount disbursed up to 31/05/2014.
Source: BCRA

In addition, within the framework of the Bicentennial Productive Financing Program (PFPB)[68], throughout 2013 and early 2014, new auctions were performed by the BCRA among participating financial entities. In particular, in 2013, there were eight auctions for over $2 billion. In turn, in early 2014, a new auction of funds for $100 million was performed. Thus, from its launch in 2010 to late May 2014, around $7.88 billion in gross terms were granted through 27 auctions (see Chart IV.11). The amount effectively disbursed to multiple borrowing companies reaches $6.33 billion (nearly 85% corresponded to financing granted by public banks), and most transactions were allocated to MiPyMEs. Over 67% of the total amount granted was provided to the industrial sector, followed by service providers (16.7%) and primary production companies (9.8%).

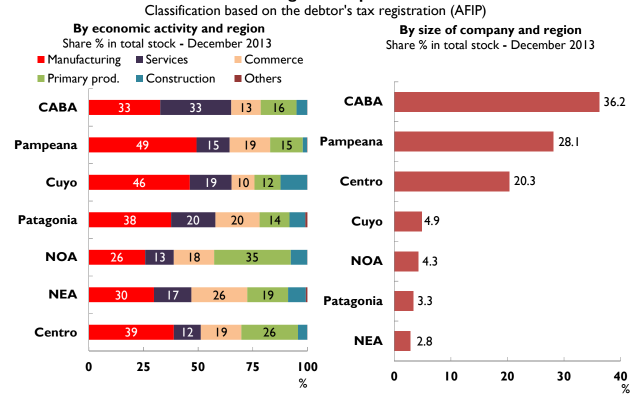
The measures driven by the BCRA promoted access to bank lending and improved financing conditions, particularly for relatively smaller companies. Thus, in

[61] Communication "A" 5449.
[62] Communication "A 5516.
[63] This fourth tranche of LCIP will have a fixed and up to 17.5% nominal annual interest rate for, at least, the first 36 months.
[64] In the case of mortgages granted through LCIP, the minimum term will be 10 years, with a fixed 17.5% nominal annual interest rate for the first year. As from the second year, if such rate were not applicable, a variable rate will be used that cannot exceed the Private Bank BADLAR in pesos plus 300 basis points.
[65] Particularly, it involves projects enlarging the productive capacity, an increase of formal and direct employment, import substitutions, development of export capacity, investments of capital goods and infrastructure works. In these cases, the interest rate will be freely agreed upon and the allocation of these financing processes requires the BCRA's prior authorization.
[66] Communication "A" 5570.
[67] Communication "A" 5554.
[68] Communication "A" 5089.

Chart IV.12

Financing to Companies

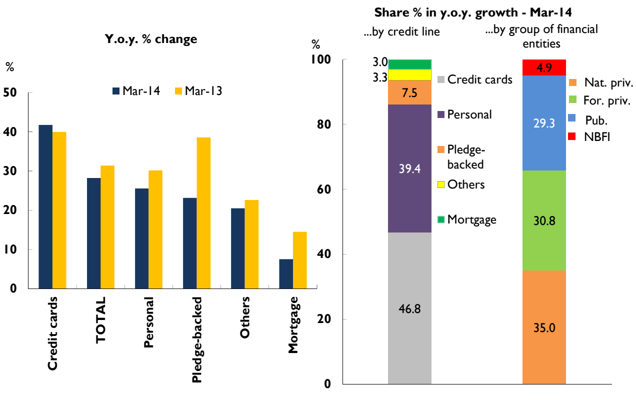
Classification based on the debtor's tax registration (AFIP)



Source: BCRA

Chart IV.13

Credit to Households



Source: BCRA

recent years, loans granted to MiPyMEs increased their share in total lending to legal persons, a trend that deepened in 2013 and in early 2014. As a result, by the end of the first quarter of 2014, over 48% of the amount corresponding to loans in pesos granted to legal persons were channeled to this segment, up 8.3 p.p. against the value observed one year ago. In turn, taking into account the total stock of loans provided to legal persons by the end of the second half of 2013, over 37% of such total corresponded to lending to MiPyMEs.

By the end of 2013, lending to the manufacturing sector continued to prevail in most regions of the country, in particular in the Pampas and the Central-West region (Cuyo) (see Chart IV.12). In turn, loans to companies showed a remarkable momentum in the City of Buenos Aires (CABA) and in the Pampas, two areas that concentrated over 64% of total financing to companies.

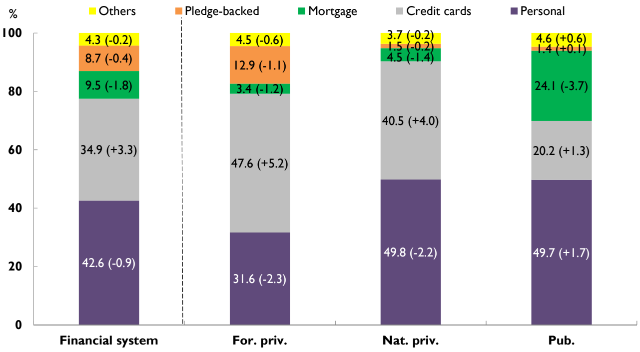
In turn, loans to households went up 28.2% y.o.y. in March 2014, standing slightly below the figures recorded one year ago and by the end of 2013 (see Chart IV.13). Among the multiple credit lines offered to families, credit cards exhibited a marked momentum throughout 2013 and so far in 2014, going up 41.8% y.o.y. in March 2014 —58.9%a. in the second half of 2013. As a result, on a year-on-year comparison basis, the share of this credit line in total loans to households went up 3.3 p.p., accounting for 34.9% (see Chart IV.14). This growth was mainly driven by foreign and national private banks. In turn, in the last 12 months, there was an increase in the share of personal loans in total lending to families granted by public banks. Almost two thirds of the year-on-year increase of financing to families may be attributed to private banks (both national and foreign).

Recently, the Central Bank, within the framework of the mandate and powers granted by its new Charter, implemented a set of measures devoted to continue driving credit for families under more favorable conditions, also improving the treatment given to non-financial providers of credit. It is worth mentioning that changes to the regulatory framework were implemented within a context where the financial system is showing low delinquency levels in its credit portfolio and high figures in terms of liquidity and solvency positions.

In the first place, the BCRA ordered that the interest rates applicable to personal and pledge-backed loans given by financial entities to natural persons that are not considered MiPyMEs cannot exceed the levels established in the regulation (Communication “A” 5590), which will result from multiplying the

Chart IV.14

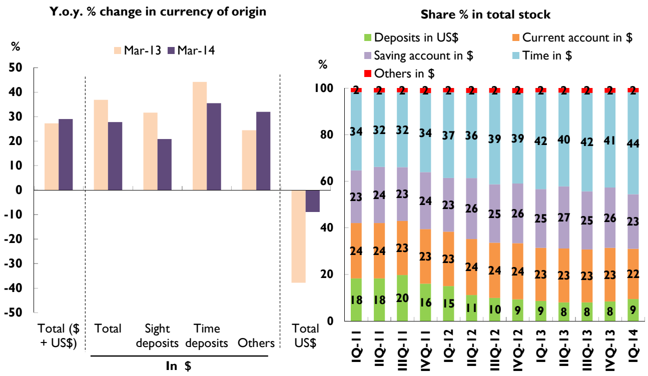
Credit to Households by Group of Banks
Share % in total stock - March 2014
(Y.o.y. change in p.p.)



Source: BCRA

Chart IV.15

Non-financial Private Sector Deposits in Financial System



Source: BCRA

"benchmark interest rate" by a multiplication factor. The "benchmark interest rate" will be based on the simple average of LEBACs cut-off rates, with a term around 90 days. In turn, the multiplication factor will stand between 1.25 and 2, depending on the type of loan and on the classification of the originating bank. In this respect, financial entities have been classified in two groups: Group I is made up of financial institutions operating as financial agents of governments at all levels and/or other entities concentrating at least 1% of total deposits of the non-financial private sector, and Group II includes all financial institutions not defined for Group I. The Central Bank will release each month the maximum interest rate for entities of Group I and Group II applicable to each type of loan (personal, pledged-backed and portfolio purchases)[69]. With this change in the regulatory framework, the BCRA enlarges the direct and indirect regulation on lending to natural persons.

In the second place, and within the framework of the regulation on "Protection of financial services users", the BCRA ordered that financial institutions and non-financial issuers of credit cards need a prior authorization by the BCRA to raise the cost of charges and commission fees of basic financial products and services (Communication "A" 5591). Likewise, it also defined in detail the financial services deemed as basic, such as maintenance fees for savings accounts, withdrawals from ATMs, replacement of debit cards and additional services related to deposit accounts for social security benefits, among others.

Additionally, and in order to improve and clarify the information available to financial services consumers with reference to the cost they have to face when borrowing money, the BCRA required that the Annual Percentage Rate (APR) be used in the future to express the Total Financial Cost of Loans (CFT), which must specify in detail the tax burden associated with the loan.

Lastly, a regulation was adopted for non-financial credit providers (PNFC) to be considered by the financial entities at the time a loan is granted (Communication "A" 5593). Within this framework, PNFCs have been defined as legal persons offering credit to individuals, such as mutuals, cooperatives, non-financial issuers of charge or credit cards, among other providers. The PNFCs must register with the BCRA to be considered credit providers by the financial entities. Institutions involved are required to submit detailed information about their shareholders and executive directors, as well

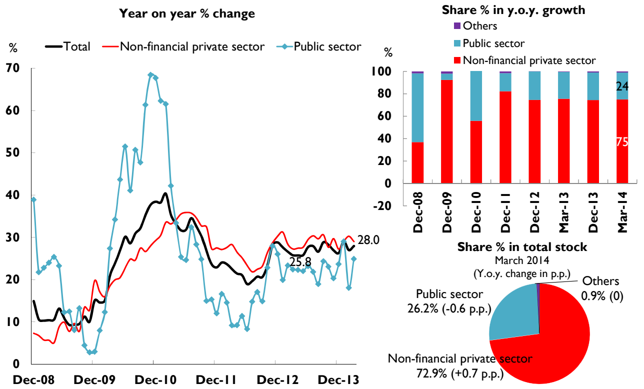
[69] Any financial entity that applies an interest rate above the limits reported by the BCRA will face an increase in the minimum cash requirement in pesos. This increase may be reversed depending on the loans granted to MiPyMEs, under the conditions set forth in LCIP and in so far as they are not allocated as application of this line.

as the credit rating of their loan takers, which will be included in the Debtors' Database of the BCRA, among other obligations.

Chart IV.16

Evolution of Total Deposits of Financial System

Includes peso and foreign currency deposits



Source: BCRA

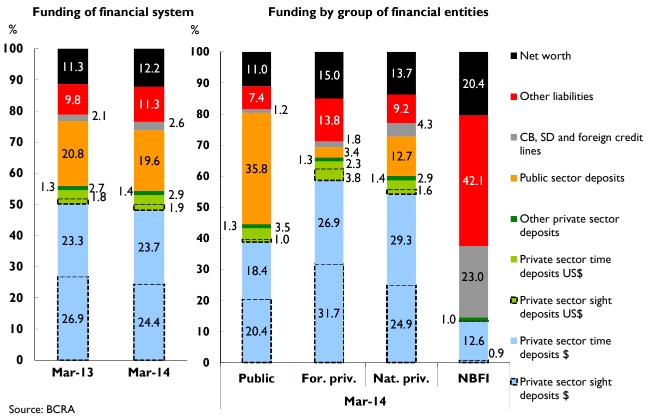
Throughout 2013 and in early 2014, time deposits in domestic currency from the private sector recorded the strongest momentum

In 2013, deposits in pesos from the private sector continued to expand, even though at a more moderate pace if compared to the year before. As a result, these deposits had grown 28.5% y.o.y. by the end of 2013. In the first quarter of 2014, deposits in pesos from the private sector expanded 18.3%a. (27.8% y.o.y.), standing slightly below the figures recorded in the same period of 2013.

At the beginning of the year, the performance of deposits in domestic currency from the private sector was driven by time deposits, which went up 35.5% y.o.y. in March 2014 (65.5%a. in the first three months of the year). Thus, an increase was observed in the relative weight of this segment in total deposits from the private sector, which accounted for nearly 44%, up 3 p.p. against December 2013 and 2 p.p. against the value recorded one year ago (see Chart IV.15). This momentum is closely related to the increased return of these deposits, driven in turn by the higher cut-off rates of LEBACs and NOBACs during this six-month period (see Chapter II).

Chart IV.17

Balance Sheet Composition



Source: BCRA

In turn, sight deposits in pesos grew 20.9% y.o.y. in March, below the value recorded in the same month of 2013. On the other hand, deposits in foreign currency fell 8.9% y.o.y.[70] in March 2014, which means that their drop pace has moderated if compared to the figures recorded one year ago. This slowdown was due, in part, to a series of measures implemented by the BCRA, aimed at attracting a higher proportion of the private sector resources in foreign currency towards the financial system. In particular, as from early 2014, the BCRA started to offer LEBACs in dollars[71] to the market, which may be underwritten by banks using the time deposits in foreign currency that they attract from the private sector.

As a result of the evolution of the different types of deposits, the private sector's total deposits expanded 29% y.o.y. in March 2014, up nearly 2 p.p. against the change recorded in the same month of 2013. The year-on-year increase of total deposits of companies and households was widespread in the ensemble of financial

[70] Taking into account variations in currency of origin.
[71] Communication "A" 5527.

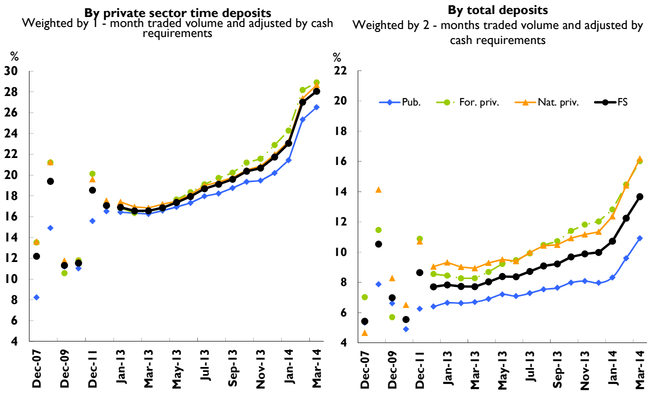
institutions, but national private banks and public banks recorded the highest relative momentum.

Total deposits from the public sector kept a positive performance throughout 2013 and in early 2014, reaching a 24.9% y.o.y. increase in the third month of the year, up 2.5 p.p. against the value reached in March 2013.

As a result, the balance sheet stock of total deposits of the public and private sectors went up 28% y.o.y. in March 2014, exceeding the growth rate recorded one year ago (see Chart IV.16). This performance was mainly driven by deposits from companies and households, which accounted for 75% of the year-on-year growth of total deposits. In particular, deposits in pesos from the private sector accounted for 66% of such increase.

Chart IV.18

Estimation of Average Funding Costs by Deposits in Pesos



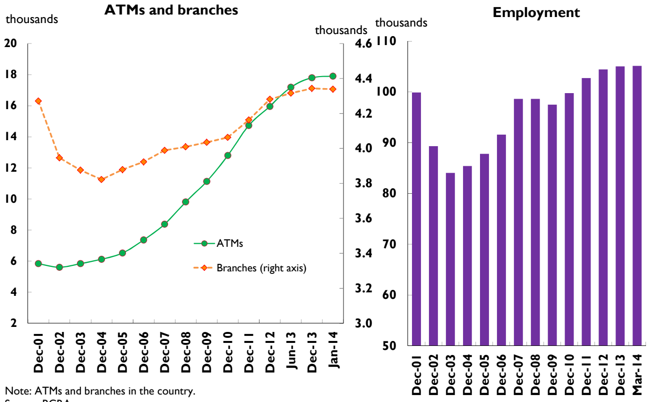
Source: BCRA

Throughout 2013 and in early 2014, deposits from companies and households in domestic currency continued to be the main funding source of the financial system

Private sector deposits and, to a lesser extent, public sector deposits continued to be the main funding source (liabilities plus net worth) of the ensemble of financial entities (see Chart IV.17). Thus, in March 2014, total deposits of companies and households accounted for 54.3% of total funding, slightly below the value recorded one year ago. In particular, the weight of private sector deposits in pesos accounted for 48.1% of total funding, standing slightly below the figure recorded in March 2013, mainly due to sight deposits in pesos. In turn, in year-on-year terms, the share of the private sector time deposits went up 0.4 p.p. in total funding, to 23.7% by the end of the first quarter of 2014, mainly driven by national and foreign private banks. Meanwhile, public sector total deposits accounted for 19.6% of total funding, down 1.2 p.p. against the value recorded one year ago. In particular, the share of public sector deposits corresponding to public banks fell almost 2 p.p. in total funding, down to 35.8% of the total.

Chart IV.19

Evolution of Financial System Operational Structure



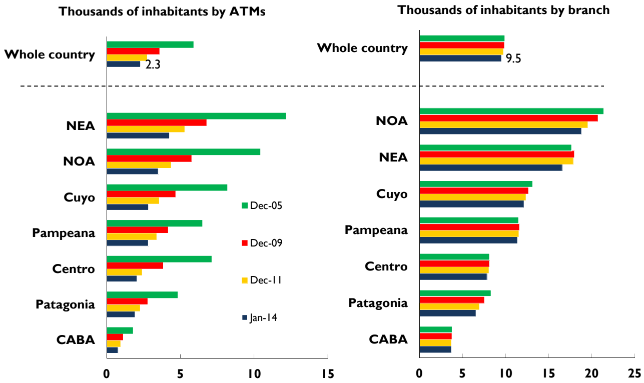
Note: ATMs and branches in the country.
Source: BCRA

Throughout 2013, the estimated funding cost[72] in terms of deposits in pesos went up in the ensemble of banks, a trend that deepened in early 2014 (see Chart IV.18). The higher funding cost in the first months of this year was driven mainly by the increase in the interest rates on private sector time deposits, mainly in national and foreign private banks.

[72] Both sight and time deposits in pesos from the private and public sectors are considered. The volume of deposits traded during two months is weighted and then adjusted on the basis of the minimum reserve requirements.

Chart IV.20

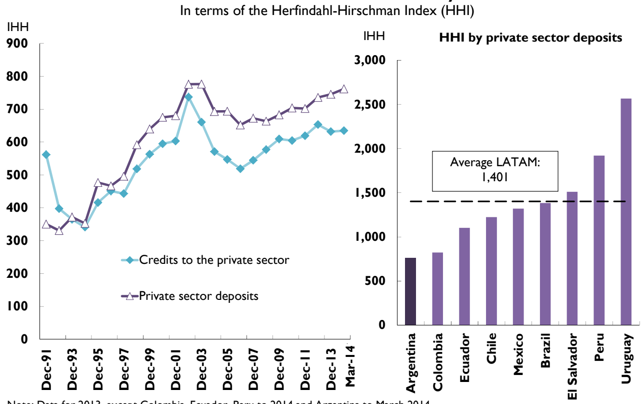
Regional Scope of the Financial System



Source: BCRA and INDEC

Chart IV.21

Concentration Level of the Financial System
In terms of the Herfindahl-Hirschman Index (HHI)



Note: Data for 2013, except Colombia, Ecuador, Peru to 2014 and Argentina to March 2014.
Source: Own elaboration based on Cental Banks and BCRA data.

In 2013, financial entities improved fund taking through corporate bonds (ON) and short-term securities (VCP). Thus, throughout 2013, issues of ON and VCP for a total amount of $8.8 billion were made, up 75% against 2012. In early 2014, the ensemble of financial entities continued issuing these instruments, all of them in domestic currency, for a total of $1.73 billion in the first three months of this year. As a result of this momentum, the share of the stock of corporate bonds, subordinated debt (OS) and foreign credit lines in the financial system went up in total assets and accounted for 3% in March 2014, standing at a slightly higher level than a year ago (see Table IV.1).

The infrastructure for the provision of financial services continued expanding throughout the country

The operating infrastructure of the financial sector continued to expand during 2013 and in early 2014 (see Chart IV.19). As a result, the number of bank branches went up 1.2% y.o.y. in January 2014 (reaching a total of 4,339 branches throughout the country), while the number of ATMs and self-service ATMs went up 8% y.o.y. (reaching a total of 17,902 units). This remarkable momentum was mainly driven by foreign private banks, even though the number of ATMs and branches increased in all groups of banks. In turn, staffing at the ensemble of banks continued to expand in early 2014, mainly in national private banks.

As a result of the regulations in force for the opening of new branches[73], aimed at reducing the disparity in financial infrastructure among the different areas of the country, the BCRA authorized in 2013 the opening of 28 new branches in locations with fewer banking services (14 in each half of 2013). Thus, in the last three years, 116 new branches have been authorized to operate in regions with fewer financial services available, accounting for over 41% of the expansion in the number of branches during this period.

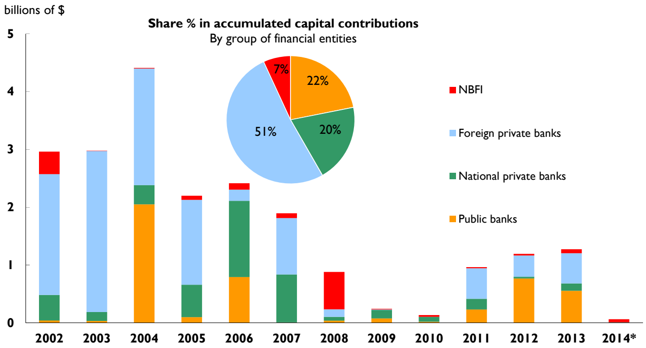
Within a context of infrastructure development for the provision of financial services throughout the country, a gradual reduction was observed in recent years in the indicators measuring the number of inhabitants per branch and per ATM in the areas with fewer banking services: the North-West (NOA) and North-East (NEA) of Argentina (see Chart IV.20). Therefore, on average, the number of inhabitants-to-bank branch ratio stood at 9,500, while the number of individuals per ATM went down to 2,300, standing below the figures recorded in

[73] Communication “A” 5168 and Communication “A” 5355.

Chart IV.22

Capital Contributions of Financial Entities

2002-2014



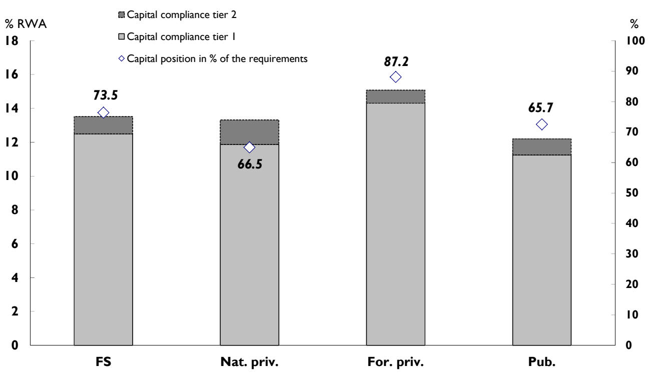
*to March

Source: BCRA

Chart IV.23

Capital Compliance and Excess of the Requirement (Position)

March 2014



Source: BCRA

previous years and also below the figure of other economies of the region.

The financial system concentration stood at limited levels throughout 2013 and in early 2014. The Herfindahl-Hirschman Index measured on loans went down in the last year, while that measured on deposits went up slightly. Nevertheless, the concentration levels of the domestic banking market continued to stand below those of other countries of the region (see Chart IV.21).

IV.1.2 Capital position

The growth pace of the financial system net worth accelerated in recent months, resulting in a reduction of the aggregate leverage level

The consolidated financial system net worth went up 35% throughout 2013, and its growth pace accelerated in the second half of 2013 —40.8%a.— and in the first quarter of 2014. This growth was mainly boosted by book profits accrued and, to a lesser extent, by new capital contributions. The capitalizations of the ensemble of banks amounted to almost $1.28 billion in 2013, which were channeled in a similar proportion to foreign private banks and public banks (see Chart IV.22). Likewise, in the first quarter of 2014, the ensemble of financial institutions received capital contributions for $62 million, mainly channeled to non-banking financial entities. In turn, in 2013, some financial institutions distributed dividends for a total amount of $222 million.

Within this framework, the financial system leverage level shrank so far in 2014, against both the end of 2013 and in year-on-year terms, since the relative growth of net worth exceeded assets expansion at aggregate level. A similar evolution was observed in all groups of banks (see Chart IV.2). As a result, the netted assets of the ensemble of banks accounted for eight times the net worth in March, 0.6 times less than a year ago. It is worth mentioning that these figures are lower than those observed in both developed and emerging economies.

The financial system continues to exhibit a surplus in the capital position

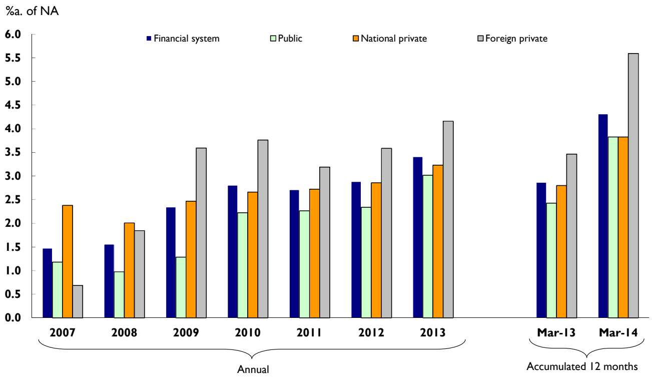
The financial system regulatory capital compliance stood at 13.3% of total risk-weighted assets (RWA) in March 2014, down 0.3 against the figure recorded by the end of 2013. In turn, as of March 2014, Tier 1 capital compliance[74] —top-quality capital in terms of its

[74] Defined as basic net worth (regular and additional capital) net of deductible accounts. See Communication "A" 5369.

Chart IV.24

Profitability by Group of Banks

As % of netted assets



Source: BCRA

Table IV.2

Profitability Structure: Financial System

Annualized indicators as % average netted assets

	2010	2011	2012	2013	Mar-13*	Mar-14*
Financial margin	8.5	8.0	9.2	10.3	9.3	11.8
Net interest income	4.3	4.6	5.7	5.9	5.7	5.9
CER and CVS adjustments	0.6	0.3	0.3	0.3	0.3	0.3
Gains on securities	3.2	2.6	2.6	2.6	2.6	2.7
Foreign exchange price adjustments	0.5	0.6	0.6	1.3	0.7	2.2
Other financial income	-0.1	0.0	0.0	0.3	0.0	0.7
Service income margin	3.8	3.9	4.2	4.3	4.2	4.2
Operating costs	-6.9	-6.7	-7.0	-7.1	-7.0	-7.1
Loan loss provision	-0.8	-0.7	-0.9	-1.1	-1.0	-1.1
Effects of the 2001-2002 crisis (**)	-0.2	-0.1	-0.1	-0.1	-0.1	-0.1
Tax charges	-1.0	-1.1	-1.3	-1.6	-1.4	-1.7
Other	0.5	0.5	0.4	0.3	0.3	0.3
Total results before income taxes	4.0	3.9	4.3	5.0	4.4	6.3
Income tax	-1.2	-1.2	-1.5	-1.6	-1.5	-2.0
ROA	**2.8**	**2.7**	**2.9**	**3.4**	**2.9**	**4.3**
Adjusted ROA (***)	**3.0**	**2.8**	**3.0**	**3.5**	**3.0**	**4.4**
ROE	24.4	25.3	25.7	29.5	25.4	36.5
ROE (before income tax)	34.5	36.5	38.8	43.7	38.6	53.5

(*) Accumulated 12 months.

(**) Includes amortization payments for court-ordered and adjustment of public sector assets.

(**) Excluding the effects of the 2001-2002 crisis.

Source: BCRA

capacity for loss absorption— accounted for 12.4% of the RWAs, over 90% of total compliance. In turn, the capital compliance in excess of the regulatory requirement (capital position) stood at 73.7% as of March 2014[75] (see Chart IV.23), accumulating a year-on-year increase of 8.1 p.p. All groups of banks have exhibited a surplus in their capital position.

In the last three months, banks' book profits were on the rise, mainly driven by the financial margin

In 2013, the financial system book profits reached $29.14 billion, equivalent to a return on assets (ROA) of 3.4%, up 0.5 p.p. against 2012. All groups of banks recorded a year-on-year profit growth (see Chart IV.24). At the beginning of 2014, there was an increase in the profitability levels of financial entities. Thus, in the aggregate of the last 12 months up to March 2014, the ROA of the ensemble of banks stood at 4.3% (see Table IV.2), up 1.4 p.p. against the same period up to March 2013. The increase of benefits in such period was widespread among the different groups of entities.

Throughout 2013, banks' financial margin stood at 10.3% of assets, up 1.1 p.p. against the value accumulated throughout 2012 (see Chart IV.25). This improvement was mainly due to profits accrued in the items related to the evolution of the exchange rate (exchange rate differences and adjustments for forward transactions in foreign currency) and, to a lesser extent, to results from interest. Even though the accumulated financial margin of all groups of banks went up in year-on-year terms, the highest relative increase was recorded by foreign private banks. A similar performance was observed in the aggregate of 12 months up to March 2014; the financial margin of the ensemble of banks went up 2.5 p.p. of assets against the same period of 2013, standing at 11.8%.

Net income from interest continued to be one of the main sources of income of the financial system

Results from interest reached 5.9% of assets throughout 2013, up 0.2 p.p. against the year before, standing at the at the same level as in the aggregate of 12 months up to March 2014. Even though all groups of banks recorded a higher income from interest against 2012, foreign private banks were the most dynamic.

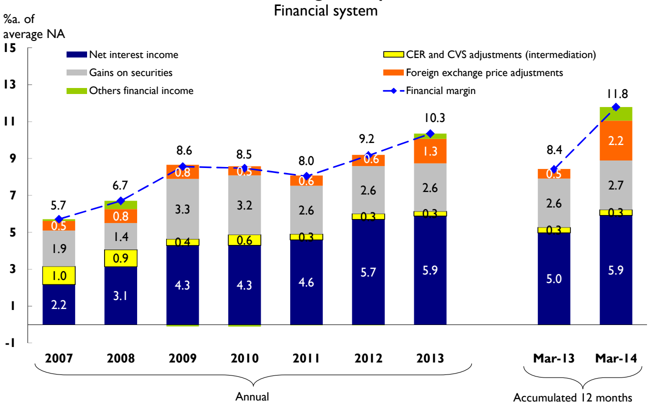
Given the banks' positive mismatching in foreign currency (see Chapter V) and the nominal peso-dollar

[75] As from early 2014, financial entities have to consider the requirement inherent to the month, while from February to December 2013, they had to take into account the higher requirement, by comparing that observed in January 2013 to that of the month. Communication "A" 5369, item 9.

Chart IV.25

Financial Margin Composition

Financial system



Source: BCRA

Table IV.3

Profitability Structure by Type of Banks

March 2014 (*) - Annualized indicators as % average netted assets

	Private banks			Public banks	NBFI
	Total	Nat.	For.		
Financial margin	13.4	11.9	14.8	9.8	12.3
Net interest income	7.7	7.2	8.3	3.3	11.4
CER and CVS adjustment	0.1	0.0	0.2	0.6	0.0
Gains on securities	2.0	2.6	1.4	3.6	0.4
Foreign exchange price adjustements	2.1	1.2	3.1	2.3	0.5
Other financial income	1.4	1.0	1.8	-0.1	0.0
Service income margin	5.5	5.4	5.6	2.5	7.4
Operating costs	-8.5	-8.7	-8.4	-5.2	-8.7
Loan loss provisions	-1.4	-1.2	-1.5	-0.7	-2.9
Efects of the 2001-2002 crisis (**)	0.0	0.0	0.0	-0.1	0.0
Tax charges	-2.3	-2.3	-2.2	-0.9	-2.6
Others	0.5	0.7	0.3	0.0	0.9
Monetary	0.0	0.0	0.0	0.0	0.9
Total result before income tax	7.2	5.7	8.6	5.3	6.4
Income tax	-2.4	-1.8	-3.1	-1.4	-2.5
ROA	**4.7**	**3.8**	**5.6**	**3.8**	**3.9**
Adjusted ROA (***)	**4.7**	**3.8**	**5.6**	**4.0**	**3.9**
ROE	36.3	32.9	39.0	38.5	19.7
ROE (before income tax)	55.1	48.6	60.4	52.9	32.2

(*) Accumulated 12 months.

(**) Includes amortization payments for court-ordered and adjustment of public sector assets.

(***) Excluding the effects of the 2001-2002 crisis.

Source: BCRA

exchange rate, the weighting of profits from exchange rate differences rose in the income statement of banks. This income went up 0.7 p.p. of assets in 2013 against 2012, and foreign private and public banks recorded the highest weighting. Evidence of this momentum continued to be seen in the aggregate of 12 months up to March 2014 (see Table IV.3). A similar effect was observed in the other financial results item, mainly through an increase in the profits derived from adjustments to forward transactions in foreign currency.

Income derived from securities rose 0.6 p.p. of assets in the second half of the year —against the figure recorded in the first half— closing 2013 at 2.6%, in line with the level reached the year before and slightly below the figure recorded in the aggregate of 12 months up to March 2014 (2.7%). From a systemic perspective, the slight increase of this item in public banks was virtually offset by the reduction observed in private banks.

Throughout 2013, net income from CER-adjusted items stood steady and at low levels for the third consecutive year, around 0.3% of assets. A breakdown analysis per group of banks reveals that public banks have been the most dynamic in terms of this income, according to their income statement. The low weighting of this income in the income statement of the financial system is consistent with the limited mismatching between assets and liabilities adjusted by this coefficient.

Results from services continued to be one of the main sources of income of the financial sector

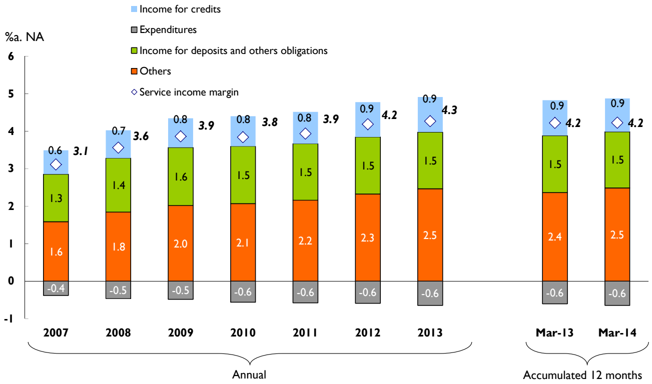
Net income from services of the financial system closed at around 4.2% of assets in the aggregate of 12 months up to March 2014 (see Chart IV.26), in line with the value recorded one year ago. This source of income is still more relevant in private banks (reaching 5.6% and 5.4% in the national and foreign private banks, respectively) and, to a lesser extent, in public banks (2.5%).

In terms of the main profitability sources that make up the income statement of the financial system, the highest volatile net income showed the highest relative momentum throughout 2013. In this sense, even though results from securities went down, the share of exchange rate differences related to the evolution of the nominal exchange rate went up; this means that the share of the most volatile items reached 27% of the sector's total resources. On the opposite front, the net income considered more stable, i.e. income from interest and services, lost share, going down to 69% of the total (see Chart IV.27).

Chart IV.26

Service Income Margin

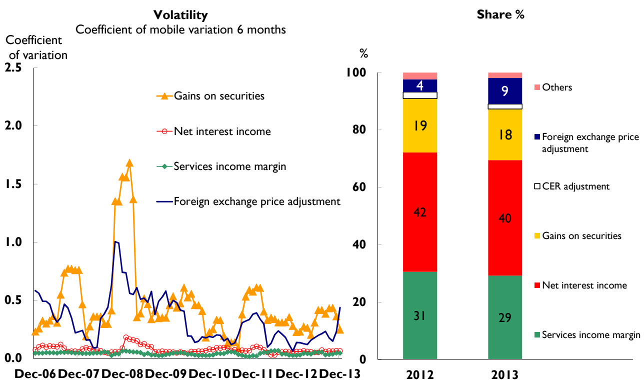
As % of netted assets



Source: BCRA

Chart IV.27

Major Sources of Financial System Income



Source: BCRA

Expenditures for operating costs and loan loss provisions went up slightly along the year

Operating costs stood at 7.1% of assets in 2013, going up slightly against the figure recorded in 2012, in line with the aggregate of 12 months up to March 2014 (see Chart IV.28). This year-on-year increase was mainly driven by the performance of private banks, both national and foreign. At system level, the increase in expenses was largely due to staff-related items (wages and social security contributions), which account for over 60% of total operating costs in the aggregate of the financial entities.

Loan loss provisions of the financial system amounted to 1.1% of assets in the aggregate of 2013, recording a slight increase against the same period of 2012 and standing at the same level as in the aggregate of 12 months up to March 2014. This performance was mainly driven by foreign private banks (see Chart IV.29).

As an indicator of the positive evolution of the operating efficiency of the financial system, it was observed that covering operating expenses with income from services and interest (net of loan loss provisions) was consistent with what had happened the year before, standing at 128% for the ensemble of institutions. The year-on-year increase of this indicator was largely seen in public banks, even though private banks have shown a relatively higher value.

In 2013, tax-related expenditures (income tax and other taxes) amounted to 3.2% of assets for the financial system, up 0.5 p.p. against last year. These expenses went up both in private and public banks, but the former recorded a higher weighting. In turn, adjustments for loans to the public sector and the amortization of the court ordered releases (an effect of the 2001-2002 crisis) accounted all together for only 0.1% of assets, in line with 2012 year-end closing.

IV.2 Institutional Investors

The net worth managed by institutional investors continued to be on the rise

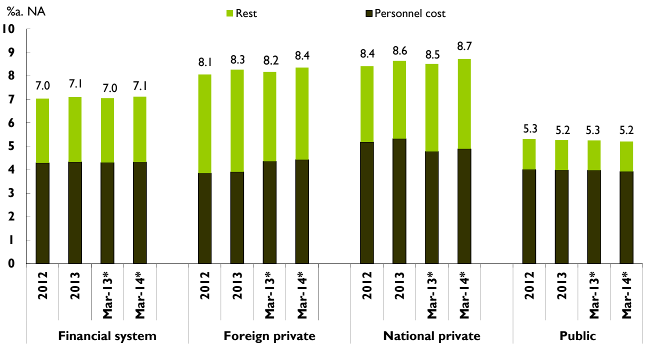
Taking into account the Sustainability Guarantee Fund (FGS), insurance companies and mutual funds (FCI), the aggregate portfolio managed by domestic institutional investors amounted to almost $502 billion[76], equivalent to 14% of GDP, by the end of 2013. This amount

[76] Latest information available in aggregate terms. The amount corresponds to the addition of unconsolidated portfolios.

Chart IV.28

Operating Costs by Group of Banks

As % of netted assets



*accumulated 12 months
Source: BCRA

represented a 38% year-on-year increase, with a ratio expansion of almost 2 p.p. in GDP terms in the same period. Regarding the composition of this aggregate portfolio, fixed income instruments continued to be the main item, accounting for more than 59% of the total, standing almost unchanged against late 2012.

The portfolio of the Sustainability Guarantee Fund (FGS) —leading institutional investor— improved markedly in the second half of 2013, up to a total amount of $329.48 billion, thus closing 2013 with an annual rise of 35%[77] (see Table IV.4). Sovereign and corporate bonds[78] continued to exhibit the highest share in total assets (65%), growing 35% throughout the year, mainly due to the increases recorded in prices[79]. In turn, the share of productive and infrastructure projects was also remarkable (14%), and went up 40% in 2013[80]. Regarding stocks, even though they still accounted for less than 10% of the portfolio, they were the item with the highest relative growth in 2013 (75%), due to the improvements observed in the prices of the stock market along the year (see Chapter 2). Lastly, unlike what had happened the year before, when there was an unwinding of positions in time deposits, the funds meant for this item went up 7% in 2013, reaching a weighting of 5% relative to the portfolio total amount.

Chart IV.29

Loan Loss Provisions by Group of Banks

As % of netted assets

*accumulated 12 months
Source: BCRA

These trends continued to prevail in the first quarter of 2014[81], when the FGS aggregate portfolio went up an additional 17% and exceeded $383.88 billion. In the first three months of the year, the increase was mainly explained by the rise in sovereign and corporate bond amounts, the weighting of which continued growing and accounted for 67% of the total[82]. An increase was also observed, even though for more limited amounts, in items such as stocks and productive and infrastructure projects and, to a lesser extent, also in cash holdings. The amount corresponding to productive and infrastructure projects exceeded $50 billion, and the most relevant projects were related to energy, housing and road infrastructure (see Chart IV.30). Lastly, and unlike the figures recorded in 2013, a decline was observed in the stock of FGS time deposits in early 2014. Thus, and in line with the performance observed in 2013, the share of FGS time deposits in the financial system total continued to fall in early 2014.

[77] This rise includes the transfer of ANSES surplus for $2 billion made in 2013.
[78] Made up mainly by sovereign bonds. Regarding corporate bonds, in 2013, the FGS participated in YPF debt issues, but for lower amounts than those acquired in 2012.
[79] According to data submitted before the Congress Two-House Committee, in 2013 –up to and including October— FGS financed the Treasury for around $4 billion in net terms (this calculation does not include the repurchase of sovereign bonds by the Treasury).
[80] In this segment, the Bicentennial Credit For Housing Program for Single and Family Housing Unit (Pro.Cre.Ar) stood out along the year, standing at $8.7 billion by the end of 2013.
[81] Latest information available.
[82] The main bonds held in FGS portfolio as of March 2014 were the Cuasipar in pesos, the Discount in dollars under Argentine legislation and the 2018 9% Bond in dollars. Other bonds with a significant weighting were bonds in pesos maturing in 2018 and 2019.

Table IV.4

Evolution of Social Security Fund (FGS) Investment Portfolio

in millions of $

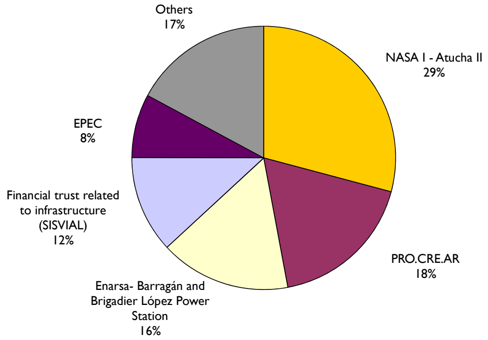
	Dec-11	Dec-12	Mar-13	Sep-13	Dec-13	Mar-14	Var. 2012 (%)	Var. 2013 (%)	Var. since Dec-13 (%)
Total FGS	**199,490**	**244,799**	**264,861**	**306,257**	**329,472**	**383,883**	123%	35%	17%
Cash, sight deposits and other*	14,356	22,631	27,632	26,518	25,378	27,678	158%	12%	9%
Time deposits	23,437	14,908	15,042	14,541	15,996	15,730	64%	7%	-2%
Corporate bonds and sovereign government bonds	117,409	159,434	170,587	200,976	215,584	256,323	136%	35%	19%
Stocks	16,462	15,905	19,370	26,278	27,838	33,842	97%	75%	22%
Productive projects and infraestructure related instruments	27,827	31,921	32,230	37,944	44,677	50,310	115%	40%	13%

(*) "Other" includes Mutual Funds, Direct Investment Funds, Foreign Securities, Futures and Options, among others.

Source: FGS- ANSeS

Chart IV.30

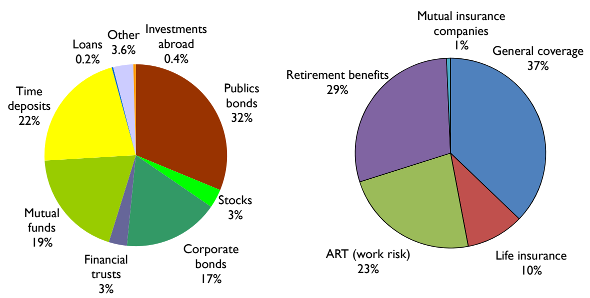
FGS - Productive and Infrastructure Investment
March 2014



Source: FGS - ANSES

Chart IV.31

Breakdown of Insurance Companies Portfolio
Data to December 2013, total $99,7 billions



Note: Foreign investment includes Government and corporates bonds, stocks, mutual funds, time deposits and other equity investments.
Source: BCRA based on Superintendencia de Seguros de la Nación

In turn, the investment portfolio of insurance companies amounted to almost $99.74 billion by the end of 2013[83], up 33% along the year. This improvement in the portfolio was mainly due to the performance of corporate bonds, which would be closely related to the fulfillment of Resolution No. 37,163/12 (as amended) of the National Insurance Superintendence[84]. Thus, portfolio corporate bonds went up almost 120%, and their share in the portfolio went from almost 10% to around 17% in this period (see Chart IV.31). Also remarkable was the increase in mutual funds' unit share holdings (with a rise in their weighting from 15% to 19%) and, to a lesser extent, of the other investments item (the share of which went up from 1% to 4% of the total). In turn, sovereign bonds and time deposits recorded increases in the amounts but, since the rises were not significant, their share in the total dropped (nevertheless, they are still the items with the highest weight on total investments). In the opposite direction, the investment in stocks continued to fall, and its weighting went down to less than 1%[85].

After growing over 60% in 2013, the net worth managed by mutual funds (FCI) went up 27% in the first five months of the year to a level around $92.65 billion by the end of May. So far in 2014, increases were observed in all types of funds, even though fixed income funds stood out in terms of amounts. So far in 2014, the highest increases were recorded by stocks (56%), infrastructure (55%) and fixed income funds (34%). Despite this figures, the share of fixed income funds went up to 49% of the total (from 46% by the end of 2013).

[83] Latest information available.
[84] Regulation known as "paragraph k".
[85] Insurance companies also have unlisted stocks. The aggregate of stocks accounts for 3% of the portfolio.

V. Financial System Risks

Summary

In a context of sound liquidity and solvency conditions where the financial system is evolving, slight changes were observed in the sector's risk map in late 2013 and early 2014. Regarding liquidity, indicators evidencing exposure to this risk showed minor changes: on the one hand, relatively shorter term liabilities gained relevance in aggregate funding; on the other hand, the concentration level of deposits went down. Institutions kept ample coverage against this risk evidencing a marginal rise.

Financial system exposure to the private sector increased throughout 2013, recording a minor drop in the first quarter of 2014 against December 2013, a trend in line with the lower growth pace observed in lending. Payment capacity held by the productive sector and households was favored by the prevailing reduced indebtedness levels. Collective bargaining agreements and transfers to lower-income sectors have contributed to maintaining households' income. Within this framework, lending non-performance has remained within a range of low values. The financial system continued evidencing sound coverage of the non-performing portfolio through provisions at the start of 2014.

The financial system has been enhancing its position to face potential losses resulting from failures in processes, staff and systems or from external events. Progress was observed in early 2014 in relation to compliance with the schedule set for the gradual implementation of minimum capital requirements for operational risks. Such schedule will be completed by the end of this year.

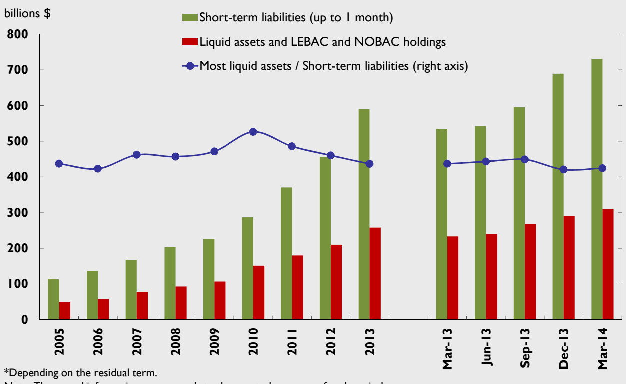
The higher share of financial assets in foreign currency marked-to-market rate in financial institutions' balance sheets, coupled with higher volatility in their prices, led to a rise in the market risk undertaken by banks. However, this risk keeps a reduced relative significance level in total exposures.

Considering the positive mismatching of foreign currency recorded by the ensemble of banks in 2013, with potential adverse effects on financial stability, the BCRA ordered regulatory amendments in early 2014. Particularly, it established, once again, the positive limit to the net global position in foreign currency of every institution, and it also set a maximum limit for the positive futures net position in foreign currency. This decision allowed reducing the currency risk undertaken by banks whilst moderating fluctuations in the foreign exchange market.

Banks slightly reduced their exposure to the interest rate risk that stems from their intermediation activity.

Chart V.1

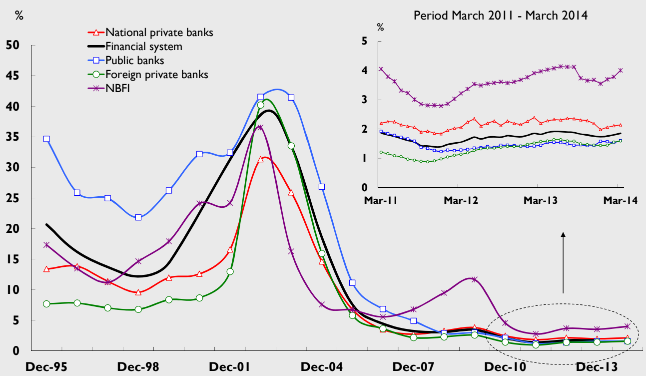
Most Liquid Assets in Terms of Short Term Liabilities*



*Depending on the residual term.
Note: The annual information corresponds to the quarterly average of each period.
Source: BCRA

Chart V.2

Private Sector Non-performing Financing
Non-performing portfolio / Total financing (%)



Source: BCRA

V.1 Liquidity Risk

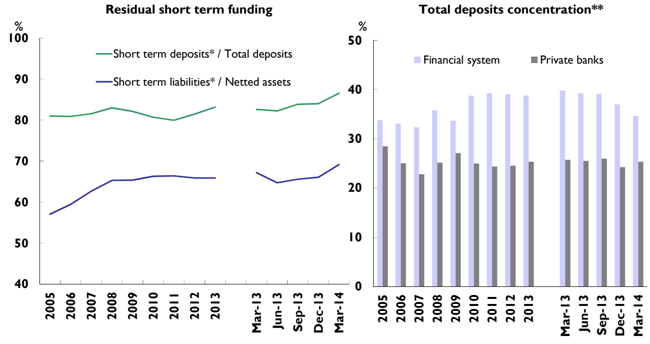
Financial institutions still evidence moderate exposure to liquidity risk

Indicators of exposure to liquidity risk undertaken by the financial system exhibited minor changes in the past few quarters. On the one hand, a rise in the share of short-term liabilities in total funding of the ensemble of banks was observed at the beginning of the year and throughout 2013 (see Chart V.3). On the other hand, concentration levels of total deposits went down in the past few quarters for the aggregate financial entities, a factor that moderates exposure to this risk.

Chart V.3

Liquidity Risk Exposure Indicators

Financial system



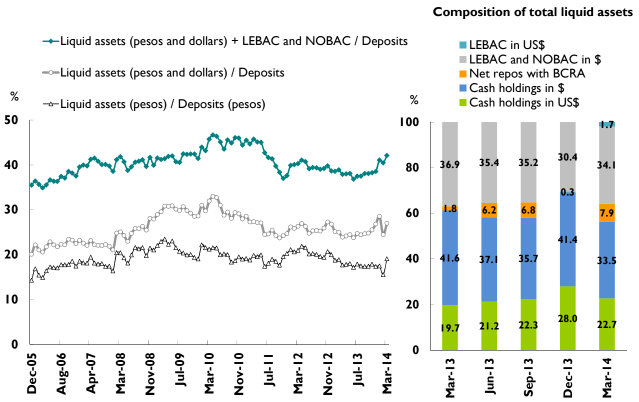
*Residual term less than 1 month. **Balance of the 110 largest customers of each entity as a percentage of total deposits.
Note: The annual information corresponds to the quarterly average of each period.
Source: BCRA

Banks' coverage against liquidity risk continues to stand at sizable levels

Liquid assets stood at 42.4% of short-term liabilities in March 2014, evidencing a minor hike against the end of 2013 (see Chart V.1). This liquidity risk coverage indicator stood slightly below the average level recorded in 2013. Similarly, liquidity indicators that only take into account items in pesos and those that include domestic and foreign currency increased in the first quarter of 2014 (see Chart V.4). The broad liquidity ratio, which includes LEBAC and NOBAC holdings in pesos and in foreign currency not related to repo transactions, also posted positive changes that were more significant: the indicator totaled 42.1% of deposits by the end of the first quarter of 2014, 3.6 p.p. above the figure recorded at the end of 2013 and up 4.2 p.p. in y.o.y. terms. All groups of institutions raised their liquidity levels (see Chart V.5).

Chart V.4

Financial System Liquidity



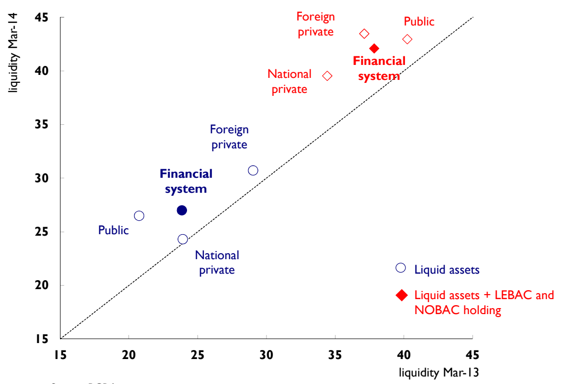
Source: BCRA

When breaking down the different items that make up liquid assets, it may be seen that, from June 2013 to March 2014, the share of repos with the BCRA, LEBACs in foreign currency and liquid assets in foreign currency increased whilst the share of cash holdings in pesos and Central Bank's instruments in domestic currency decreased. In order to promote that private sector deposits be kept within the financial system, this Institution started to auction, as from early 2014, LEBACs in dollars[86] in the market that may be underwritten by banks using time deposits in foreign currency received from the private sector.

Chart V.5

Liquidity by Group of Banks

% of non-financial deposits



Source: BCRA

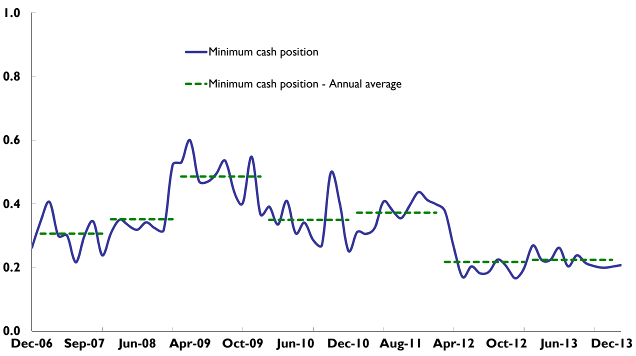
The financial system continues complying with the minimum cash regulatory requirements

[86] Communication "A" 5527.

Chart V.6

Liquidity in Pesos

Minimum cash position - In % of deposits - Average daily stocks



Note: Decembers reflect position of the quarterly period (December to February).
Source: BCRA

Banks recorded a surplus in liquidity compliance in pesos of around 0.2% of deposits[87] both at the end of 2013 and at the beginning of 2014 (see Chart V.6). Since January 2014 the BCRA reduced the minimum cash requirement for liabilities in pesos as higher the lending granted to micro, small and medium-sized enterprises (MiPyMES)[88]. Thus, and to channel lending to these companies within the framework of the Credit Line for Productive Investment (LCIP), the requirement was decreased by an amount equal to 16% of financing provided to this segment so long as it may be verified that the term for such loans at the time of granting exceeded 5 years and that their average term was not shorter than 30 months[89].

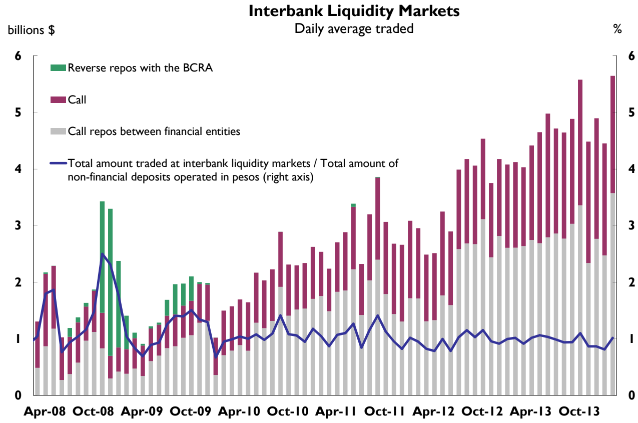
Banks exhibited a rise in surplus liquidity in dollars exceeding the regulatory requirement[90] from mid-2012 to January 2014 in a context of reduction of loans in dollars to the private sector. Within this framework, the BCRA ordered a rise in the minimum reserve requirement for deposits in foreign currency[91] in January 2014.

Interbank markets gained depth on the margin

Chart V.7

Interbank Liquidity Markets

Daily average traded



Source: BCRA

Amounts traded in the call money market and the repo market between financial institutions continued growing in the last months of 2013 and the beginning of this year (see Chart V.7), accounting for around 1% of the total amount traded in non-financial deposits in pesos. Regarding the call market, foreign private banks continued being the main fund borrowers in the past few quarters (see Chart V.8), thereby sustaining their net borrowing position. Supply of these funds was mainly met by national private and public banks. Unlike the situation in previous quarters, Non-Banking Financial Institutions (NBFI) became net borrowers of these funds in early 2014. It should be noted that interest rates arranged for these transactions among banks exhibited some volatility by the end of 2013 and the beginning of 2014, and began to stand at lower values than those observed in the first quarter of the year.

[87] Considering the average of daily data.
[88] Communication "A" 5524.
[89] This reduction will also be applied to those financial institutions not falling within the scope of the LCIP but which provide lending to micro, small and medium-sized enterprises under the same conditions set for the LCIP.
[90] It consists of the minimum cash requirement and the shortfall application of funds.
[91] Communication "A" 5534. In the case of sight deposits, they will be applied a minimum reserve requirement amounting to 30% in February, 40% in March and 50% as from April; in contrast, in the case of time deposits, the minimum cash requirement will increase based on the deposit term to maturity (deposits at up to 29 days will be applied a rate standing at 30% in February, 40% in March and 50% as from April; regarding time deposits at a term ranging from 30 to 59 days, the rate will amount to 23% in February, 30% in March and 38% as from April; and so on so forth with the remaining terms).

Box 3 / Basel Committee's New Liquidity Standards

Within the framework of the decisions that followed the onset of the international crisis, the G20 entrusted the Basel Committee (Basel Committee on Banking Supervision—BCBS—) with the promotion of improvements in the management of liquidity risk at banks and the development of tools to assess and improve their resilience in view of potential shocks of this nature. Consequently, liquidity risk management standards[92] were revised and reinforced and an international framework was drafted for the assessment and monitoring of this risk[93]. The most prominent new feature of these standards is that minimum values will be applied to quantitative liquidity measures, whereas, so far, there only existed management standards

Following an assessment and consultation period at an international level, the BCBS implemented two liquidity quantitative ratios to be complied with by financial institutions in a consolidated fashion: the Liquidity Coverage Ratio —LCR— and the Net Stable Funding Ratio —NSFR.

The purpose of the LCR is that institutions maintain their own liquidity buffer to be able to properly face a potential net outflow (outflows net of inflows) in a context of acute, individual and systemic stress for a 30-day period. Eligible assets must have liquid and deep markets, their value must not be affected during systemic crisis situations and they must be freely available to be monetized immediately.

The LCR may be defined as follows:

$$\frac{\textit{Stock of high-quality liquid assets}}{\textit{net cash outflow}} \geq 1$$

The stock of liquid assets includes two levels in the international standard:

- Level 1: notes and coins, deposits with central banks, government bonds rated AA or higher, and securities issued by the central government of every jurisdiction (with specific limits when they are denominated in foreign currency);
- Level 2: securities with very low volatility at times of systemic crises and the markets of which comply with a set of minimum liquidity criteria. Given their higher risk, these assets are computed with a haircut and are subject to limits.

In order to quantify the net flow of outflows, every bank must classify their balance sheet stock and potential commitments based on criteria that distinguish the stability degree of liabilities and assets' "liquidity value". Contractual flows of the next 30 days are measured for every category identified and a weighting factor is applied to them which, in most cases, is defined by international rules, although in some cases the weighting factor is set at national discretion. Expenses estimated in this manner are subject to deductions of income calculated in the same fashion. For the stock of liquid assets to have a minimum value, income counted in the indicator may not exceed 75% of expenses.

In order to define the categories that allow estimating inflows and outflows of funds, the basic criterion consists in considering the counterparty: the national government, the central bank, a retail client, companies or other financial institutions. Next, these large groups are subdivided into subcategories by applying new criteria included in the regulation. For example, the concept of "stable" deposit is created for the retail segment, which is applied to transaction deposits covered by deposit insurance. In contrast, the category of "operational" deposit is created for the wholesale tranche, and it is determined that the deposit must be related to cash management, clearing or custodial services provided by the bank to clients pertaining to this segment. In the case of repo transactions, their stability is associated to the quality of the asset used as collateral.

Basel international standard also introduced the NSFR, which is generally deemed as "structural" or "long term" as it tends to promote the expansion of the funding medium term so that institutions have a suitable structure in this aspect in line with the business they develop. Like the LCR, components of this ratio are calculated by classifying on and off-balance sheet items and weighing them by predetermined factors thereby generating a minimum funding requirement called "stable".

In addition to the two metrics abovementioned, a set of monitoring tools for flows of funds were defined as well as the balance sheet structure, collaterals, market data and the LCR calculation by significant currency.

At an international level, the LCR was finally defined by January 2013 and will become effective as from early 2015 with a 60% minimum requirement which will be increased by 10 percentage points annually, reaching 100% in 2019. The calculation of the

[92] BCBS, "Principles for Sound Liquidity Risk Management and Supervision", 2008. http://www.bis.org/publ/bcbs144.pdf
[93] BCBS, "Basel III: International framework for liquidity risk measurement, standards and monitoring", 2010 and "Basel III: The Liquidity Coverage Ratio and liquidity risk monitoring tools", 2013.

monitoring tools will also be introduced in 2015. In turn, the NSFR is still under discussion at an international level, even though the objective is to have it ready by January 2015 and implement it as from January 2018. In this context, the BCRA has been following this process, in line with the international schedule.

Regarding global banks, that had not been previously subject to liquidity regulations, the LCR implies a dramatic rise in the amount of high-quality financial assets and liquidity they must maintain without using them for any kind of transaction. This will result in very significant demand for these securities in the markets. On the other hand, the NSFR will impact on the financial institutions' balance sheet structure. As a whole, it has been estimated that standards will impact on these banks' profitability and will discourage transactions with a high liquidity risk, such as those that contributed to the seriousness of the international crisis, thus favoring greater stability in the global financial system.

In this regard, the BCBS has been conducting quantitative impact studies since 2010, initiatives that allowed working on an adjustment process for these liquidity requirements and boosting improvements in available information. This task made it possible to have a clearer picture of the challenges related to interactions existing amongst different regulatory changes that are currently being put in place worldwide.

Apart from potential impacts on the international markets abovementioned, the new ratios imply significant challenges in terms of implementation and control. New definitions were created for categories that did not previously exist in the regulation or in banks' reports by using criteria that are also new and that banks must implement at a consolidated level.

At a local level, the BCRA has been working with four institutions with different equity profile on the impact study structured by the BCBS. The experience allowed confirming the challenges for Argentina regarding the application of the new categories and criteria, and no problems were found for compliance with the requirements for liquid assets. Nevertheless, as work was conducted with banks of a universal nature, it is not possible to rule out the fact that financial institutions with other business profiles may have to make greater efforts to accomplish compliance therewith.

The BCRA published a reporting system (Communication "A" 5494, as amended), asking all financial institutions for information relative to the necessary categories to calculate the LCR, even though the applicable weighting factors and caps have not been published yet. Once the process of entering all the information is over, it will be possible to estimate impacts in an ample manner and to adjust the aspects that the international regulation defines as national discretion.

Meanwhile, the BCRA continues participating in the international debate regarding the NSFR and in the impact study conducted by the BCBS.

V.2 Credit Risk

V.2.1 Private sector

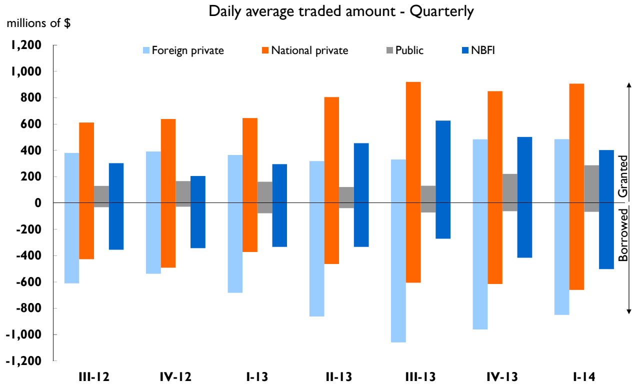
Balance sheet exposure to credit risk has remained at low levels

Financial system gross exposure to the private sector posted a minor increase in 2013 (see Chart V.9), evidencing a higher relative rise in foreign private banks. Last year, lending to the private sector raised its share in banks' netted assets by 0.8 p.p., accounting for 52% of the total. This indicator exhibited a slight fall in the first months of 2014 against the level observed by the end of 2013. The income evolution recorded by households and companies—in a context with moderate indebtedness levels for both sectors (see Chapter III)—was reflected in low bank credit delinquency levels. This situation was coupled with sizeable coverage of the non-performing portfolio with provisions, thereby contributing to maintaining limited financial system balance sheet net exposure to credit risk.

Chart V.8

Call Market

Daily average traded amount - Quarterly



Source: BCRA

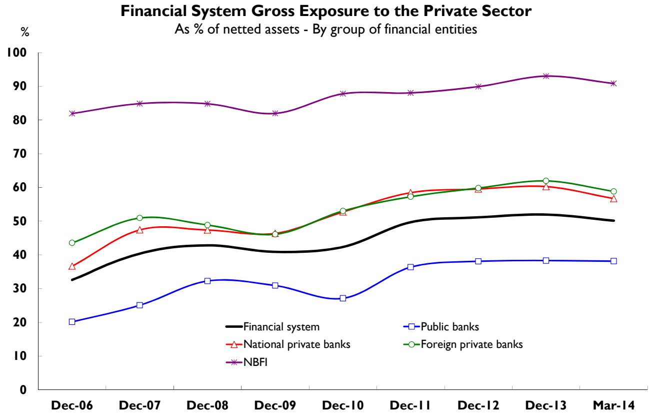
The ratio of the non-performing loan portfolio to the private sector has remained at low levels over the period under study

Delinquency of credit granted to the private sector reached 1.7% of total lending by the end of last year, standing at the same level observed in late 2012. The group of loans covered by preferred guarantees[94] recorded a 1.3% non-performance ratio by the end of 2013; such ratio reached 1.8% in the case of the loan portfolio without those guarantees. Private sector lending delinquency for the aggregate system exhibited a slight 0.2 p.p. rise in the first quarter of 2014, amounting to a 1.9% ratio in March.

Chart V.9

Financial System Gross Exposure to the Private Sector

As % of netted assets - By group of financial entities



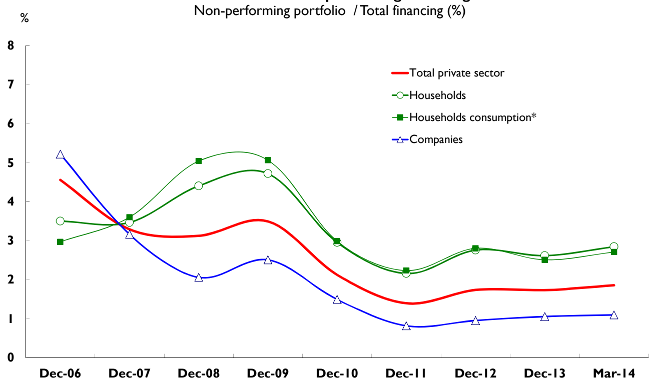
Source: BCRA

Financing non-performance recorded a heterogeneous evolution amongst groups of financial institutions in 2013, with drops in the case of NBFI and national private banks —which recorded indicators that were higher than those of the other groups— and slight rises in the case of foreign private and public banks. The evolution observed in non-performance also exhibited different types of performance depending on the loan use. On the one hand, lending to households decreased by 0.2 p.p. —mainly due to the performance of loans for consumption purposes— in 2013 totaling 2.6%; on the other hand, loans to companies climbed 0.1 p.p., up to 1.1% of the portfolio (see Chart V.10). In regional terms, non-performance of lending granted to the private sector also posted mixed changes in 2013, with drops

[94] Financing covered by preferred guarantees accounted for 16.5% of the total as of December 2013, a value similar to that of 2012.

Chart V.10

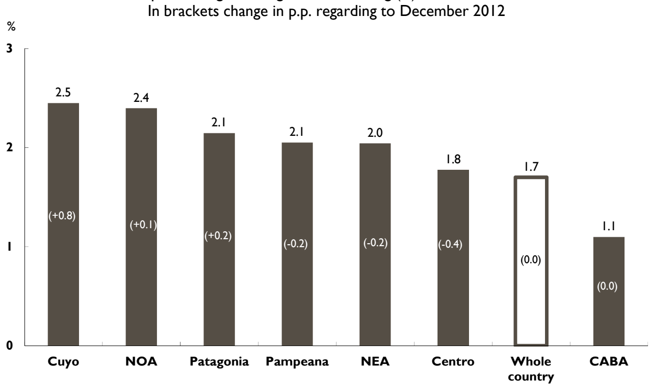
Private Sector Non-performing Financing
Non-performing portfolio / Total financing (%)



*Note: includes personal and credit cards.
Source: BCRA

Chart V.11

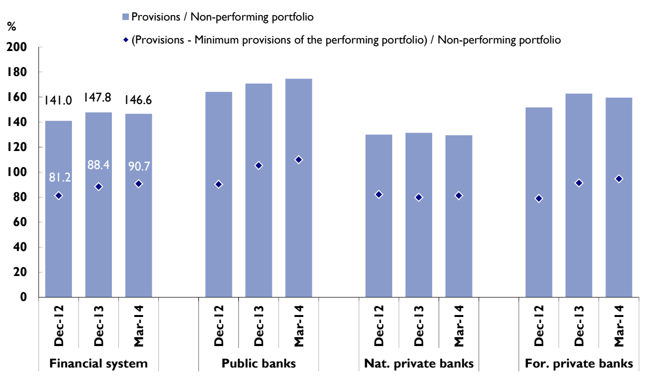
Private Sector Non-performing Financing by Region
Non-performing financing / Total financing (%) - December 2013
In brackets change in p.p. regarding to December 2012



Source: BCRA

Chart V.12

Non-performing Portfolio Coverage with Provisions by Group of Banks



Source: BCRA

being observed in the Centro, NEA and Pampeana regions while rises were observed in the Cuyo, Patagonia and NOA area (see Chart V.11).

Looking ahead, current non-performance levels stand well below those recorded in the international financial crisis peaks (2008 – 2009) and figures registered up to 2006 (see Chart V.2). These delinquency levels are also lower than the ones currently observed on average in other economies within the region.

Loan loss provisions continued exceeding regulatory requirements, easily covering the non-performing portfolio

The financial system continued exhibiting sizeable coverage of the delinquent portfolio with loan loss provisions, reaching 147.8% of non-performing loans by the end of 2013. This coverage ratio exceeded 100% in all ensembles of banks (see Chart V.12). If minimum provisions applicable to the performing portfolio are excluded, the coverage ratio would amount to 88.4% for the financial system, a value that easily surpasses regulatory minimum provisions required for non-performing financing (59.3%). Thus, even though the provisioning ratio posted a minor fall in the first months of 2014 in terms of the total portfolio, the comfortable levels of coverage of the delinquent portfolio were kept.

Financial system exposure to credit risk derived from potential changes to the exchange rate is limited

The ratio of the stock of loans granted to the non-financial private sector denominated in foreign currency stood at 6% at the end of the first quarter of 2014, after falling 1 p.p. against March 2013 (see Chart V.13). This performance, coupled with the fact that, under the macroprudential framework implemented by the BCRA, the stock of loans in foreign currency is primarily granted to the producing sector of tradable goods, reduced the financing risk undertaken by the financial system and resulting from potential currency mismatches in the debtor's balance sheet.

Companies

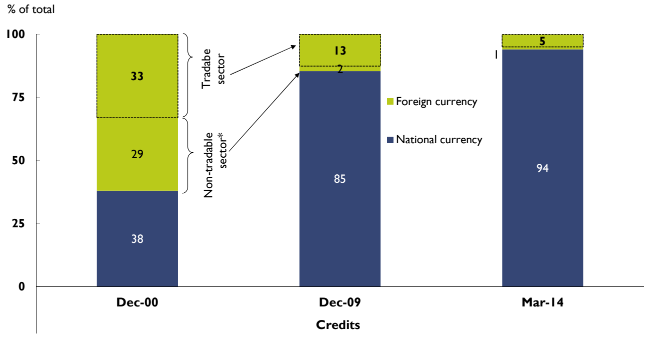
The financial system increased its gross exposure to the productive sector in 2013, a situation that was moderated at the beginning of 2014

The share of lending granted by the ensemble of financial institutions to companies stood at 29.4% in terms of netted assets by the end of 2013, exhibiting a

Chart V.13

Credit to Private Sector by Currency

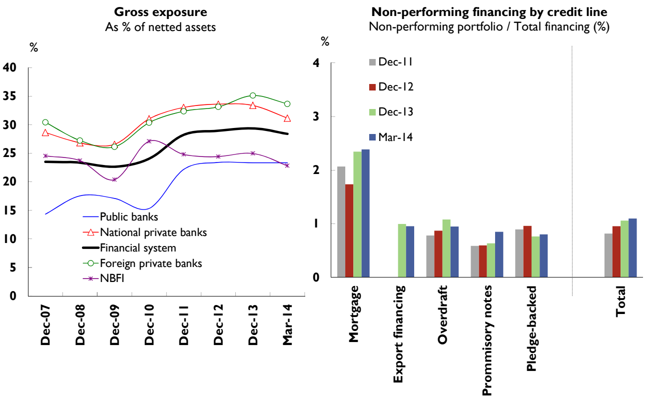
Financial system



*Note: Non-tradable sector financing estimation considers loans in foreign currency to households, construction sector, gas, water, electricity and other services. (December 2013 last available information).
Source: BCRA

Chart V.14

Companies' Financing

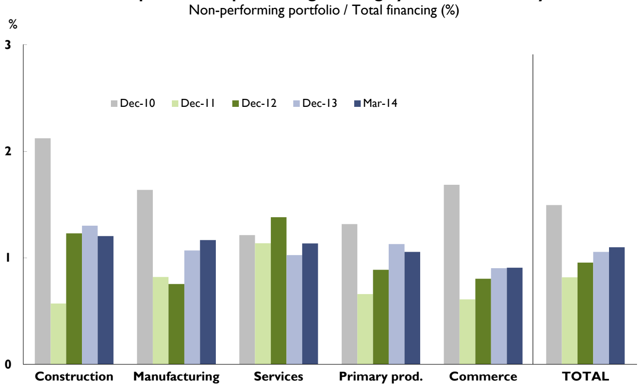


Note: Export financing credit line's information is available from 2013. Source: BCRA

Chart V.15

Companies' Non-performing Financing by Economic Activity

Non-performing portfolio / Total financing (%)



Source: BCRA

minor rise against the end of 2012. This trend was mainly explained by foreign private banks and NBFI (see Chart V.14). In contrast, in 2014 and in a context of lower momentum in lending in the first quarter, the ensemble of banks reduced its gross exposure to companies slightly.

Companies' lending non-performance remained at reduced levels

The companies' lending non-performance ratio posted a slight rise in 2013 and at the beginning of 2014. Nevertheless, this indicator has stood at historically low levels and is lower than that of lending to households. This situation, together with companies' reduced level of aggregate debt, contributes to maintaining the sector's repayment risk at a moderate level (see Chapter III).

Non-performing loans to companies stood at 1.1% of the total portfolio at the end of 2013, slightly above the figure recorded a year before. Credit lines mostly used by the productive sector —overdrafts and promissory notes— recorded a lower relative delinquency than total lending to such segment (see Chart V.14). Except for the group of companies engaged in service provision, all productive branches contributed to the rise recorded by the non-performance ratio corresponding to lending granted to companies (see Chart V.15). A heterogeneous performance was observed in the first months of 2014, with minor rises in delinquency in loans granted to manufacturing and services; in contrast, drops were recorded in non-performance in lending given to construction and primary production.

From the total stock of loans to companies recorded by the end of 2013, it is estimated that around 83% corresponds to financing granted between 2011 and 2013. The non-performance ratio for such loans would evidence a lower level than that of loans under longer terms granted to the productive sector (see Chart V.16).

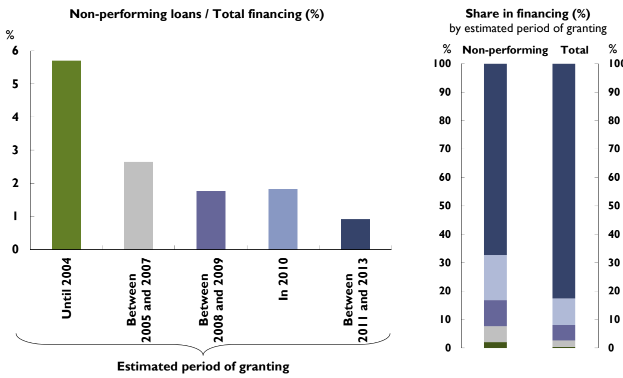
Households

The banking sector increased its gross exposure to households in 2013, falling slightly at the start of 2014 against the end of 2013

Gross exposure recorded by the aggregate financial system to households was 22.6% of netted assets in December 2013 (see Chart V.17), exhibiting a 0.4 p.p. growth against December 2012. Over this period, all ensembles of financial institutions recorded rises in the share of lending to households in their assets, especially, in the case of NBFI and national private banks. In turn,

Chart V.16

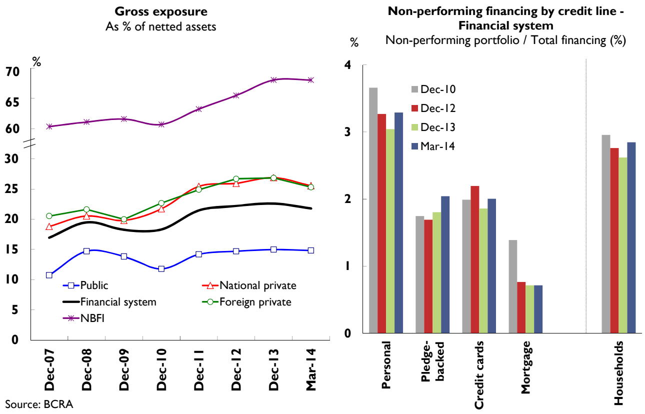
Companies' Credit Non-performing Ratio
By estimated period of granting - December 2013



Source: BCRA

Chart V.17

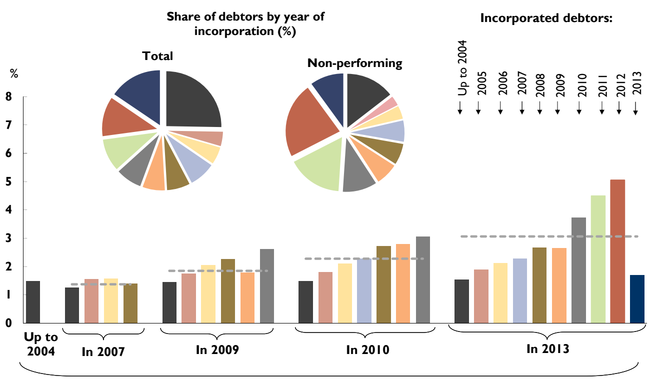
Households Financing



Source: BCRA

Chart V.18

Households' Credit by Estimated Period of Debtor Incorporation to the Financial System
Non-performing financing / Total financing (%) - December 2013



Source: BCRA

financial system exposure to households in the first quarter of 2014 fell slightly against the end of the previous year derived, mainly, from private banks. Within this framework, it should be noted that households' indebtedness level is still moderate (see Chapter III). In addition, the policies on income transfer to the most vulnerable sectors and the retirement and pension sector are expected to be kept and labor market conditions are also expected to be favored by the implementation of wage agreements and job stability (see Chapter II); these situations would contribute to maintaining households' payment capacity.

A marginal rise, from low levels, is observed in the delinquency ratio of loans granted to households

Non-performance of loans granted to households decreased in 2013 in y.o.y. terms, reaching 2.6% of the total portfolio as of December, and it was mainly driven by the performance of lending for consumption purposes: credit cards and personal loans (see Chart V.17). This reduction in households' delinquency ratio was observed amidst a context of sustained growth in lending to such segment over the year (see Chapter IV). Non-performance of loans to households decreased during last year at a system level, especially in national private banks and NBFI. At the beginning of 2014, the delinquency ratio started to partially reverse the performance of the previous year, a movement primarily accounted for by lines for consumption purposes and pledge-backed loans.

Considering the stock of loans to households at the end of 2013, it is estimated that debtors that entered the financial system between 2010 and 2012 recorded non-performance levels that were relatively higher than those corresponding to debtors already existing. In turn, debtors included in 2013 exhibited, by the end of 2013, a lower delinquency ratio than the average recorded by households, with an estimated share in the stock of lending to households of around 15% (see Chart V.18).

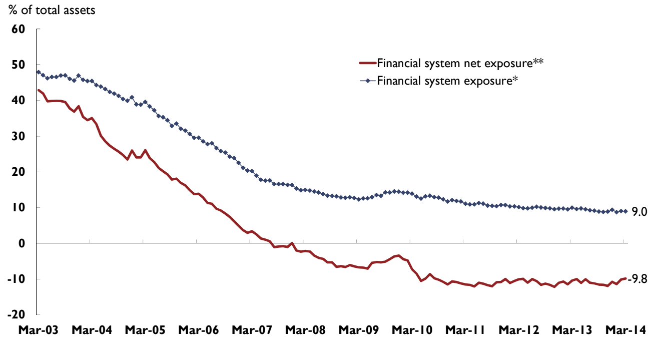
V.2.2 Public sector

Financial system gross exposure to the public sector continued falling

Financial system gross exposure to the public sector stood at 9.4% of total assets by the end of 2013, down 0.3 p.p. against December 2012. The stock of public sector deposits —considering the three governmental levels— in the financial system continued being higher than the stock of loans to this segment. Consequently, the public

Chart V.19

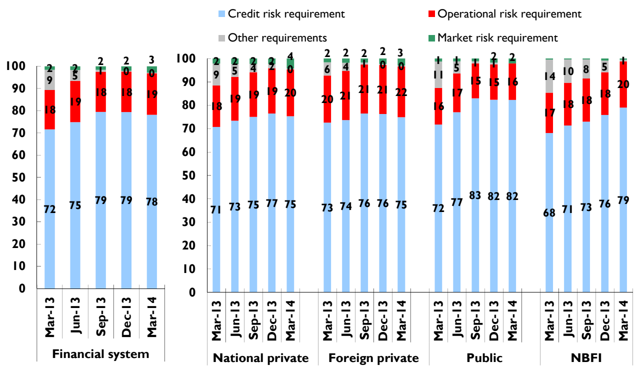
Financial System Exposure to the Public Sector
As % of total assets



*(Position in government securities (not including Lebac or Nobac) + Loans to the public sector) / Total Assets.
**(Position in government securities (not including Lebac or Nobac) + Loans to the public sector - Public sector deposits) / Total Assets.
Public sector includes all jurisdictions (national, provincial and municipal). Source: BCRA

Chart V.20

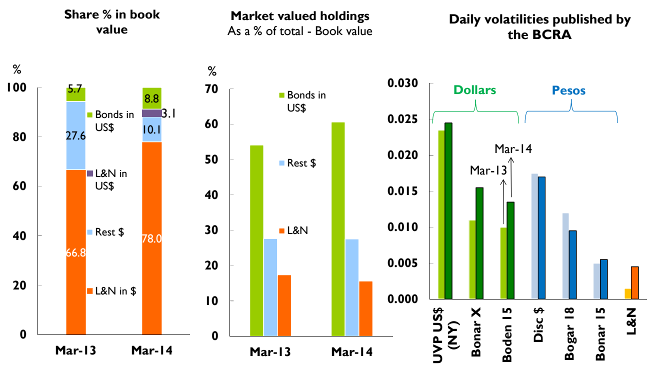
Capital Requirements by Group of Financial Entities
Share in regulatory requirements



Note: Requirements are adjusted by exemptions and the effects of the Com. "A" 5396. Source: BCRA

Chart V.21

Public Bonds, LEBAC and NOBAC in Banks' Porfolio



Source: BCRA

sector kept its net creditor position in the financial system at a level equivalent to 10.8% of total bank assets as of December 2013 (see Chart V.19). A slight decrease in gross exposure to the public sector, down to 9% of assets, was observed in the first months of 2014. Given the evolution of public sector deposits, the public sector net creditor position in the financial system also fell slightly in the first quarter of the year, amounting to 9.8% of financial system assets.

V.3 Operational Risk

The share of the capital requirement for operational risk in the financial system total requirement is gradually increasing

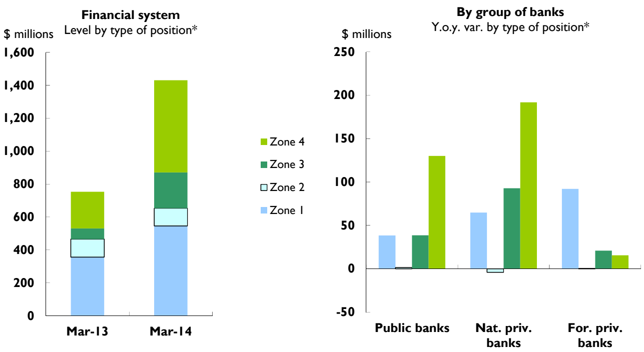
The requirement for operational risk, aimed at providing a reserve of funds for institutions to face potential unexpected losses that may result from failures in processes, personnel and systems or from external events, is gradually increasing its share in the total capital requirement of the financial system. Thus, the capital requirement for operational risk —defined in the domestic prudential regulation as the amount equivalent to 15% of average positive "gross income" recorded in the past three years[95]— accounted for 18.7% of the total regulatory capital requirement in March 2014 —around 1 p.p. higher y.o.y.— (see Chart V.20) and 11.3% of total compliance (adjusted stockholders' equity) —up 0.3 p.p. in y.o.y. terms. The requirement for operational risk is around 22% for foreign banks, 20% of the total for national private banks and for NBFI and a bit lower for public banks (16%).

The abovementioned rise in the share of the requirement for operational risk in the total takes place in a context of higher levels of financial intermediation with the private sector and of a rise in spreads of transactions[96]. Such rise also results from the regulatory change in minimum capital implemented at the end of 2012 (Communication "A" 5369) that became effective in early 2013. Even though the requirement for operational risk has been in effect for large financial institutions (Group "A") since December 2012, and will become effective as from December 2014 for smaller institutions (Groups "B" and "C")[97], Communication "A" 5369, by introducing relative changes to the domestic capital requirement—in line with Basel III—, established that if by virtue of its application, the total requirement is lower than that set in January 2013 by the regulation previously in force, the higher of both values shall be applied. The difference between both

[95] For further information, see Box 3 of the Financial Stability Report, First Half 2012.
[96] For further information, see Chapter IV.
[97] See Section 10 of the Consolidated Text on Financial Institutions' Minimum Capital.

Chart V.22

Capital Requirements due to National Bonds

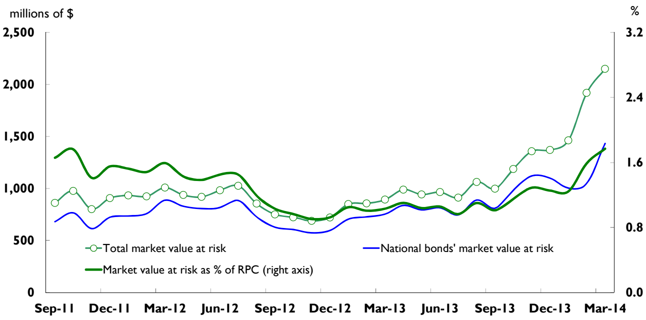


*Types of position by Compiled Texts of Financial Institution Minimum Capital Requirements. Section 6. Bonds are classified depending their currency and their average term ("modified duration", MD): Zone 1 (pesos, MD less than 2.5 years), Zone 2 (pesos, MD more than 2.5 years), Zone 3 (dollars, MD less than 2.5 years) and Zone 4 (dollars, MD more than 2.5 years). Source: BCRA

Chart V.23

Market Value at Risk

Total and national bonds'* capital requirements



*Included positions: (i) public bonds, LEBAC and NOBAC considerated in the list of volatilities (issued by this Institution) and recorded to fair market value and (ii) share of MF which concern the securities and instruments mentioned previously.
Source: BCRA

values shall be allocated to a set of uses which include the reductions of forbearances granted to comply with the requirement for credit risk in the first place and, in the second place, to comply with the proportion of the requirement for operational risk that has not been complied with yet due to the application of the abovementioned adjustment schedule[98].

V.4 Market Risk

Market risk undertaken by financial institutions increased slightly even though it still holds a low share in the set of bank risks

The financial system balance sheet is exposed to market price fluctuations of financial assets due to their impact on positions marked-to-market. In this context, it should be noted that instruments entered with this kind of valuation accounted for only 3.5% of financial system netted assets, considering the position of sovereign bonds and monetary regulation instruments — instruments that concentrate the greatest part of exposure by the financial system to market risk.

Considering the portfolio of aggregate positions of securities for the ensemble of financial institutions, a rise in the share of LEBAC and NOBAC holdings and of national bonds in foreign currency was observed in y.o.y. terms (see Chart V.21). Particularly, the share of holdings marked-to-market increased in the segment of sovereign bonds in foreign currency but remained practically unchanged in the portfolio of securities in pesos and in that of monetary regulation instruments. In addition, volatility observed in the segment of bonds in dollars and in that of LEBACs and NOBACs stood slightly above the volatility recorded twelve months ago (see Chart V.21).

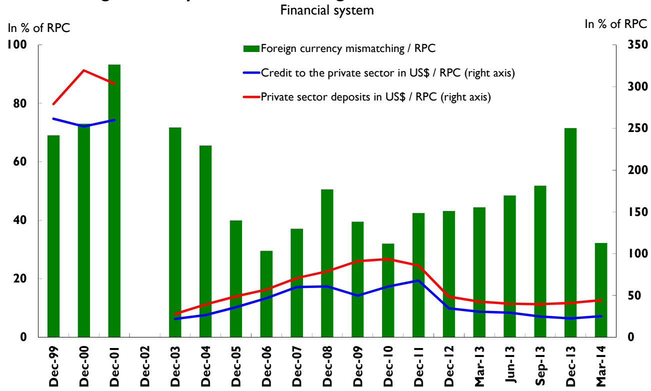
The evolution of the value at market risk in the past 12 months —as defined by the current regulation at a domestic level— for the aggregate financial system was mainly explained by the component of national bonds[99], which accounted for two thirds of the total[100] by the end of the first quarter of 2014. In general, a rise in the market risk was observed in almost all kinds of positions of these assets, with the segment that comprises bonds in dollars with an estimated modified duration exceeding 2.5 years being the most relevant, which led to a higher capital requirement at an aggregate level (see Chart

[98] The third use mentioned is the decrease in the capital requirement for credit risk over financing granted by the institution, which purpose, currency and term are those provided for in the regulation on the Credit Line for Productive Investment (LCIP).
[99] Sovereign bonds, LEBACs and NOBACs and, to a lesser extent, mutual funds' unit shares.
[100] The rest corresponded to the requirement for volatility of positions in foreign currency.

Chart V.24

Foreign Currency Broad Mismatching* and Balance Sheet Dollarization

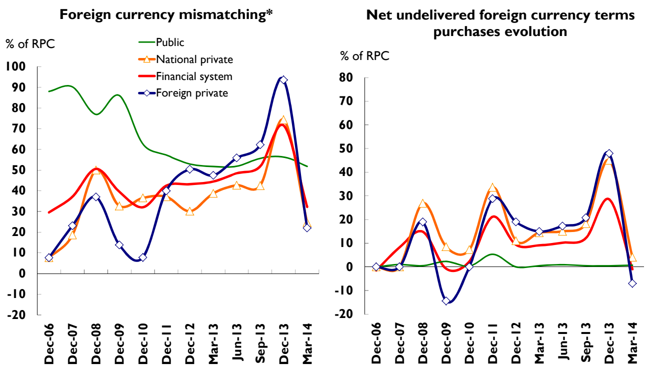
Financial system



*Note: (Assets - Liabilites + Net undelivered purchases) / RPC.
Source: BCRA

Chart V.25

Foreign Currency Mismatching by Group of Banks



*Note: (Assets - Liabilites + Net undelivered purchases) / RPC.
Source: BCRA

V.22). The higher y.o.y. requirement for market risk was recorded in all ensembles of banks.

Despite the rise recorded in the past few months, the value at market risk recorded by the ensemble of banks remains at limited levels: it only reached 1.8% of adjusted stockholders' equity (RPC) in March and 2.9% of the total minimum capital requirement (see Chart V.23). Thus, the financial system has continued exhibiting low exposure to market risk. Within this framework, it should be noted that, by mid-June the US Supreme Court dismissed Argentina's appeal in the litigation with the debt bondholders that did not agree to the debt restructuring, which would define a new context for the price evolution of domestic financial assets in the short term.

V.5 Currency Risk

The BCRA implemented a set of measures in early 2014 that limited the currency risk that financial institutions may undertake

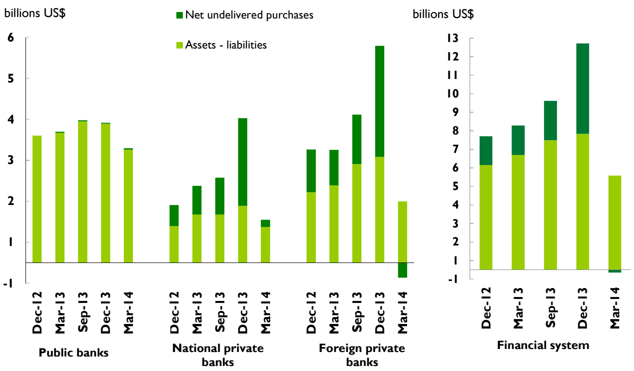
The broad mismatching of foreign currency recorded by the ensemble of financial institutions in the last month of 2013 stood at about 70% of their adjusted stockholders' equity (RPC), evidencing a significant 28 p.p. rise against December 2012 (see Chart V.24). Thus, the aggregate of institutions recorded a rise of almost 66% in their broad mismatching ratio in 2013, a trend that accelerated in the second half of the year and that was mainly related to the hike in forward net purchases of foreign currency by private banks (see Chart V.25). The aggregate of foreign private banks ended the year evidencing a broad mismatching close to 94% of their RPC, followed by national private institutions (74% of their RPC), and finally, public banks (a little over 56%).

In view of this context of banks' growing exposure to currency risk, the BCRA implemented amendments to the regulation on the Net Global Position in Foreign Currency (PGNME). This regulation was created in early 2003 and resulted from the sharp negative impact of the 2001-2002 crisis on the financial system, in a context of broad currency mismatches in banks' balance sheets within the regulatory framework that existed in the past decade. The purpose of the PGNME was to reduce bank's net worth potential impact due to changes in the nominal exchange rate in cases of both appreciation and depreciation. Originally, there was a limit, in terms of banks' RPC, to their positive mismatch and another limit for the negative one, but the positive limit was suspended in 2005.

Chart V.26

Foreign Currency Broad Mismatching* Composition

By group of banks



*Note: (Assets - Liabilites + Net undelivered purchases) / RPC.
Source: BCRA

From a macroprudential standpoint, the BCRA ordered, once again, regulatory changes[101] in February 2014 with a view to reducing financial system currency risk and preventing potential negative effects on the foreign exchange market that may adversely affect the evolution of real economy. On the one hand, it reintroduced the positive limit for the PGNME of every institution at a level equivalent to 30% of adjusted stockholders' equity corresponding to the month prior to the relevant month or its own liquid funds, whichever the lower[102]. On the other hand, it set a limit for a subgroup of the PGNME that did not previously exist in the regulation: as from February 2014, the future positive net global position in foreign currency may not exceed 10% of adjusted stockholders' equity of the month prior to the relevant one[103].

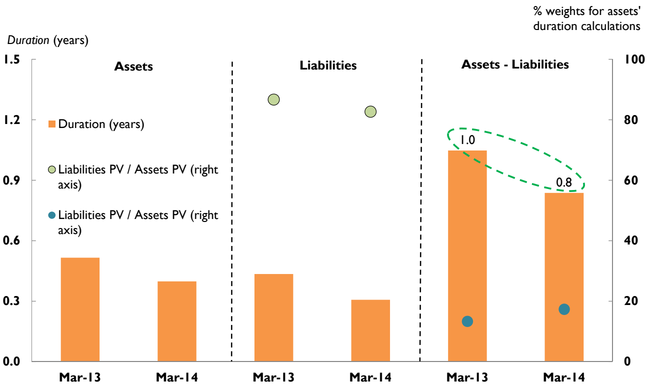
In addition, by mid-February, the BCRA raised charges related to non-compliance with the ratios set in the PGNME[104] and determined that any surplus shall be subject to a charge equivalent to 1.5 times the annual nominal interest rate already matured that results from auctions of BCRA Bills in pesos[105]. Furthermore, by mid-March, forward sales by institutions to related companies[106] were excluded from the calculation of the forward net position to comply with the limit established.

Following these measures implemented by the BCRA, a swift reduction in banks' currency mismatching was observed. Thus, banks' broad currency mismatching was slightly above 32% of RPC by late March, evidencing a drop of almost 39 p.p. in the first quarter. This decline was mainly accounted for by private banks and was primarily derived from sales of liquid assets in foreign currency and from the reversal in the forward net position in foreign currency, which went from long to slightly short for the aggregate of the financial system (see Chart V.26).

[101] Communication "A" 5536.
[102] The regulation has an adjustment schedule: an amount equivalent to a ratio of the difference between the spot PGNME observed in January 2014 and 30% of RPC recorded in December 2013 shall not be deemed non-compliance with the general limit of the PGNME. The ratio stands at 75% for February; 50% for March; and 25% for April and no surplus is allowed as from May.
[103] This 10% limit of RPC for forward net purchases is counted within the 30% general limit of the PGNME.
[104] Communication "A" 5550.
[105] Furthermore, potential penalties for the provisions of section 41 and related provisions of the Financial Institutions Act are set that include: 1. Reprimand, 2. Warning, 3. Fines, 4. Permanent or temporary disqualification to use the bank checking account, 5. Permanent or temporary disqualification to act as organizers, founding members, directors, administrators, members of the surveillance committee, receivers, liquidators, managers, auditors, partners, or shareholders of institutions; 6. Revocation of license to operate.
[106] Communication "A" 5563.

Chart V.27

Estimated Domestic Currency Banking Book Portfolio Duration



Source: BCRA

V.6 Interest Rate Risk

The financial system slightly reduced its exposure to this risk

The interest rate risk is inherent to financial intermediation activity. Banks' balance sheets are usually exposed to rises in different interest rates in place in the economy. This results from the fact that, generally, a rise in rates quickly translates into higher levels of expenditures, against income levels, for the sector given the different sensitivity to adjustment of assets and liabilities. The portfolio of transactions arranged at a fixed interest rate concentrates exposure to this risk due to the relative longer term of assets against liabilities.

A slight reduction in the exposure to the interest rate risk was observed at an aggregate level in the past 12 months partly in response to institutions' management process regarding the new interest rate context. Particularly, the duration of assets net of liabilities in pesos in the banking book[107] portfolio was reduced (see Chart V.27), which means that, at the start of 2014, the estimated economic value for this portfolio segment recorded less sensitivity to changes in view of the volatility of the interest rate when compared to a year before. It has been estimated that both assets and liabilities pertaining to this portfolio recorded a reduction in their duration over the period, especially in the case of the former. Thus, the impact of the rise in interest rates recorded at the end of 2013 and the beginning of 2014 on the evolution of part of financial institutions' net income throughout the year was observed on the margin.

The local regulation included, as from 2013, the interest rate risk within Pillar II[108] of Basel standards, in line with the most widespread international practice in this regard. In this context, the Superintendence of Financial and Exchange Institutions —SEFyC— assesses institutions' capacity to face this risk and may, at a certain time, order them to execute a capital increase, a reduction in exposure or a combination of both alternatives. Amongst other elements, the SEFyC assesses the results of the economic value sensitivity exercises of the banking book positions in view of potential shocks that imply permanent rises in interest rates[109].

Considering one of the regulatory criteria —permanent rise by 200 bp in interest rates—, it is estimated that a

[107] It includes all assets and liabilities for financial intermediation not considered for the market risk assessment.
[108] Communication "A" 5369.
[109] Communication "A" 5398, Section 5.

decrease in the economic value of the financial system banking book[110] portfolio of only 1.8% of adjusted stockholders' equity would have been recorded by March 2014. As a result of a lower exposure by the financial system to this risk when compared to the previous 12 months, the hypothetical exercise of an identical 200 bp hike in interest rates would currently imply a more limited effect on net income and the sector's economic value[111].

[110] Considering information from the Reporting System of Minimum Capital Requirement and Compliance of the BCRA. Data from a public institution are excluded due to information inconsistency.
[111] The Superintendence of Financial and Exchange Institutions uses an alternative criterion: rise equivalent to the 99th percentile of the moving distribution of the past 5 years of annual changes in the interest rate.

Box 4 / Progress on the Design and Implementation of a Regulatory Framework for Domestic Systemically Important Banks

In order to continue promoting financial stability conditions that favor the smooth evolution of the different economic sectors in the economy, the BCRA kept on working on the implementation of Basel III recommendations considering the specific characteristics of the local financial system. In this regard, a framework was recently published to make progress on the identification of domestic systemically important banks as a first element in the development of the regulation that will be supplemented in the second half of 2014

The Basel Committee on Banking Supervision —BCBS— published a methodology[112] in November 2011 to identify Global Systemically Important Banks —G-SIBs. The adoption of a framework with these characteristics aims at reducing the negative effects that a context of financial problems in a systemic institution (or in several) may have on financial stability conditions at a global level and, thus, on the evolution of global GDP. The methodology agreed upon by the BCBS regarding G-SIBs, approved by the G20, allows identifying which banks fall within such category and how much additional capital they must hold as a result of their systemic importance[113].

Next, and within the framework of the G20 Summit in Cannes (France, 2011), the Financial Stability Board —FSB— was urged to extend the analysis of systemically important banks to also comprise those institutions that acquire systemic importance at the level of each country (Domestic Systemically Important Banks [D-SIBs]). As a result, the BCBS spread a set of principles in October 2012 that banking regulators/supervisors must follow to establish the system to be applied to financial institutions considered domestically systemic[114]. Considering that financial systems of every economy have specific characteristics, the objective was to provide greater national discretion in the D-SIB scheme compared to the one previously prepared for the discussion of G-SIBs.

Following the implementation terms set within the context of G-SIBs, the spreading of regulatory frameworks for D-SIBS in 2014 was agreed upon at an international level. Additional capital requirements for this type of institutions will be introduced between 2016 and 2019.

In line with the G20's request and commitments undertaken within the BCBS, the BCRA recently prepared and published a methodology for the construction of an internal regulation for financial institutions operating locally[115] to use it in the future during the definition process of every institution's degree of systemic importance. According to the methodology proposed by the BCBS, the rating granted to each bank acting in the Argentine market considers the following individual aspects: a) size, b) interconnectedness between financial institutions, c) substitutability degree of activities, and d) business complexity. These concepts are made up by a set of variables that have specific weighting factors with the following description:

Size. It includes the following as variables: i. Volume of total assets, net of liquid assets in a broad sense[116] (20% weighing); ii. Number of branches (15% weighing); iii. Number of ATMs (including self-service terminals; 15%).

Interconnectedness between financial institutions. Variables: i. Inter-financial assets, considering stocks of loans to other financial institutions and of repo loans when the counterparty is another financial institution (6.66%); ii. Inter-financial liabilities; stocks of deposits received from other financial institutions and of reverse repos when the counterparty is another financial institution (6.66%); iii. Wholesale funding, including the stock of financial loans received (6.66%).

Substitutability degree of activities. Variables: i. Provision of securities custody services (6.66%); ii. Creation of payment service systems, considering debits (issue) and credits (reception) of checks by every financial institution (6.66%); iii. Origination and administration of financial trusts including the activity of every institution in terms of their share as trustor and trustee of financial trusts with underlying assets that are bank loans (6.66%);

112 "Global systemically important banks: Assessment methodology and the additional loss absorbency requirement", Statutory Text, BIS, November 2011. See also "Global systemically important banks: updated assessment methodology and the higher loss absorbency requirement", BIS, July 2013.

113 For further information, see Box 4 "Progress Made in the Identification and Supervision of Systemically Important Banks", BEF II-12.

114 "A framework for dealing with domestic systemically important banks", BIS, October 2012.

115 http://www.bcra.gob.ar/pdfs/marco/D_SIBs.pdf

116 They include cash in banks, financial institutions' deposits with the BCRA, repo loans for banks with the BCRA through LEBACs and NOBACs, and own holdings of LEBACs and NOBACs.

Business complexity. Variables: i. Trading of derivatives considering the notional amounts traded in forward and swap transactions in the Electronically Open Market (MAE) and over the counter transactions (OTC) (5%); ii. Holdings of securities marked-to-market, considering sovereign securities recorded at a fair value, excluding LEBAC and NOBAC holdings (5%).

For every of the variables mentioned —taking into account their respective scale and unit— the relative share of each bank in the total Argentine financial system is calculated. Next, the relative share obtained for each variable is multiplied by the specific weight coefficient of every indicator[117]. The score obtained by every institution, used to determine their relative internal regulation, results from adding their respective weighted values obtained for every variable included in the analysis. The addition of the score obtained by all financial institutions amounts to "1".

In line with the recommendations made by the BCBS, in order to classify an institution as D-SIB, the specific characteristics of the Argentine financial system will be weighted, including, for example, its relationship to GDP of the economy, the concentration level recorded by activity, its substitutability degree with other segments that may provide financing to productive activities in the economy (especially, with the capital market). Indeed, determining, or not, the D-SIB status will also be subject to the discretion of the local banking supervisor and regulator and in line with the principles set by the BCBS, and such condition must be updated and reviewed regularly (once a year).

In order to continue working on the development of a regulatory framework for D-SIBs, the BCRA is currently analyzing different alternatives to gauge future requirements of core capital—common stock and retained earnings[118]—to be established for financial institutions that are identified with systemic characteristics. Particularly, the different methods used by the BCBS to gauge additional capital requirements for G-SIBs are being assessed as well as the methodologies used by those countries that have already implemented a regulatory scheme with these characteristics; in all cases, the specific features of the Argentine capital market and financial system being considered.

In this regard, it has been observed —at the international level— that a group of countries already has schemes for the specific treatment of systemic banks from a local standpoint. Thus, in early 2013, Canada included an additional requirement to be complied with through core capital equivalent to 1% of risk-weighted assets (RWA) of institutions deemed as systemic. Australia announced the identification of a group of banks considered D-SIB last December, with an additional core capital requirement equal to 1% of RWA. In turn, the Central Bank of India recently published a proposal —currently under analysis— with similar characteristics whereby a rising capital requirement is designed depending on an institution's systemic importance, with a maximum value of 1% of RWAs. Countries like Sweden, Singapore, and Switzerland introduced, over the past few years, measures to mitigate the systemic impact of part of their institutions considering, in their design, the specific characteristics of their economies.

In Argentina, as indicated by international principles, initiatives to be implemented on systemic banks not only include determining an additional capital requirement for this kind of institutions. For those systemic banks, work will be conducted on a deeper supervision, the design of specific resolution plans, and more transparency in the provision of information on risks; these measures would help promote a sounder domestic financial system, less likely to generate negative effects on the economy as a whole.

[117] In the case of the wholesale funding variable, the following should be noted: in line with the BIS methodology, the indicator for every bank is taken into account in its calculation which is then normalized using the addition of indicators obtained by all financial institutions. Next, the corresponding weighting factor is included as mentioned above.

[118] In line with the principles submitted by the BCBS in the 2012 document already mentioned.

VI. Payment system

Summary

By late 2013 and early 2014, the Central Bank of Argentina (BCRA) continued giving tools to the National Payment System so as to expand the use of alternative payments methods to cash, particularly electronic means. The use of these tools represents an improvement in terms of security, efficiency and agility for the regular transactions of the economy. In turn, policies continued to be implemented with a view to widening the access of the population to banking services.

In 2013, there was a remarkable increase in the use of immediate bank transfers, which went up 40.6% in terms of the number of transactions and 74% in terms of the amounts transferred, significantly exceeding the growth pace shown by other means of payment. This trend continued to prevail during the first quarter of 2014. As from the implementation of the regulatory changes by the Central Bank of Argentina, the number of immediate transactions without fees for users stood at almost 97% of the total (first quarter of 2014).

The issue of credit and debit cards went up 9.3% last year, mainly due to the activity of private banks. Consequently, the number of debit and credit cards per inhabitant was on the rise and reached a ratio of 0.73 by the end of 2013.

The use of checks as method of payment remained relatively stagnant and virtually unchanged in the number of documents cleared throughout the year, evidencing a 24.2% rise in terms of amounts.

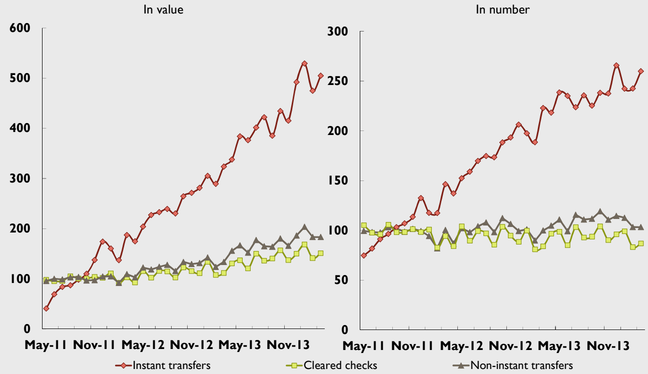
The number of Free Universal Bank Accounts (CGU) exhibited once again a positive change in 2013 (21.3%), thus contributing to improve the access of the population to banking services.

In turn, transactions through the Electronic Means of Payment (MEP) —a high-value payment system— also expanded during 2013, and they accounted for three times the GDP.

Chart VI.1

Use of Means of Payment's Evolution

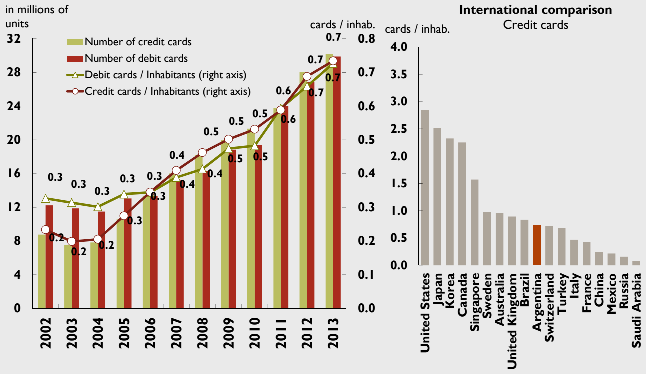
Index number / base: average May-December 2011 = 100



Source: BCRA

Chart VI.2

Credit and Debit Cards



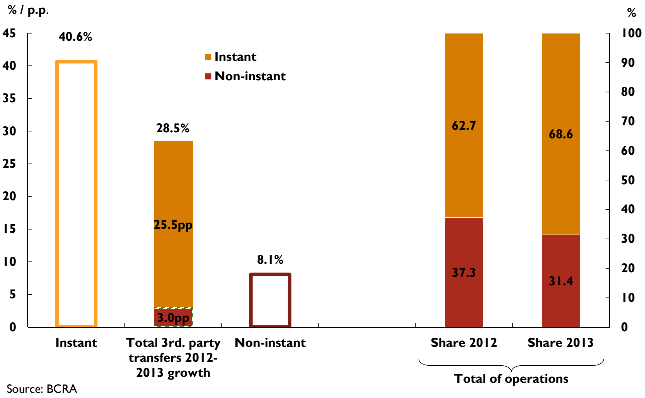
Note: To December each year / Credit cards data up to 2012, except Japan and USA up to 2011, Saudi Arabia up to 2009, and Argentina up to 2013. Source: BCRA.

VI.1 National Payment System

Chart VI.3

Third Party Transfers by Type

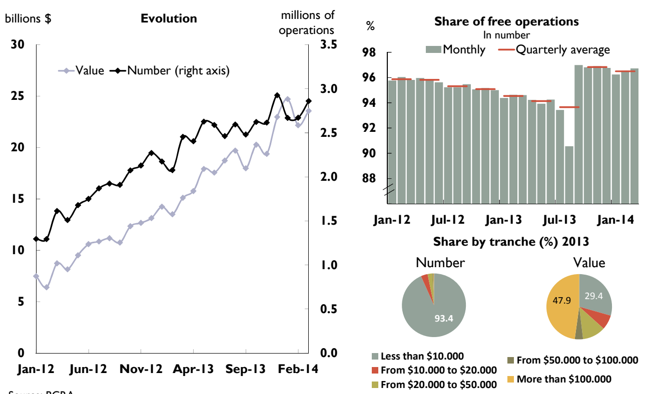
Number of operations



Source: BCRA

Chart VI.4

Instant Transfers



Source: BCRA

Throughout 2013 and at the beginning of 2014, the BCRA continued implementing several measures relative to the National Payment System (SNP) with a view to ensuring the diversity, security, efficiency and reliability of the means of payment in general and the electronic means in particular, as well as expanding the coverage of financial services available to the population.

In 2013, transfers to third parties –i.e., transfers made by banks on behalf and to the order of their clients[119]– continued to be on the rise, both in terms of amount (37.7%) and of the number of transactions performed (28.5%) (see Chart VI.3). Among this type of transfers, immediate bank transfers stood out[120], which posted a 40.6% growth in the number of transactions —and 74% in amount–, quite above the rise posted by non-immediate bank transfers— 8.1% in number and 35.5% in amount — and accounted for 25.5 p.p. of the total increase of transfers to third parties. Thus, the weighing of immediate transfers kept on increasing and reached 68.6% (+5.9 p.p.) of the total number of transactions to third parties; this trend remained during the first three months of 2014, when immediate transfers accounted for 70.7% of all the transfers made to third parties.

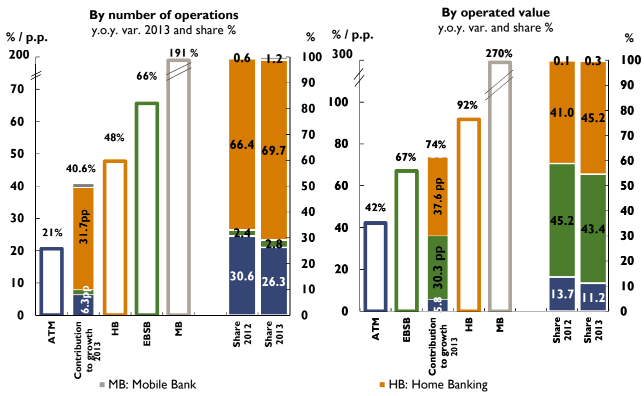
If analyzed according to size segments, immediate transfers in the low amount segment (up to $10,000) continued showing a significant share in the total (93.4%) in the number of transactions in 2013 (see Chart VI.4). It is worth stating that until August 2013, the maximum amount for free-of-charge transfers through electronic means was $10,000 per day, and this limit was extended to $20,000 as from September 2013[121]. As from this change in the regulation, the percentage of immediate transactions at no cost for users went up from 91% in August to 97% in September, and this figure remained virtually unchanged in the first quarter of 2014.

As regards the different channels available to make immediate transfers, home-banking transactions, both in terms of number (31.7 p.p. of 40.6%) and of amount (37.6 p.p. of 74%), contributed remarkably to their growth in 2013 (see Chart VI.5). In turn, transfers made through ATMs recorded a relatively lower growth than immediate transfer total –both in amount and number–, thus losing share against 2012. Lastly, although mobile

[119] These transfers do not include payment of wages, payments to suppliers, family allowances, retirements and pensions and garnishment of social security benefits.
[120] As from April 2011, the BCRA required the banks to offer their clients the possibility of making transfers which are credited in the system on a real-time basis (Communication “A” 5194).
[121] See Communication “A” 5473.

Chart VI.5

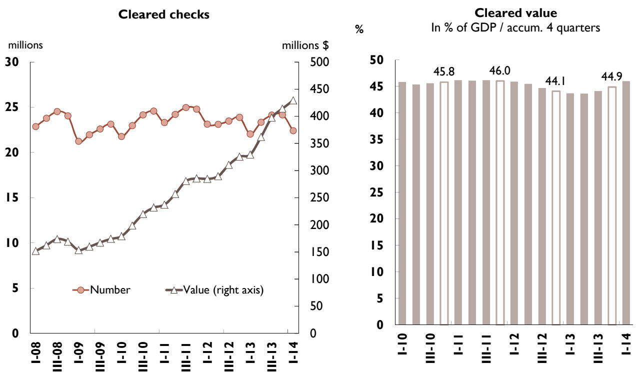
Instant Transfers by Channel



Source: BCRA

Chart VI.6

Checks



Source: BCRA

banking still holds a small share –1.1% in number and 0.4% in amount–, it has experienced a remarkable growth pace in 2013 (192% in number and 271% in amount).

In 2013, the use of checks went up 24.2% in terms of the total amount cleared and remained almost unchanged in terms of the total number of checks used (see Chart VI.6), exhibiting a mixed quarterly performance. In turn, during the first quarter of 2014, the use of this payment alternative experienced a 1.6% year-on-year (y.o.y.) growth in the number of documents. Relative to GDP, the amount of cleared checks recorded a slight rise in 2013, a trend that continued in the first quarter of 2014.

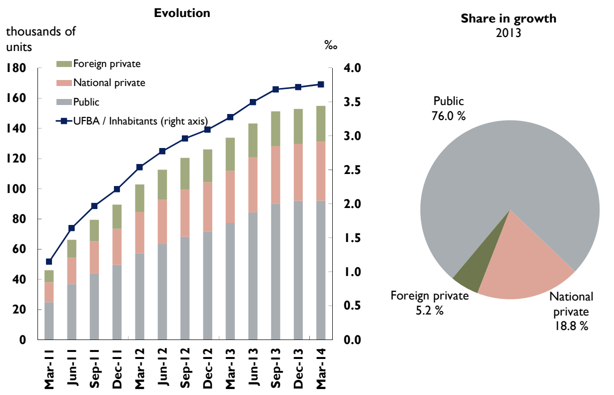
A comparison of the evolution of the main means of payment –alternative to cash– reveals a significant growth of the tools promoted by the BCRA —immediate electronic transfers— which would explain, in part and due to the replacement effect, the lower growth pace of other means of payment such as checks and non-immediate third party transfers (both in amount and number of monthly transactions) (see Chart VI.1). A medium-term comparison indicates that, by late 2013, whereas the amount of immediate transfers recorded a five-fold increase relative to their average monthly amount of 2011 (166% in transactions), the monthly amount of cleared checks went up 50% (down 4.1% in number) and non-immediate transfers increased 86% (15% in number).

As a sign of the ongoing diversification of payment instruments, the number of credit and debit cards continued to be on the rise during 2013, even though with a slight deceleration with respect to the growth pace they exhibited in previous years (see Chart VI.2). Total increase along the year was 9.3%, mainly driven by debit cards (up 11.2%), which accounted for 58.4% of the total change, while the expansion of credit cards contracted and reached a 7.6% y.o.y. growth. As regards the type of issuer, private banks recorded once again the highest relative expansion (8.6% in credit cards and 12.7% in debit cards), thus keeping the largest share in the cards in circulation (73.2% in total, 80% credit cards and 66.2% debit cards). The credit cards/population ratio continued to increase along the year and reached 0.73 per person —as well as debit cards ratio— in December. If this ratio is compared to that of other emerging and developed nations, there is still room to expand the use of this payment instrument.

For the purpose of continue increasing the use of banking services by the population, in September 2010, the Central Bank provided for the creation of the Free

Chart VI.7

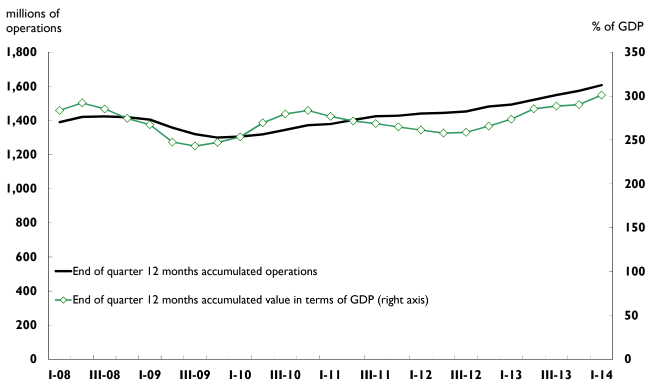
Universal Free Bank Accounts



Source: BCRA

Chart VI.8

Electronic Means of Payment - Peso Transactions Cleared



Source: BCRA

Universal Bank Account (CGU). During 2013, the use of CGUs kept on expanding, both in terms of number of accounts activated and in the proportion relative to the population, and by the end of 2013 there was a total of over 153,000 accounts, which entails a 21.3% rise in year-or-year terms (see Chart VI.7). The evolution of such accounts was mostly driven by public banks, accounting for 76% of the year-on-year growth. In early 2014, this trend continued to prevail, reaching a total stock of 155,000 accounts by the end of the first quarter of the current year.

Transactions in pesos made through Electronic Means of Payment (MEP) —a high-value payment system— rose by 6.2% y.o.y. in terms of amount and 31.6% y.o.y. in number during 2013. Transactions made through MEP expanded their share by 24 p.p. to almost three times the GDP (see Chart VI.8). On the other hand, this type of high-value transactions grew 9.4% y.o.y. in number and 41% in amount during the first months of 2014.

VI.2 Payment System Modernization

The Central Bank continues to promote measures to optimize the electronic means of payment and the use of alternative payments methods to cash within a context of remarkable relevance of these tools for the promotion of financial inclusion in our country.

To this effect, a general regulatory framework is being analyzed so as to cover the entire scope of pre-paid cards, i.e. the cards subject to an early payment scheme whereby an issuer other than the direct seller or supplier of the good or service receives a monetary amount that can be later used in a chain of stores or affiliated entities. In this sense, the pre-paid card SUBE is now available to pay tolls and it can also be used as pre-paid instrument to pay small amounts in stores.

In turn, in order to design a suitable and efficient regulatory framework for the normal development of the transactions made with mobile money[122], this Institution is working on the definition of regulations that may include appropriate incentives for the participants, giving predictability to the market while protecting the rights of the consumers of these services.

Recently, through the Bank Client Portal, the BCRA warned the public in general about the potential risks related to the use of the so-called "virtual currencies"[123]. Particularly, it has highlighted that this instrument is neither issued by central banks nor by any international

[122] E-money supported by the mobile phone. It includes virtual wallet and mobile banking.
[123] http://www.clientebancario.gov.ar/

monetary authority. As a result, these currencies do not have the status of legal tender money and have no support of any sort. Moreover, the price of virtual currencies has experienced a significant volatility in recent times, a risk that is exclusively taken by users. In this context, the BCRA is currently analyzing different scenarios so as to check that the transactions made with these assets do not become a risk for the aspects whose surveillance is expressly stated in the Central Bank Charter.

Lastly, it is worth stating that the Central Bank is constantly working to adjust all its procedures to the international basic principles in force in terms of the payment system. In this sense, it ordered the self-assessment of the principles of the CPSS (Committee on Payment and Settlement Systems) and the IOSCO (International Organization of Securities Commissions) for all the financial market infrastructures subject to the operation and/or regulation scope of the Central Bank in order to identify opportunities for improvement and verify the fulfillment of such principles at domestic level.

Statistics Annex* – Financial System

Chart 1 | Financial Soundness Indicators

As %	Dec 2005	Dec 2006	Dec 2007	Dec 2008	Dec 2009	Dec 2010	Dec 2011	Dec 2012	Mar 2013	Dec 2013	Mar 2014
1.- Liquidity	20.1	22.5	23.0	27.9	28.6	28.0	24.7	26.8	23.9	26.8	27.0
2.- Credit to the public sector	31.5	22.5	16.3	12.7	14.4	12.1	10.7	9.7	10.0	9.4	9.1
3.- Credit to the private sector	25.8	31.0	38.2	39.4	38.3	39.8	47.4	49.5	50.1	50.9	47.9
4.- Private non-performing loans	7.6	4.5	3.2	3.1	3.5	2.1	1.4	1.7	1.8	1.7	1.9
5.- Net worth exposure to the private sector	-2.5	-0.8	-1.5	-1.7	-1.3	-3.2	-4.3	-3.1	-2.8	-3.5	-3.3
6.- ROA	0.9	1.9	1.5	1.6	2.3	2.8	2.7	2.9	2.8	3.4	6.2
7.- ROE	7.0	14.3	11.0	13.4	19.2	24.4	25.3	25.7	24.9	29.5	49.9
8.- Efficiency	151	167	160	167	185	179	179	190	195	206	267
9a.- Capital compliance	-	-	-	-	-	-	-	-	14.3	13.6	13.3
9b.- Capital compliance (credit risk)	15.9	16.9	16.9	16.9	18.8	17.7	15.6	17.1	-	-	-
10a.- Capital compliance Tier I	-	-	-	-	-	-	-	-	12.9	12.5	12.4
10b.- Capital compliance Tier I (credit risk)	14.1	14.1	14.6	14.2	14.5	13.0	11.0	11.9	-	-	-
11.- Excess capital compliance	169	134	93	90	100	87	69	59	66	76	74

Note: According to Communication "A" 5369, since February 2013 methodological changes in some indicators were carried out. Among others changes, risk weighing coefficients considered to determine capital requirements were redefined, concepts included in the different segments of capital compliance were rearranged and new minimum limits in terms of the Total Risk Weighted Assets (RWA) were added. A wider definition of RWA is considered since Communication "A" 5369, including not only credit risk, but also market and operational risk.

Source: BCRA

Methodological note (chart 1)

1.- (Minimum cash compliance at the BCRA + Other cash holding + Financial entities net credit balance by LEBAC and NOBAC repo operations against the BCRA) / Total deposits; **2.-** (Public bonds position (without LEBAC and NOBAC) + Loans to the public sector + Compensation receivable) / Total assets; **3.-** (Loans to the private sector + Leases) / Total assets; **4.-** Non-performing loans to the non-financial private sector / Loans to the non-financial private sector; **5.-** (Total nonperforming private sector financing – Private sector financing loss provisions) / Net worth. The non-performing loans includes loans classified in situation 3,4,5 and 6; **6.-** Accumulated annual results / Average monthly netted assets - % Annualized; **7.-** Accumulated annual results / Average monthly net worth - % Annualized; **8.-** (Financial margin (Net interest income + CER and CVS adjustments + Gains on securities + Foreign exchange price adjustments + Other financial income) + Service income margin) / Operating costs; **9a.-** Capital compliance / Total risk weighted assets, according to the BCRA rule on minimum capital (Com. "A" 5369). Includes exemptions; **9b.-** Capital compliance / Credit risk weighted assets. Includes exemptions; **10a.-** Capital compliance Tier 1 (net of deductions) / Total risk weighted assets, according to the BCRA rule on minimum capital (Com. "A" 5369); **10b.-** Capital compliance Tier 1 (net of total deductions) / Credit risk weighted assets; **11.-** (Capital compliance - Capital requirement) / Capital requirement. Exemptions are

*Note | Data available in Excel in www.bcra.gov.ar

Statistics Annex* – Financial System (cont.)

Chart 2 | Balance Sheet

In million of current pesos	Dec 08	Dec 09	Dec 10	Dec 11	Dec 12	Mar 13	Dec 13	Mar 14	Change (in %) IT-14	Change (in %) Last 12 months
Assets	**346,762**	**387,381**	**510,304**	**628,381**	**790,026**	**812,195**	**1,004,892**	**1,099,941**	**9.5**	**35.4**
Cash disposal[1]	58,676	71,067	93,085	104,389	148,254	142,926	200,925	186,612	-7.1	30.6
Public bonds	65,255	86,318	117,951	112,906	123,491	135,720	141,494	199,640	41.1	47.1
Lebac/Nobac	37,093	43,867	76,948	71,050	84,057	92,167	89,641	145,753	62.6	58.1
Portfolio	25,652	34,748	61,855	59,664	70,569	86,197	88,091	118,964	35.0	38.0
Repo[2]	11,442	9,119	15,093	11,386	13,488	5,971	1,550	26,789	1,628.5	348.7
Private bonds	203	307	209	212	251	285	434	601	38.6	111.3
Loans	154,719	169,868	230,127	332,317	433,925	450,016	563,344	578,724	2.7	28.6
Public sector	17,083	20,570	25,907	31,346	39,951	40,270	48,438	49,252	1.7	22.3
Private sector	132,844	145,247	199,202	291,708	383,674	399,497	501,857	517,023	3.0	29.4
Financial sector	4,793	4,052	5,018	9,263	10,299	10,249	13,049	12,449	-4.6	21.5
Provisions over loans	-4,744	-5,824	-6,232	-7,173	-9,596	-10,102	-12,388	-13,596	9.8	34.6
Other netted credits due to financial intermediation	38,152	33,498	39,009	40,805	38,769	34,652	42,435	71,937	69.5	107.6
Corporate bonds and subordinated debt	912	1,146	1,433	1,657	2,255	2,183	5,421	5,675	4.7	159.9
Unquoted trusts	5,714	5,942	6,824	7,967	10,822	11,541	12,656	13,822	9.2	19.8
Leasing	3,935	2,933	3,936	6,222	7,203	7,294	9,460	9,572	1.2	31.2
Shares in other companies	7,236	6,711	7,921	9,123	11,682	12,463	15,205	16,648	9.5	33.6
Fixed assets and miscellaneous	7,903	8,239	9,071	10,111	11,251	11,468	14,226	15,041	5.7	31.1
Foreign branches	3,153	3,926	3,283	3,525	4,354	4,540	5,611	6,918	23.3	52.4
Other assets	12,275	10,337	11,943	15,944	20,441	22,937	24,933	28,579	14.6	24.6
Liabilities	**305,382**	**339,047**	**452,752**	**558,264**	**699,205**	**714,415**	**883,889**	**962,470**	**8.9**	**34.7**
Deposits	236,217	271,853	376,344	462,517	595,764	616,098	752,422	788,348	4.8	28.0
Public sector[3]	67,151	69,143	115,954	129,885	163,691	165,556	202,434	206,850	2.2	24.9
Private sector[3]	166,378	199,278	257,595	328,463	427,857	445,299	544,332	574,498	5.5	29.0
Current account	39,619	45,752	61,306	76,804	103,192	101,696	125,237	123,799	-1.1	21.7
Savings account	50,966	62,807	82,575	103,636	125,210	126,087	158,523	154,995	-2.2	22.9
Time deposit	69,484	83,967	104,492	135,082	183,736	202,492	241,281	276,066	14.4	36.3
Other netted liabilities due to financial intermediation	57,662	52,114	60,029	76,038	75,106	67,141	92,634	125,197	35.2	86.5
Interbanking obligations	3,895	3,251	4,201	7,947	8,329	8,075	10,596	9,927	-6.3	22.9
BCRA lines	1,885	270	262	1,920	3,535	3,927	4,693	4,776	1.8	21.6
Outstanding bonds	5,984	5,033	3,432	6,856	9,101	9,551	14,198	15,749	10.9	64.9
Foreign lines of credit	4,541	3,369	3,897	6,467	4,992	4,485	6,328	8,278	30.8	84.5
Other	13,974	14,891	17,426	24,137	26,280	23,724	41,345	42,068	1.7	77.3
Subordinated debts	1,763	1,922	2,165	2,065	2,647	2,462	3,425	3,971	15.9	61.3
Other liabilities	9,740	13,159	14,213	17,644	25,688	28,669	35,407	44,860	26.7	56.5
Net worth	**41,380**	**48,335**	**57,552**	**70,117**	**90,820**	**97,505**	**121,800**	**138,171**	**13.4**	**41.7**
Memo										
Netted assets	321,075	364,726	482,532	601,380	767,744	795,317	990,614	1,057,919	6.8	33.0
Consolidated netted assets	312,002	357,118	472,934	586,805	750,598	778,015	969,247	1,036,701	7.0	33.2

(1) Includes margin accounts with the BCRA. (2) Booked value from balance sheet (it includes all the counterparts). (3) Does not include accrual on interest or CER.

Source: BCRA

*Note | Data available in Excel in www.bcra.gov.ar

Statistics Annex* – Financial System (cont.)

Chart 3 | Profitability Structure

Amount in million of pesos	Annual						Semester		Last 12 months*
	2008	2009	2010	2011	2012	2013	I-13	II-13	
Financial margin	20,462	28,937	35,490	43,670	61,667	88,509	36,638	51,870	108,391
Net interest income	9,573	14,488	17,963	24,903	38,365	50,336	23,152	27,184	54,372
CER and CVS adjustments	2,822	1,196	2,434	1,725	2,080	2,153	1,068	1,085	2,876
Foreign exchange price adjustments	2,307	2,588	2,100	3,025	4,127	11,287	3,454	7,833	19,854
Gains on securities	4,398	11,004	13,449	14,228	17,356	22,280	9,057	13,223	24,548
Other financial income	1,362	-339	-457	-211	-261	2,454	-91	2,545	6,740
Service income margin	10,870	13,052	16,089	21,391	28,172	36,503	17,133	19,370	38,875
Loan loss provisions	-2,839	-3,814	-3,267	-3,736	-6,127	-9,349	-3,979	-5,370	-10,316
Operating costs	-18,767	-22,710	-28,756	-36,365	-47,318	-60,722	-28,703	-32,019	-65,384
Tax charges	-2,318	-3,272	-4,120	-6,047	-8,981	-13,916	-6,140	-7,776	-15,706
Adjust. to the valuation of gov. Securities[1]	-1,757	-262	-214	-336	-338	-377	-182	-196	-534
Amort. payments for court-ordered releases	-994	-703	-635	-290	-274	-128	-60	-68	-109
Other	1,441	918	2,079	2,963	2,475	2,576	1,721	855	2,919
Total results before tax[2]	6,100	12,145	16,665	21,251	29,276	43,094	16,428	26,666	58,136
Income tax	-1,342	-4,226	-4,904	-6,531	-9,861	-13,951	-5,637	-8,314	-18,456
Total result[2]	**4,757**	**7,920**	**11,761**	**14,720**	**19,415**	**29,143**	10,791	18,352	39,680
Adjusted Result[3]	7,508	8,885	12,610	15,345	20,027	29,649	11,033	18,615	40,322
Annualized indicators - As % of netted assets									
Financial margin	6.7	8.6	8.5	8.0	9.2	10.3	9.2	11.4	11.8
Net interest income	3.1	4.3	4.3	4.6	5.7	5.9	5.8	6.0	5.9
CER and CVS adjustments	0.9	0.4	0.6	0.3	0.3	0.3	0.3	0.2	0.3
Foreign exchange price adjustments	0.8	0.8	0.5	0.6	0.6	1.3	0.9	1.7	2.2
Gains on securities	1.4	3.3	3.2	2.6	2.6	2.6	2.3	2.9	2.7
Other financial income	0.4	-0.1	-0.1	0.0	0.0	0.3	0.0	0.6	0.7
Service income margin	3.6	3.9	3.8	3.9	4.2	4.3	4.3	4.3	4.2
Loan loss provisions	-0.9	-1.1	-0.8	-0.7	-0.9	-1.1	-1.0	-1.2	-1.1
Operating costs	-6.1	-6.7	-6.9	-6.7	-7.0	-7.1	-7.2	-7.0	-7.1
Tax charges	-0.8	-1.0	-1.0	-1.1	-1.3	-1.6	-1.5	-1.7	-1.7
Adjust. to the valuation of gov. Securities[1]	-0.6	-0.1	-0.1	-0.1	-0.1	0.0	0.0	0.0	-0.1
Amort. payments for court-ordered releases	-0.3	-0.2	-0.2	-0.1	0.0	0.0	0.0	0.0	0.0
Other	0.5	0.3	0.5	0.5	0.4	0.3	0.4	0.2	0.3
Total results before tax[2]	2.0	3.6	4.0	3.9	4.3	5.0	4.1	5.9	6.3
Income tax	-0.4	-1.3	-1.2	-1.2	-1.5	-1.6	-1.4	-1.8	-2.0
ROA[2]	**1.6**	**2.3**	**2.8**	**2.7**	**2.9**	**3.4**	**2.7**	**4.0**	**4.3**
ROA adjusted[3]	2.5	2.6	3.0	2.8	3.0	3.5	2.8	4.1	4.4
ROE before tax	*17.2*	*29.5*	*34.5*	*36.5*	*38.8*	*43.7*	*35.8*	*50.5*	*53.5*
ROE [2]	*13.4*	*19.2*	*24.4*	*25.3*	*25.7*	*29.5*	*23.5*	*34.7*	*36.5*

((1) Com. "A" 3911. Adjustments to the valuation of government unlisted securities according to Com. "A" 4084 are included under the "gains from securities" heading.
(2) As of January 2008, data to calculate financial system consolidated result is available. This indicator excludes results and asset headings related to shares and participation in other local financial entities.
(3) Excluding amortization of payments for court-ordered releases and the effects of Com. "A" 3911 and 4084.
* to March 2014
Source: BCRA

Chart 4 | Porfolio Quality

As percentage	Dec 05	Dec 06	Dec 07	Dec 08	Dec 09	Dec 10	Dec 11	Dec 12	Mar 13	Dec 13	Mar 14
Non-performing loans (overall)	**5.2**	**3.4**	**2.7**	**2.7**	**3.0**	**1.8**	**1.2**	**1.5**	**1.6**	**1.5**	**1.6**
Provisions / Non-performing loans	115	108	115	117	115	148	176	144	140	150	149
(Total non-perfoming - Provisions) / Overall financing	-0.8	-0.3	-0.4	-0.5	-0.5	-0.9	-0.9	-0.7	-0.6	-0.8	-0.8
(Total non-perfoming - Provisions) / Net worth	-2.6	-0.9	-1.6	-1.8	-1.7	-3.6	-4.6	-3.4	-3.1	-3.7	-3.5
Non-performing loans to the non-financial private sector	**7.6**	**4.5**	**3.2**	**3.1**	**3.5**	**2.1**	**1.4**	**1.7**	**1.8**	**1.7**	**1.9**
Provisions / Non-performing loans	115	108	114	116	112	143	171	141	137	148	147
(Total non-perfoming - Provisions) / Overall financing	-1.1	-0.3	-0.5	-0.5	-0.4	-0.9	-1.0	-0.7	-0.7	-0.8	-0.9
(Total non-perfoming - Provisions) / Net worth	-2.5	-0.8	-1.5	-1.7	-1.3	-3.2	-4.3	-3.1	-2.8	-3.5	-3.3

Source: BCRA

Abbreviations and Acronyms

AEIRR: Annual Effective Internal Rate of Return

AFJP: *Administradora de Fondos de Jubilaciones y Pensiones.*

ANSES: *Administración Nacional de Seguridad Social*. National Social Security Administration.

APE: *Acuerdos Preventivos Extra-judiciales.* Preliminary out-of-court agreements.

APR: Annual Percentage Rate.

b.p.: basis points.

BADLAR: Interest rate for time deposits over one million pesos between 30 and 35 days for the average of financial institutions.

BCBA: *Bolsa de Comercio de Buenos Aires.* Buenos Aires Stock Exchange.

BCRA: *Banco Central de la República Argentina*. Central Bank of Argentina.

BIS: Bank of International Settlements.

BM: Monetary Base. Defined as money in circulation plus current account deposits in pesos by financial institutions in the BCRA.

Boden: *Bonos del Estado Nacional.*Federal Bonds.

Bogar: *Bonos Garantizados.* Guaranteed Bonds.

BoJ: Bank of Japan.

Bonar: *Bonos de la Nación Argentina.* Argentine National Bonds.

BOVESPA: São Paulo Stock Exchange.

CAMEL: Capital, Assets, Management, Earnings and Liquidity.

Cdad. de Bs. As.: *Ciudad de Buenos Aires. Buenos Aires City.*

CDS: Credit Default Swaps

CEC: *Cámaras Electrónicas de Compensación.* Electronic Clearing Houses.

CEDEM: *Centro de Estudios para el Desarrollo Económico Metropolitano.* Study Center for Metropolitan Economic Development.

CEDRO: *Certificado de Depósito Reprogramado.* Rescheduled Deposit Certificate.

CER: *Coeficiente de Estabilización de Referencia.* Reference Stabilization Coefficient.

CIMPRA: *Comisión Interbancaria para Medios de Pago de la República Argentina.*

CNV: *Comisión Nacional de Valores.* National Securities Commission

CPI: Consumer Price Index.

CPI Others: *CPI excluidos los bienes y servicios con alta estacionalidad, volatilidad o los sujetos a regulación o alto componente impositivo*. CPI excluded goods and services with high seasonal and irregular components, regulated prices or high tax components

Credit to the public sector: includes the position in government securities (excluding LEBAC and NOBAC), loans to the public sector and compensation receivable.

CVS: *Coeficiente de Variación Salarial.* Wage variation coefficient.

DGF: Deposit Guarantee Fund.

Disc: Discount bond.

EB: Executive Branch.

ECB: European Central Bank.

EMBI: Emerging Markets Bond Index.

EMI: *Estimador Mensual Industrial.* Monthly Industrial Indicator

EPH: *Encuesta Permanente de Hogares.* Permanent Household Survey.

Fed: Federal Reserve of US.

FOMC: Federal Open Market Committee (US).

FS: Financial Stability.

FSR: Financial Stability Report.

FT: Financial trust.

FUCO: *Fondo Unificado de Cuentas Corrientes Oficiales*. Unified Official Current Account Fund.

FV: Face value.

GDP: Gross Domestic Product.

HHI: Herfindahl-Hirschman Index.

IADB: Inter-American Development Bank.

IAMC: *Instituto Argentino de Mercado de Capitales.*

ICs: Insurance Companies.

IDCCB: *Impuesto a los Débitos y Créditos en Cuentas Bancarias*. Tax on Current Account Debits and Credits.

IFI: International Financial Institutions: IMF, IADB and WB.

IFS: International Financial Statistics.

IMF: International Monetary Fund.

INDEC: *Instituto Nacional de Estadísticas y Censos*. National Institute of Statistics and Censuses.

IndeR: *Instituto Nacional de Reaseguros.* National Institute of Reinsurance.

IPMP: *Índice de Precios de las Materias Primas*. Central Bank Commodities Price Index.

IPSA: *Índice de Precios Selectivo de Acciones*. Chile Stock Exchange Index.

IRR: Internal Rate of Return.

ISAC: *Índice Sintético de Actividad de la Construcción.* Construction Activity Index.

ISDA: International Swaps and Derivates Association.

ISSP: *Índice Sintético de Servicios Públicos.* Synthetic Indicator of Public Services.

Lebac: *Letras del Banco Central de la República Argentina*. BCRA bills.

LIBOR: London Interbank Offered Rate.

m.a.: Moving average.

M2: Currency held by public + quasi-monies + $ saving and current accounts.

M3: Currency held by public + quasi-monies + $ total deposits.

MAE: *Mercado Abierto Electrónico*. Electronic over-the-counter market.

MAS: Mutual Assurance Societes.

MC: Minimum cash.

MEC: Electronic Open Market.

MECON: Ministerio de Economía y Producción. Ministry of Economy and Production.

MEP: *Medio Electrónico de Pagos*. Electronic Means of Payment.

MERCOSUR*: Mercado Común del Sur***.** Southern Common Market.

MERVAL: *Mercado de Valores de Buenos Aires.* Executes, settles and guarantees security trades at the BCBA.

MEXBOL: *Índice de la Bolsa Mexicana de Valores.* México Stock Exchange Index.

MF: Mutual Funds.

MIPyME: *Micro, Pequeñas y Medianas Empresas.* Micro, Small and Medium Sized Enterprises.

MOA: *Manufacturas de Origen Agropecuario.* Manufactures of Agricultural Origin.

MOI: *Manufacturas de Origen Industrial.* Manufactures of Industrial Origin.

MP: Monetary Program.

MR: Market rate.

MRO: *Main refinancing operations.*

MSCI: Morgan Stanley Capital International.

NA: Netted assets.

NACHA: National Automated Clearinghouse Association.

NBFI: Non-Bank Financial Institutions (under Central Bank scope)

NBFI : Non-Bank Financial Intermediaries (out of Central Bank scope)

NDP: National public debt.

NFPS: Non-financial national public sector's.

Nobac: *Notas del Banco Central*. BCRA notes.

NPS: National Payments System.

NW: Net worth.

O/N: Overnight rate.

OCT : *Operaciones Compensadas a Término***.** Futures Settlement Round.

OECD: Organization for Economic Co-operation and Development.

ON: *Obligaciones Negociables*. Corporate bonds.

ONCCA: *Oficina Nacional de Control Comercial Agropecuario*

OS: *Obligaciones Subordinadas*. Subordinated debt.

P / BV : Price over book value.

p.p.: Percentage point.

Par: Par bond.

PGN: *Préstamos Garantizados Nacionales*. National Guaranteed Loans.

PF: Pension Funds.

PPP: Purchasing power parity.

PPS: Provincial public sector.

PS: Price Stability.

PV: Par Value.

q.o.q: quarter-on-quarter % change.

REM: BCRA Market expectation survey.

ROA: Return on Assets.

ROE: Return on Equity.

Rofex: Rosario Futures Exchange.

RPC: *Responsabilidad Patrimonial Computable*. Adjusted stockholder's equity, calculated towards meeting capital regulations.

RTGS: Real-Time Gross Settlement.

s.a.: Seasonally adjusted.

SAFJP: *Superintendencia de Administradoras de Fondos de Jubilaciones y Pensiones*. Superintendency of Retirement and Pension Funds Administrations.

SAGPyA: *Secretaría de Agricultura, Ganadería, Pesca y Alimentos*. Secretariat for agriculture, livestock, fisheries, and food.

SEDESA: *Seguro de Depósitos Sociedad Anónima.*

SEFyC: Superintendence of Financial and Exchange Institutions.

SIOPEL: *Sistema de Operaciones Electrónicas.* Trading software used on the over-the-counter market.

SME: Small and Medium Enterprises.

SSN: *Superintendencia de Seguros de la Nación.*

TA: *Adelantos transitorios del BCRA al Tesoro*. Temporary advances.

TD: Time Deposits.

TFC: Total financial cost.

TGN: *Tesorería General de la Nación.* National Treasury

UFC: Uniform Federal Clearing.

UIC: Use of Installed Capacity.

UK: United Kingdom.

US$: United States dollar.

US: United States of America.

UTDT: Universidad Torcuato Di Tella.

VaR: Value at Risk.

VAT: Value added Tax.

WB: World Bank.

WPI: Wholesale Price Index.

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