



Financial Stability Report

Second Half 2010



BANCO CENTRAL
DE LA REPÚBLICA ARGENTINA

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Preface

Financial stability is a state of affairs in which the financial services sector can channel the savings of the population and provide a nationwide payments system in a manner that is efficient, secure and sustainable over time. In the framework of the execution of consistent and stable macroeconomic policies, the resilience of the financial sector in the face of negative shocks serves to define the degree of approach towards a financial stability scheme.

The strong interrelationship between financial stability and sustained economic growth explains why the former is a social good that the state has to generate and protect. This is why the promotion of financial stability is one of the principal functions of most central banks.

The Central Bank of Argentina, according to article 4 of its charter, has a mandate “to supervise the sound operation of the financial market”. It is the Central Bank understanding that in order to enhance the effectiveness of the policies that it undertakes its usual regulatory and supervisory powers must be complemented by a communications strategy that is transparent and accessible to the public in general.

With this purpose in mind it publishes the Financial Stability Report (FSR) that presents an overall assessment of developments in the conditions of financial stability. In the FSR the different channels of information that are available on the subject are merged, to provide the Central Bank’s views on the outlook for the financial system. Furthermore, between each half-yearly issue of the FSR, the Central Bank releases a monthly Report on Banks to keep the public up to date about the more recent developments in the financial system.

According to the depth of detail that the reader requires, the FSR can be approached in two different ways. Reading the Central Bank Outlook and the Balance of Risks, together with the summary and main topics of each chapter, enables the reader to grasp the gist of the FSR. Naturally, a full reading of the FSR provides an in depth evaluation of the issues it covers, enriched by the treatment of special topics that are included in the Boxes.

The date of publication of the next issue of the FSR will be on March 31, 2011, on the Central Bank website.

Buenos Aires, September 30, 2010

Contents

Pag. 7 | Central Bank Outlook

Pag. 11 | I. International Context

Pag. 17 | Box 1 / Vulnerable Economies of the Euro Area and Situation of the International Markets

Pag. 19 | II. Local Context

Pag. 24 | Box 2 / Implications of the 2010 Sovereign Debt Swap

Pag. 29 | III. Debtors Performance

Pag. 37 | IV. Financial Sector

Pag. 42 | Box 3 / Banking Services in Argentina

Pag. 46 | Box 4 / Regional Credit Distribution

Pag. 52 | Box 5 / Financial Conglomerates

Pag. 57 | V. Financial System Risks

Pag. 59 | Box 6 / International Consensus on Financial Regulation Proposals

Pag. 70 | Box 7 / Outline of the Financial Reform in the United States

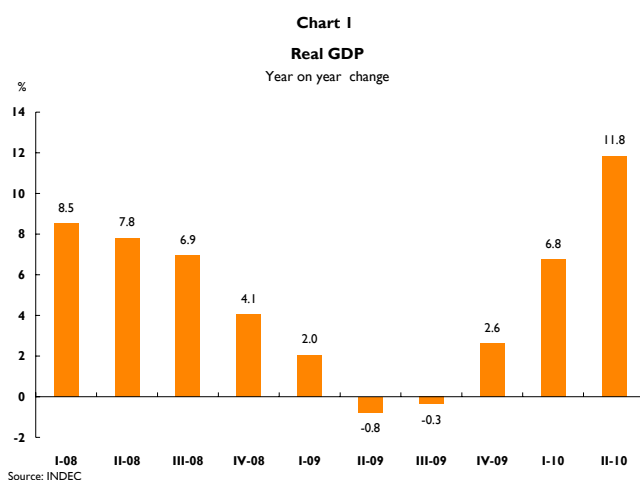
Pag. 73 | VI. Payments System

Pag. 77 | Statistics Annex

Pag. 81 | Abbreviations and Acronyms

Pag. 83 | Index of Charts and Tables

Central Bank Outlook



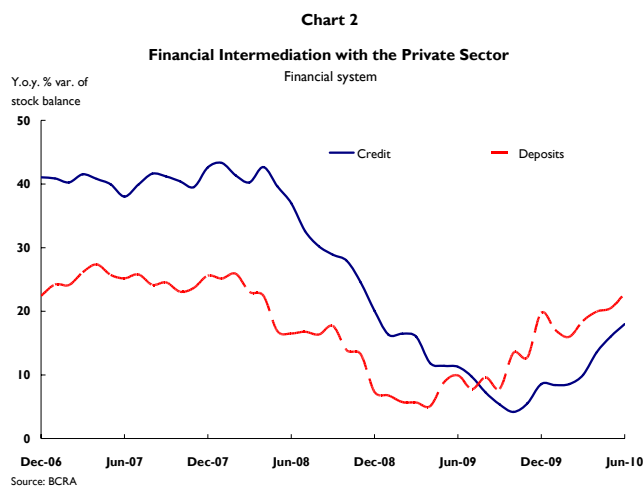
The international scenario evidenced new episodes of financial turbulence during the first half 2010, mainly related to the uncertainty regarding the financial capacity of the most vulnerable states of the Euro Area (see Box 1). This context was deepened by concerns surrounding the weak momentum shown by the world economy, especially by the US, which led authorities of most developed countries to postpone the exit of stimulus policies implemented over the last years. In this framework, a different performance is taking place between emerging and developed economies, where the former are leading the world growth, which would amount to 3.8% in 2010¹, while the latter would record lower expansions. Emerging economies are evidencing a positive perspective which implies a constructive overview for their asset prices.

Regarding the local context, **the improvement of the economic activity deepened over the last months reaching growth rates similar to those recorded prior to the international crisis that started in 2008.** This evolution is led by households' consumption and investment recovery. It should be considered that the upturn of economic activity has been generalized among all productive sectors and households' income, and is being reflected on their respective financial and economic performance.

The expansion rate shown by banks' financial intermediation with the private sector accelerated at the beginning of the year. Both **lending to companies and households as well as deposits improved their year-on-year (y.o.y.) growth even though the financial system's depth levels remain relatively low** against other emerging economies. The share of assets with greater liquidity posted an increase while financing to the private sector weighting rose again over the last months.

The rising credit expansion was mainly channeled towards short term commercial credit lines and consumption loans to households which was reflected on the average maturity of new loans. **From a policy aimed at achieving higher credit depth especially in the case of productive investment, the BCRA implemented a new line of loans for financial entities with a maximum 5-year term.** Such funds should be used by banks to finance private sector investment projects with a period equal to or exceeding two and half years. Credit lines will have a fixed interest rate to be determined through an auction process.

¹ Source: FocusEconomic



Bank funding through deposits of the private and public sector continued gaining share while foreign funds exhibited a low and decreasing weighting. In a context where international markets' volatility persists, this characteristic is a sign of strength for the sector by reducing a source of potential contagion.

During the first half of 2010, **the financial system evidenced certain improvements on its intrinsic risks map related to its traditional activity of financial intermediation.** The position of banks in the face of liquidity risk was favored by the increase of liquid assets, greater depth of financial markets and less volatility of interest rates.

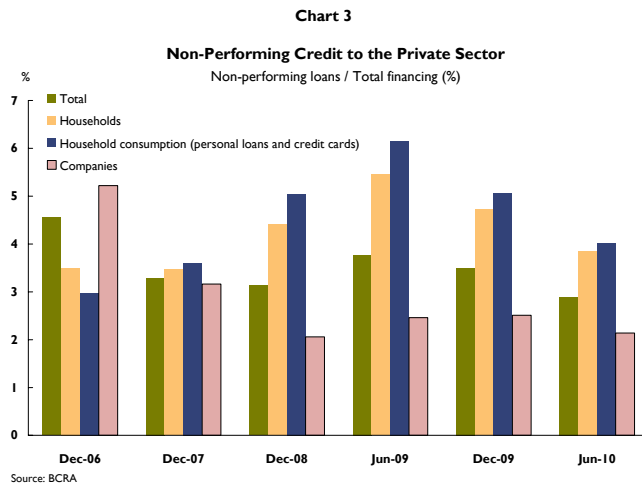
Over the last months **financial system's loans portfolio quality continued improving and this was reflected on a lower credit risk faced by banks.** Progress made in economic activity coupled with moderate indebtedness levels favored the payment capacity of the main debtors. As a sign of these developments, bank financing delinquency kept falling in 2010. The improvement in credit portfolio quality was primarily accounted for consumption loans to households and, to a lesser extent, by lending to companies. Non-performing loan provision coverage continued growing. Banks are expected to gradually increase their exposure to the private sector during the rest of 2010, thereby remaining at a favorable position when considering the credit risk faced.

Banks' exposure to the public sector fell slightly during the first part of 2010, within a context where positive perspectives prevail for the sector resulting from the recent sovereign debt swap (see Box 2), from the maintenance of the primary fiscal result and from moderate indebtedness level. **When considering the public sector deposits stocks the Government remains as a net creditor of the financial system (approximately 10% of total assets).**

During the first part of the year, the mismatching of banks' maturities did not show significant changes, within a context of slight reduction in the maturity of assets and liabilities. The main interest rates dropped gradually and exhibited less volatility thereby decreasing the interest rate risk taken by banks in their intermediation activity. The BCRA continues participating in the interest rate futures market through the so-called "función giro", providing an additional tool to manage part of this risk. An increase in holdings of mark to market instruments in banks' portfolios together with improved values of the leading securities,

led to a small increase in the system's exposure to market risk, even though it is still low.

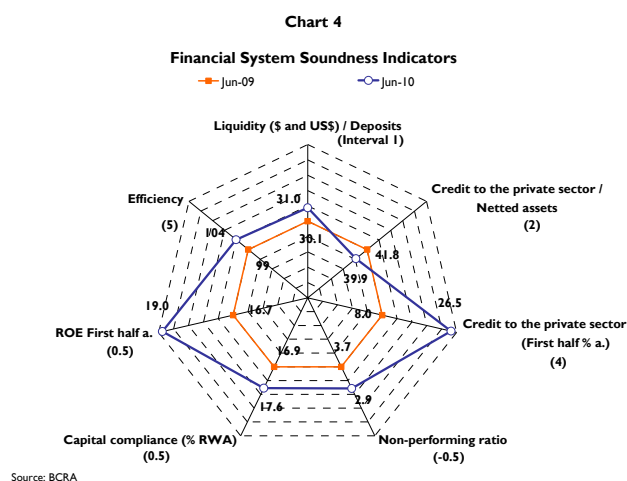
Financial system's balance sheet exposure to foreign currency mismatch risk increased slightly during the first part of 2010, remaining at historically low levels. It is noticeable that the counterparty risk faced by the financial system derived from potential fluctuations in the peso-dollar exchange rate remained limited.



Banks continued developing their transactions in a context of high solvency levels. Financial system capital compliance continued exceeding the regulatory requirement with accounting profits that boost the sector's net-worth position. The rise observed by the sector's profitability over the last periods as a consequence of higher net interest income and service income margin, and the recovery of gains on securities resulting from holdings of public sector instruments, led some private financial entities to distribute significant dividends over the first part of 2010. This took place without affecting entities' solvency or their capacity to continue increasing lending to companies and households during the coming months.

The National Payment System (NPS) continued improving the instruments available to speed up periodic economic transactions and to provide a greater security framework. Clearing checks increased (with lower levels of bounced checks for non-sufficient funds) while the number of debit and credit cards handled by households and companies rose, as well as the use of direct debits and retail transfers. **Recently, the BCRA decided to boost the use of electronic means of payments in the economy** and discourage the use of cash. This would allow to increase the safety of transactions, as well as favor the banking access of different socioeconomic segments of the population and companies (particularly, small and medium size companies) which, at present, cannot access financial services (see Box 3). In Particular, a free universal banking account "Cuenta Gratuita Universal" was created (with a maximum balance amounting to \$10,000) –Comm. "A" 5127- that banks will have to make available to households, free of charge, in pesos and with the submission of the National Identity Document (DNI) as the only requirement. Such accounts include a free debit card for transactions conducted in automatic teller machines belonging to the issuing entity.

Meanwhile, a cost reduction of inter-bank transfers was promoted, allowing free transactions in those cases that do not exceed \$10,000 daily, both for transfers



conducted through the home banking system (internet) or automatic teller machines. Commissions for transactions made at the branches' offices will have a maximum charge depending on the amount, which will also serve as a reference for transfers exceeding \$10,000 via home banking. The use of settlement checks issued by the BCRA both in pesos and in dollars will also be promoted.

The level of employment and operating infrastructure of the financial system expanded along the last months accompanying the growth of the financial intermediation activity and the provision of means of payment of the economy. Notwithstanding the foregoing, there exists significant heterogeneity in different regions of Argentina regarding the availability of bank infrastructure, being in general less provided those localities with less population. Taking this situation into account, the BCRA authorized the settlement of special service offices to conduct specific transactions in localities having less than 30,000 inhabitants, providing facilities for financial entities that decide to lead the banking process (as a matter of fact, an entity has recently started to use this mechanism).

The positive economic scenario expected for the coming periods would allow anticipating that the configuration of risks faced by the financial sector would improve gradually with higher levels of financial intermediation with companies and households. The BCRA will continue designing policies that will contribute to favor greater credit deepening to the private sector, giving rise to further use of electronic means of payment that provide greater security to the population when conducting their regular transactions, and extending banking in the most homogeneous manner at a regional level and among different socioeconomic segments of the population.

I. International Context

Summary

The global economic activity continues to expand, with a growth that would be around of 3.8% over the course of 2010, driven primarily by emerging economies. In recent months slower growth rates of advanced economies are observed, in a scenario in which neither the job market nor the financial services sector fully recovered.

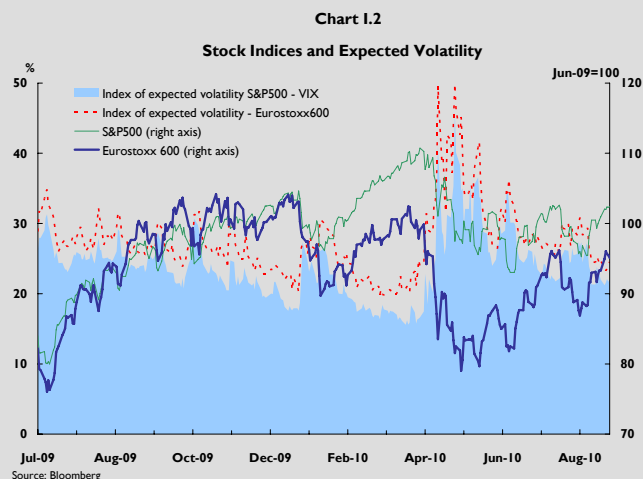
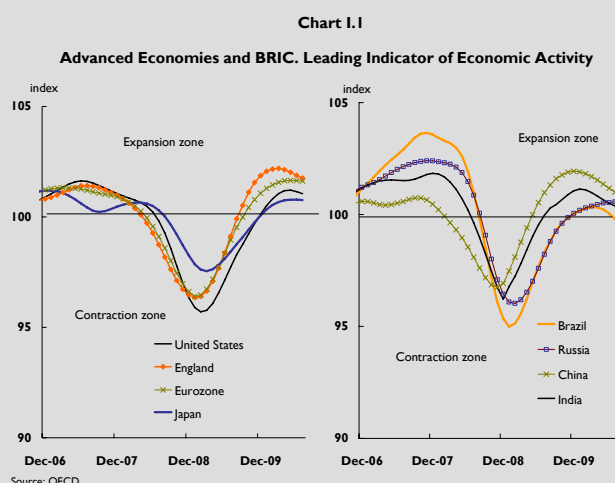
The international context exhibited new focuses of financial turbulence in the early months of 2010, mainly related with the uncertainty about the ability of the most vulnerable economies in the euro area to meet their debt service payments. This situation, coupled with concerns over the slowdown of the global economy in general and that of the US in particular, led the authorities of most developed economies to maintain the commitment to support markets in a still weak scenario, delaying the exit from stimulus policies implemented in the context of the international crisis.

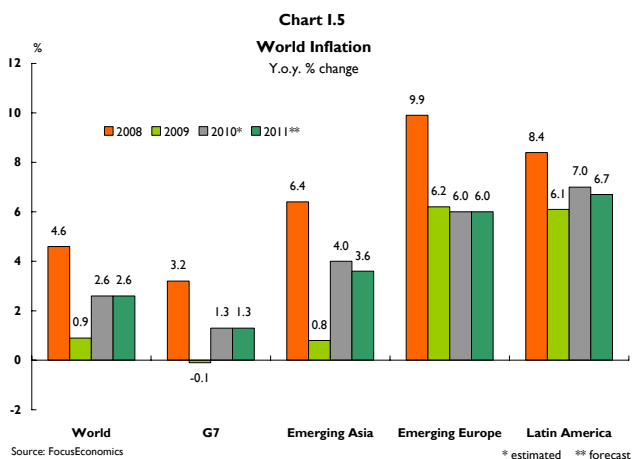
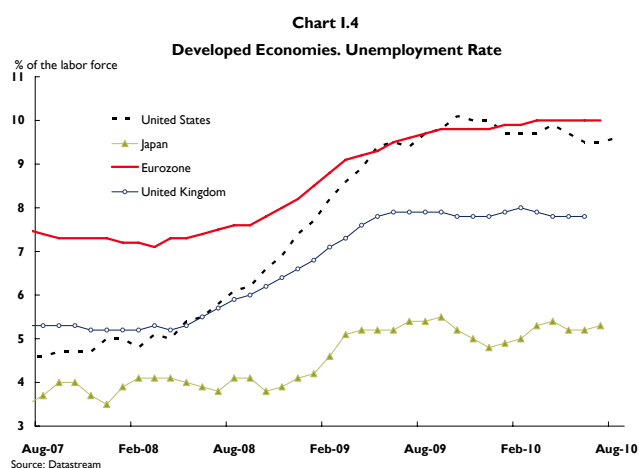
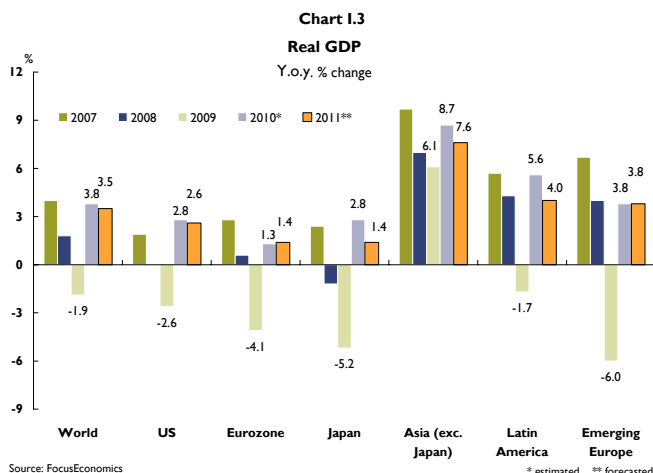
The uncertainty in international financial markets implied certain volatility to the trend of raw materials prices, showing a decline so far this year. For the remainder of 2010, commodity prices are expected to remain at similar levels, given the weak global economic recovery and the record harvests of corn and soybeans. However, upward pressure on prices due to weather events that could affect grain production in the coming months are not ruled out.

The broader uncertain context of financial markets led to a more selective behavior by investors. While risky assets (equities and debt of vulnerable economies) exhibited less support and showed greater volatility, yields on long-term government bonds of countries like the US and Germany shrank steadily since May, returning to historically low levels.

The best macroeconomic outlook for emerging economies generated a positive performance of stock indexes in recent months, although this trend was not without its ups and downs, accompanying changes in the global risk aversion. Spreads on sovereign debt in dollars also showed a changing pattern, although levels are located near the minimum of the year.

The Latin American financial systems recovered their dynamism of granting loans to companies and households, after the regional impact of the international financial crisis. The levels of liquidity and solvency continued to represent the main strength of these sectors, in a scenario where reduced credit risk continued (which is reflected in the low delinquency levels regarding other emerging and developed economies). The good economic growth prospects for the coming period would contribute to the establishment of a suitable framework to consolidate the conditions for financial stability in the region.





I.1 International context

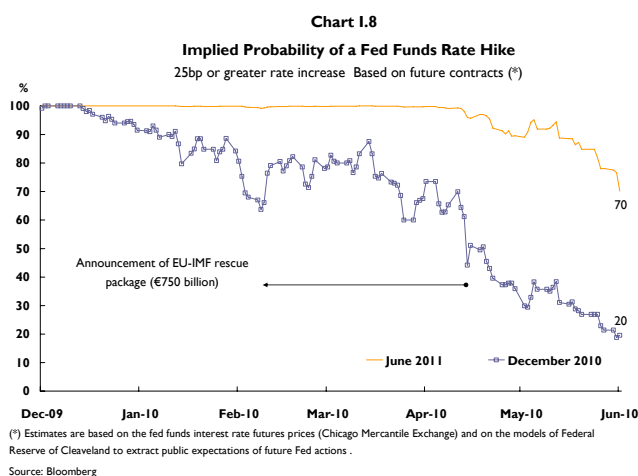
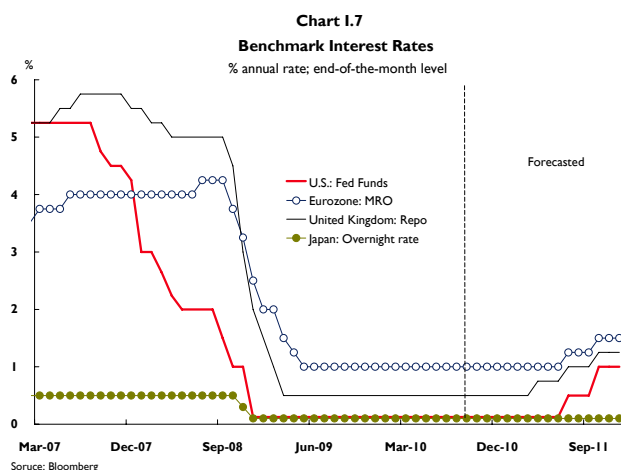
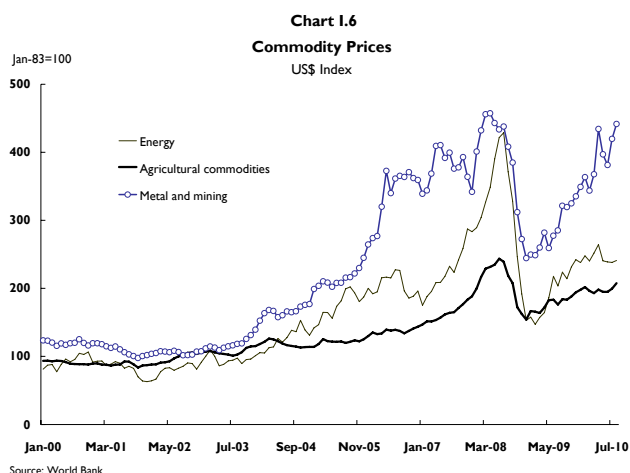
In 2010 the global economic activity continued to expand, being mainly driven by emerging countries

Global economic activity showed an expansion in the first half of the year, led by emerging economies. In recent months, however, some signs of a widespread slow down are observed (see Chart I.1), a trend likely to persist until the end of 2010. International trade continues to grow with prospects for further improvement albeit at a lower pace.

World GDP would grow about 3.8% in 2010 (see Chart I.3), 2.6% and 6.8% in advanced and in emerging countries respectively, with a significant contribution to this latter case of the Asian countries (particularly China and India). The gradual economic slowdown observed in recent months, coupled with both high levels of unemployment (see Chart I.4) and a still incomplete normalization of the international financial system, would increase to some extent the risks related to the economic recovery of industrialized countries. During the first semester the international context exhibited new sources of financial turmoil associated with the uncertainty surrounding the ability to refinance the debt service on certain European economies.

A slight increase in retail prices in 2010 (close to 1.3% year-on-year-) would be observed in advanced countries while in most of the economies would be below the targets set by the monetary authorities. Emerging countries would also show an increase in the rate of price change, mainly as a result of economic recovery. These levels would remain below those observed before the beginning of the international financial crisis (see Chart I.5).

The uncertainty in international financial markets implied some volatility to the path of commodity prices (see Chart I.6). On the other hand, the best weather conditions contributed to reach the world record harvests in the main export products of Argentina, pushing their prices down. The strong demand for these products for food and fodder and for the development of biofuels, limited the downward trend. However, in recent months significant rises in the price of wheat was observed dragging other grain prices higher, given the drought that occurred in the Black Sea area and affected the production of wheat from Russia, Ukraine and other Eastern European countries (in all cases scale global producers). Prices of industrial products grew due to higher demand compared to 2009, although limited by the uncertainty of the impact of the economic crisis in



Europe on the world and, more recently, by the weak US growth.

Thus, the Commodities Price Index (IPMP)² accumulated so far in 2010 an increase of 2.6%. For the remainder of the year some stability in prices of primary commodities is expected, given the global economic recovery and record harvests of corn and soybeans, while possible increases arising on climatic factors that could affect the grain production in the coming months are not ruled out.

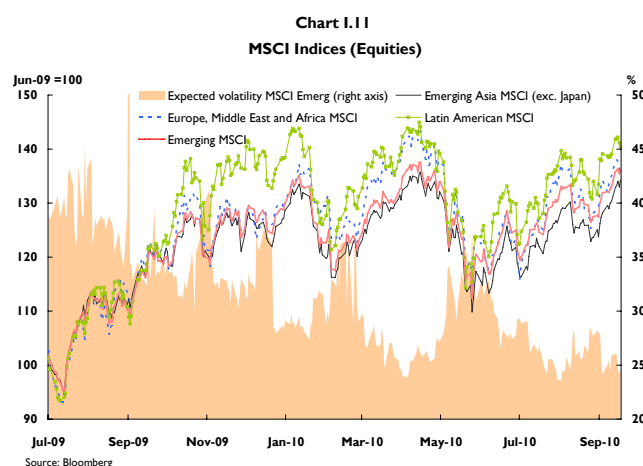
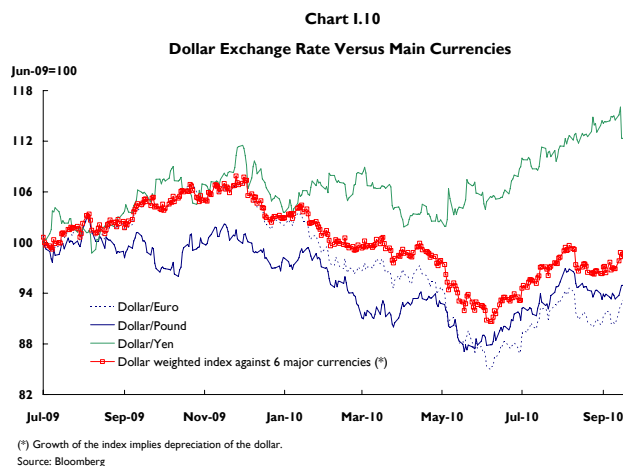
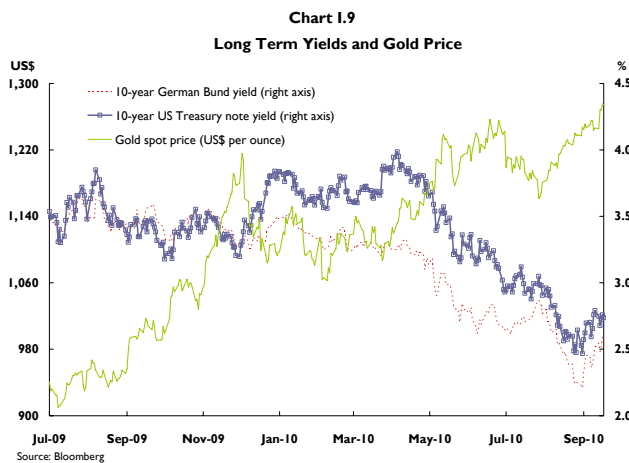
In recent months there has been more caution in financial markets because of the sovereign debt crises in Europe, and due to concerns about the pace of US growth

Since April the context of increased volatility in financial markets deepened, leading to a more selective behavior by investors. This was explained by the increase in risk aversion due to a deterioration of the situation in Europe (see Box 1) and, more recently, by concerns about the slowdown in the global economy in general and the US in particular. This changing context of international financial markets was evident in equity assets, whose performance so far this year contrasts with the sustained improvement between March 2009 and later that year (see Chart I.2). This scenario is far from being comparable to that observed during the international financial crisis of 2008-2009, while more recently, a positive trend has been registered.

Growing concerns about specific risks brought about a change in the decisions of policy makers, leading them to reaffirm the commitment to support the market due to a still weak context and postpone the exit from stimulus policies implemented under the international financial crisis. This is clearer in Europe, the main region affected by the Greek debt crisis and the subsequent deterioration of the prices of sovereign debt of other vulnerable economies of the region. In this case, it changed from reducing the terms of the liquidity facilities to coordinate efforts between the European Union (EU) and the International Monetary Fund (IMF) to implement a program to allow strengthening the financial stability of the region, in addition to the asset public purchase policy of the European Central Bank (ECB).

Regarding the US, while earlier this year the amounts offered in the liquidity facilities were reduced and the asset purchases came to an end (while the Federal

² The IPMP prepared by the Central Bank, reflects the evolution of the more relevant primary products prices of the local exports.



Reserve -Fed- was expected to increase the reference interest rates at the end of 2010), this political bias had to be adjusted over the course of months (see Chart I.7). In line with the evolution of the activity and the risks identified, the scenario of expected low interest rates for the US was extended: nowadays the current expectations of any increase are for 2011 (see Chart I.8). Moreover, in August the Fed announced the reinvestment of principal payments on its asset holdings of official agencies and of mortgages holdings into longer-term treasuries and more recently it was reported that there may be additional measures to sustain the recovery.

Thus, while the higher-risk assets (especially debt and equity of vulnerable economies) had less support and showed greater volatility, returns on long-term government bonds from countries like US and Germany declined steadily (see Chart I.9) returning to historic lows. The price of gold began to show a clearly positive trend since the beginning of the second quarter, based on an increase in demand for this asset as an investment.

The changing context was also evident in the price of the dollar. Until the middle of the year the dollar tended to appreciate across the board (in a euro deterioration scenario), while it later began to correct against the euro, the pound and the yen³ (see Chart I.10). It should be noted the announcement about the beginning of a less rigid exchange rate regime in China.

The evolution of emerging market assets was influenced by changes in global risk aversion

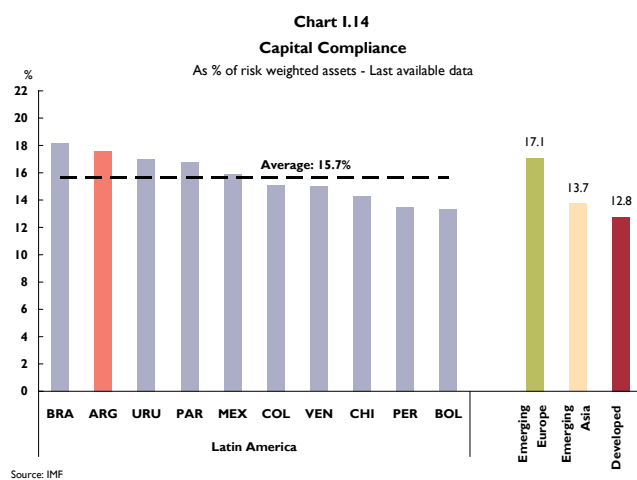
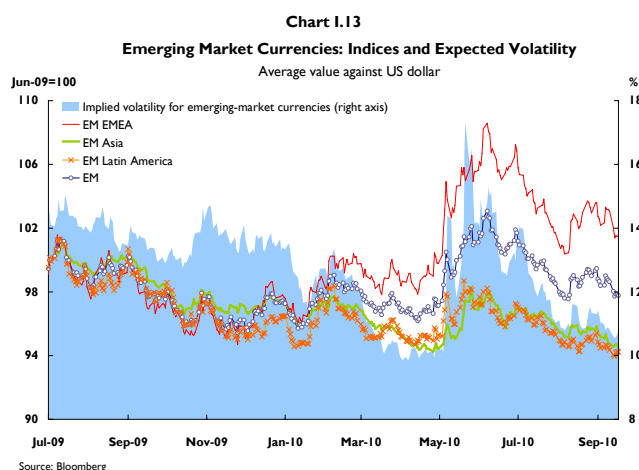
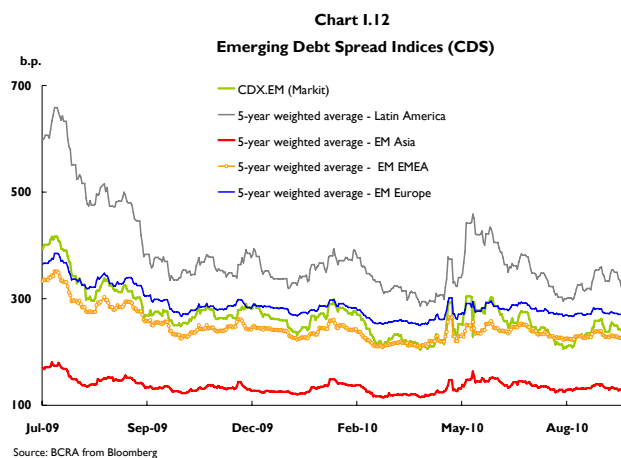
Despite the improved macroeconomic outlook for emerging markets, stock prices tended to deteriorate in the second quarter, although some recovery was observed later (see Chart I.11). A similar behavior exhibits the expected volatility of the most important emerging markets stocks⁴.

Spreads on sovereign debt in dollars of emerging economies also remained volatile in recent months but are now at levels close to the minimum of the year (see Chart I.12). In a context of liquidity and low yields in international markets, investors have shown increasing interest in fixed income assets, as evidenced by the flows to investment funds specialized in emerging market debt⁵. In addition, in recent months sovereign placements in international markets show a fluctuating pattern, with countries taking advantage of certain

³ More recently, Japan began to intervene in markets to curb the yen's sustained appreciation in a context where several emerging countries discussed measures to lessen the excessive appreciation.

⁴ Forward looking volatility, calculated based on option prices.

⁵ These flows showed also a growing interest in local currency instruments.



windows of opportunity (March-April, July) to get funding in the markets. So far this year sovereign issues show an annual increase, with a predominance of operations of economies with investment grade rating.

In line with that observed for equities and securities of emerging economies, the evolution of their currencies was conditioned by the absence of a clear pattern in international markets (see Chart I.13). As counterpart to the evolution of the dollar, in the second quarter a depreciation tendency was observed for currencies of emerging countries (with an increase in expected volatility), as well as some recovery in recent months (though with ups and downs).

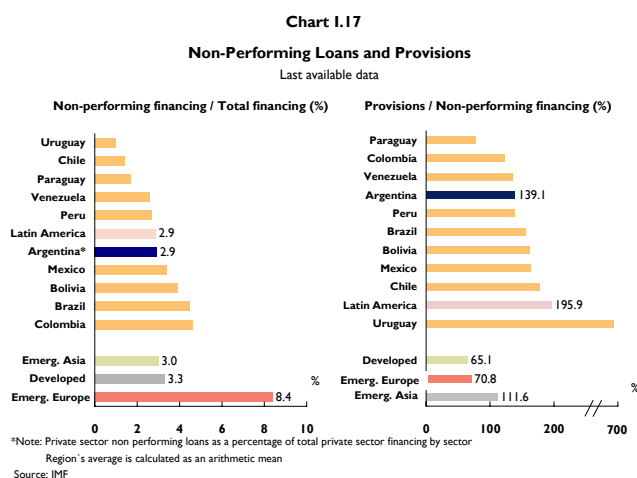
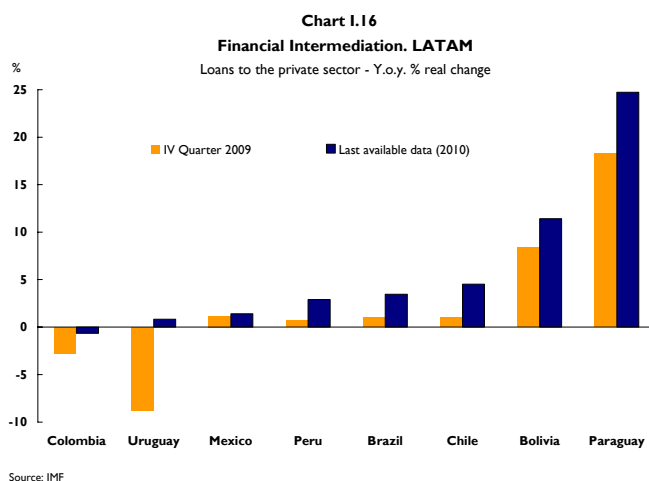
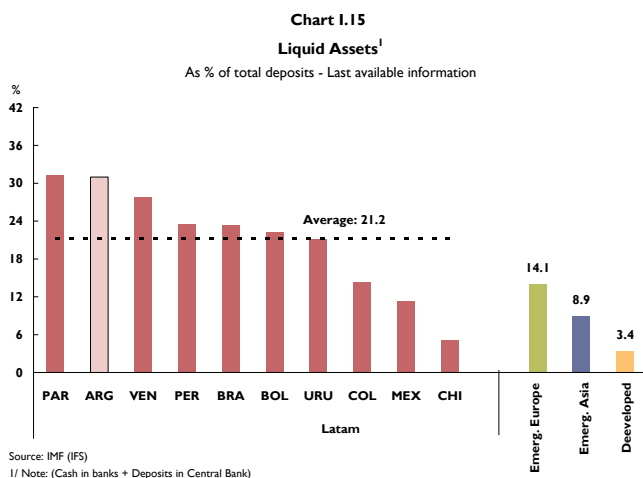
Since there are still some concerns (pace of US growth) investors are expected to keep on showing cautious behavior while markets continue without indicating a definite trend in the coming months. As long as a considerable level of liquidity is maintained in developed economies, the emergence of more favorable news will invigorate the search for yield while markets will resume their upward trend.

I.2 Latin American banking systems

In a scenario of increased volatility in international markets, Latin American financial systems continued to show strength

Although turbulence in international financial markets increased after the crisis of the vulnerable economies of the euro area, the Latin American financial systems continued to show a robust position. The economies of the region continued to recover from the effects of the international crisis at a relatively faster rate than other emerging regions. The macroeconomic performance of recent years, coupled with the financial measures contributed to maintain liquidity and solvency at relatively high levels for their financial systems (see Charts I.14 and I.15). Until the early months of 2010 the Latin American countries received a significant inflow of capital that allowed increasing the liquidity of local markets and improving, to some extent, the conditions for funding. This evolution exhibited some reversal from mid-year due to the more volatile international environment.

The financial intermediation activity with the private sector in Latin American economies continued to recover, although the pace of growth is more moderate than in previous periods of crisis. In recent months, there was a better performance of the credit to the private sector in most countries of the region after the relative

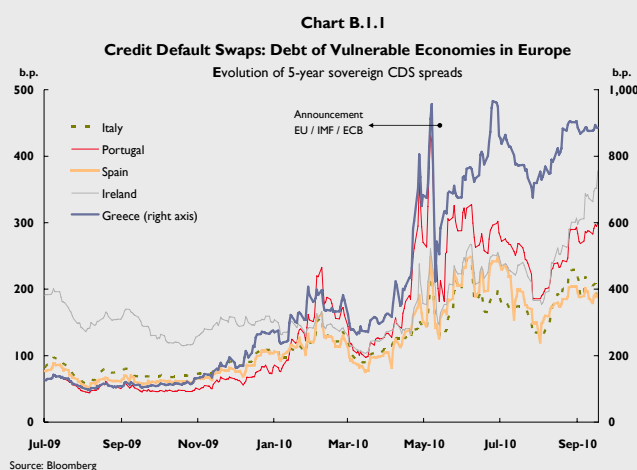


minimum observed at the end of 2009 (see Chart I.16). The cross-border credit issued by global banks and the finance provided by the subsidiaries of international banks have not yet fully recovered its momentum after the crisis, and this is one of the challenges of the region. The credit risk assumed by the Latin American financial systems are at limited levels both from a historical perspective as compared to other emerging markets (see Chart I.17). The significant economic growth forecasted for the region for the remainder of 2010 is expected to result in an improvement in the payment ability of the private sector

High rates of growth of the economies of the region in recent periods coupled with the fundamentals of Latin American financial systems lead to forecast a gradual increase in the dynamism of intermediation in the coming periods. However, the fragility of the recovery of developed economies remains a potential source of vulnerability for Latin American banks.

Box 1 / Vulnerable Economies of the Euro Area and Situation of the International Markets

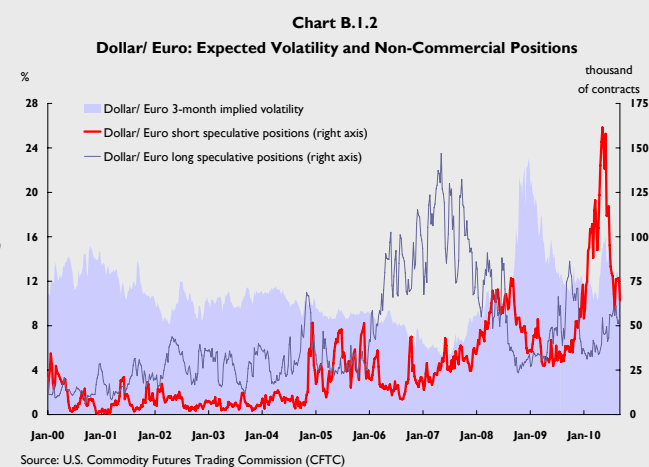
After the increase in tension in international financial markets during the May-June period (identified in the pressure on prices of financial assets of relatively higher risk, including those of emerging economies), several factors led to moderate the concerns about the situation in countries like Greece, Spain and Portugal in recent months. However, elements of risk that could eventually lead to changes in markets still continue, being able to affect the financial context of emerging economies, including Argentina



Despite the announcement of significant support measures in early May, among which the establishment of the Financial Stability Facility of the European Union, the contributions by the IMF and purchases of financial instruments by the European Central Bank (ECB), by mid-2010 concerns have deepened about the financial situation in Europe. This was based primarily on three factors. First, the challenge involved in the concentration in the third quarter of strong sovereign debt payments for certain vulnerable economies⁶. On the other hand, doubts about the fiscal measures announced in the region, specifically with regard to their implementation, impact on the activity level and eventual spill-over to other regions, among others aspects. Finally, the distrust in relation to the European banks situation in terms of their exposure to sovereign assets as well as the potential second-round effects on portfolios of loans as well as any unknown risk positions and

⁶ Maturities estimated in €190 billion (Greece, Spain, Portugal, Italy and Ireland).

funding problems. Given these concerns, renewed turbulence was observed in international markets during May and good part of June (increases in sovereign debt spreads and impact on the euro exchange rate), forcing the authorities of major economies to set aside, at least momentarily, the emerging debate about exit strategies for policy stimulus.



The context of growing global risk aversion began to decompress from early July when several factors, that allowed the most extreme assumptions about the situation in the euro area weakened. On the one hand, the packages of assistance originally announced were implemented. Moreover, the publication of economic data of the countries of the region did not lead to major negative surprises, while in the second quarter corporate balances showed more positive data than expected⁷. Additionally, the governments of the most vulnerable economies could place debt in the market without mishap, in many cases with acceptable conditions of demand⁸. In this context, although the spreads of the debt of the most vulnerable economies continued to rank well above the levels of late 2009 (with significant volatility and no clear trend), in most cases⁹ they are below the maximum of the beginning of the year (see Chart B.1.1). This slight improvement occurred even in a context of lower purchases of debt instruments by the ECB.

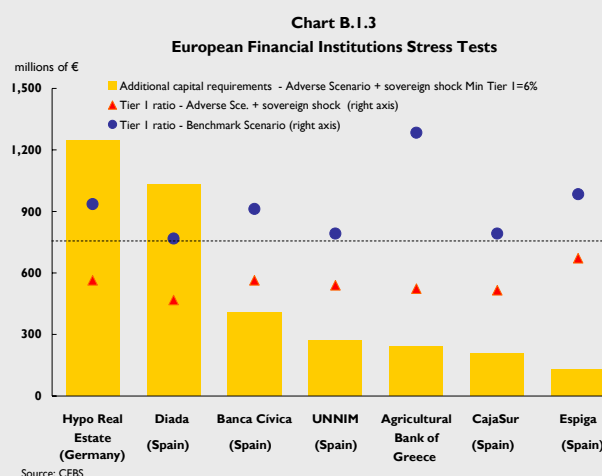
The euro managed to curb its weakening against the dollar (see Chart I.9) in recent months as a result of a scenario of lower speculative pressure. Indeed, since mid-June, a

⁷ With profits exceeding expectations even for several large banks.

⁸ Although for the last placements of September, high financial costs for the debt of Portugal and Ireland were observed.

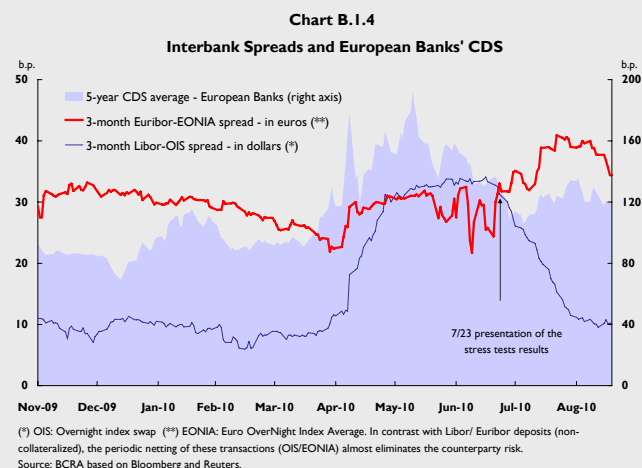
⁹ The Irish case is an exception.

decline in short non-commercial positions of exchange rate dollar /euro was recorded in the derivatives markets (see Chart B.1.2), after growing steadily (generating a short net non-commercial position which reached record levels) during November 2009-May 2010. In this context, after falling more than 20% between late 2009 and mid-year 2010, the exchange rate US\$/ € recovered over 10% in the last four months¹⁰. At the same time, after rising sharply in May, the implied volatility in options on this exchange rate began to shrink.



Regarding the situation of the European banks, starting in July, they were able to confront without problems a considerable maturity of ECB's long-term financing facilities (more than €442 billion¹¹). In the same month the results of stress tests for financial institutions in the region (period 2010-2011) were published, involving capital needs for €3.5 billion in total (significantly lower than previous estimates¹²; see Chart B.1.3), for seven entities (none of considerable size). While these tests were not free from criticism¹³, they represented a positive contribution in terms of transparency (without negative surprises of consideration), also contributing to the coordination of expectations and the weakening of the most extreme assumptions with respect to the European financial entities. In this regard, the Eurostoxx financial sub-

index measured in dollars rose 22% in July (while the Eurostoxx 600 improved 12%).



In this context, given that several risk factors linked to the European case continue, along with some concerns about the pace of growth in leading economies (like the US), a sustained context of caution and increasing selectivity in the markets is expected for the coming months. On the one hand, it is unknown how the economic indicators will continue to evolve in the euro area as a whole (possibility of a double dip) as well as most vulnerable economies in particular, with a potential impact on the balance sheets of financial institutions¹⁴. On the other hand, the situation of the European banks in terms of funding remains an issue to be monitored, according to the considerable dependence on the wholesale market (in a context in which the euro interbank spreads remain relatively high (see Chart B.1.4) and the need to refinance significant amounts in the capital market, taking into account the significant placements to be made by governments. In turn, this will force policy makers to continue making efforts to coordinate and maintain various support measures, in order to avoid a renewed cycle of deterioration in financial markets and a possible abrupt change in global risk aversion which will end up affecting the real economy.

¹⁰ Some of this correction was in September, when the U.S. confirmed the scenario of low interest rates for an extended period.

¹¹ Under the Longer-Term Refinancing Operation, the auction made a year ago had collected a record amount of bids in terms of the history of the ECB's operations.

¹² Previous estimates were between €30- 100 billion.

¹³ From different market sectors objections were made regarding the characteristics of the adverse scenario and how strict the capital requirements were (6% of Tier one, regulatory capital definition broader than common shares and retained profits).

¹⁴ In September, for example, concerns about losses in Irish banks deepened.

II. Local Context

Summary

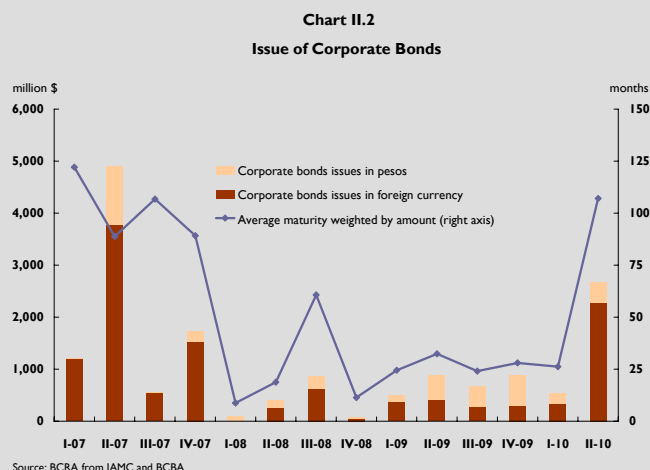
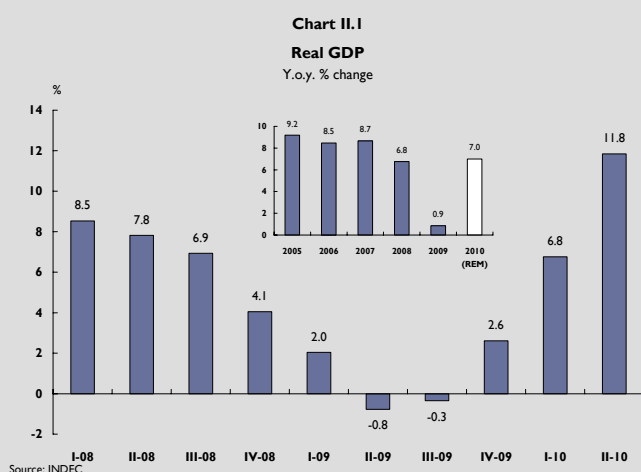
The economic growth process gained strength in the first half of 2010, underpinned mainly by household consumption, a situation that is expected to persist during the rest of the year. This was possible by improved family income levels within the context of recovery in the labor market, increased transfers from the public sector - for the Universal Child Allowance and pensions - and the installment plans and promotions offered by banks, as well as because of improved economic expectations. Local prices recorded a slowing rate of growth in the second quarter, mainly from lower pressure on food and beverage prices both locally and internationally. With the increase in foreign trade flows, the trade surplus has continued to run at a high level.

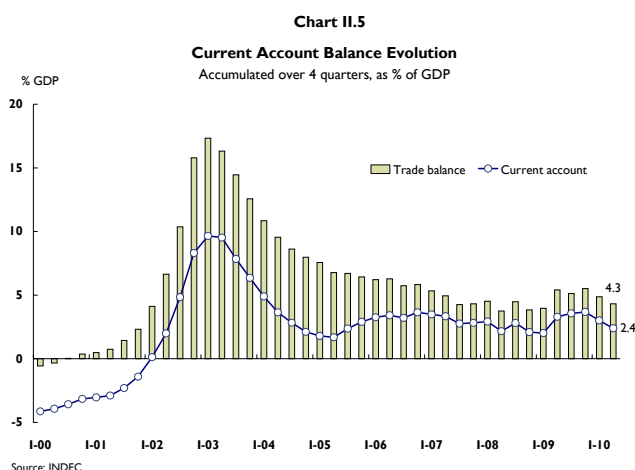
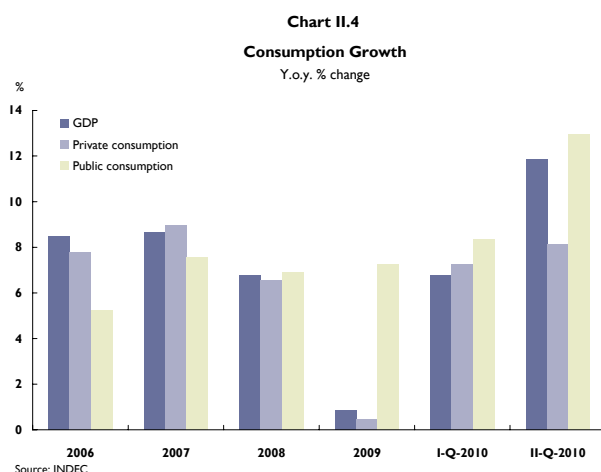
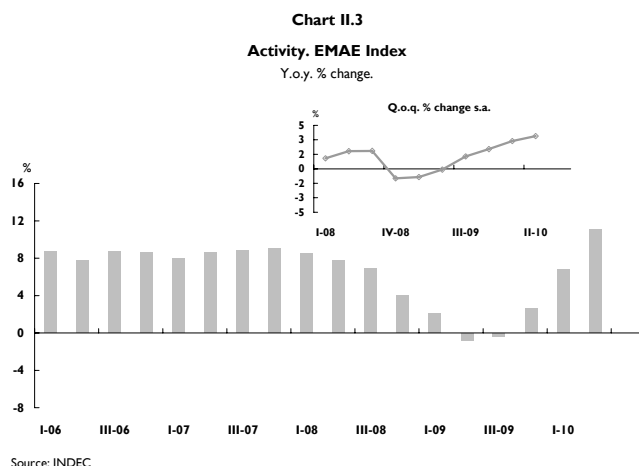
Market currency purchases by the Central Bank and loans to the private sector were the main factors driving growth in means of payment (M2) in the first part of 2010, a movement that was partially offset by an increase in time deposits. In the first two quarters of 2010 the Monetary Program (PM) targets were reached thanks to the sterilization efforts by the Central Bank at a time when the demand for money was recovering. Revised forecasts for an increase in GDP in the order of 9.1% y.o.y., much higher than the forecasts used when originally preparing the 2010 Monetary Program (PM), have led to an updating of the targets that were initially laid down. In the year to date the Central Bank has kept the reference interest rates that it establishes by means of its repo transactions unchanged.

Following the positive impulse from the debt swap, sovereign bond prices improved and Argentine risk spreads narrowed, with a recovery in trading volumes despite persistent volatility on international markets. The demand for Central Bank instruments continued to focus on Lebac, at a time when the BADLAR rate (the reference rate for Nobac) has remained steady. There has been growth in trading volumes on the secondary bill market. This trend towards recovery in the trading volume of fixed income instruments is expected to continue due to greater demand for sovereign debt securities.

Private sector financing via the domestic capital market increased in the first half of the year. The main mechanism used continued to be financial trusts, and lower rates were demanded for the securities that were placed. Underlying assets were mainly related to consumption (personal loans and credit cards) and infrastructural works associated with the provision of public services. Companies placed bonds for far larger amounts than in previous periods, with reductions in the cut-off rates and a recovery in bond terms to maturity. A year-on-year increase has been recorded in the negotiation of deferred payment checks, which have continued to dominate the market for Small and Medium Enterprises (SME) financing.

Stock trading recovered slightly in the first half of the year, but remained restricted in the highly volatile context. Amounts traded in forward exchange contracts and Badlar rate futures have risen in recent months.





II.1 Macroeconomic context

In the first half of 2010 the process of economic growth continued to gain strength

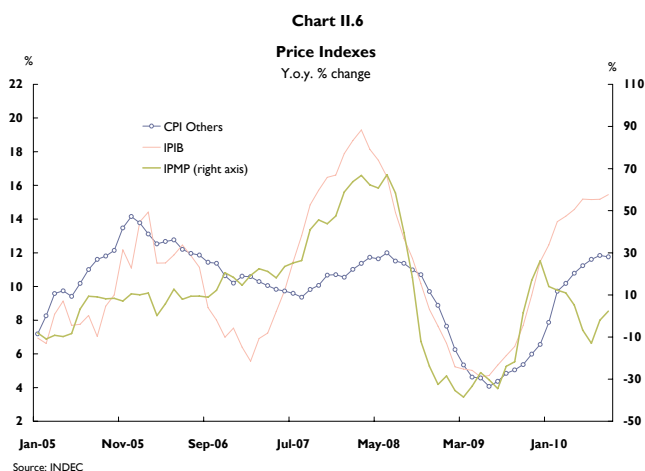
The improvement in domestic economic activity gained strength in the first months of the year (see Charts II.1 and II.3), with the recording of growth rates similar to those prior to the international financial crisis. Household consumption was the main force behind aggregate demand, to which was added a positive contribution from investment. The increase in activity was widespread across many sectors, with notable development in the case of manufacturing industry and the farming sector.

Local economic growth expectations have encouraged families to continue to increase their spending. This situation has benefited from the possibility of improved borrowing conditions and the promotions offered by stores in conjunction with banks. Transfers from the public sector, such as the Universal Child Allowance for Social Protection and the updating of social security payment amounts have had a similar impact (see Chart II.4).

Investment has recorded marked recovery, mainly from the addition of durable production equipment, at the same time as there has been a moderate increase in construction. Looking forward, investment is expected to continue rising in response to the more favorable macroeconomic scenario and the introduction of stimulus policies.

This consolidation of economic growth has been reflected in the labor market, where the unemployment rate stands at levels similar to those of 2009. The impact of the international crisis on the labor market was lower than that seen in previous episodes, and was less than that experienced by other economies, in part a reflection of the effect of the local implementation of active policies (see Chapter III, Section 3).

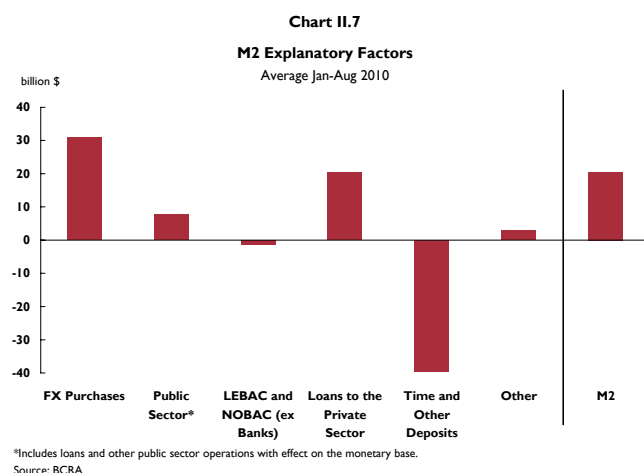
Exports rose, led by shipments of agricultural goods from the 2009/2010 harvest and a steady increase in the sale of manufactured goods, driven by growth in Brazil. Imports have risen at an even faster rate, led by purchases of consumer goods, industrial input and energy purchases. As a result, the trade balance will record a slight drop compared to the previous year's record, although it will remain at a high level, and the Current Account will show a positive result for the ninth consecutive year (see Chart II.5).



Following acceleration in the first months of the year, the various indicators for prices in the economy moderated their rate of increase in the second quarter (see Chart II.6). The first quarter dynamic was mainly due to the behavior of food prices (beef in particular), to a large extent related to the development of international prices, as well as certain local factors¹⁵.

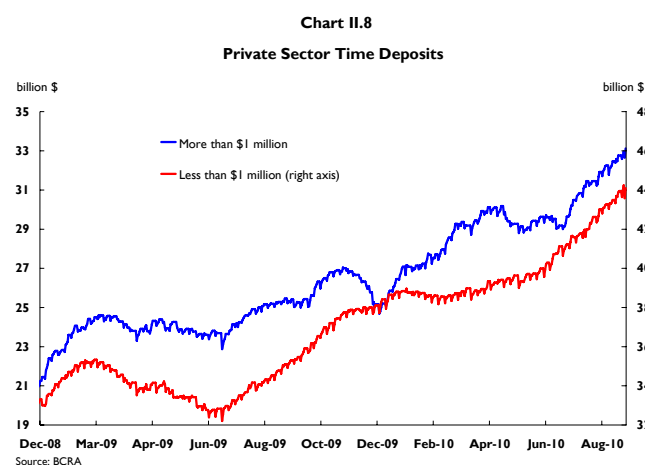
During the first half of 2010 the process of normalization of monetary and financial variables that began in mid-2009 gained strength

In the first eight months of 2010 means of payment (M2) grew by \$20.4 billion (10.4%), while private sector M2 rose \$25.5 billion (15.4%). The main factors explaining changes in M2 included Central Bank foreign currency purchases on the market, and increased lending to the private sector, partly offset by time deposits growth (see Chart II.7).



Since January, private sector time deposits in local currency have continued to display their renewed momentum in both the retail and wholesale segments (see Chart II.8), reflecting recovered demand for domestic currency.

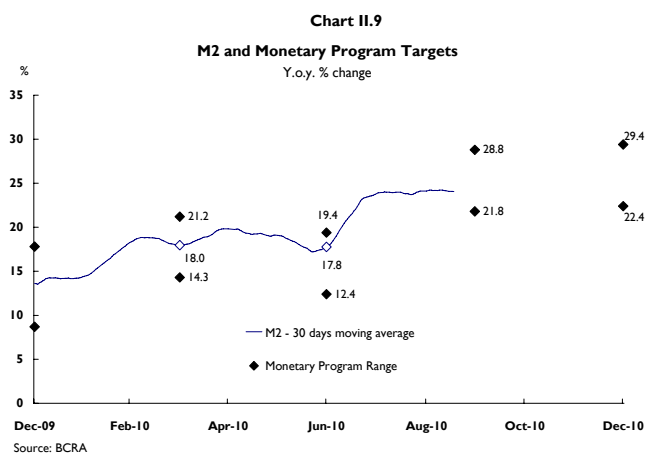
During 2010 the Central Bank has kept the reference interest rate unchanged: reverse repos have continued at 9% and 9.5% for 1 and 7 days respectively, while the rates for repos have been 11% and 11.5%. Leading short-term money market interest rates, as well as the Central Bank repo band, have remained relatively stable (see Chart V.8).



Monetary Program (PM) targets were reached in the first two quarters of 2010, closer to the band center in the first quarter, and the upper limit of the range in the second quarter (see Chart II.9). At the end of June the average M2 stock was \$206.2 billion, showing growth of 17.7% year-on-year (y.o.y.), 1.7 p.p. below the upper limit of the range established in the PM for the second quarter of 2010. In June private M2 averaged \$179.2 billion, recording growth of 23% compared with the same month of 2009. As a result, PM targets were reached in the first two quarters, as this Institution neutralized the monetary expansion that took place mainly as a result of the purchase of foreign currency (see Charts II.10 and II.11).

Recently the Central Bank decided to update the Monetary Program targets in view of the fact that economic activity growth in 2010 was exceeding the

¹⁵ For a more detailed analysis, see the Inflation Report for the Second Quarter of 2010.

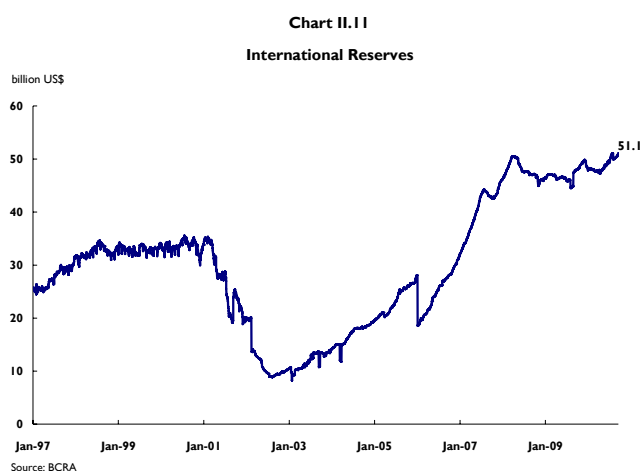
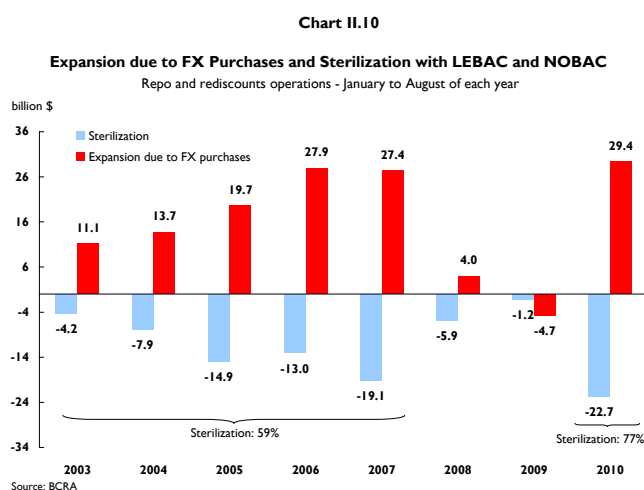


most optimistic forecasts made at the end of last year and is currently almost four times the level used when preparing the 2010 PM.

Compliance with the original targets for the rest of 2010 would have meant implementing such a tight monetary policy that it would have impacted on output growth and job creation by reducing the availability of credit. For this reason it became necessary to restate the 2010 PM targets, taking into account GDP growth forecast of 9.1%, although anchoring the prices originally forecasted. The updated forecasts for the base scenario of the 2010 PM imply an average y.o.y. growth of 24.8% for M2 and 23.2% for private M2 in December 2010.

II.2 Capital Markets

Following the positive impulse from the debt swap with the holdouts, prices improved and local trading volumes recovered, despite the volatile context persisting on international markets



In recent months sovereign bond prices have shown improvement compared with the levels in force at the beginning of 2010, although they continue to reflect the impact of the situation on international financial markets. The official announcement of the debt swap with the holdouts in mid-April had a positive impact on prices, which later deteriorated because of the effect the crisis was having on certain European countries (Portugal, Ireland, Greece and Spain). More recently, sovereign bond prices rose significantly, a movement associated with the actual implementation of the swap with the holdouts (see Box 2), an improved credit rating, and greater international appetite for emerging market bonds. Government security prices reached levels close to those at the start of 2007¹⁶, with a recovery in local trading volumes. Since the end of March, both bonds in dollars and in pesos adjusted by CER index as well as those in nominal pesos recorded lower yields, particularly in the case of shorter-term instruments (see Chart II.12).

This improvement in the prices of dollar-denominated bonds in the context of an increased risk appetite has meant a reduction in Argentine risk spreads, which stand at 700 basic points (b.p.) in the case of the EMBI+ prepared by J.P. Morgan and close to 770 b.p. on 5-year credit default swap (CDS). A drop has been observed in the differential required by investors seeking positions in Argentine bonds compared with the emerging market

¹⁶ A moment of low volatility on international financial markets.

bond benchmarks (drop that is more pronounced in the case of the longer terms bonds) (see Chart II.13).

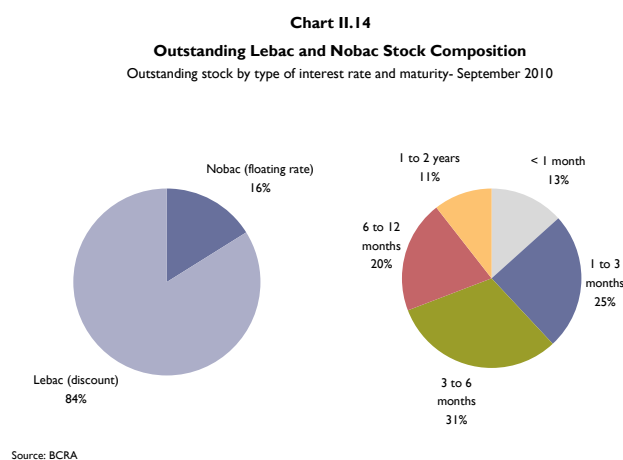
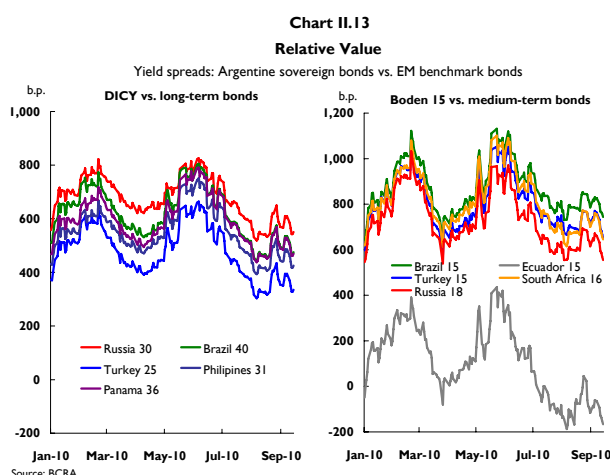
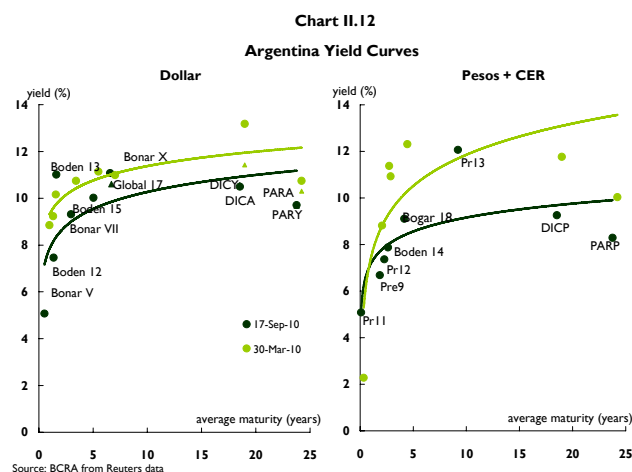
As long as volatility on international financial markets declines and there are renewed indications of economic recovery in developed countries, it is considered that there is a margin for improvement in the prices of Argentine sovereign bonds (given the existing macro fundamentals) with a consequent potential for a reduction in risk spreads.

During 2010 the Government continued to place bonds, and to a lesser extent short-term bills, directly with public sector entities, with the aim of covering its financing requirements. A placement with the Central Bank was also made of a non-transferrable bill for a total of US\$6.6 billion to offset the use of international reserves to make debt repayments¹⁷. The outstanding stock of short-term bills totaled almost \$1.95 billion, significantly below the \$10.5 billion at the end of 2009. The direct placement of bonds increased, totaling over \$11.77 billion cash value when adding the value of the reopening of the Bonar X and Discount series in dollars under Argentine law and new Banco de la Nación Argentina financing.

Federal Government debt amounted to US\$156.7 billion at the end of the second quarter of 2010, slightly above the level in December 2009. This increase is explained by the placing of new debt, and to a lesser extent, by the capitalization of interest and CER adjustment, movements that were partly offset by the development of the exchange rate. It should be noted that instrument placed has included the partial settlement of the new bonds handed over in exchange as part of the sovereign debt swap¹⁸, a transaction that made it possible to progress with the normalization of the situation with investors and improve the debt profile in terms of its average maturity. According to the information at June 2010, 47% of the debt is in dollars, 24% is in CER-adjusted peso, 18% is in nominal pesos, and 9% in euros (with the rest in other currencies).

Demand for Central Bank instruments has continued to focus on Lebac

In recent months there has been a significant increase in amounts tendered and awarded at the auctions of Central Bank instruments. The resulting rise in the amount outstanding (to approximately \$71.4 billion) has taken place in a context of steadily declining borrowing costs. It should be noted that the amount outstanding is



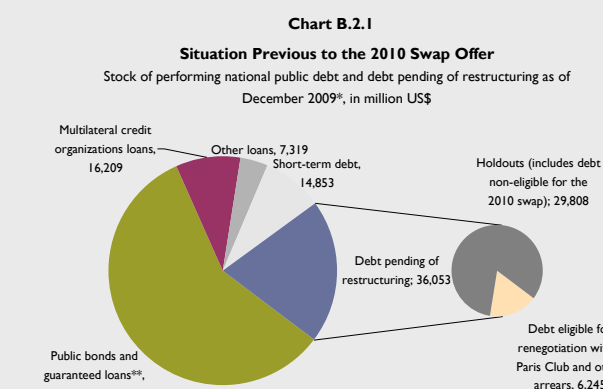
¹⁷ These repayments were made via the Argentine Debt Repayment Fund and from the Payments to International Financial Agencies account.

¹⁸ Instruments were placed corresponding to the early stage of the debt exchange for a value of US\$4 billion.

Box 2 / Implications of the 2010 Sovereign Debt Swap

The debt swap with the holdouts carried out recently is a fundamental step towards overcoming the suspension of payments in 2001. With 91% of the amount in default now restructured, the possibility of obtaining financing on international markets has improved. Nevertheless, despite better prices for sovereign bonds, there is still considerable room for improvement

The sovereign debt on which payment was suspended at the end of 2001 was restructured in 2005 in an operation that involved an eligible amount of US\$81.8 billion and was accepted by 76.15% of the total. Given the size of the operation, the result was considered a success.



(*) Outstanding gross national public debt statistics usually exclude securities tendered in the 2005 exchange (holdouts). These figures are usually disclosed separately.

(**) Includes Bogar 18 and 20 bonds.

Source: BCRA from Ministry of Economy and Public Finance

At December 31, 2009 the restated value of the liabilities to holdouts¹⁹ totaled US\$29.8 billion²⁰, while the total public debt outstanding was US\$147.1 billion (excluding the aforementioned amount) (see Chart B.2.1). In last April the official launch of the restructuring proposal for these holdouts took place. The amount eligible for the operation totaled US\$18.3 billion, representing principal and interest accrued through to December 31, 2001²¹. The operation took place over seven weeks (from May 3 to June 22), and was carried out in two stages: an early period for institutional investors (those with holdings in excess of US\$1,000,000 in eligible defaulted debt or its equivalent in other currencies), and a subsequent stage intended for retail investors.

¹⁹ Those holders of defaulted debt who did not take part in the 2005 swap.

²⁰ Includes unpaid accrued interest together with the principal.

²¹ As in the case of the previous debt exchange, no recognition was given to interest accrued from December 31, 2001 to December 31, 2003.

The 2010 exchange was similar to the one carried out in 2005 in terms of the types of bond offered. In terms of the way it was implemented, on this occasion a Discount Option was designed for institutional investors, while a Par Option was offered to retail investors²². Furthermore, it was initially proposed that the Government would require institutional investors to jointly make a market bid for US\$1.0 billion of the new Global 17 bond to be launched during the exchange operation, with the aim of obtaining financing on international financial markets.

At the end of June it was announced that the amount presented for exchange totaled US\$12.2 billion²³, equivalent to an acceptance level of 67%. Taking together the exchange operations in 2005 and 2010, 91% of the debt defaulted on in 2001 has been regularized. In addition to representing a reduction of the debt on which payment had been suspended, this operation implies a less than proportionate increase in the performing debt (given the discount in nominal terms made on that debt). In the end the requirement for a concurrent bid for US\$1.0 billion in Global 2017 bonds was waived because of the financial conditions on international markets in mid-May (related to the crisis in the more vulnerable European economies - see Box 1), as in such a scenario the cost of borrowing would have been excessive.

The latest debt swap implied new debt issuance for an approximate total of US\$7.2 billion in 11 bonds, including a total of US\$950 million in Global 17 bonds²⁴ (see Chart B.2.2). Settlement took place in two stages: in June the early period offers were settled (the Discount

²² Discount bonds due 2033 were offered for the Discount Option, with Par bonds due 2038 offered for the Par Option. In both cases GDP-linked coupons (UVPIB) were included in the offer. The main difference with regard to the 2005 exchange lay in the way the coupons of the new bonds were paid for the period from the issue date of the new bonds (December 31, 2003, exactly the same as in 2005) and the date of their delivery. In the case of the 2005 exchange, the coupons were paid in full in cash when the transaction was settled (June 05). In the current exchange, however, a distinction was made between the Discount Option (paid by means of the Global bond due 2017) and the Par Option (paid in cash in August). In addition, payments made on the UVPIB through to the exchange date were not given recognition. Unlike in the 2005 exchange, the Quasi-par bond was not offered.

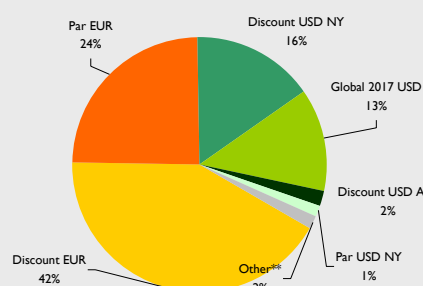
²³ This excludes debt restructures in the 2005 exchange and re-submitted to the 2010 exchange (known as retenders). Almost 80% of the debt presented corresponded to institutional investors, the remaining 20% corresponding to retail investors.

²⁴ Residual value restated as of June 2010. Five kinds of UVPIB coupons were also issued for a total amount of approximately US\$12.8 billion.

Option)²⁵, and it was established that the remaining bonds would begin to be handed over in August together with the payments due in cash.

Chart B.2.2

Issuance due to the 2010 Debt Swap
As percentage of a US\$7,200 million estimated total in actual value*



(*) As of Jun 30, 2010.

(**) Includes approximately US\$70 million of USD-denominated Par bonds with Argentine Law, US\$70 million of Peso-denominated Discount bonds, US\$35 million of Yen-denominated Discount bonds and US\$14 million Yen-denominated and Peso-denominated Par bonds.

Source: BCRA from Ministry of Economy and Public Finance

The new bonds issue increased the types of securities listed on local markets. The new Discount and Global 17 bonds issued for the early settlement began to list at the end of June and the beginning of July. Trading in Global 2017 bonds has steadily increased (see Chart B.2.3), while trading in the remaining securities is still low. The Global 17 bond could therefore become the new benchmark for Argentine debt on international financial markets because of its structure (bullet amortization, fixed rate coupon), the legislation governing it (New York jurisdiction), and the term to maturity.

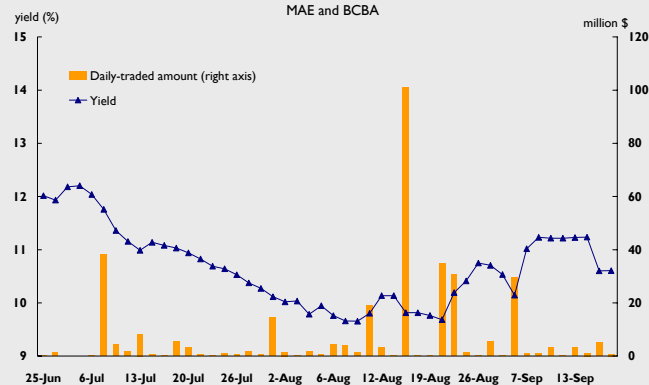
Fitch Ratings, Moody's and Standard & Poor's (S&P) highlighted the positive nature of the operation, and subsequently Fitch, and more recently S&P, have improved Argentina's sovereign debt rating²⁶. According to Fitch, relatively manageable public sector borrowing requirements, improved short-term economic prospects, and the demonstrated ability to respond to external and domestic confidence shocks in 2009, indicated Argentina's capacity to meet its obligations. S&P justified the rating increase on the basis of the improvement in the Government's financial profile as a result of its lower debt levels and the reduction in short term liquidity pressure.

The initial impact of the exchange on the prices of sovereign bonds was initially modest. Nevertheless, in following weeks bonds and the UVPIB made significant

gains, and a price improvement was recorded²⁷ (in the case of the latter, benefiting from the high growth levels expected for 2010).

Chart B.2.3

Global 17: Secondary Market
MAE and BCBA



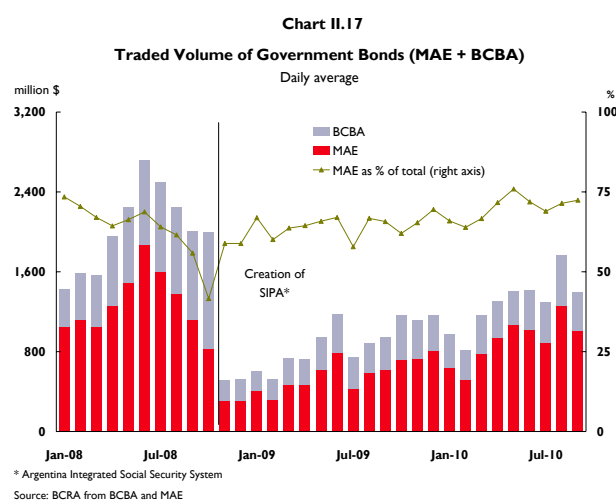
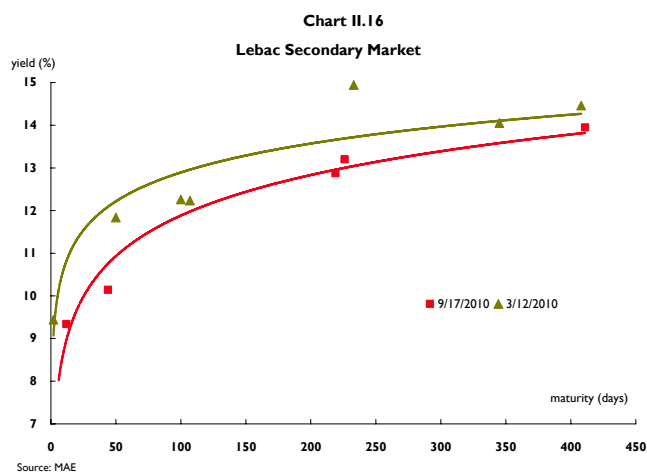
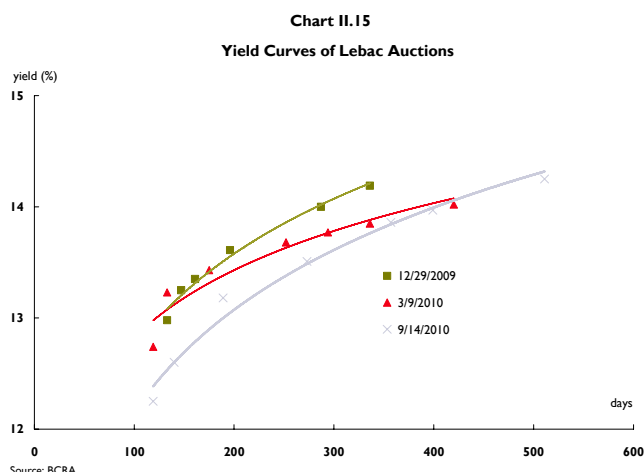
Source: BCRA from MAE, BCBA and Reuters.

The implementation of the recent debt swap represents a fundamental step towards overcoming the 2001 default and normalizing investor relations. The operation has potentially contributed to a reduction in the cost of Government borrowing on both local and international markets, with the consequent trickle-down effect on the borrowing possibilities of Argentine corporations and provincial governments, as well as having other positive effects for the economy in general.

²⁵ Based on information on public debt at 30 June 2010, bonds under this heading were issued for US\$4.05 billion.

²⁶ Fitch Ratings had been rating long term debt in foreign currency at "B-" since 2008, and on July 12 it improved it to "B". The Moody's rate is "B3" since 2005 and for S&P the grade was "B-" as from 2008, rising to "B" with a stable outlook on September 13.

²⁷ This improvement was partly reversed subsequently, as a consequence of the rise in international financial market risk aversion.



equivalent to 35% of total foreign reserves, 11 p.p. below the maximum level recorded prior to the international financial crisis. The principal instrument, Lebac (accounting for 84% of the total outstanding amount) (see Chart II.14), has recorded a lengthening of duration at the same time as there has been a reduction in the cut-off rate averaging almost 30 b.p. for equivalent terms against rates in mid-March 2010. This drop was sharpest in the case of the shorter terms (see Chart II.15). Although there was a slight improvement in the demand for Nobac in the context of relative stability in the Private Bank BADLAR rate, interest remains principally centered on the bills.

There has been an increase in the volume traded on secondary bills markets (accounting for almost all the amount of Central Bank instruments traded), with the focus on fewer instruments compared with the first quarter of the year. Lebac yields have fallen in the case of all comparable maturities, with a stronger emphasis on the middle sector of the curve (approximately 9 months of residual term) (see Chart II.16). Interest in Nobac has continued weak, with sporadic transactions that recorded an increase in their yield.

Local market bond trading volumes increase

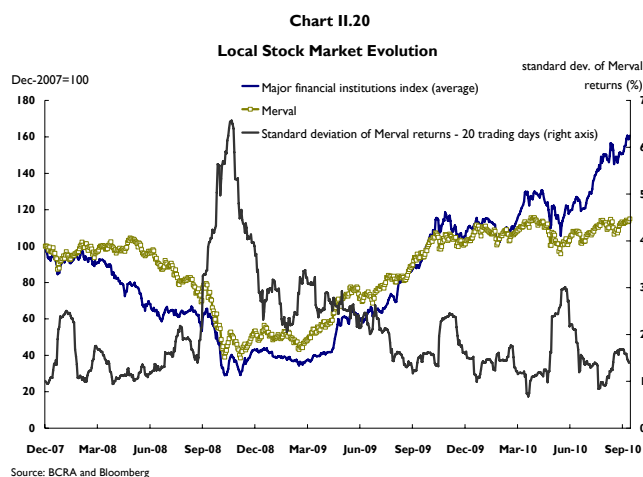
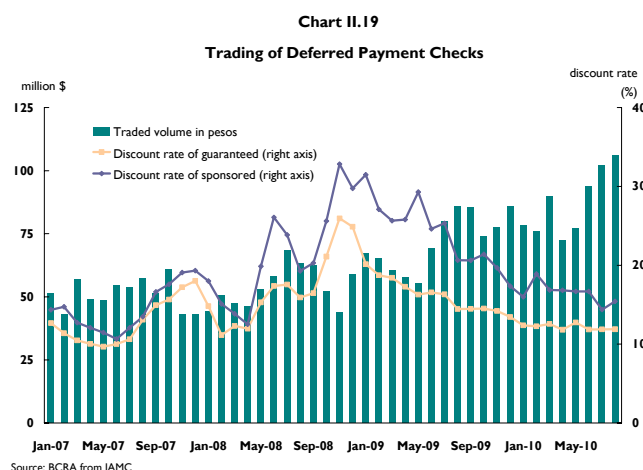
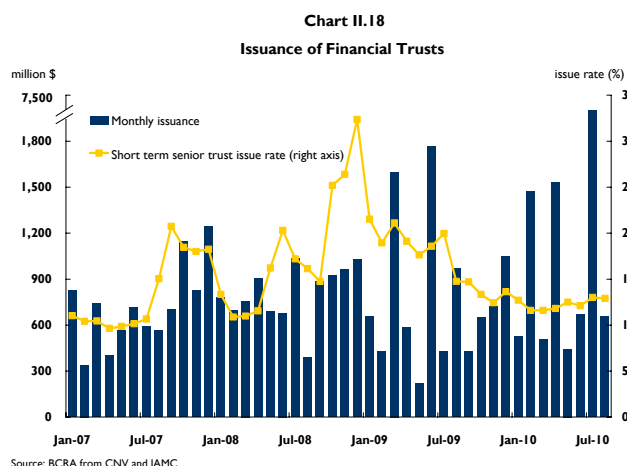
There have been some signs of recovery in the volumes of fixed income instruments traded on local markets (BCBA and MAE). Since March the daily average volume has been close to \$1.4 billion, higher than the level recorded after the change in the social security system at the end of 2008²⁸ (see Chart II.17). This trend is expected to continue, given the greater demand for sovereign debt securities.

Capital market financing of private sector increases

Capital market financing for the private sector has shown a recovery, with a rise of 16% compared with the end of 2009. In recent months market lending has recorded strong growth following some major transactions (particularly in July).

Financial trusts continued to be the main financing instrument in the local capital market, showing a recovery in the first six months of the year against the second half of 2009 (although remaining at a level similar to that of the same period of the previous year) (see Chart II.18), and there was a strong increase in July when some major issues took place. Almost two-thirds of the assets

²⁸ More recently, following the improved sovereign debt rating awarded by S&P, a further increase took place in trading volumes. On several days volumes were similar to those traded prior to the change in the social security system.



securitized were consumption-related (personal loans and credit card coupons), followed by trusts for the implementation of infrastructural works associated with the provision of public services. In the first half of 2010 there was a further drop in borrowing costs, despite the uncertainty prevailing on international markets during much of the period. The local situation had a positive impact on the preference for investments in domestic currency, which encouraged a fall in the interest rates required on placements made in the order of 150 b.p. and 650 b.p. compared with the end of the second and first six months of 2009, respectively.

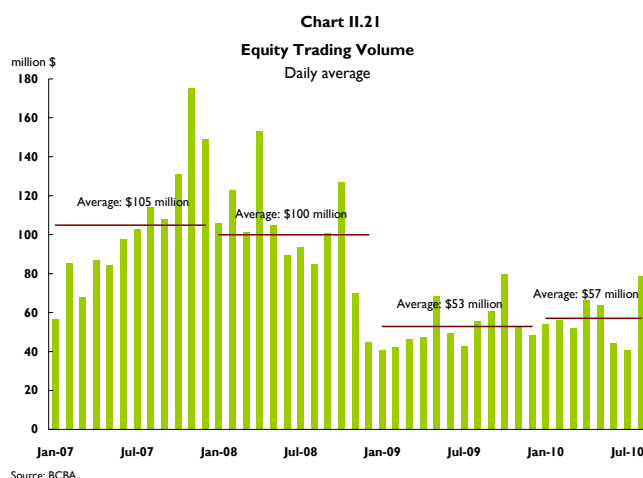
Companies placed 21 bonds on the local market in the first part of 2010 for a total amount well in excess of the placements in previous periods (see Chart II.2). The recorded financing levels had not been seen since the first half of 2007. This improvement in domestic conditions was noted even in months of high volatility and rising uncertainty on international markets. In May and June almost a dozen bond issues took place on the domestic bond market, and a further four issues were made in August. Cut-off rates for short-term peso and dollar financing fell, while there was a recovery in the duration of the instruments.

Short-term financing through the negotiation of deferred payment checks posted a significant year-on-year increase (30% up on the level of the previous year), although close to the levels seen in the last six months of 2009 (see Chart II.19). The volume of checks discounted on the market continued to grow strongly in July and August, when new records were set. Checks continued to provide the main source of market financing for SMEs, accounting for almost 90% of the total²⁹. Terms to maturity continued to lengthen until reaching levels of over three months in the case of checks backed by an SGR (Reciprocal Guarantee Company), and 75 days in the case of those guaranteed by the borrower itself. The cost of borrowing declined steadily during the year, with drops for the six-month period of 160 b.p. for SGR-backed checks and 70 b.p. for those guaranteed by the borrower.

The stock market remained highly volatile, and transaction volume was low

The Merval index has recorded modest gains in the year to date, with a clearly volatile behavior (see Chart II.20), while trading volumes picked up slightly, although remaining at a low level (see Chart II.21). In the first

²⁹ This year the CNV authorized the discounting of deferred payment checks secured by warrants in favor of a local stock exchange. Under this mechanism, the drawer can obtain financing with a guarantee, endorsing the warrant in favor of a local stock exchange. In June this new financing instrument began to be traded on the Rosario Stock Exchange.

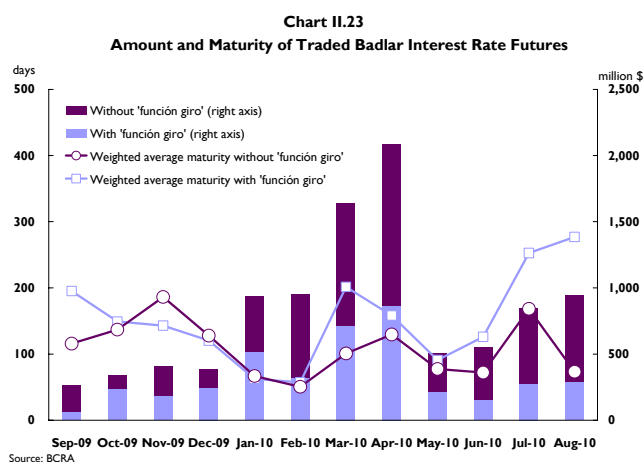
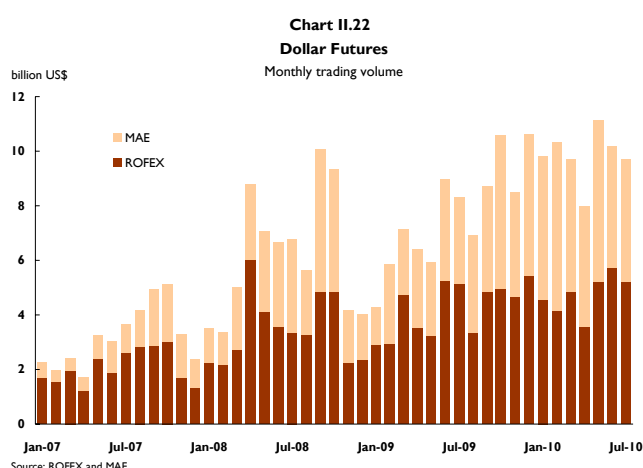


part of the year prices fell because of the European crisis and its impact on the main stock markets in this region. Once the peaks of tension on international markets had passed, shares recovered, and in September the local index in peso terms set a new record. No new share subscriptions have taken place since 2009.

Over the course of 2010 local bank stock market capitalization increased by close to 55%, showing certain stagnation in the first half of the year followed by a sharp recovery since mid-July. Financial sector shares have been the best performers on the leader board, and have continued to improve since July. Factors favoring this rise included the recent growth in loans and deposits, and improved government security prices.

Trading volumes for forward exchange contracts have continued to rise

In the first half of the year there was a further increase in exchange rate derivatives trading (see Chart II.22), with a monthly record being set at the end of the six-month period. Badlar rate futures continued to trade at a good pace, with a record number of transactions in April and a greater proportion of transactions being carried out without Central Bank intervention (see Chart II.23).



III. Debtors Performance

Summary

The economic activity exhibited a significant expansion rate in the cumulative of 2010 enhancing the trend that started by late 2009. The activity's improvement was recorded by service and goods producing sectors and was reflected in its financial and economic situation. The economic recovery also impacted on households from the improvement experienced by the labor market.

Companies from the manufacturing sector recorded a relevant increase in their activity level in the cumulative of 2010 boosted by both domestic and foreign demand, while some slowdown has been forecasted for the coming periods. The sector's performance influenced the evolution of the use of production factors with a rise in the number of hours worked and employed workers over the year. The indebtedness level of these companies fell gradually while foreign lending decreased moderately. The expected economic growth coupled with the decreasing indebtedness levels would allow manufacturing companies to continue improving its financial position.

The activity of the agricultural sector improved with crops reaching a record level within a context with suitable climate conditions for the 2009/10 harvest season. The livestock activity continued falling partly as a result from the need to rebuild cattle stocks. The context of higher meat international prices would affect producers' financial situation positively by raising their income and the value of their capital stock.

The indebtedness of the primary sector remained exceeding the values prior to 2009, even though it reached moderate levels (almost 44% of the sector GDP with a high share of foreign financing). The growing activity of firms in the sector together with reduced exchange rate volatility would allow them to continue improving their financial position.

The increased demand for public services favored the financial situation of service companies. The retail segment, in particular that of durable goods, rose in response of the campaigns and financing plans carried out by stores and bank institutions.

Households' payment capacity continued improving in a favorable macroeconomic context, with higher income available resulting from wage rises and government transfers. Total households' indebtedness remained stable and the consumption-related segment (personal loans and credit cards) grew gradually.

Tax revenue and primary spending have increased considerably so far in 2010 and would continue evidencing a positive primary result over the year. So far this year, financing needs of the Treasury were met primarily with intra-public sector funds.

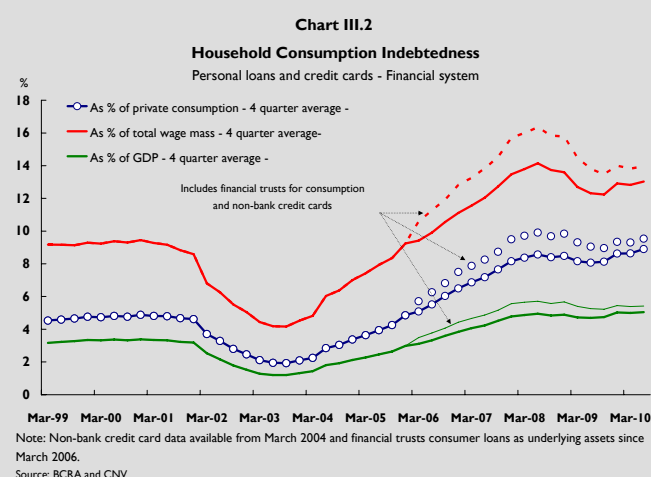
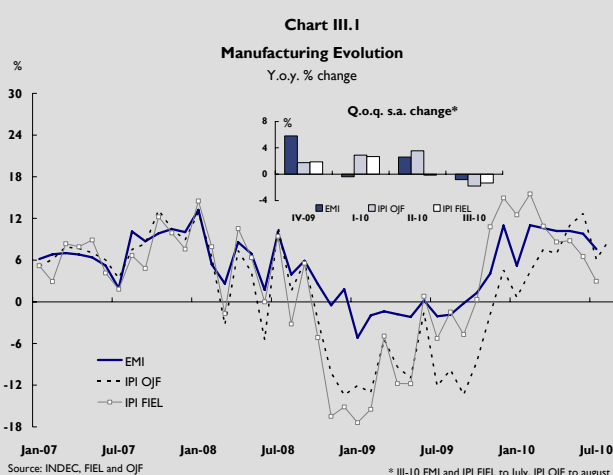


Chart III.3

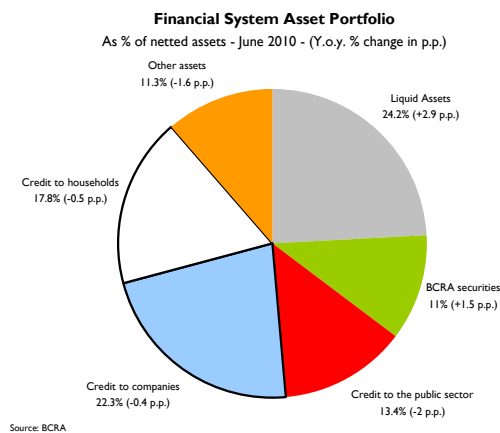


Chart III.4

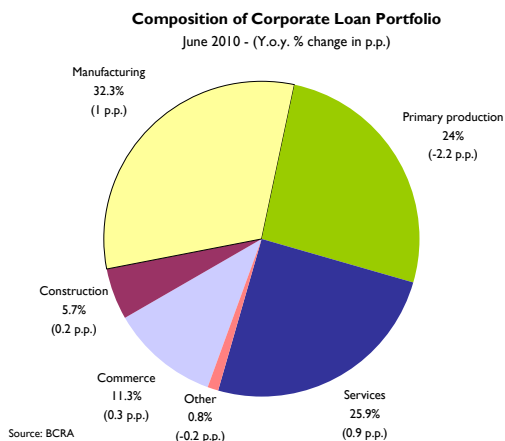
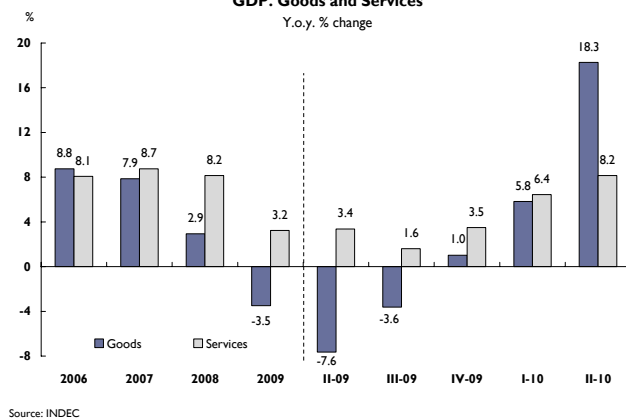


Chart III.5
GDP. Goods and Services
Y.o.y. % change



III.1 Financial System Debtors

Following the local effects from the international crisis, financing to corporations and households has increased

By mid-2010, approximately 40% of banks assets were made up of finance to corporations and households (see Chart III.3); these sectors started increasing their share in bank resources as from May following the domestic impact of the international crisis during 2009. The precautionary creation of liquidity buffers over last periods allowed re-launching lending to the private sector and this trend is expected to reach longer terms lines in the coming years.

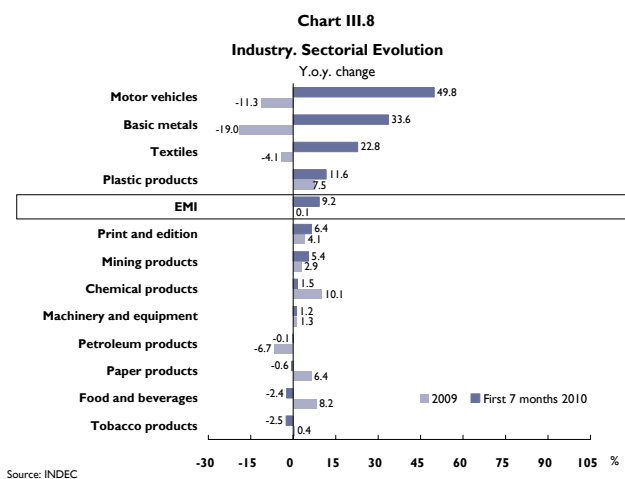
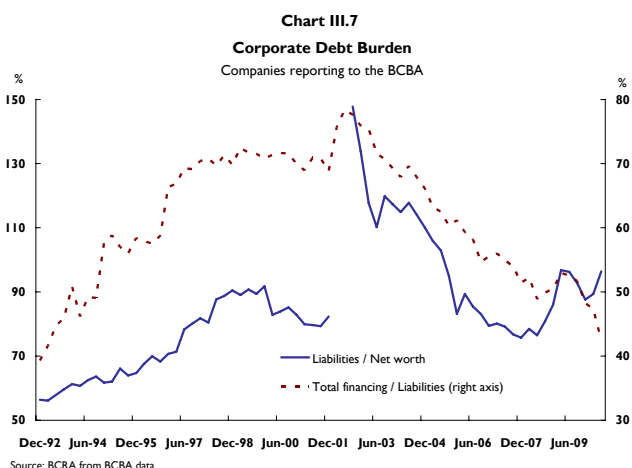
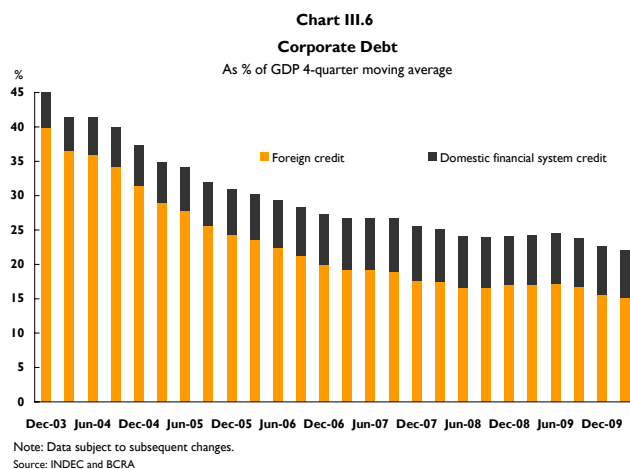
Industrial companies continued being the main corporate debtor of the financial system followed by service companies, a sector that recently exceeded primary production as the second recipient of bank funds (see Chart III.4). Lending to households exhibited a growing expansion pace especially in the case of consumption lines. The momentum generalized among all productive sectors would have an influence on further credit demand by late 2010.

III.2 Corporate sector

The financial position of the corporate sector improves along with the economic recovery

Economy exhibited a high growth rate over the first part of 2010 consolidating the expansion process that started during the second half of 2009. The improvement shown by the activity was recorded by both service and goods producing sectors (see Chart III.5). Manufacturing continued growing boosted by high households' consumption levels and foreign demand. The normalization of climate conditions contributed to the growth of the agricultural activity while the construction sector started to improve during the first half of the year. Services remained evidencing an upward trend, while the production of goods drove commercial activities and transport.

The indebtedness of the domestic corporate sector fell over the last periods standing at about 22% of its GDP (see Chart III.6), almost 3 p.p. lower than the value recorded two years ago. Foreign financing continued leading this decline accounting for slightly more than 68% of the total, below the amount recorded in previous years (it should be noted that this evolution was reinforced in a context where the exchange rate had shown a gradual depreciation). Thus, the evolution of



the domestic economic activity coupled with the indebtedness levels of the sector are factors that contribute to companies' payment capacity positively. Companies participating in the local Stock Exchange would gradually evidence greater leverage degrees (see Chart III.7), recovering the profits originated in their regular activity (information available in the balance sheets submitted to the Stock Exchange).

The economic activity is expected to keep on growing during the rest of 2010 led by the momentum evidenced by services; additionally, it has been forecasted that the production of goods will continue growing.

Productive sectors

Companies in the manufacturing sector are keeping their growth, which is reflected in their financial position

Manufacturing increased significantly in the cumulative of 2010 (see Chart III.1), continuing the positive trend that started by mid-2009. Expansion is expected to slow down over the rest of the year considering a greater comparison basis and less momentum exhibited by households' spending.

Automotive and basic metal industries boosted the sector's growth after having been the segments that suffered the most relevant drop as a consequence of the 2009 crisis (see Chart III.8). Automobile manufacturing reached record levels once again favored both by the increase of sales in the domestic market and the rise of exports, mainly to Brazil. The improvement of this sector together with the rest of durable consumption goods benefited the growth of basic metal industries and plastic and rubber products. Sectors related to the domestic market, such as the textile segment, publishing and printing products, as well as non-metal minerals also improved; in the case of the latter, it was due to the recovery exhibited by construction. The food industry continued falling, even though a lower decrease is expected given the incorporation of the latest harvest season and the recovery of the dairy sector.

The manufacturing performance was reflected in the evolution of the use of production factors with a rise in the number of hours worked and workers employed during the year. The installed capacity utilization also rose at an aggregate level.

Manufacturing companies' indebtedness fell gradually down to a level of almost 47% of its GDP (see Chart III.9). Foreign financing posted a moderate decline even

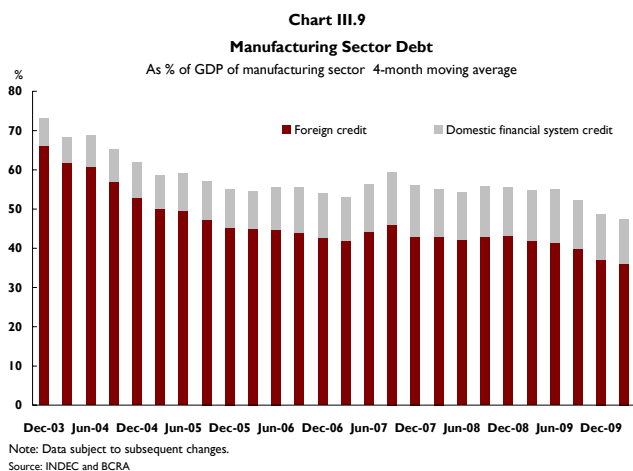
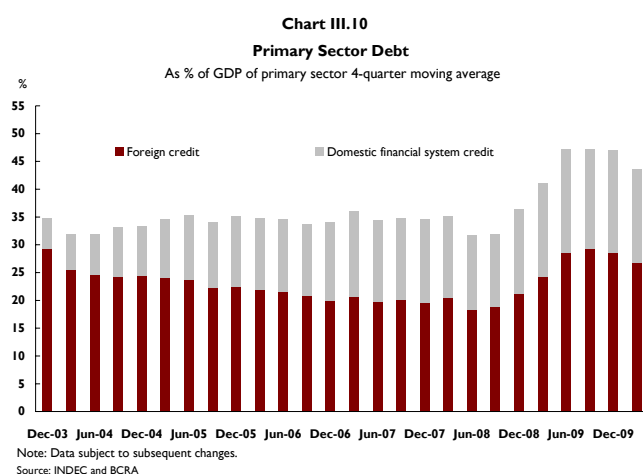


Table III.I
Grain and Oilseed Production

	2007-08 thousand tns	2008-09 thousand tns	2009-10 thousand tns (estimation)	% change of 2009-10 production vs 2008-09	Diff. in thousand of tns 2009-10 vs 2008-09
Cereals	44,725	26,740	36,720	37.3	9,980
Corn	22,000	13,121	22,500	71.5	9,379
Wheat	16,350	8,373	7,490	-10.5	-883
Sorghum	2,937	1,752	3,600	105.5	1,848
Other	3,438	3,494	3,130	-10.4	-364
Oilseeds	51,518	34,205	55,615	62.6	21,410
Soybean	46,200	31,000	52,700	70.0	21,700
Sunflower	4,630	2,440	2,250	-7.8	-190
Other	688	765	665	-13.1	-100
Cotton	494	389	681	75.1	292
Total	96,737	61,334	93,016	51.7	31,682

Source: BCRA from Ministry of Agriculture, Livestock and Fisheries and USDA data



though it still accounts for over three quarters of the total. The growth forecasted for the sector would allow it to continue improving its financial position and payment capacity.

The improvement exhibited by the agricultural activity and the gradual indebtedness reduction contribute to recovering the financial situation of agricultural companies

The agricultural sector grew sharply over the year with some crops reaching maximum production levels (see Table III.1). Favorable climate conditions allowed the normal development of the 2009/10 harvest season with a rise in the production of cereals and oil seeds. Soybean harvest would reach a new record resulting from the increase of yields and a maximum in the surface area sown. Corn harvest is recovering as a consequence of high yields while wheat production shrank due to a fall in the surface area sown.

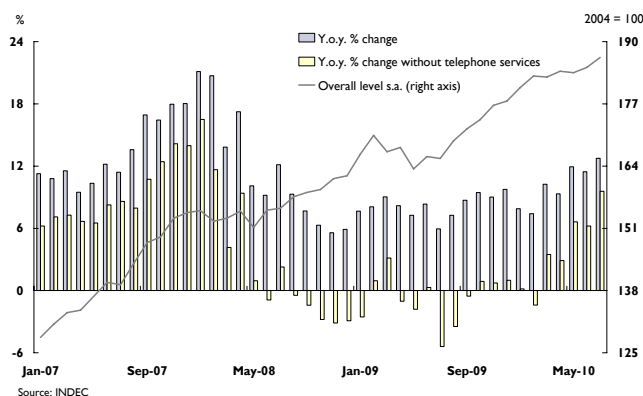
Livestock activity continued declining with a sharp reduction of animals sent to slaughterhouses against 2009. Part of this result was generalized by the high comparison basis but it would have also resulted from the need to rebuild cattle stocks and productive capacity. These factors, together with the rise of the international meat price, impacted on domestic prices for this product with a positive effect on the financial situation of producers by raising their income and the value of capital stock. No significant change has been forecasted for the rest of the year in the sector's activity given the duration of the livestock production cycle.

Indebtedness of the primary sector stood above the values prior to 2009 (see Chart III.10), even though it accounted for almost 44% of the sector GDP (foreign financing equaled about two thirds of the total). It should be noted that the recovery exhibited by the sector activity would allow continuing recovering its financial position following the impact from international and domestic factors over the last months.

The growing demand for services would allow maintaining the payment capacity of companies within the sector

Public services consumption has been growing since the beginning of the year (see Chart III.11), standing at historically high values. This performance would continue during the rest of 2010, accompanying the hike shown by the production of goods and households' spending.

Chart III.11
Synthetic Indicator of Public Services



Telephony led the growth of services, as in previous years, given the ongoing rise in the use of cellular phones. The remaining public services continued the hike that started by late 2009. Trade, manufacturing, and the agricultural activity boosted the use of tolls and freight transportation. The transport of passenger also grew resulting from the recovery of tourism; meanwhile, the demand for electricity, gas and water continued rising.

Service companies recorded low indebtedness levels that stood at almost 17% of their GDP, with a relevant share of foreign resources (see Chart III.12). This situation, coupled with the activity's expansion context, would allow maintaining the sector's financial position.

Commercial activities took off enhancing the sector's financial situation

The retail trade remained exhibiting a positive trend given the sustained spending by households and this growth is expected to continue during the rest of 2010 albeit at a lower pace.

Supermarket sales recovered their momentum while they also rose sharply in malls (see Chart III.13), boosted by campaigns and financing plans implemented by stores and bank institutions. Additionally, sales of durable goods exhibited a sharp increase. The increase evidenced by consumers' confidence, together with higher income, made households purchase cars and home appliances. Furthermore, discounts and financing plans implemented by commercial chains with financial institutions impacted on this segment positively.

It is worth mentioning that commercial companies continued recording low indebtedness levels amounting to approximately 16% of their GDP thereby contributing to their financial situation.

A gradual recovery has been evidenced by the construction activity

The activity of the construction sector has improved since the beginning of the year and is expected to continue this trend during the rest of 2010 (see Chart III.14).

Works related to both the public and private sector performed favorably although they started to show differences over the last months. Constructions for housing purposes and those related to commercial and industrial purposes remained growing leading the sector growth. Even though they accumulated a hike over the

Chart III.12
Service Sector Debt
As % of GDP of the service sector - 4-quarter moving average

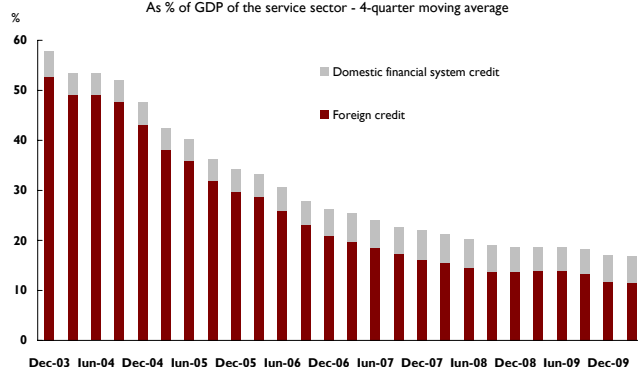
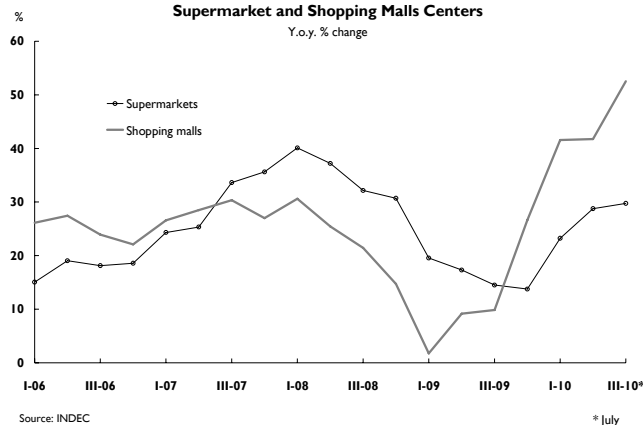
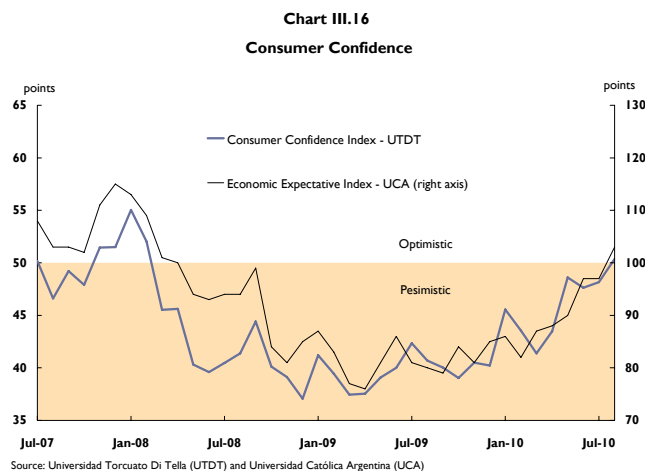
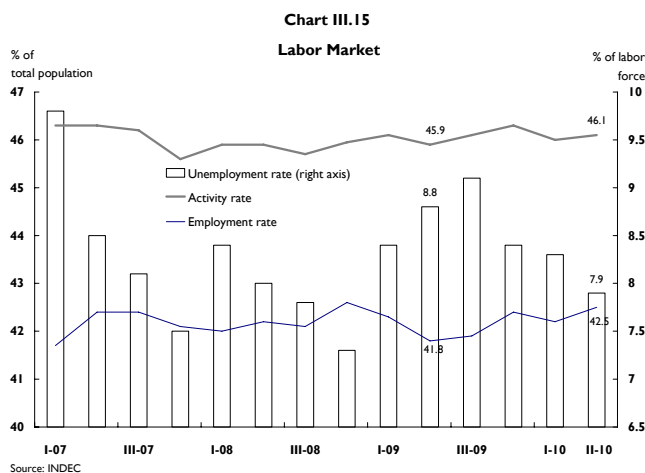
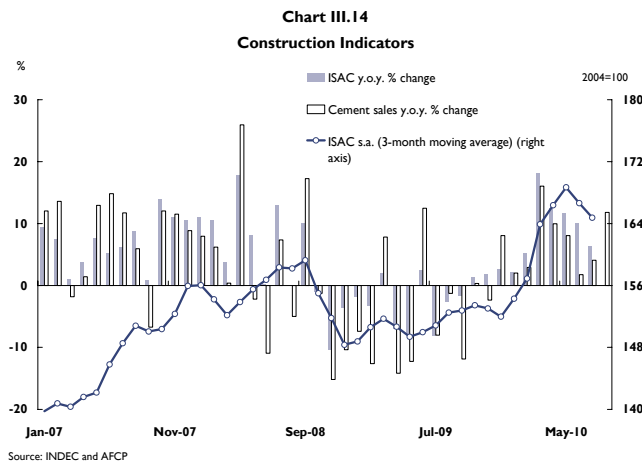


Chart III.13
Supermarket and Shopping Malls Centers
Y.o.y. % change





year, road and infrastructure works exhibited a slow down during the last months. The sector continued depending very little on foreign and domestic bank lending (almost 13% of its GDP).

III.3 Households

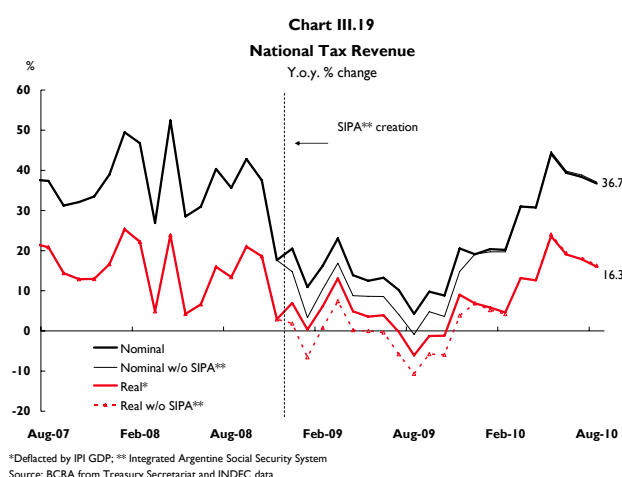
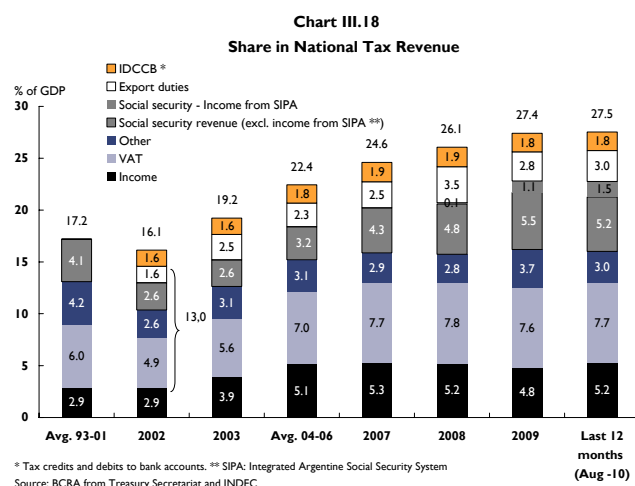
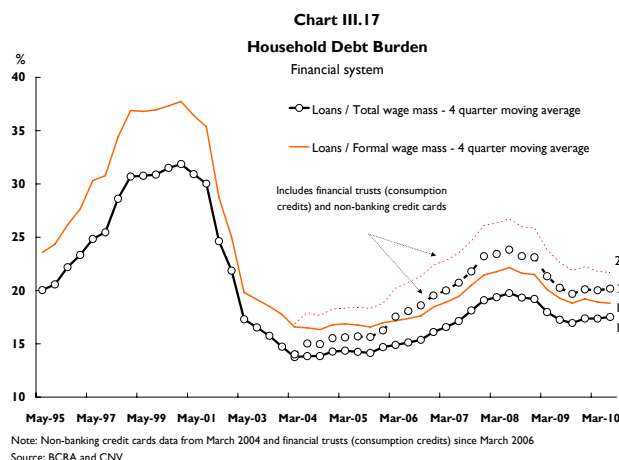
Households' payment capacity improved on account of the recovery of the labor market, the increase of available income resulting from wage rises and greater government transfers

Over the first part of 2010, households accentuated the reduction process of precautionary savings that began by late 2009, in a context of strong economic activity recovery. This scenario was accompanied by the improvement of the labor market and the raise of households' available income (see Chart III.15). Employment rose over the first half of the year, while the improvement in the quality of job creation is to be highlighted with a rise in the case of full time jobs.

The economy's momentum and the lower uncertainty contributed to recovering consumers' confidence which was reflected in the improvement shown by future expectations (see Chart III.16). This process took place in a context of wage improvements and the increase of government transfers, including the Universal Child Allowance for Social Protection (AUH). Households increased their consumption and were also benefited by greater lending possibilities.

Considering this evolution shown by households' income and the gradual recovery of the momentum of their financing (see Page 37), the sector has kept its total indebtedness level relatively stable in terms of its income over the last periods (see Chart III.17). These values were below those observed prior to the international crisis of 2008 as well as those recorded in the 1997-2001 period. Regarding to indebtedness exclusively through lines aimed at consumption, even though it is still below the figures recorded in 2008, it exceeds the levels observed before the 2001-2002 crisis (see Chart III.2).

The improvements forecasted for the labor market as well as the rise of government transfers would continue boosting a hike in households' income. Households are expected to continue raising their consumption levels though at a lower pace, in a context where their payment capacity would be kept relatively stable.



III.4 Public sector

Tax revenue and primary spending grew strongly over 2010 while the primary result continues performing positively

Tax revenue increased by 33% year-on-year (y.o.y.) in nominal terms during the first eight months of the year. Tax revenue was boosted basically by the value added tax (VAT), income tax, social security funds and taxes related to foreign trade, accounting for 84% of the y.o.y. growth. Thus, accumulated revenue collection over the last 12 months reached slightly more than 27% of the GDP³⁰, thereby recording a new historical maximum (see Charts III.18 and III.19).

Primary spending of the Non-Financial Public Sector (NFPS) grew 31% y.o.y. over the first seven months of the year recording a growth rate below that of revenues over the last periods. The increase of spending was boosted mainly by social security benefits, current transfers to the private sector and public employees' wages, as a whole, for 76% of the y.o.y. hike. Meanwhile, a significant acceleration was observed in the growth pace of budgetary transfers to provinces³¹ (both current and capital ones). Thus, primary spending accumulated over the last 12 months reached a historical maximum amounting close to 28% of the GDP, considering automatic transfers of funds to provinces (federal tax revenue-sharing system, special laws among others) (see Chart III.20).

Primary surplus of the NFPS accumulated \$14.983 billion between January and July 2010³², evidencing a \$7.049 billion y.o.y. hike; meanwhile, the financial result was positive, standing at \$2.852 billion. Thus, primary surplus totaled 1.9% of the GDP over the last 12 months (see Chart III.21) and is expected to remain positive along 2010. According to the Market Expectation Survey (REM), the NFPS would reach a primary surplus amounting to \$22.25 billion in 2010, accounting for 1.5% of the GDP.

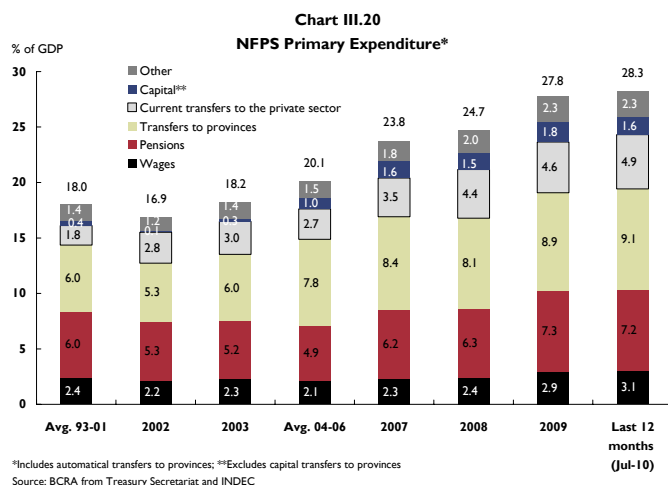
The 2010 National Public Debt swap allowed the normalizing of over 91% of the total debt originally eligible for the 2005 swap

The preliminary results of the 2010 National Public Debt swap were disclosed in early July (see Box 2) with a 66.7% acceptance level normalizing over 91% of the total

³⁰ For a more detailed analysis on revenue and spending of the Public Sector, see the Inflation Reports corresponding to the second and third quarter of 2010.

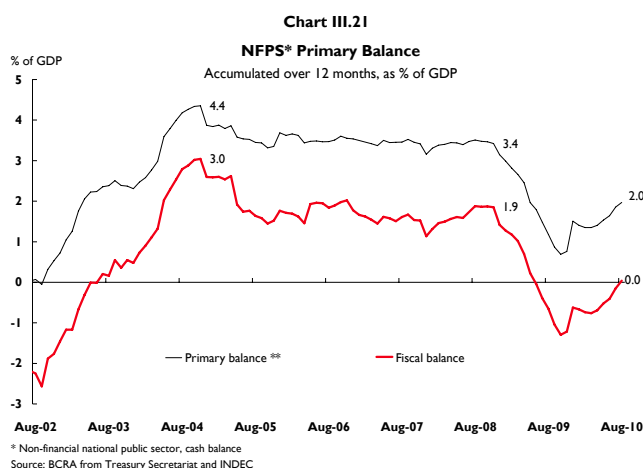
³¹ It includes automatic transfers to provinces (federal tax revenue-sharing system and special laws).

³² The BCRA transferred \$4.67 billion to the National Treasury between January and July 2010 as Profits and Contributions.



debt originally eligible for the 2005 swap. Thus, financial needs anticipated for the year increased by about US\$500 million, with a higher impact in 2011 when they will have to face the services of GDP-linked coupons.

During 2010, the National Treasury has so far met its financing needs mainly through the use of intra-public sector domestic funds. Debt maturities with international institutions and private holders of sovereign debt were complied with using part of the international reserves of free availability that fed the account of Payments to International Financial Organizations and the Argentine Debt Reduction Fund³³. The main intra-public sector funds of the National Treasury were related to temporary advances by the BCRA, Banco de la Nación Argentina (BNA) loans and the issue of non-financial intra-public sector debt.



³³ Decree N°297/2010 and Decree N°298/2010.

IV. Financial Sector

Summary

Banks' financial intermediation with the private sector showed an improved pace of expansion over the first part of the year in a context of better economic perspectives at a local level. Moreover, the financial system continued developing its transactions with high solvency indicators. The value of institutional investors' portfolios grew mainly driven by the funds of the Guarantee Sustainability Fund (FGS) which had increased in productive and infrastructure projects as well as in public credit transactions.

During the first half of 2010, bank lending to households and companies grew at a faster rate compared to the same period of the previous year, movement that was mainly accounted for by private banks. On the other hand, public financial entities led the increase of liquid assets in the group of financial entities following the anticyclical role they had in 2009. The greater momentum shown by loans was primarily channeled through short term commercial credit lines and lending at households' consumption, which was reflected in the relatively low average maturity of new loans granted to the private sector. Despite the growth of banking lending to the private sector, credit depth in the economy continues at low levels, even lower than those of other economies of the region, showing a high development potential.

Public sector deposits raised its share in total funding, while the private sector ones improved their growth rate against last year. From low levels, the financial system's exposure to foreign funding continued shrinking thereby preventing the system from the possibility of being affected by adverse effects derived from a still volatile international context.

Even though the financial system infrastructure improved, recording an increase in jobs and ATM's, its presence is still a relative low in the country at aggregate levels and there exist some geographical concentration in the provision of banking services.

Capital compliance by the financial system continued exceeding the regulatory requirement easily. The consolidated net worth of the group of banks continued to grow boosted by accounting profits, even though leverage increased slightly.

The volume of funds obtained through financial intermediation is expected to keep climbing, and it is foreseeing that banks will keep increasing the most stable revenue sources derived from their activities, within a context that would continue recording suitable levels of liquidity and capital.

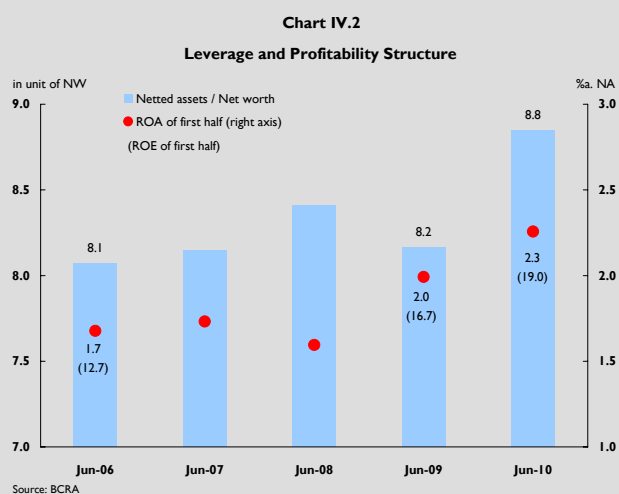
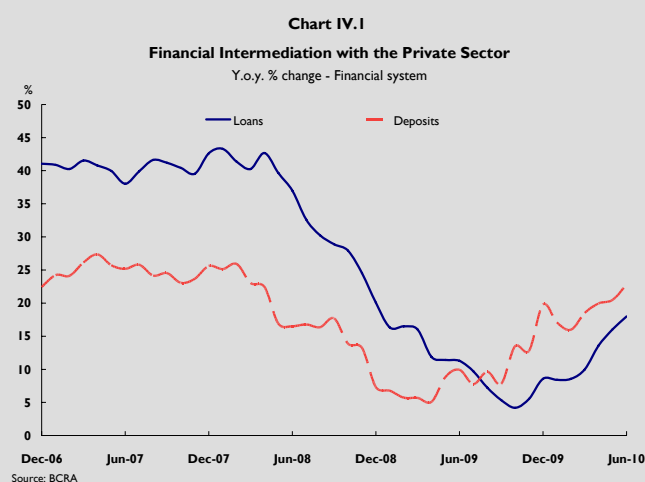


Table IV.1

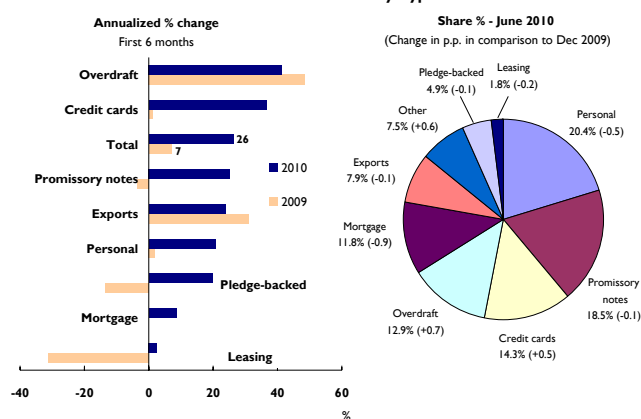
Balance Sheet

Financial system - As % of netted assets

	Jun-09	Dec-09	Jun-10	Change in p.p.		Stock change	
				II H-10	y.o.y.	II H-10 (%a.)	Last 12 months (%)
Assets	100	100	100				
Liquid assets	22	21	24	2.9	1.9	68	34
Lebac and Nobac	8	10	11	1.5	3.2	75	74
Loans to the public sector	14	15	13	-2.0	-0.2	-1	21
Loans to the private sector	41	40	39	-0.6	-1.7	26	18
Other assets	15	14	12	-1.8	-3.2	-2	-3
Liabilities + Net Worth	100	100	100				
Public sector deposits	20	19	24	5.5	4.6	117	51
Private sector deposits	53	55	53	-1.8	-0.1	22	23
Liabilities with the BCRA	0	0	0	0.0	-0.2	-1	-73
ON, OS & foreign credit lines	3	3	2	-0.6	-1.1	-19	-17
Other liabilities	13	13	12	-1.2	-1.2	7	12
Net worth	10	10	8	-1.9	-1.9	-13	0

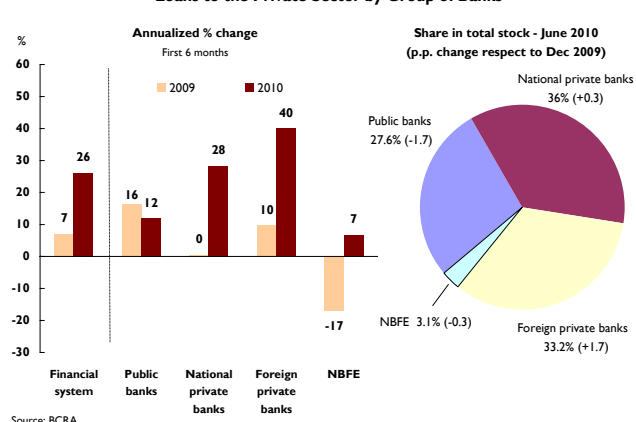
Source: BCRA

Chart IV.3

Loans to the Private Sector by Type of Line

Source: BCRA

Chart IV.4

Loans to the Private Sector by Group of Banks

Source: BCRA

IV.1 Financial entities³⁴**Activity*****The pace of expansion of banks' financial intermediation with the private sector rose***

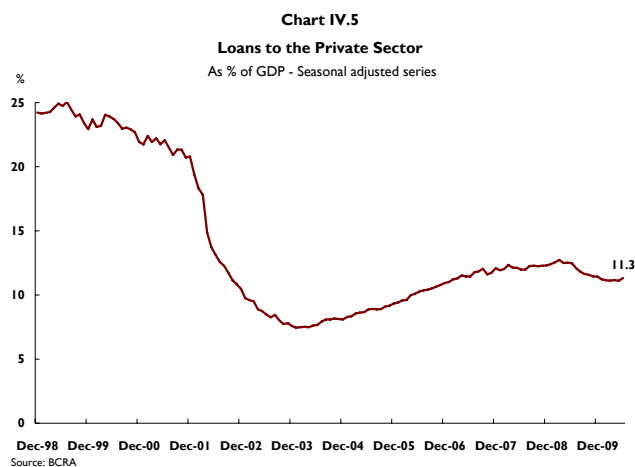
Accompanying better financial and economic perspectives in the domestic context, a renewed momentum in banks' financial intermediation with the private sector was observed during the first part of the year. Both loans and deposits by companies and households increased their expansion rate reinforcing the boost recorded in the last quarter of 2009 (see Chart IV.1). Netted assets of the financial system increased 30% annually (a.) so far this year (23% year-on-year; y.o.y.), driven mainly by the performance of public banks and, to a lesser extent, by foreign and national private banks.

Liquid assets raised their share in netted assets of the financial system during the first part of the year as the case of Lebac and Nobac holdings (see Table IV.1), mainly due to the performance of public banks. As a result of the meaningful momentum shown by these assets, lending to the private sector decreased its share in netted assets, even though some reversal in this trend has been observed since May primarily due to the performance exhibited by foreign private entities.

The increase in the stock of lending to the private sector (both companies and households) was generalized among credit lines amounting 26%a. during the first 6 months of 2010, almost four times above the value recorded over the same period last year (see Chart IV.3). Commercial loans (overdrafts, promissory notes, exports and leasing) expanded by 28%a., and overdrafts recorded an outstanding pace (41%a.). Among loans with real collateral (12%a.), the momentum shown by pledge-backed loans should be highlighted (in line with the evolution of the automotive sector) while mortgage loans had a lower boost.

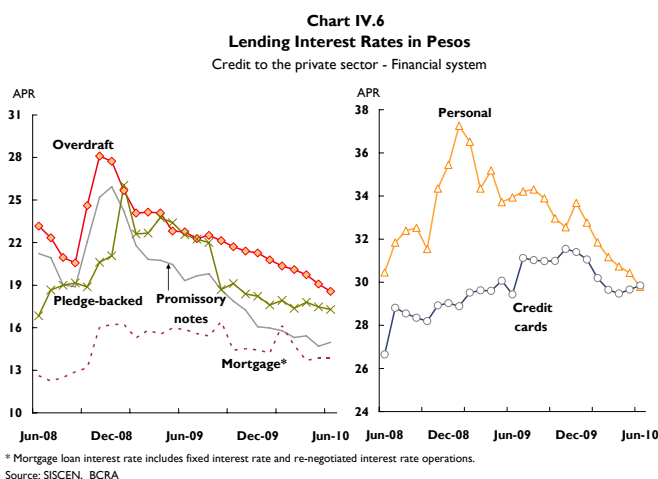
In recent months, the growth of credit to households and companies was primarily accounted for by private banks (both national and foreign) and so they increased their share in financing (see Chart IV.4). It should be noted that over the same period in 2009, amidst the domestic effects derived from the international economic crisis, public financial entities led the rise of credit to the private sector thereby exhibiting a countercyclical performance.

³⁴ Only financial entities regulated and supervised by the BCRA are included in the analysis herein (Act N°21.526).



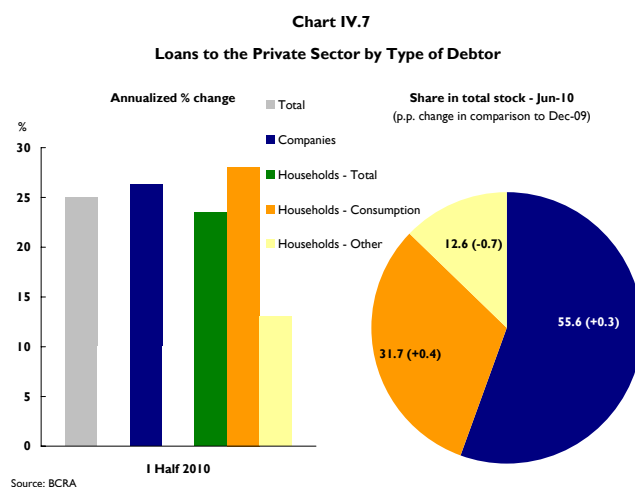
Within this framework, bank lending to companies and households accounted for a bit more than 11% of GDP by mid year (see Chart IV.5) and was slightly below the value recorded at the end of 2009 in a context of growing economic activity. Even though this ratio exceeds by 4 p.p. the minimum value recorded after the 2001-2002 crisis, it is at relatively low values against its own history and when compared to other countries of the region, pointing out the sector's ample growth potential.

Lending interest rates fell in a generalized manner during the first part of 2010 (see Chart IV.6), accompanying the improvement of the economic context. Among commercial lines, the most relevant falls were evidenced by overdrafts and promissory notes while among loans aimed at consumption, personal loans were those that exhibited a greater reduction. Real collateral finance costs' decreased less, and such reduction was relatively more important in the case of pledge-backed loans.



Financing to companies and households accelerates through shorter term lines

Financing to the corporate sector³⁵ has grown 26%a. over 2010, a bit more than loans granted to households (23%a.). Thus, lending to companies increased slightly its share in the stock of financing to the private sector, accounting for almost 56% of the total (see Chart IV.7). The distribution of lending between households and companies has been heterogeneous among the different regions of the country with greater weighting of corporate finance in the regions of the Ciudad Autónoma de Buenos Aires –CABA- (Autonomous City of Buenos Aires), Centro and Cuyo (see Box 4).

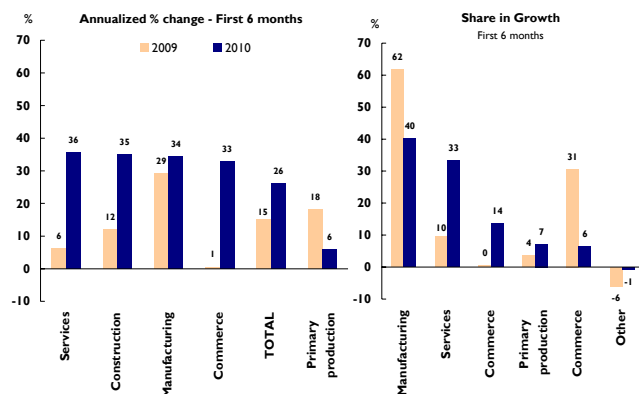


During the first months of the year, bank lending aimed at all productive sectors increased its pace of expansion with the exception of the primary segment (see Chart IV.8). The contribution from different productive sectors to the growth of corporate lending was more homogenous over the first part of 2010 in y.o.y. terms, even though almost three quarters of this rise were accounted for by loans to the manufacturing sector and service companies. Thus, manufacturing continued being the economic sector with greatest weighting in the total stock of finance to companies, followed by service companies, which have recently displaced the primary sector down to the third place.

The increase in lending to the corporate sector during the first half of the year was instrumented mainly

³⁵ Financing to companies is that granted to corporations and commercial financing granted to individuals, the rest of financing to individuals is considered within the concept of households.

Chart IV.8
Loans to Companies by Economic Sector



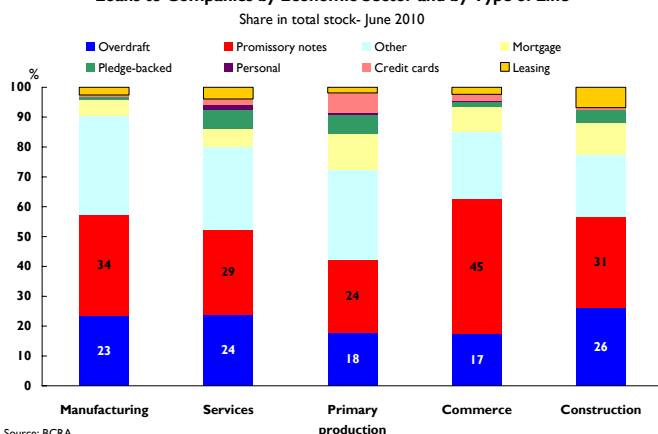
Source: BCRA

through overdrafts and promissory notes (particularly, manufacturing and service sectors). On the other hand, corporate loans with real collateral (of longer term) had a lower performance. Therefore, shorter term loans (overdrafts and promissory notes) accounted for over 50% of the total stock of funds in all economic sectors with a slightly lower value in primary production (see Chart IV.9).

Loans of a relatively larger size³⁶ granted to companies (over \$5 million) exhibited a higher expansion rate than that of smaller loans during the first part of 2010, amounting to almost 55% of the total stock.

Meanwhile, the rise of lending channeled particularly to households was driven mainly by consumption lines which, as a whole, rose 28%a. during the first months of the year (loans arranged through credit cards grew 41%a. and personal loans did so by 21%a.). Lending with real collateral granted to households improved over the period. While the performance of pledge-backed loans is to be noted (almost 30%a.), mortgage loans exhibited a moderate increase.

Chart IV.9
Loans to Companies by Economic Sector and by Type of Line

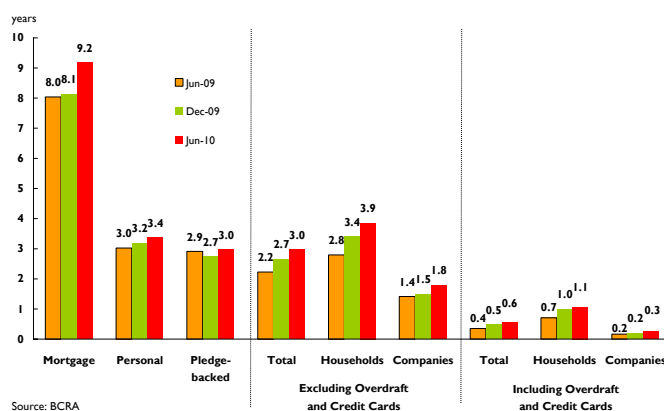


Source: BCRA

The performance of bank financing recorded so far 2010 has exhibited a reduced average maturity (see Chart IV.10), both in the case of loans to households and companies. In this context, the BCRA decided to take an active role by taking measures aimed at extending the terms with which the financial system works and to promote financing to the private sector. Thus, in early June, the BCRA decided to implement a line of overdrafts for financial entities and for a maximum 5-year term. These funds must be applied by banks to investment projects of the productive sector with an average term equal to or exceeding two and a half years and will have a fixed interest rate to be determined when there is an auction call³⁷. Financial entities must provide as guarantee instruments issued by the National Government valued at the market price at, at least, 125% of the balance owed in this kind of overdrafts.

Chart IV.10
Lending to the Private Sector

Average maturity weighted by amount - Financial system



Source: BCRA

Credit to private sector growth took place together with a reduction of the exposure of the financial sector to the public sector (it has fallen 1.6 p.p. from netted assets down to 14% so far this year), and this movement was mainly accounted for by official banks and national private entities.

Public sector deposits rose, gaining share in the total funding of banks

³⁶ For segments of residual balance.

³⁷ See Communication "A" 5089.

Chart IV.11

Funding Composition by Group of Financial Entities

In % - June 2010

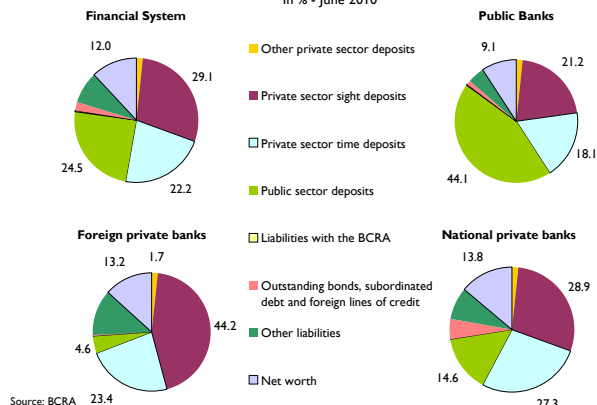


Chart IV.12

Private Sector Time Deposits in Pesos

Annual percentage rate operated by contractual maturity - Financial system

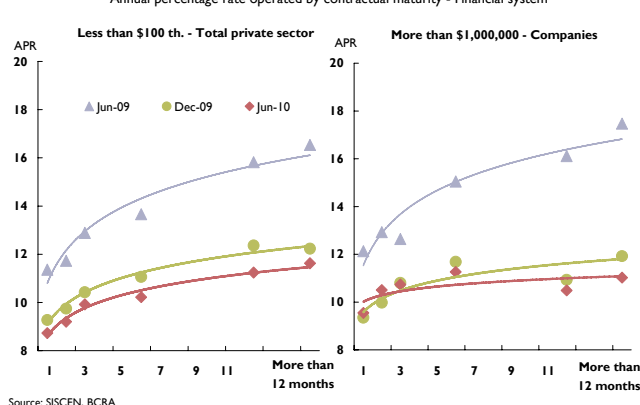
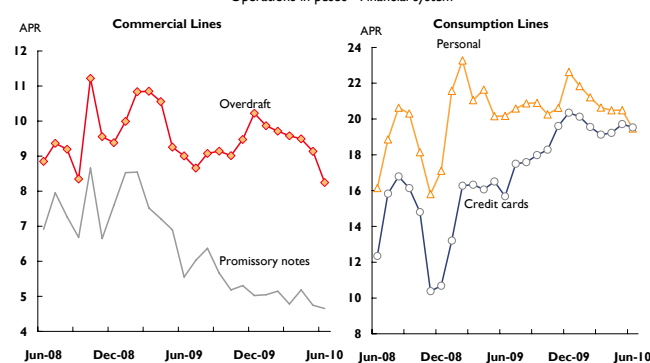


Chart IV.13

Spread of Lending Interest Rates - Loans to the Private Sector

Operations in pesos - Financial system



Non-financial sector³⁸ deposits increased 44%a. so far this year and were basically boosted by public sector deposits and, to a lesser extent, by those of the private sector.

Deposits by companies and households peaked 22%a. over the first part of the year, almost 6 p.p. more in y.o.y. terms. This greater momentum resulted from sight and term deposits in pesos since those in foreign currency slowed down.

Therefore, private sector deposits reached 53% of netted assets by mid-2010 (sight deposits amounted to 29% while time deposits equaled 22%³⁹). These funds recorded the greatest share in private banks funding (both national and foreign) (see Chart IV.11). On the other hand, public sector deposits were the main funding source of public entities.

Better macroeconomic conditions coupled with the rise of private sector time deposits in pesos favored a slight reduction of borrowing interest rates against late 2009. Such decrease was evidenced in all terms in the case of retail deposits while in the case of deposits of greater relative amounts, it was evidenced in longer terms (see Chart IV.12). This drop in the cost of funding through time deposits combined with the downturn mentioned for lending rates (see Chart IV.6), made the financial system record smaller spreads both in commercial and consumption loans (see Chart IV.13). This is a similar trend if a comparison in terms of total private funding of banks is made.

Financial entities exposure to foreign funding remained at reduced and decreasing levels. Within a context where volatility in international capital markets persists, this characteristic is a strong factor for the sector by reducing a potential contagion source.

Progress on bank infrastructure, even though heterogeneity exists among the different country regions

Along with the growth of financial intermediation and the provision of means of payment, employment and the operating infrastructure of the financial system expanded over the last months. Once the domestic effects derived from the international crisis were overcome, the financial system payroll went up in the first half of 2010. Meanwhile, the number of branches remained relatively stable, while the setting up of

³⁸ It includes deposits by the private and public sector, interest accrued and CER adjustments.

³⁹ The difference corresponds mainly to fixed balances and other balances from deposits of the private sector that were not considered in specific accounts.

Box 3 / Banking Services in Argentina

As a promoter and rulemaker of public policies aimed to favoring the banking services access, the BCRA makes regular efforts to measure, study, and analyze access to and use of financial services. Thus, it conducted the second round of the National Survey on Access to and Use of Financial Services in 2009 (the first round had been carried out in 2007), and, therefore, it has an additional diagnosis tool for the banking process in Argentina and a useful instrument to design policies to help extend access to the consumption of financial services and products

The survey⁴⁰ results show that the banking services access⁴¹ in Argentine households increased from 55% to 61% between 2007 and 2009 (considering localities of at least 20,000 inhabitants referred to as “R1”) (see Chart B.3.1). This evolution arises mainly from the rise of the proportion of households that have had access to credit cards and loans granted by financial entities supervised and regulated by the BCRA (EFIS).

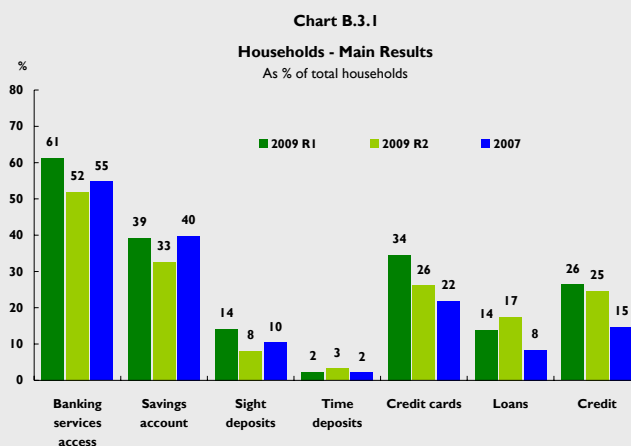
The latest edition of the survey contained, as a new methodology, an independent study conducted in localities having a population exceeding 2,000 and located between more than 10 kilometers (km) and less than 50 km away from the nearest office of an entity falling under the scope of the BCRA (referred to as R2)⁴². This new study suggested that the access level of the population living in localities having an infrastructure of services (R1) is almost 10 p.p. higher than those with infrastructure deficit (R2). Furthermore, it may also be seen that despite the percentages of households in every region that have access to EFIS⁴³ credit are similar, ratios in relation to credit cards favor R1 inhabitants while those related to loans benefit R2 inhabitants.

⁴⁰ Coordinated by the Subgerencia General de Investigaciones Económicas.

⁴¹ A broad definition of the banking term is used, which includes clients assisted by financial entities regulated and supervised by the BCRA.

⁴² 2,532 households, 642 companies and 159 financial service providers were surveyed in R1; 402 households, 86 companies and 35 financial service providers, in R2.

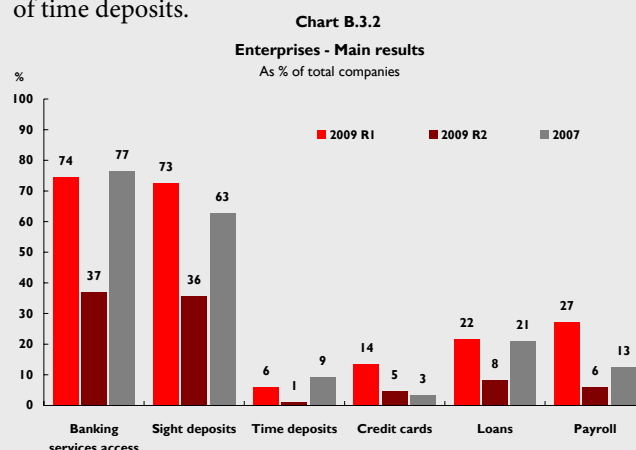
⁴³ Which are financed by an EFI through loans (personal loans, pledge-backed loans, mortgage loans, etc.) and/or through credit cards (purchases in installments, balance financing, advances through automatic teller machines, etc.)



Source: BCRA

Companies have shown minimum changes in their access to financial services over the last years (see Chart B.3.2). While the percentage of companies with banking access fell marginally from 77% to 74% between 2007 and 2009, a positive evolution is recorded regarding access to current accounts and corporate credit cards and the use of electronic methods to pay wages in bank accounts. On the other hand, the proportion of companies that make time deposits with their economic surpluses dropped slightly against 2007.

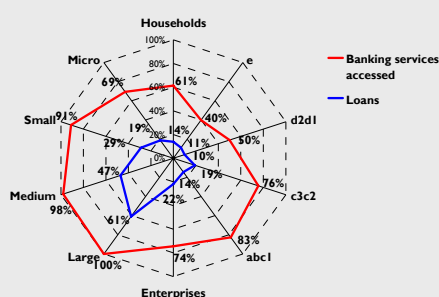
Although changes in the temporary dynamics have been small in the corporate sector, there are significant changes when localities with infrastructure (R1) are compared to those without infrastructure (R2). The proportion of companies with banking access in R1 almost doubles that of those located in R2. This ratio is similar if current account access is considered, amounting to about 3 to 1 in the case of corporate credit cards and loans and increasing to almost 5 to 1 in the payment of wages through bank accounts and the issue of time deposits.



Source: BCRA

Access levels to financial services and products in general and to loans in particular change considerably depending on the socioeconomic level of households and on the size of companies (see Chart B.3.3). Thus, the survey suggests that the proportion of households that have banking access from the highest socioeconomic level⁴⁴ doubles that of those with the lowest level⁴⁵. When the use of loans is observed, the minimum and maximum end values (10% and 19%) correspond to two of the lower levels (D2 and D1) and other two that are relatively higher in the scale (C3 and C2), respectively⁴⁶.

Chart B.3.3
Bank Services Access - Summary
As %



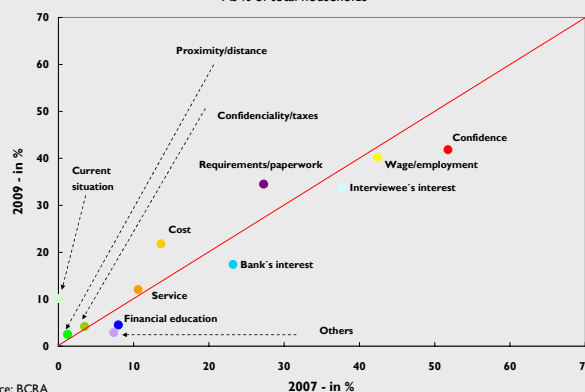
Source: BCRA

Differences in banking access levels among companies of different sizes are less marked than those existing between households' socioeconomic levels: banking reaches a maximum of almost 69% in the case of micro companies; it tops 91% in small companies and peaks 100% in the case of large ones. Nevertheless, there are more significant differences in terms of the companies that receive loans from EFIS: while only 19% of micro companies have access to them, 61% of large ones use them.

Households underscore lack of confidence as the most common reason why they do not make transactions with banks (or do not do it intensively) even though this motive is minor when compared against 2007 (see Chart B.3.4). Barriers related to work instability and the level of income follow. Requirements and excessive paperwork are also relevant obstacles in the 2009 study, while lack of interest on the part of interviewee was a

major issue 2007. In 2009, the perception of higher costs for financial services became more relevant whereas the lack of interest by banks was reduced.

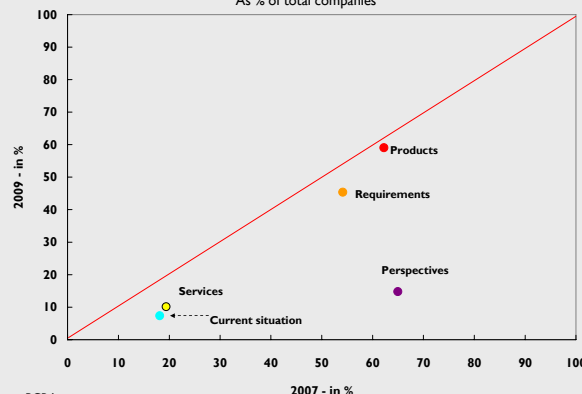
Chart B.3.4
Barriers to Banking Services Access for Households
As % of total households



Source: BCRA

Obstacles evidenced by companies to access bank lending (see Chart B.3.5) have recorded, in general, less intensity against 2007, even in a context where the percentage of companies having access to loans has remained practically unchanged. While in 2007 unfavorable perspectives were at the top of all obstacles, the characteristics of the products offered and its requirements prevailed in the 2009 scenario.

Chart B.3.5
Barriers to Banking Services Access for Companies
As % of total companies



Source: BCRA

From the standpoint of financial service providers, the domestic economic scenario would be among the main obstacles to be faced to achieve a rise in loan generation (of short, medium and long term) for companies and to increase the number of households receiving services (see Charts B.3.6 and B.3.7). Regarding the inclusion of new households as clients, the most relevant barriers are related to the regulatory framework, the existence of scarce and improper demand, and charges derived from taxes. When considering obstacles hindering the sale of additional products and services to households receiving

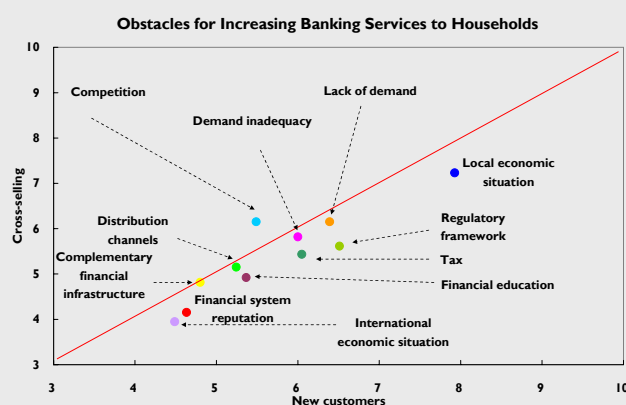
⁴⁴ For further detailed information on the definition and construction of socioeconomic levels, see NSE (Nivel Socio-Económico – Socioeconomic Level) 2006, by the Asociación Argentina de Marketing, December 2006.

⁴⁵ The NSE nomenclature comprises from the lowest to the highest levels: E, D2, D1, C3, C2, C1 and AB.

⁴⁶ It should be highlighted that the percentage of highest socioeconomic levels (AB and C1) that counts on financing via credit cards is almost four times higher than that of households pertaining to the lowest socioeconomic level (38% versus 11%).

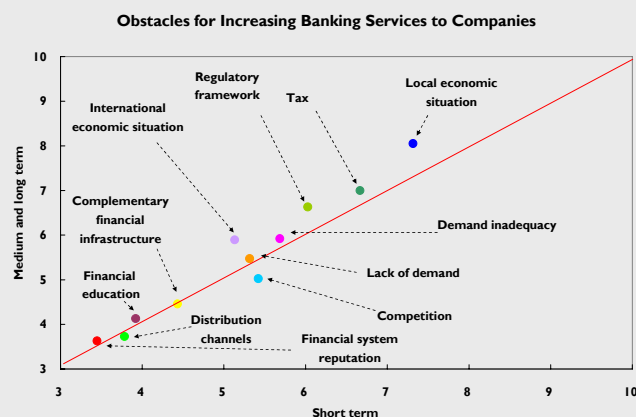
the services, competition against other entities is another relevant barrier. As far loans granted to companies are concerned, there exist impediments similar to those of households and the most significant ones are those related to tax charges, the regulatory framework and improper demand. Additionally, factors associated to competition, lack of demand to issue credit (of all terms) and the international economic scenario are present.

Chart B.3.6



Note: From 1 (a less important obstacle) to 10 (a very important obstacle)
Source: BCRA

Chart B.3.7

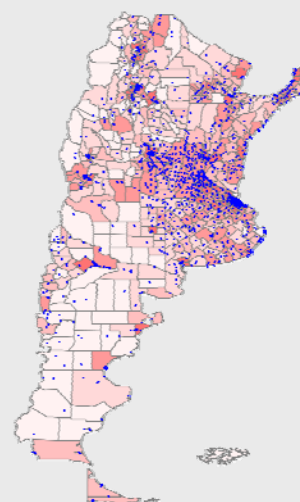


Source: BCRA

With 60% of households and 75% of companies using some financial service or product provided by EFIS, Argentina has indicators of access to financial services that are higher than the regional average (even though in GDP terms, financial intermediation is lower than the regional average). Nevertheless, there stills exist high potential of development that requires facing challenges such as: 1) stimulating greater equality of financial inclusion opportunities per socioeconomic level, 2) boosting the development of an infrastructure to provide services with a wider geographical scope, given that approximately 66% of localities lack banks points to

provide services and the infrastructure of automatic teller machines tends to be focused on the center and north of the country (see Chart B.3.8), 3) promoting improvements in the depth and conditions of access to credit (of long term in particular), and 4) fostering the increase in the scale of the financial sector to reduce unit costs of the services rendered.

Chart B.3.8
ATM Distribution



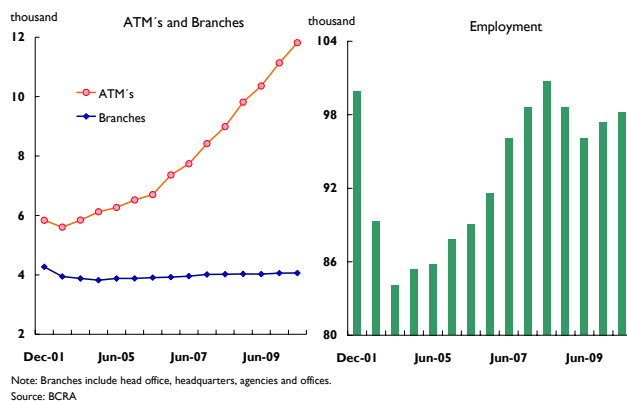
Source: BCRA

The challenge from now on is to catalyze a dynamic and sustained banking process in order to advance towards a financial system that has further scope to include those that are excluded at present, that provides a wider supply of financial services, that has a greater scale and lower unit costs, that assures protection to consumers and that does not disregard financial stability conditions or the ultimate purpose which is to favor sustainable development.

In this regard, the BCRA has been working to implement a set of specific measures. Particularly, it recently boosted the setting up of special offices to provide services in relation to certain transactions in localities having less than 30,000 inhabitants (generating facilities for entities that adhere to this regulation); in addition, it also promoted the use of electronic means of payment through the implementation of a universal free bank account with a related debit card for all the population and the reduction of inter-bank transfer costs, among the main measures⁴⁷.

⁴⁷ For further information, see Chapter VI, Section 2.

Chart IV.14
Financial System Operational Structure

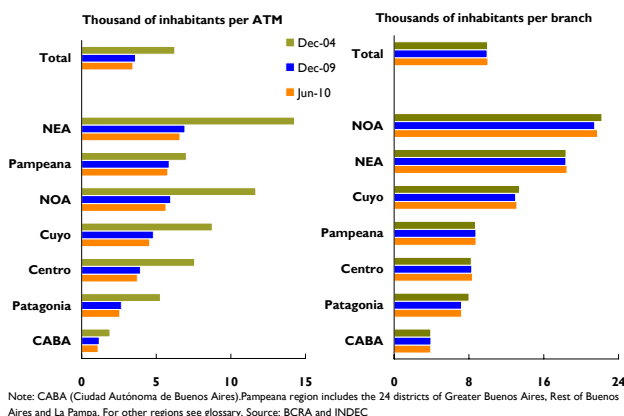


automatic teller machines (ATMs) rose at a 14.1% y.o.y. rate over the first half of 2010 (see Chart IV.14).

Significant heterogeneity exists in the different regions of the country regarding the availability of financial services infrastructure (see Chart IV.15). The City of Buenos Aires and several cities in the Patagonia have fewer inhabitants per branch as well as ATM's, while provinces in the Argentine North West Region (NOA) and in the Argentine North East Region (NEA) face the opposite situation. It is worth noting that provinces recording the highest levels of human development⁴⁸ are those that have greater availability of financial service infrastructure per inhabitant (see Chart IV.16). Even though no significant changes were recorded over the last year in the population/branch ratio, regions that are less supplied recorded some progress on the inhabitant/automatic teller machine indicator. In contrast, before the 2001-2002 crisis, the zone with less coverage had ten times more of inhabitants per automatic teller machine than the regions that were supplied more, this gap has decreased by 6 times, to date.

Chart IV.15

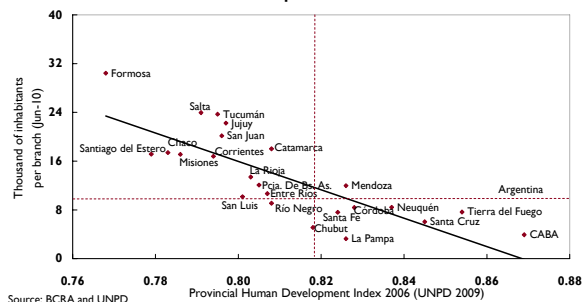
Financial System Regional Coverage



It has been estimated for all the country as a whole, that while urban population residing in localities that have branches and/or automatic teller machines accounts for 90% of the total (88% in 2001), the ratio would stand at 75% in localities having less than 30,000 inhabitants (70% in 2001).

Chart IV.16

Financial System Coverage with Branches and Human Development Index



In order to continue promoting the extension of the financial system's operating infrastructure, fostering greater coverage of banking services in the different sectors of the population (especially those with less access), the BCRA authorized in May the setting up of special service offices to conduct some specific transactions in localities having less than 30,000 inhabitants providing facilities to financial entities that adhere to this regulation⁴⁹.

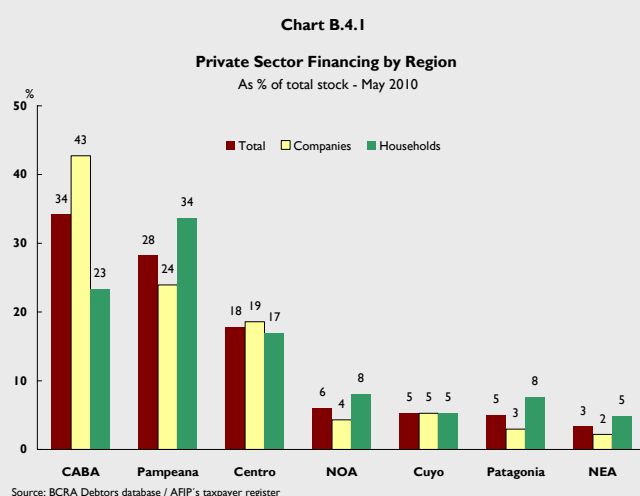
⁴⁸ Measured here through the Human Development Index prepared within the framework of the United Nations Development Programme-UNDP. When preparing this index, life expectancy upon birth, adults' literacy rate, the rate of enrollment at schools and gross domestic product (GDP) per capita are taken into account (expressed in parity with purchasing power in American dollars). The value of the index ranges from 0 to 1 (the closer to 1, the higher the human development level is). Source: "Aportes para el desarrollo humano en Argentina / 2009" - PNUD.

⁴⁹ Communication "A" 5079.

Box 4 / Regional Credit Distribution

Geographical distribution of credit to the private sector is still exhibiting high territorial concentration, a performance that is being observed in lending to both corporations and households. The policies implemented by the BCRA together with a favorable macroeconomic context would allow contributing to greater credit development to the private sector in all the regions of the country

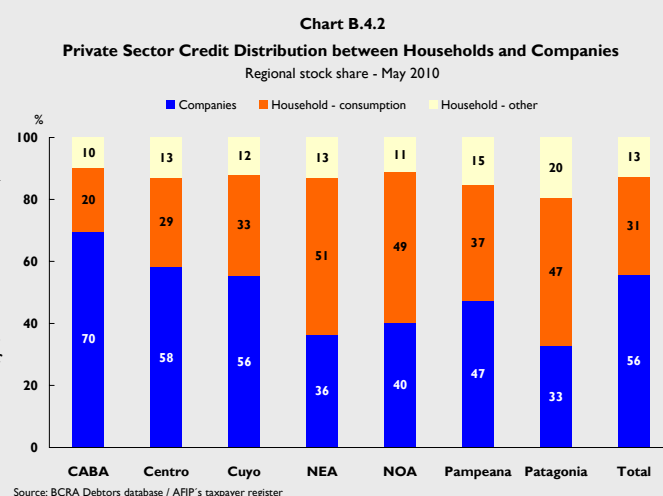
Some advances have been observed over the last years on the geographical coverage of the domestic financial system infrastructure (see Chapter IV, Section 1). This performance coupled with sustained economic growth helped record a generalized increase of lending to the private sector in the different regions of Argentina. However, and accompanying most of the geographical economic and population growth distribution, bank lending to corporations and households continues recording a high territorial concentration: the Autonomous City of Buenos Aires (CABA), the Centro and the Pampeana regions gather 80% of all lending to the private sector while the remaining 20% is distributed in a relatively uniform manner among the regions of Cuyo, the North West Region (NOA), the North East Region (NEA) and the Patagonia⁵⁰. Regional concentration is relatively more marked in loans granted to companies⁵¹ (see Chart B.4.1). It is worth mentioning that credit allocation per region is carried out depending on the debtor's tax domicile so that there is a criterion in place to locate loans that tends to be close to the place where the financial sources were used.



⁵⁰ See the Glossary for a detailed definition of the regions.

⁵¹ Financing to companies is that granted to corporations and commercial financing granted to individuals. The rest corresponds to households.

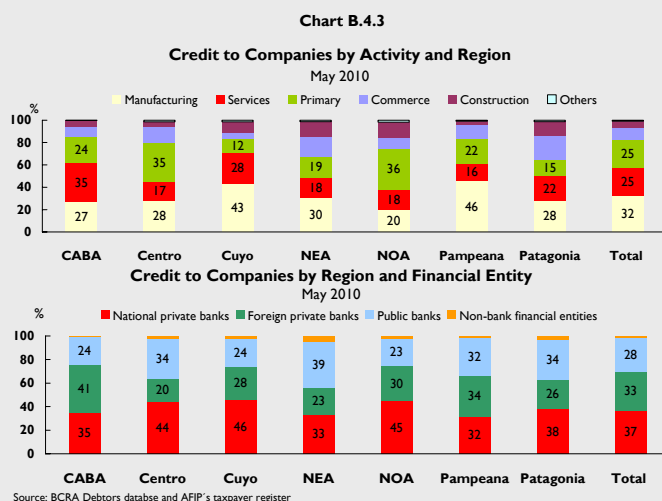
Lending distribution between companies and households varies significantly in the different jurisdictions of the country (see Chart B.4.2). Loans to the corporate sector as a share of total lending, become more relevant in the CABA (reaching almost 70% of the total) and in the regions of the Centro (58%) and Cuyo (almost 56%). In contrast, in the NOA, the NEA, the Patagonia, and the Pampeana region, households financing accounts for over half of the available bank funds, with a significant share of lending aimed at consumption mainly.



Loans to the corporate sector have evidenced considerable regional heterogeneity regarding their availability per productive sector. Lending to manufacturing has recorded the greatest relative weight in the Pampeana and Cuyo regions (about 46% and 43% of the total, respectively); meanwhile, financing to primary production is relatively more significant in the Centro region and the NOA region (36% and 35% of the total) (see Chart B.4.3). On the other hand, credit to the service sector accounts for over one third of the total in the CABA, a proportion that is relatively smaller for the rest of the country.

Foreign private banks have gained a relative share in financing to companies in the CABA and the Pampeana region (see Chart B.4.3), in line with the high geographical concentration of its infrastructure in the country. On the other hand, public banks are exhibiting the highest weighting in the lending markets for companies in the NEA region, while national private banks are making a contribution that is relatively more significant to lending in the remaining regions of the country.

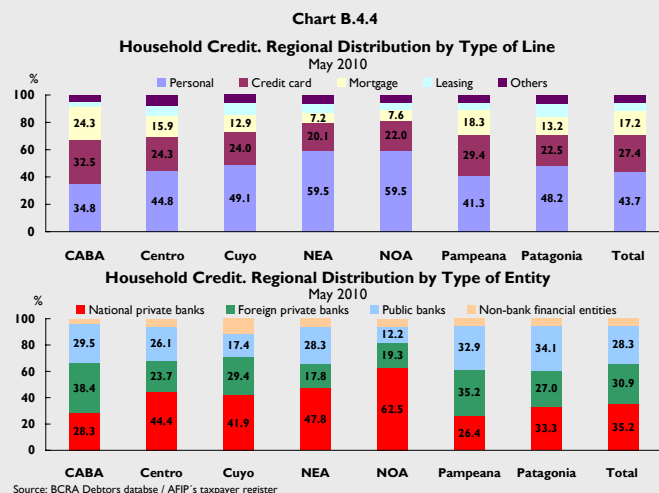
There are two additional dimensions that characterize the regional structure of credit to the corporate sector: i) in CABA, relatively large lending of residual stock (over \$5 million) equals almost three quarters of the total whereas the distribution among sectors is relatively more uniform in the rest of the country and ii) overdrafts and promissory notes in all geographical zones are the most prevailing credit lines.



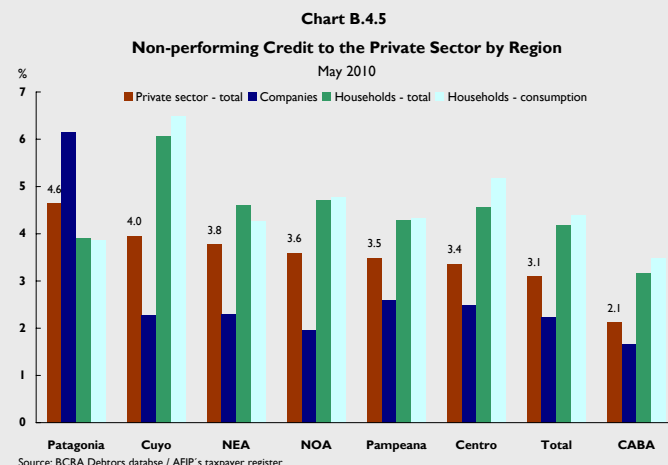
Consumer-related credit lines (personal loans and credit cards) gained participation in total household financing, accounting for over 70% of the total at national level⁵². This proportion is especially high in the NEA and NOA regions where it reaches a little over 80% of households lending (see Chart B.4.4). Particularly, among credits for consumption purposes a large share of personal loans may be observed in all regions (with a minimum amounting to 34.8% in CABA and a maximum of almost 60% in the NEA and NOA regions). On the other hand, loans with real collateral only exceed 25% of the total granted to households in CABA (with mortgage loans showing more relevance and accounting for 24.3 p.p.), followed by the Centro and Pampeana regions.

National private banks make the greatest contribution to households' lending both at a national level and in most districts with the exception of the CABA and the Pampeana region where foreign financial entities reach the greatest relative weighting (see Chart B.4.4). This trend is slightly marked if only consumption lines are taken into account.

⁵² Financing for consumption purposes has exhibited sustained growth over the last 5 years gaining share in the total balance of credit to the private sector.



Non-performing loans to the private sector remains at reduced levels at a national and regional level (see Chart B.4.5). Regarding companies (with the exception of the Patagonia region), little dispersion in the delinquency ratio is observed. It stands at reduced levels in regions with high share in lending as well as in those with less weighting in the total. Among financing to households, the Centro region, the Cuyo region and the NOA region evidence the highest nonperforming ratios resulting from a worse relative performance of lending aimed at consumption.



Even though some progress was observed regarding credit distribution to the private sector over the last years, there still exists considerable regional heterogeneity. Economic growth expected for the coming years together with the policies of the BCRA aimed at promoting the extension of the operating infrastructure of the financial system as well as its use, should create an adequate scenario to deepen financing to companies and households in the different jurisdictions of the country.

Chart IV.17

Leverage
Financial system

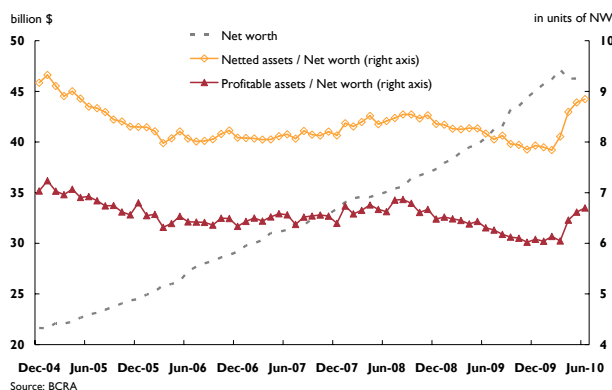


Chart IV.18

Prudential Requirement and Capital Compliance
As % of total capital compliance - June 2010

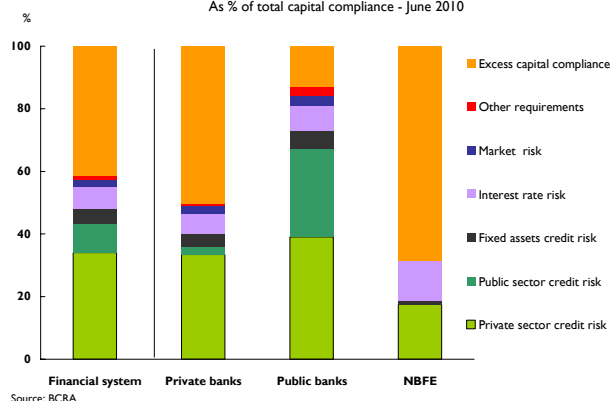
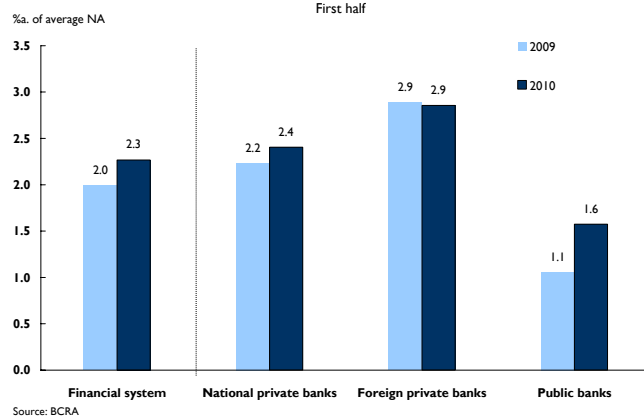


Chart IV.19

Profitability Structure by Group of Banks
First half



Capital position

In a context of a sound financial system position, in 2010 banks have distributed more dividends than in previous years

The consolidated net worth of the financial system grew at a 14% y.o.y. rate over the first part of 2010 in line with the average recorded over the last 3 years. This evolution showed some slowdown in the second quarter of the year due to the distribution of dividends (derived from results accumulated from previous fiscal years) of some foreign and national private financial for an amount close to \$2.5 billion⁵³. The strengthening of entities' solvency over the last periods led to a decrease of the needs of new capital contributions, which topped \$80 million during the first part of 2010, below the value recorded in previous years.

The leverage of the financial system increased slightly over the last months resulting from further relative rise of netted assets against net worth. Thus, netted assets equaled almost 9 times the net worth (see Chart IV.17). This trend of gradual increase of leverage was homogeneous among the different bank groups.

As a consequence of the recovery of momentum evidenced by lending to the private sector and of the net worth evolution, the ratio of capital compliance fell 1.2 p.p. down to 17.6% in the first half of 2010, even though a 0.7 p.p. y.o.y. rise was observed. Capital compliance continued exceeding the regulatory requirement easily and this was generalized among financial entities (see Chart IV.18).

National private and public banks accounted for the rise in profitability

During the first part of the year, the financial system recorded accounting profits equivalent to 2.3%a. of assets exceeding those observed during the same period in 2009 (see Chart IV.19). While ROA and the banking sector's leverage increased, ROE stood at 19%a. in the first part of 2010, exceeding by 2.4 p.p. the previous year figure (see Chart IV.2). Even though a lower financial margin was accrued, especially in those items related to the exchange rate and results from securities, the fall of spending (loan loss provisions and taxes) as well as various income sources more than offset those effects (see Table IV.2). Public banks recorded the greatest relative rise in profitability followed by national private financial entities, while foreign private banks accrued

⁵³ Additionally, by the end of the six-month period, a private bank obtained more share in an NBFE, and this movement impacted the net worth of the financial system.

Table IV.2

Profitability Structure: Financial System

In annualized terms - As % of average netted assets

	93-00	2007	2008	2009	I-H-09	II-H-09	I-H-10
Financial margin	6.1	5.7	6.7	8.5	8.3	8.8	7.5
Net interest income	4.9	2.2	3.1	4.1	4.1	4.2	4.1
CER y CVS adjustments	0.0	1.0	0.9	0.4	0.3	0.4	0.5
Gains on securities	0.8	1.9	1.4	3.3	2.6	3.9	2.2
Foreign exchange price adjustments	0.0	0.5	0.8	0.7	0.9	0.4	0.5
Other financial income	0.3	0.1	0.4	0.1	0.5	-0.2	0.0
Service income margin	3.5	3.1	3.6	3.9	3.7	4.0	3.8
Operating costs	-6.7	-5.5	-6.1	-6.7	-6.6	-6.8	-6.9
Loan loss provisions	-2.2	-0.7	-0.9	-1.1	-1.2	-1.0	-0.8
Adjustments to the valuation of gov. securities (*)	-	-0.3	-0.6	-0.1	-0.1	0.0	-0.1
Tax charges	-0.5	-0.6	-0.8	-1.0	-1.0	-1.0	-0.9
Amortization payments for court-ordered releases	-	-0.7	-0.3	-0.1	-0.1	-0.2	-0.2
Other	0.7	0.9	0.5	0.2	-0.1	0.5	0.5
Income tax	-0.3	-0.4	-0.4	-1.3	-1.0	-1.5	-0.7
ROA	0.5	1.5	1.6	2.3	2.0	2.7	2.3
ROE	3.4	11.0	13.4	19.2	16.7	21.6	19.0
Adjusted ROA (**)	-	2.5	2.5	2.5	2.1	2.9	2.5

(*) Com. "A" 3911 and complementary communications. (**) Excluding amortization of payments for court-ordered releases and the effects of Com. "A" 3911 and complementary communications.

Source: BCRA

Chart IV.20

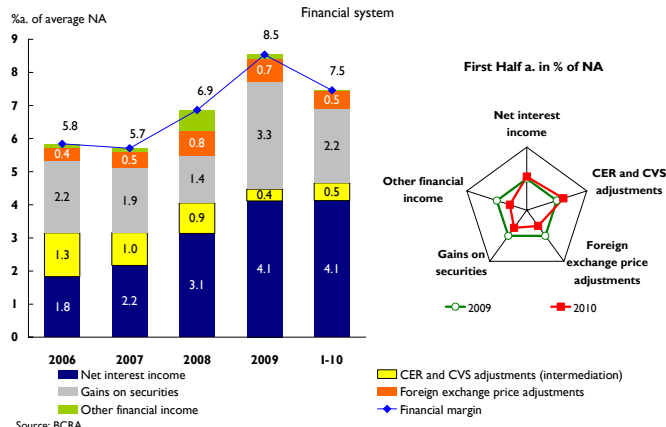
Financial Margin Composition
Financial system

Table IV.3

Profitability Structure by Type of Bank

In annualized terms - As % of average netted assets - First half 2010

	Private banks			Public banks	NBFE
	Total	National	Foreign		
Financial margin	8.7	8.5	8.9	5.3	19.6
Net interest income	5.1	4.5	5.8	2.2	17.9
CER y CVS adjustments	0.1	0.1	0.1	1.1	0.0
Gains on securities	2.7	3.3	1.9	1.7	0.6
Foreign exchange price adjustments	0.6	0.5	0.8	0.4	1.0
Other financial income	0.1	0.0	0.3	-0.1	0.1
Service income margin	4.8	4.8	4.8	2.4	6.8
Operating costs	-8.0	-7.8	-8.1	-5.2	-12.1
Loan loss provisions	-1.0	-0.9	-1.0	-0.4	-4.2
Adjustments to the valuation of gov. securities (*)	0.0	0.0	0.0	-0.2	0.0
Tax charges	-1.2	-1.4	-1.0	-0.5	-2.0
Amortization payments of court-ordered releases	-0.2	-0.3	-0.1	-0.1	0.0
Other	0.5	0.6	0.5	0.6	2.3
Income tax	-1.1	-1.0	-1.1	-0.2	-2.6
ROA	2.6	2.4	2.9	1.6	8.0
ROE	19.6	18.3	21.1	17.7	21.6
Adjusted ROA (**)	2.8	2.7	3.0	1.9	8.0

(*) Com. "A" 3911 and complementary communications.

(**) Excluding amortization of payments for court-ordered releases.

Source: BCRA

profits lower than those recorded in the same period a year ago.

More stable income strengthens in a context where less spending is observed in the main income statement cost headings

The financial margin of banks decreased 0.8 p.p. of assets against a year ago mainly resulting from the decline observed in exchange rate differences⁵⁴ and other financial results (mainly from adjustments made in net forward transactions of foreign currency) (see Chart IV.20). In a context of less increase in the peso-dollar exchange rate over 2010 against the same period in 2009, these incomes reduced their share in the financial margin, trend that was observed mainly at national and foreign private banks (see Table IV.3).

Gains on securities also recorded a 0.4 p.p. reduction of assets against previous periods totaling 2.2%a. of assets. Despite this fall, results from securities remain being the second source of income of banks' financial margin. The drop in this item of the income statement was higher in public banks in accordance with its exposure levels, followed by national private banks, while in the case of foreign banks more benefits were accrued.

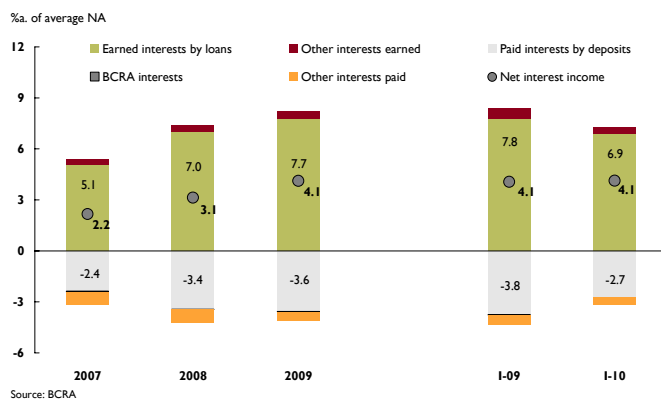
Net interest income still accounts for the main source of funds of the financial system staying relatively stable in 2010 against the last 2 half-year periods (see Chart IV.21). This evolution took place in a context of recovery of the volume of financial intermediation with the private sector and lower spread levels (see page 41). National private and public banks evidenced increases in results from interest during 2010, while foreign ones recorded a year-on-year fall even though they still exhibit the highest level (with the exception of NBFE).

In a context where CER-adjusted mismatching items did not change significantly in the financial system balance sheet over the last months, income derived there from increased slightly during the first half of 2010 as a result of the performance of the index. Thus, CER adjustments evidenced a greater share within the financial margin being particularly relevant in public banks.

Results derived from services increased gradually during the year mainly boosted by the operation of national private banks. Income through services resulted mainly from deposit commissions while incomes related to insurance and the issue of credit cards are gaining relative share.

⁵⁴ Results derived from the monthly update of assets and liabilities in foreign currency. The item includes also the results originated by the purchase and sale of foreign currency.

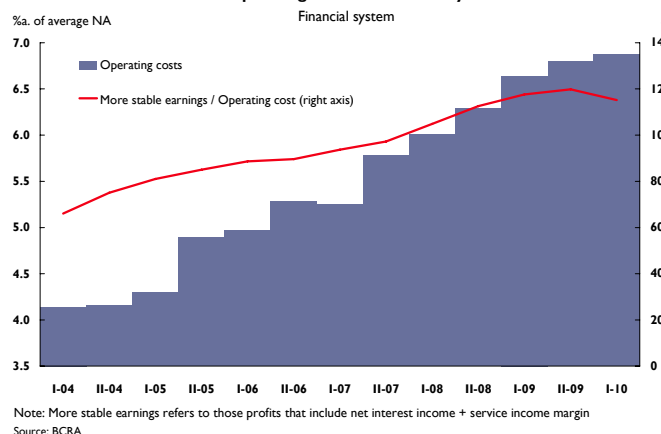
Chart IV.21
Net Interest Income
Financial system



Loan loss provisions fell while operating costs increased gradually

Operating costs grew at a moderate rate in the first part of 2010, together with certain wage adjustments made in a context where the sector's personnel are recovering. This increase was mainly boosted by private banks, especially, foreign ones. At a systemic level, the coverage ratio of operating costs with more stable income remained aligned with the values recorded in early 2009, even though it fell slightly against the values exhibited at the end of the year (see Chart IV.22). Less coverage was evidenced both for public and private banks. Loan loss provisions decreased significantly (see Chart IV.23), in accordance with the improvement seen in the credit portfolio of the private sector (see Page 61).

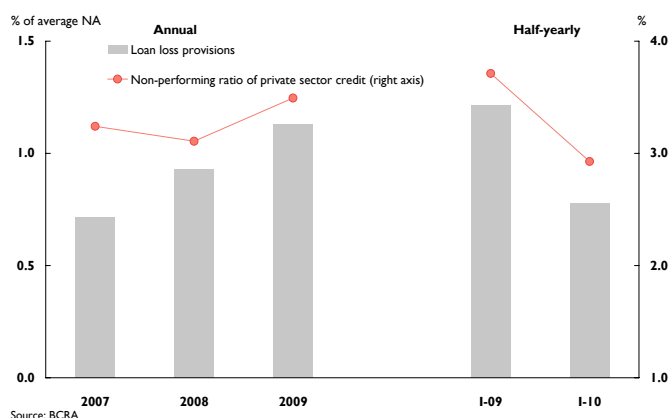
Chart IV.22
Operating Costs and Efficiency
Financial system



During 2010, the financial system faced tax charges that accounted for 1.6%a. of assets staying slightly below the figure recorded a year ago. Meanwhile, the amortization of payments of court order releases and the adjustments to the valuation of government securities (effects from the 2001-2002 crisis) equaled, as a whole, only 0.3%a. of assets, with low dispersion per homogeneous group of banks.

With good perspectives regarding financial intermediation activity, it is estimated that the financial system will end 2010 recording suitable solvency levels

Chart IV.23
Loan Loss Provisions



Considering a context of growing financial intermediation expected for the coming months, it is estimated that the financial system will continue accruing profits coupled with higher income derived from interest and services. In addition, the quality of credit portfolio is projected to stay the same and this would keep loan loss provisions at reduced levels. On the other hand, operating costs would continue growing gradually in a context of deepening of the scope of the financial system's infrastructure and employment.

IV.2 Institutional Investors

The value of international investors' portfolio is increasing driven primarily by the performance of fixed income assets

Investments of the Guarantee Sustainability Fund (FGS), insurance companies and mutual funds (FCI) continued exhibiting sustained growth. Thus, the aggregate portfolio⁵⁵ by the end of the second quarter of the year⁵⁶

⁵⁵ In gross terms (without consolidating).

⁵⁶ Latest information available coincides for the three institutional investors.

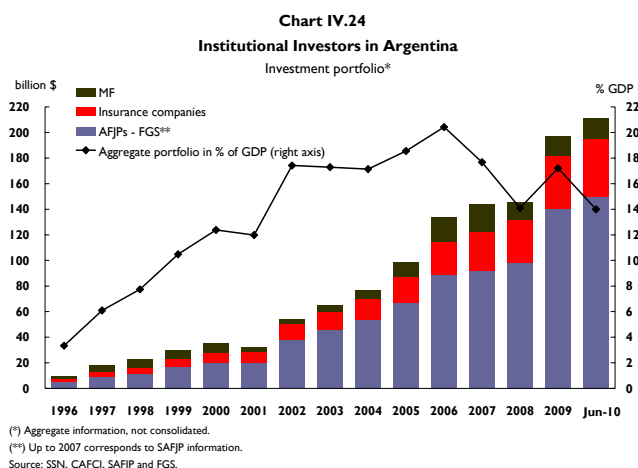


Table IV.4
Social Security Fund FGS-ANSES Portfolio
Million \$

Instrument	Jul-10	% of total	Dec-09	Variation (%)
Investments	148,691	95.2	135,090	10.1
National Government Securities	96,427	61.7	88,028	9.5
Corporate Bonds	1,881	1.2	2,309	-18.5
Time deposits	12,477	8.0	9,574	30.3
Equities of companies	15,847	10.1	13,551	16.9
Equities of privatized companies	290	0.2	280	3.7
Mutual funds	2,174	1.4	1,833	18.6
Foreign Securities (Include equities and bonds)	1,940	1.2	6,760	-71.3
Other financial trusts	4,164	2.7	4,354	-4.4
Investments and infrastructure	13,489	8.6	8,400	60.6
Liquid assets	7,269	4.7	4,075	78.4
Other credits and investments	258	0.2	1,688	-84.7
Total portfolio FGS	156,218	100.0	140,853	10.9

Source: FGS

topped \$211.089 billion (equivalent to 14% of GDP), exceeding the amount of \$197 billion recorded at the end of last year. This represented a 7% rise in the first months of 2010, after having grown 35% in 2009. It should be considered that the evolution of fixed income assets accounted for half of the performance of the aggregate portfolio of institutional investors (see Chart IV.24).

The FGS continued being the main institutional investor at a domestic level and its managed portfolio climbed up to approximately \$156.2 billion as of July 2010 (latest information available). A rise of almost 11% was observed in the portfolio value against late 2009, and this movement was primarily accounted for by a considerable increase of funds aimed at productive or infrastructure projects and at term deposits, and to a lesser extent, by a rise of public credit transactions of the nation (sovereign bonds) (see Table IV.4). Regarding the latter, even though such rise would be mainly accounted for by an expansion of finance to the National Government⁵⁷, bond prices over the January-July period exhibited an average hike of 10%⁵⁸. On the other hand, investments in infrastructure projects have recorded a growth in excess of 60% over 2010 and stand at 8.6% of the total at present. Meanwhile, a significant rise was observed in the value of investments in domestic shares (mainly accounted for by the improvement of their prices) and mutual funds (which rose 17% and 19% respectively over the same period). Liquid assets grew almost \$3.2 billion (78%), while unwinding of positions in foreign bonds was observed.

Insurance companies accumulated assets for over \$61 billion as of last June, showing an expansion exceeding 8% against December 2009. The performance of the portfolio of general insurance companies in 2010 (the main insurance branch) was slightly above the average while companies related to work risks grew 17% in their portfolio⁵⁹. In general terms, the rise of the value of investments in sovereign bonds increased significantly in the first part of 2010 and this component accounts for the growth of most of the aggregate portfolio of insurance companies. Additionally, rises in the value of investments in shares and corporate bonds were relevant even though they had a lower aggregate impact given their corresponding weightings in the portfolio.

⁵⁷ In net terms, it would be approximately \$6.3 billion so far this year.

⁵⁸ According to the index of bonds measured in pesos prepared by the Instituto Argentino de Mercado de Capitales (IAMC).

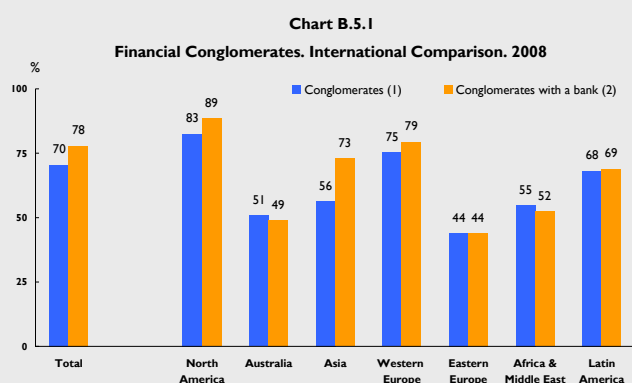
⁵⁹ With data as of March.

Box 5 / Financial Conglomerates

The financial conglomerates phenomenon is a characteristic of international financial markets that has become deeper over the last decades being present in developed and emerging economies, including Argentina. This kind of entities pose a challenge for organizations entrusted with financial regulation and supervision. They are the ultimate responsible parties to mitigate potential risks regarding financial stability and likely abuses committed against financial services consumers, they are required to design regulatory and monitoring alternatives that have a wide scope on the activities of conglomerates

In general terms, a financial conglomerate (FC) is a group of financial entities under a common scope of control and which are involved in at least two of the activities of: banks, insurance and/or investment funds⁶⁰. Several countries have their own definitions to identify the phenomenon of financial conglomerates depending on the characteristics this kind of entities have in their economies (for example, considering an economic-financial concept taking into account the relevance of the magnitude of companies in the real sector).

Some estimations suggest that financial assets in the hands of FC accounted for almost 80% of global financial assets at the start of the decade, amounting to 80% in developed economies and 77% in emerging ones⁶¹. This proportion remains high at present (see Chart B.5.1), emphasizing the existence of strong market incentives (partly associated to technological advances and financial innovations) to sustain the trend towards conglomeration.



. G-20 w/o Argentina, includes Chile and Colombia. Includes listed companies in stock exchanges

. (1) Financial groups with more than one financial activity: Ratio= (Assets of Holdings or at least 2 activities between banks, insurance and investment) / Total assets; (2) Financial groups with a bank: Ratio= (Assets in banks with at least 1 activity in insurance or investment) / Banks assets

Source: Worldscope

The organization structure of FC provides them with a set of advantages. As long as they provide a wide variety of financial services to their clients (cross-selling), there is room to take advantage of scale economies that are generated by distributing fixed costs among various lines of business. In addition, this facilitates gathering information on clients' characteristics (preferences, financial situation, etc.). On the other hand, by diversifying the offer of financial services (at a national and international level), potential losses should decrease regarding the companies that depend on a single line of business. Meanwhile, FC could give rise to benefits for financial services consumers by reducing costs related to the search of providers (investments, insurance, pensions, etc.) as well as those related to the monitoring of their assets.

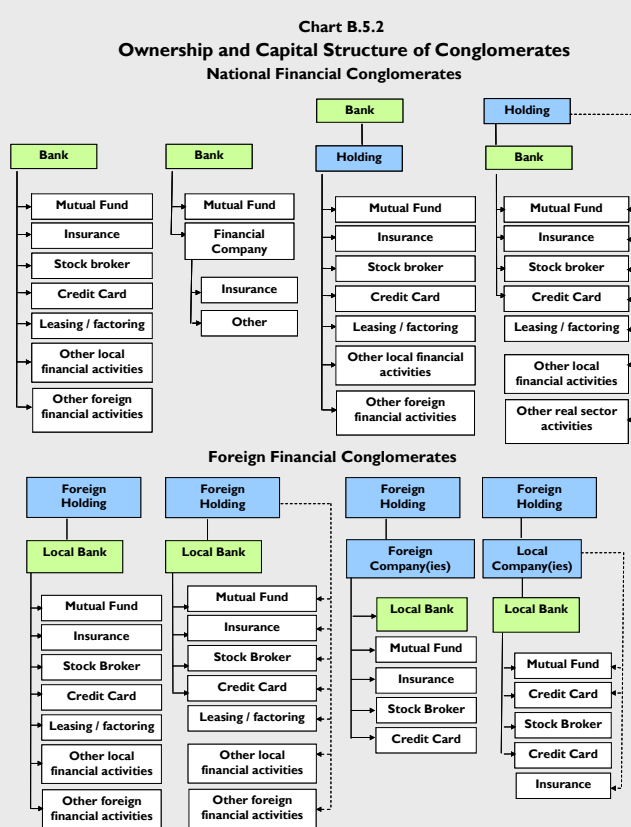
Nevertheless, this kind of entities may be a source of risks for financial services consumers and financial stability. On the one hand, there are incentives to carry out transactions benefiting the group, and coming into conflicts with clients' interests, such as the sale of products without providing objective advice to companies and/or households (for examples cases where the portfolio of third parties is invested into other units of FC or when the services of other units of the group are used without cause). The integration of activities in a FC would also generate potential situations of moral risk if consumers (wrongly) suppose that the bank security network will extend to all FC transactions, or if the managers of an entity take excessive risks anticipating that they will have governmental insurance given their systemic relevance (too-big-to-fail). On the other hand, financial difficulties of a single company may be passed on to others of the FC affecting, in an extreme case, the financial system as a whole. The concentration of financial activity in few companies maximizes non-competitive behaviors with impacts on the quantity, price or quality of services.

In this context, FC pose significant challenges for the effectiveness of the supervision and financial regulation. The complexity of their corporate structure and of the transactions conducted makes the gathering of suitable information to assess their solvency and risks taken difficult. FC also have the possibility to use certain regulatory arbitrages among financial segments channeling activities towards companies of the group where the regulatory or tax burden is less.

⁶⁰ Joint Forum within the context of the Basel Committee (BCBS).

⁶¹ De Nicoló et al (2003), IMF WP/03/158.

The conglomerates phenomenon has a significant presence in Latin America⁶², a fact that is also observed in Argentina (see Chapter IV, which contains information on the dimension). Company structures of FC at a domestic level are heterogeneous depending partly on the origin of the capital and their business strategy. Thus, FC of national capitals (private and public) tend to focus on a bank that acts as center on which other companies depend or through a holding standing above the bank and other entities. Foreign capital FC which tend to be focused on a bank established locally (corporation or branch) on which other companies depend or through a foreign holding on which companies with domestic financial activity depend (see Chart B.5.2).



Source: BCRA

The Argentine regulatory framework includes certain criteria regarding the creation of FC. The Law on Financial Entities prevents banks from exploiting on their own⁶³ commercial, industrial, agricultural or other kind of companies unless they have the express authorization of the BCRA. This Institution allows holding greater stock percentages in supplementary financial services companies (stock exchange, automatic

teller machines, mutual funds, etc.) whose activities could be performed by the entity though it would be more convenient for the entity to establish a separate corporation from the commercial standpoint. The BCRA regulates and monitors banks through the SEFyC (Superintendencia de Entidades Financieras y Cambiarias - Superintendence of Financial and Exchange Institutions) in an individual and consolidated manner. Apart from complying with the regulations for transactions conducted individually, the financial entity must consolidate the transactions of its subsidiaries⁶⁴, which means adding to its balance sheet their assets and liabilities and consider them in the technical relations to analyze risks. In practice, the supervision also analyses, to some extent, in a qualitative fashion holding-related risks.

Accompanying the changes of the global financial industry, some countries have shifted to more integrated regulatory schemes to mitigate risks generated by FC. On the other hand, different institutions and international work groups have established principles to achieve better regulation and supervision of FC. In order to create a scheme that comprises in an integral manner all activities and risks of FC, the Joint Forum has recommended: *i.* adjusting capital in a consolidated fashion identifying potential situations of multiple counting; *ii.* tending to make supervisors appointed to an entity belonging to a FC assess if it is being managed in a fit and proper fashion; *iii.* tending to information exchange between supervisors and different segments of the FC; and *iv.* identifying a coordinator among supervisors indicating responsibilities in emergency situations. Recommendations of Basel II include applying a framework of capital in a consolidated basis for groups (including activities that are regulated or not) among other aspects. The G-20 group issued recommendations on the regulation of institutions with systemic relevance, defined depending on its complexity and interconnections. Such recommendations include establishing a regulatory context similar to that of similar activities, regardless of their legal status.

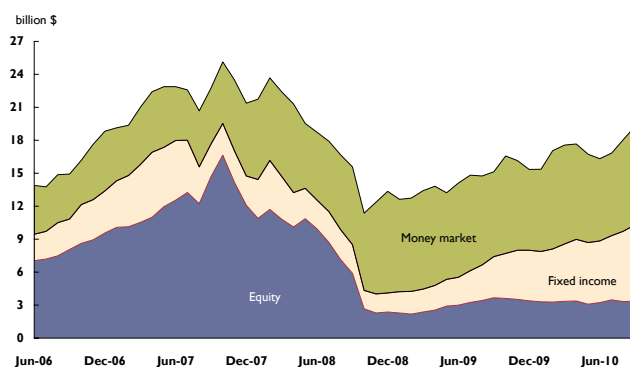
The phenomenon of conglomerates is a challenge in financial markets and reaches financial service consumers and regulating parties. International recommendations on the topic have progressed towards more specific monitoring of their performance boosting consecutive regulatory answers in developed and emerging economies.

⁶² Assets of the 10 first banks creating conglomerates account for almost 77% of the total of banking assets in Brazil, 93% in Colombia and 98% in Mexico.

⁶³ Direct or indirect interest exceeding 12.5% in this kind of company means use by their own.

⁶⁴ Deemed as those financial entities or companies where it has or controls, directly or indirectly, more than 50% of total of votes or has majority of management bodies

Chart IV.25
Mutual Funds Net Worth Evolution



Note: mixed funds are included in equity funds, time deposits are included in money market funds
Source: BCRA from Cámara Argentina de FCI data.

On the other hand, the entire net worth of mutual funds (FCI) reached \$19.3 billion (according to the latest information available as of September 2010). Thus, the growing trend observed during the first quarter of the year persists with a rise amounting to 10% against March and to 26% to date (see Chart IV.25). Even though funds addressed to money markets remain being the main component of the portfolio, their weighting has fallen considerably and they currently account of almost 46% of net worth when they had reached almost 70% of share during the financial crisis, by late 2008. The growth close to 78% in net worth of funds aimed at the mixed income segment since late March 2010 is to be highlighted while those in the fixed-income segment grew 33%.

IV.3 Financial conglomerates

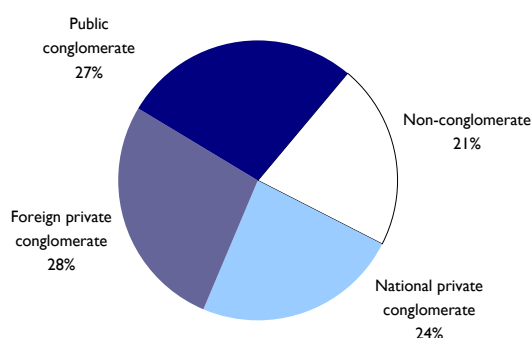
The phenomenon of financial conglomerates is relevant in the Argentine financial sector, reaching banks, the insurance market and mutual funds

In order to have a diagnosis of the domestic financial intermediation process, sections IV.1 and IV.2 contain an analysis on the evolution of the main financial companies per business segments: banks, insurance companies, and mutual funds. This kind of analysis may be deepened if the relations of ownership and common control existing among companies, both inside every segment of financial services and among them are considered. Thus, a phenomenon regularly known as financial conglomeration may be identified (see Box 5 for a concept analysis), which is present in developed and emerging economies including Argentina.

Therefore, considering the banking sector as an axis, those capital links to insurance companies, mutual funds, and stock brokers may be sought and in case of identifying a financial conglomerate or group, managed assets⁶⁵ are added. This analysis is carried out with the balance sheets corresponding to the end of 2009 of all financial entities⁶⁶, and their updates have been estimated to be systematized in the coming editions of the Financial Stability Report.

Out of the 83 financial entities present on the local market by late 2009 under the scope of supervision of the SEFyC, 27 have interest in one or more segments of

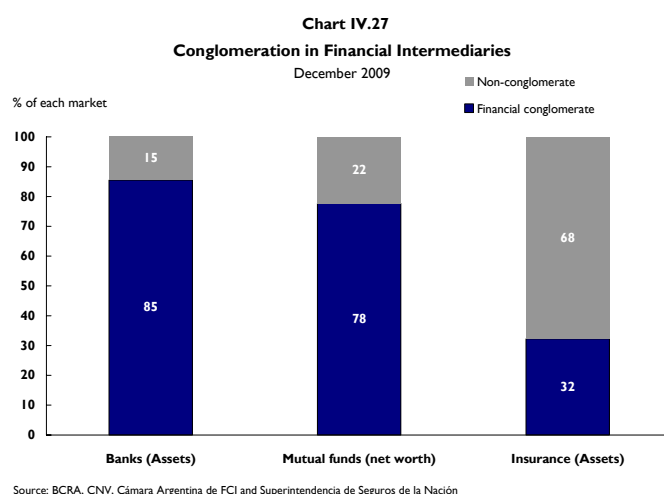
Chart IV.26
Assets. Banks, Insurance Companies and Mutual Funds
December 2009



Source: BCRA, CNV, Cámara Argentina de FCI and Superintendencia de Seguros de la Nación

⁶⁵ If a conglomerate is identified according to the parameters mentioned, bank and insurance assets and of mutual funds are added. No interest among sectors is consolidated.

⁶⁶ It should be noted that for qualitative purposes, groups of financial entities that, without having a bank component, include brokerage house, mutual fund managers, insurances and/or bureau de change are not included. Information on the activity of management of trusts is not included either.



the remaining financial services mentioned⁶⁷. From this group of entities, 12 participate in only one financial segment, 8 in two of them, 1 in three, and 6 in all the businesses mentioned.

The volume of assets of the financial sector as of December 2009 (almost \$459 billion) was mainly made up of banks (84%), followed by insurance companies (12%) and by mutual funds (4%). Out of this total of assets, about 79% was made up of financial entities that were financial conglomerates of public origin (27% of total assets), national private origin (24% of total assets) and foreign origin (28% of total assets) (see Chart IV.26). Conglomerates have reached almost 85% of assets of the banking segment evidencing also a significant level in the mutual funds sector (78%) and, to a lesser extent, the insurance market (32%) (see Chart IV.27)

⁶⁷ Shares in other financial entities are also presented.

V. Financial System Risks

Summary

With the faster growth in lending to companies and households seen in recent months, the financial system has recorded some improvement in relation to the intrinsic risks assumed.

Financial entities have maintained their sound position in the face of liquidity risk. Liquid assets remained at a high level during a period in which private sector deposits consolidated their growth. This performance provided an appropriate starting-point for the renewed dynamism seen recently in lending to companies and households, and has established considerable potential for coming periods. Leading interest rates declined gradually in the first part of 2010, with a reduction in volatility at the same time as interbank liquidity markets gained in importance.

In recent months there have been positive signs related to private sector credit risk faced by the financial system. Corporate and household non-performance indicators continued to fall in the first part of 2010, mainly from the performance by household consumer credit granted by private banks and non-bank financial entities. Corporate loan quality also posted improvement. Coverage of non-performing loans by means of provisions has continued to rise.

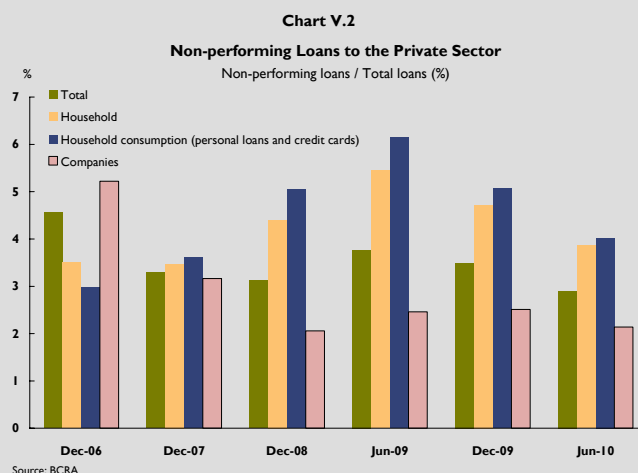
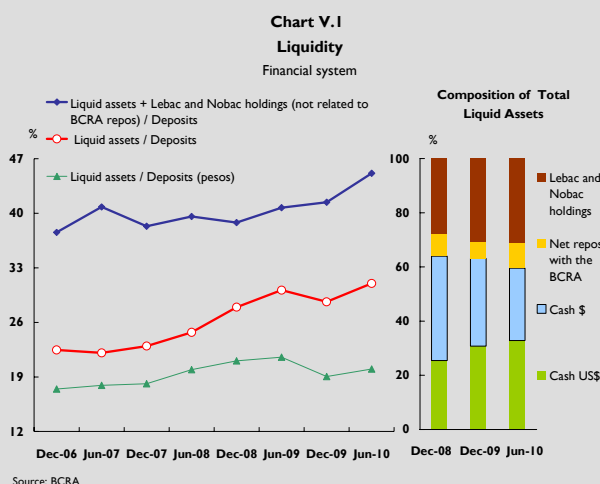
At the beginning of the year there was a slight increase in the exposure of the financial system to currency risk, which rose from the relatively low level it had been recording. System foreign currency mismatching increased mainly because of greater net undelivered

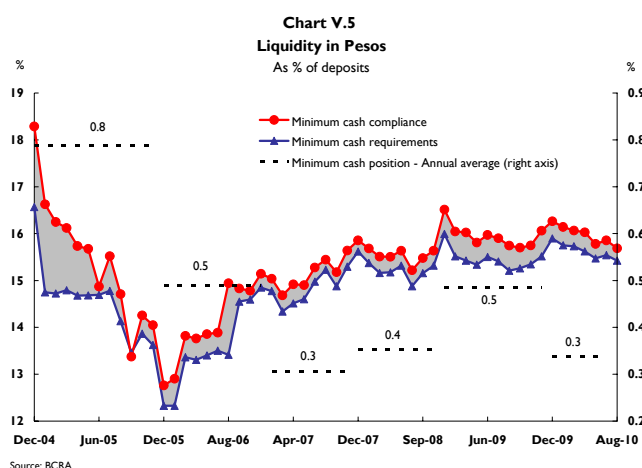
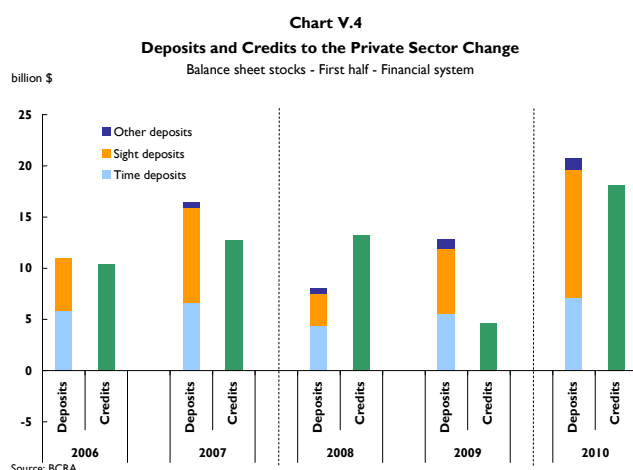
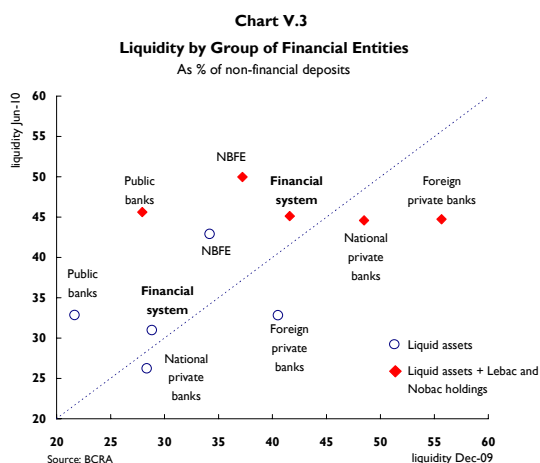
forward purchases of foreign currency, mainly reflecting the behavior of private banks. The impact of the increased foreign currency mismatching was partly offset by the lower exchange rate volatility compared with the peaks in the previous year.

Financial system exposure to interest rate risk was kept well within bounds. In the first part of the year there was a modest reduction in the residual term of bank assets and liabilities, with no significant change in the mismatching of maturities faced by banks. Leading interest rates continued to fall gradually, with a reduction in volatility that has reduced the probability of any materialization of this type of risk.

Market risk has remained stable in the first part of the year. The increased bank participation of Lebac and Nobac holdings with market quotation in their asset portfolios, added to higher prices for the main government securities during the first part of the year, have generated a gradual increase in the exposure of the financial system to market risk that was compensated for by the declining volatility of securities.

Considering the overall balance of exposures and volatilities, the financial system has shown improvements in terms of the risk map. This performance is expected to gain strength based on the positive domestic macroeconomic performance anticipated for coming periods within the framework of the implementation of public policies aimed at sustainable development.





V.1 Liquidity risk

Financial entities maintain their favorable position in the face of liquidity risk

In the first half of 2010 the financial system slightly increased its liquidity indicators, although this trend gradually began to reverse following the acceleration of growth in lending to the private sector seen in recent months. Private sector deposits continue to provide the main source of bank funding, having increased significantly in the year to date. Financial entities continue to count on tools to enable them to manage the liquidity risk faced, and the Central Bank maintains its role as the lender of last resort.

Liquid assets⁶⁸ in domestic and foreign currency held by financial entities rose by over 2 p.p. of total deposits in the first half of the year to a level of 31%⁶⁹ (see Chart V.1), those denominated in foreign currency increasing their share. Official banks and non-bank financial entities increased their liquidity indicators, while private banks saw a slight drop (see Chart V.3). Taking into account holdings of Lebac and Nobac not linked to repo transactions, total bank liquidity amounted to slightly over 45% of deposits.

Although in mid-year financial system liquidity levels were higher than they were at the end of 2009, a gradual reduction had begun to take place as from April. This trend was recorded at a time when financial intermediation returned to a growth pattern similar to that seen prior to the international crisis (see Chart V.4), driven mainly by private banks (see page 38).

Financial entities' liquidity continued to exceed regulatory requirements. Banks have therefore met the minimum cash requirement, with an excess compliance of 0.3% of peso deposits in 2010 to date, slightly less than at the end of 2009 (see Chart V.5). The requirement has declined gradually compared with the end of 2009, as there was an increase in the participation of time deposits⁷⁰ in the peso deposit total stock. In the case of foreign currency deposits, excess compliance has amounted to 54% of total deposits in dollars.

⁶⁸ These include cash, current accounts at the Central Bank, and net repos with the Central Bank using Lebac and Nobac.

⁶⁹ Financial system liquidity in local currency stood at 20% of deposits in mid-2010, having risen slightly in the year to date.

⁷⁰ These have a lower reserve requirement than sight deposits.

Box 6 / International Consensus on Financial Regulation Proposals

In response to the mandate from the G-20, the Basel Committee on Banking Supervision (BCBS) has issued a series of proposals for reforms designed to strengthen the international financial system. Consensus has progressed towards the search for improved quality for regulatory capital, mitigation of the pro-cyclical nature of the financial system, promotion of more prudent behavior by systemically-significant entities, and the incorporation of liquidity standards, among other recommendations that are expected to contribute to reducing the probability of the development of financial crises

In July 2009 the BCBS introduced various reforms to the minimum capital framework then existing, known as Basel II. In the case of Pillar I on minimum capital requirements, the treatment of off-balance-sheet (OBS) activities linked to securitization was reinforced, and the capital requirement for market risk was increased for approaches based on internal models. In the case of Pillar II on supervision, new standards were included for liquidity risk management, stress tests, valuation and OBS activities, and the Financial Stability Board Principles for Sound Compensation Practice were adopted. For Pillar III on market discipline, greater disclosure has been required on liquidity risk exposure, securitization, and OBS activity.

The BCBS is also working on a broader and deeper reformulation of the regulatory framework that will contribute to the stability of the financial system, helping to avoid the occurrence of crises such as the one that broke out in 2008. This work is being carried out in conjunction with other tasks being led by the International Organization of Securities Commissions (IOSCO) and the International Accounting Standards Board (IASB), coordinated by the FSB. In December 2009 the BCBS published the first consultative draft of this program of reforms. This document on Strengthening the Resilience of the Banking Sector proposed a review of the capital framework, while the International Framework for Liquidity Risk Measurement, Standards and Monitoring introduces quantitative standards for the regulation of liquidity (see Box 5, FSR I-10).

On the basis of the comments received and the progress made by the working groups, the BCBS is obtaining a consensus for the proposals it will submit to the approval of the G-20 leaders next November. At its July

and September meetings the governing body of the BCBS (the Group of Governors and Heads of Supervision -GHOS-) reviewed the progress on the reform package for the capital and liquidity framework. At those times agreement was reached on the structure and scope of the proposals, their calibration and implementation schedule (see Table B.6.1). Decisions by the GHOS were mainly based on the results of the last quantitative impact study and the estimated short and long term effects.

One of the aims of the BCBS with these developments has been to raise the **quality, consistency and transparency** of regulatory capital to absorb losses when risks materialize, harmonize their calculation internationally, and facilitate understanding of their composition. The BCBS proposal consists of: *i.* Requiring financial entities to publish the components of their capital, relating them to their financial statements; *ii.* Disallowing Tier 3 capital⁷¹; *iii.* Disallowing certain hybrid instruments included in Tier 1 capital⁷²; *iv.* Requiring banks to apply deductions and other regulatory adjustments to common equity - ordinary shares and retained earnings - rather than on overall capital; and *v.* Ensuring that Tier 1 capital consists mainly of common equity. The new system also contemplates an increase in capitalization levels. It is currently recommended that banks should keep a minimum coverage with total capital for 8% of risk-weighted assets (RWA), which may consist of up to 50% of Tier 2 capital, implicitly defining a minimum for Tier 1 capital of 4% of RWA. The proposal that will take effect as from 2013 is based on a series of minimum ratios established in terms of common equity (net of deductions), Tier 1 capital, and total capital: 4.5%, 6% and 8% of RWA.

The GHOS also approved changes to Basel II to **increase counterpart risk coverage** that complement those added to Pillar I in July 2009. It was resolved to introduce an explicit capital charge in Pillar 1 linked to

⁷¹ Core bank capital, basically made up of stock and reserves, is known as Tier 1. The second level of capital, made up of subordinated debt among other items, is Tier 2. Tier 3 is formed by other instruments (debt instruments, for example) that can be used as bank capital, with a lower capacity to confront losses than the previous two Tiers.

⁷² "Perpetual" financial instruments may form part of Tier 1 capital in addition to common equity as long as they guarantee their ability to absorb losses "on a going concern" and do not possess incentives for early redemption.

the risk that arises when the probability of default of counterparties is positively correlated with general market risk factors (general wrong way risk⁷³), increase the correlation ratio for interbank lending and increase incentives to use central counterparts for OTC⁷⁴ derivatives, among others.

Another element of the new system is the **leverage ratio**. This is a simple non-risk-based measure that seeks to complement minimum regulatory capital in constraining the build-up of bank leverage. It is defined as the ratio between Tier 1 capital and assets (as per the balance sheet) plus derivatives and OBS exposure. The latter will be included using a 100% credit conversion factor, unless they are lines that can be freely cancelled by the bank (10% factor). The GHOS agreed an initial calibration of 3% that will be used during the transition until their definitive incorporation to Pillar 1 in 2018.

Most of the proposed changes are in response to the request by the G-20 to constrain the pro-cyclical nature of financial systems, discouraging the excessive growth of credit in the expansive stage of the cycle that then become translated into episodes of sharp decline in moments of crisis. At the BCBS **mechanisms have been analyzed to make minimum regulatory capital less cyclical**. Some progress has been made –still not approved by the GHOS– on mitigating the impact of changes in ratings of risk of credit rating agencies on the requirement for securitization credit risk. Other areas in which the regulatory minimum is also cyclical –the internal ratings-based approach for changes in default probabilities, or the standardized approach in the event of changes in credit ratings– have recorded less progress. Credit risk provisions have also had a cyclical behavior, particularly those based on the loss incurred accounting concept. The BCBS has developed a proposal for a new approach based on expected loss in line with the IASB initiative, with the aim of making **provisions more stable over the economic cycle**.

The GHOS also agreed on the introduction of two anti-cyclical credit buffers. First a **buffer** that will force banks to hold capital above the regulatory minimum by means of restrictions on dividend distributions, stock repurchases and bonus payments. The purpose is to ensure banks hold a level of additional capital that can be used to absorb losses during stress periods. This buffer is to consist of common shares and retained earnings (common equity, net of deductions) in an

amount equivalent to 2.5% of RWA, and will be introduced gradually as from 2016 and fully in 2019. In addition, an **anti-cyclical capital buffer** will be required, that will only be used in excess credit growth situations that might generate vulnerabilities. This buffer extends the conservation buffer –by between 0% and 2.5% of RWA–.

These efforts to constrain the pro-cyclical nature of the financial system are part of the macro-prudential approach to regulation and supervision. One important aspect of this approach is the containment of contagion and domino effects that occur during crises, which among other things are associated with the existence of systemically important financial institutions (SIFIs). These banks are noted for being large and/or being very interconnected, and/or providing services that are hard to replace. The purpose is to reduce the probability of an adverse event, reduce the impact of the failure of a SIFI, lower the cost to the public sector of any rescue, and remove the competitive advantages of SIFIs derived from their awareness that they are too big to fail. In addition, work is being carried out on further tools to align incentives and promote more prudent behavior, such as additional capital and liquidity burdens, special supervision, and the introduction of restrictions on their operations.

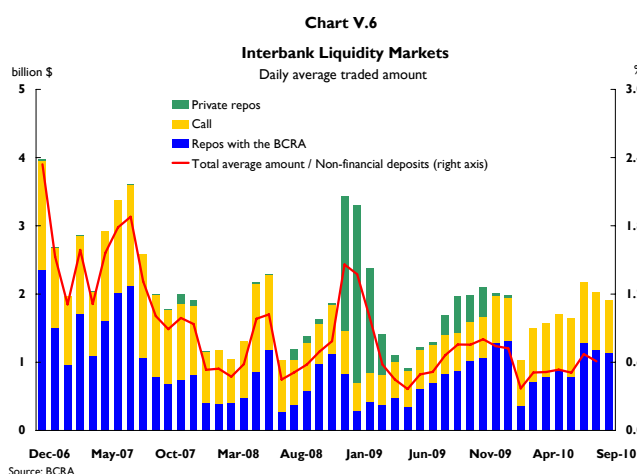
Lastly, a **global minimum liquidity standard** will be introduced, consisting of two elements: a **Liquidity Coverage Ratio** intended to ensure that banks have sufficient high-quality liquid assets to withstand a stressed funding scenario, and a **Net Stable Funding Ratio** focusing on structural and long-term mismatching in the composition of funding. Work is still being performed on the design and calibration of these ratios.

Table B.6.1
Phase-in arrangements (shading indicates transition periods)
(all dates are as of 1 January)

	2011	2012	2013	2014	2015	2016	2017	2018	As of 2019
Leverage ratio	Supervisory monitoring		Parallel run Disclosure starts as from 2015					Tier 1	
Minimum Common Equity Capital Ratio (CET1)			3.5%	4.0%	4.5%	4.5%	4.5%	4.5%	4.5%
Phase-in of deduction from CET1				20%	40%	60%	80%	100%	100%
Minimum Tier 1 Capital			4.5%	5.5%	6.0%	6.0%	6.0%	6.0%	6.0%
Minimum Total Capital			8.0%	8.0%	8.0%	8.0%	8.0%	8.0%	8.0%
Capital conservation buffer						0.625%	1.250%	1.875%	2.500%
Liquidity coverage ratio	Observation period				Minimum standard				
Net stable funding ratio			Observation period						Minimum standard

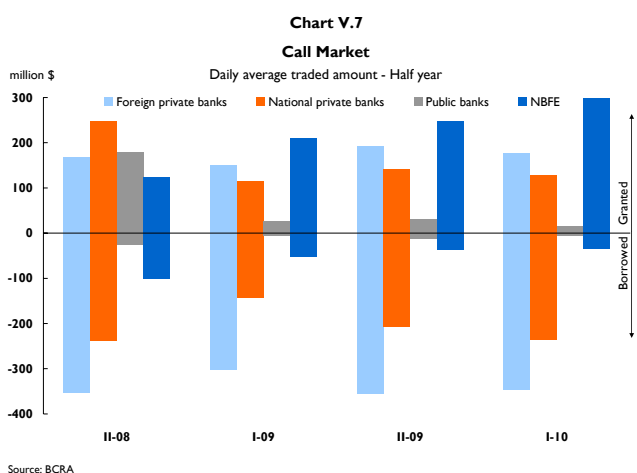
⁷³ It also includes the risk that arises when an increases in the counterparty credit risk is positively correlated with the exposure level - typically in the trading book (specific wrong-way risk)-.

⁷⁴ Over the counter



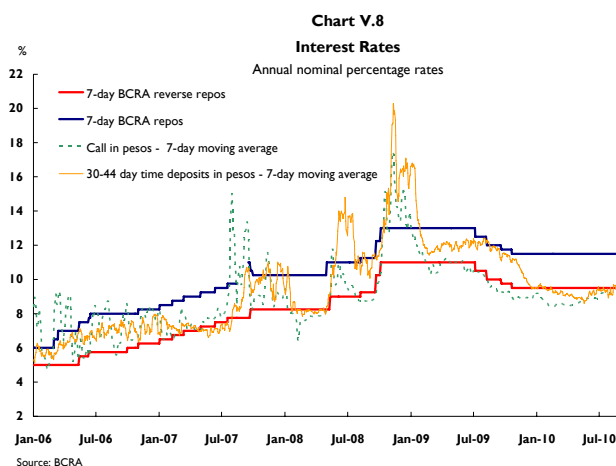
Volumes traded on interbank liquidity markets have continued to rise

In the first part of 2010 volume traded on the call market and interbank repo transactions continued to rise (see Chart V.6). Non-bank financial entities continued to increase their share as supplier on the call money market, while foreign private and national private banks were once again net takers of funds (see Chart V.7). Leading interest rates remained at levels similar to those of the end of 2009, displaying lower volatility (see Chart V.8). In the first half of 2010 interest rates for repo and reverse repos traded by the Central Bank remained at the same level as those recorded at the end of last year. In this framework, the Central Bank continued to encourage the growth of the interest rate futures market by means of its participation through the “función giro” mechanism.



It is expected that there will be a gradual reduction in liquid assets within the context of improved credit performance, a situation that will not modify liquidity risk coverage by the financial system

It is expected that for the rest of the year banking resources will continue to be channeled to companies and households, generating an adjustment in bank liquid asset levels. Precautionary liquidity built up during the height of the international crisis, added to the operation of interbank markets and the performance by private sector deposits will continue to consolidate the strength of the financial system in the face of liquidity risk. The full effectiveness of the Central Bank’s role as a lender of last resort in specific instances provides additional insurance.

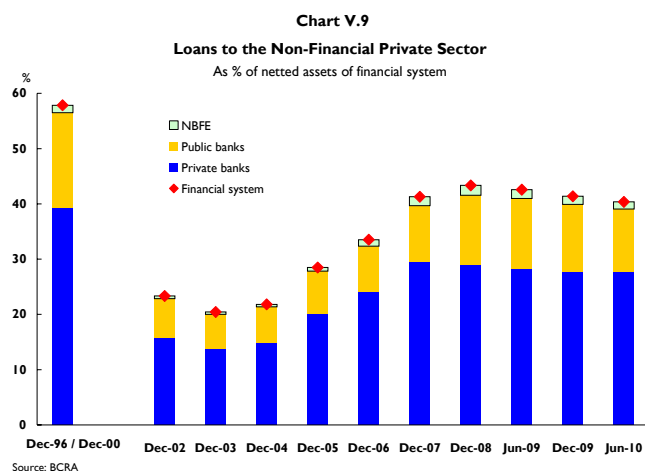


V.2 Credit risk

V.2.1 Private sector

At the beginning of 2010 financial system exposure to the private sector fell slightly, and credit risk was maintained at a moderate level

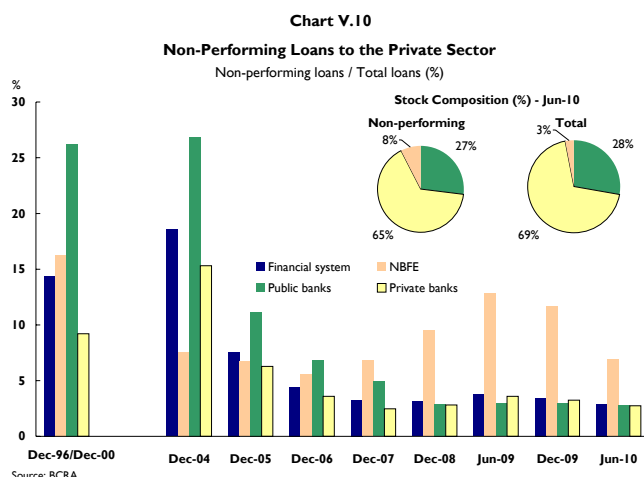
In the first part of 2010 financial system exposure to the private sector fell moderately (see Chart V.9), during a period in which although the growth rate for lending to companies and households began to recover after the effects of the international financial crisis, the increase was lower than that of total assets. Following the improvement in macroeconomic conditions, progress was made in the payment capacity of the corporate sector and households, contributing to reduce credit risk



faced by banks. As a result, the growing dynamism of lending to the private sector was accompanied by a reduction in non-performing loans.

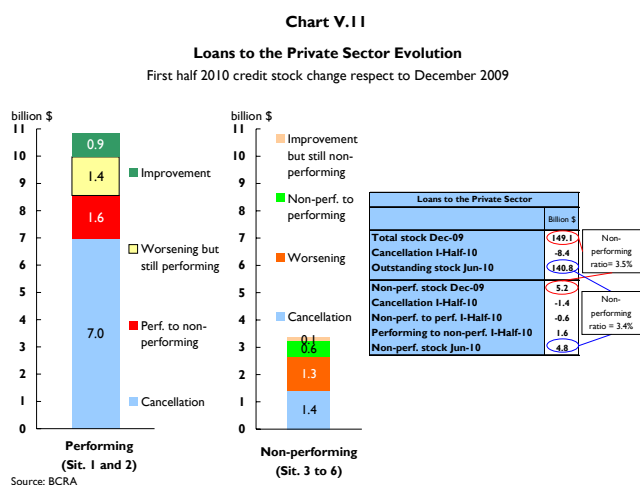
Private sector loan non-performance continued to decline, mainly in consumer loans

Private sector lending non-performance dropped 0.6 p.p. in the first half of 2010 to a level of 2.9%. The improvement in portfolio quality was mainly explained by the performance of household consumption loans⁷⁵ (see Chart V.2), and to a lesser extent, by lending to companies. Household lending delinquency reached 3.9%, falling for the second six-month period in succession, mainly in consumer loan lines. Corporate lending non-performance fell slightly to 2.1%. The drop in private sector portfolio delinquency was recorded by all groups of financial entities (see Chart V.10).



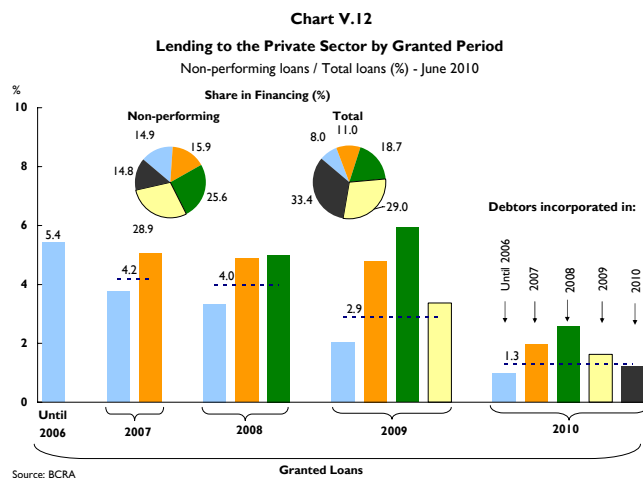
Outstanding loans at the end of 2009 recorded a slight improvement in their situation in the first part of 2010. The non-performance ratio for these loans stood at 3.4% by the middle of the year, slightly below the level recorded in December 2009 (see Chart V.11). It is estimated that loans to the private sector granted until 2008 (38% of the total balance at mid-2010) recorded a greater non-performance rate than that of loans granted in 2009 and 2010. Debtors entering the financial system in 2007 and 2008 have tended to record a slightly higher delinquency rate than the rest (see Chart V.12).

In the first half of 2010 there continued to be an improvement in provision coverage for non-performing loans. Despite the reduction in total non-performing loans for the period, the financial system has increased its provisioning level. The increase in the coverage indicator took place among both private and public banks (see Chart V.13).



The counterpart risk faced by the financial system derived from possible fluctuations in the peso-dollar exchange rate has remained low. Foreign currency lending to the private sector continued at a low level (just 15% of the total), compared with the levels recorded prior to the crisis in 2001-2002, and has mainly been directed at tradable goods sectors of the economy (see Chart V.14). In addition, there are several prudential regulations that establish that deposits in foreign currency can only be used to finance sectors that regularly record income derived directly or indirectly from foreign trade transactions and related activities.

⁷⁵ Loans granted to individuals are considered to be loans to households, except when commercial loans are granted to individuals. These latter loans, together with loans to legal persons, are considered within loans to companies.



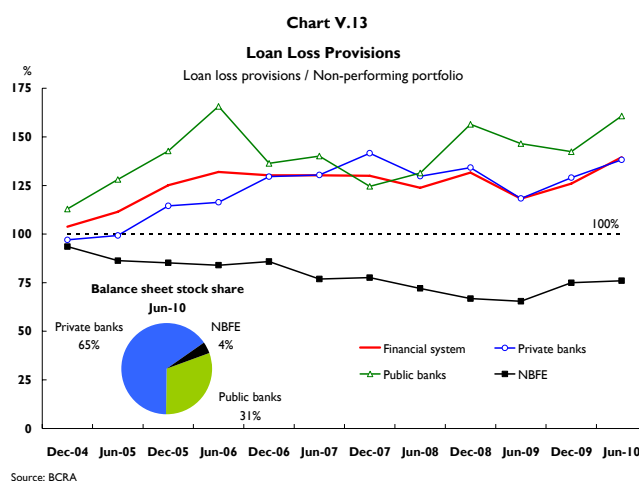
Lending to the private sector is expected to increase its share of financial system assets over the rest of the year, with banks maintaining a sound position in the face of counterpart risk

It is expected that companies and families will continue to accelerate their pace of bank borrowing, during a period when it is anticipated that private sector payment capacity will continue to improve on the basis of the sound macroeconomic performance (see Page 30). Financial entities' liquidity levels constitute a resource cushion that will enable banks to adequately meet the expected increase in the demand for credit. The financial system will continue to maintain a limited exposure to credit risk during the rest of the year.

Companies

The financial system's exposure to the corporate sector fell slightly in the first part of 2010, with a moderate improvement in portfolio quality

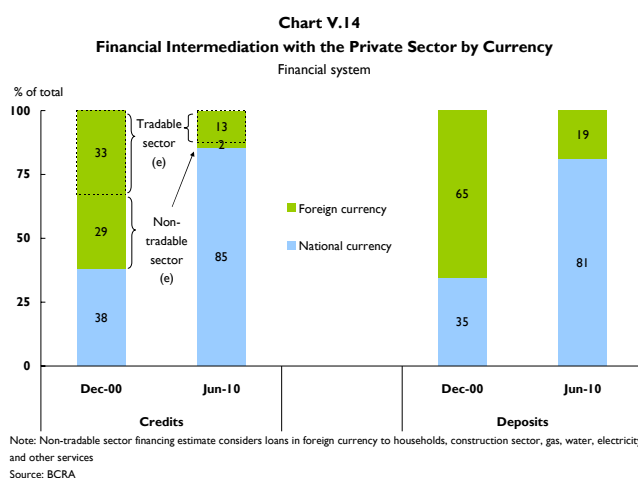
Despite the recent acceleration in the growth rate for lending to companies, the financial system recorded a mild reduction in its exposure to the corporate sector in the first part of the year (see Chart V.15). Corporate payment capacity improved in 2010 in line with the positive performance of the local economy (see Page 31), while the sector has continued to record moderate levels of indebtedness. This situation has contributed to a moderate drop in loan delinquency in the first part of 2010, to a level of 2.1%. The progress recorded in portfolio quality in recent months has been widespread across the various corporate loan lines.

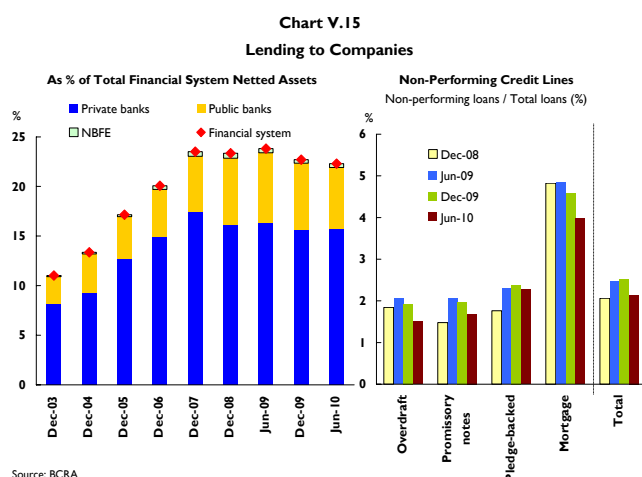


With the exception of certain primary activity sectors, loans to all productive sectors recorded declines in their non-performance (see Chart V.16). Construction loans posted the greatest improvement to their credit performance, mainly as a result of the transfer of certain loans to off-balance sheet accounts as unrecoverable. It is estimated that the newer the loans in force in mid-year, the lower their delinquency ratio (see Chart V.17).

The improvement in corporate loan portfolio quality as well as the declining trend in the value and number of bounced checks by nonsufficient funds (see Page 74), have represented indications of the gains in corporate sector payment capacity.

Financial system exposure to companies is expected to increase gradually over the rest of 2010, in a low credit risk context

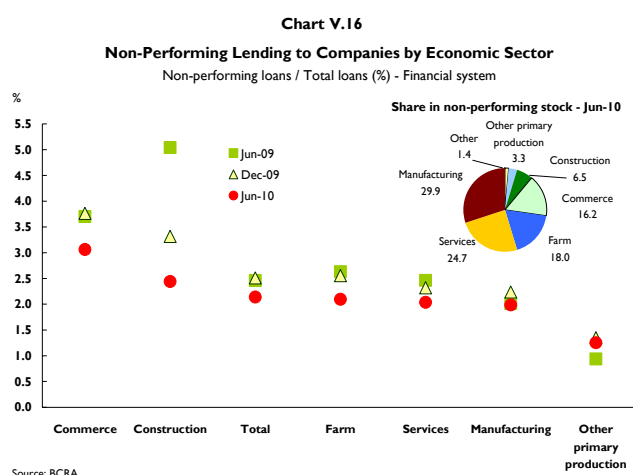




In view of the greater economic dynamism seen recently and expected in coming months, lending to the corporate sector will likely gradually increase its share of total financial system assets. Manufacturing industry, which takes up approximately one third of bank credit to the corporate sector, is showing signs of increasing its need for loans in coming months (see Chart V.18). This pattern is similar to that expected for the remaining economic sectors, and the financial system is adequately equipped to meet such demand. Note should be taken of the measure adopted by the Central Bank to lengthen the terms of financial system transactions, with the encouragement of lending to the productive sector through the use of assistances granted by this Institution (see Page 40).

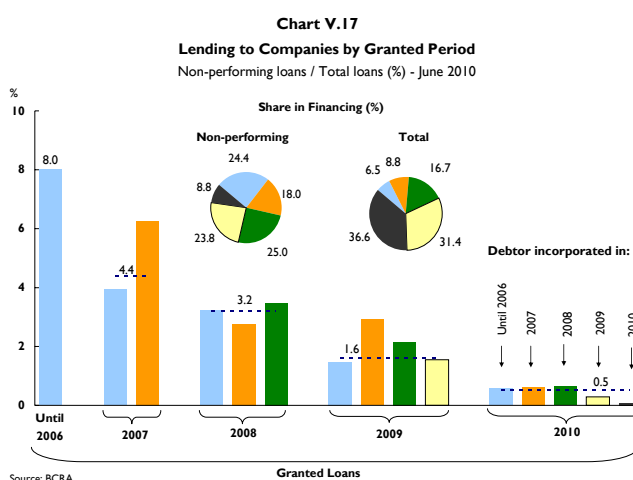
Households

Financial system exposure to households showed a moderate decline, while the improvement in sector credit quality was maintained



The financial system slightly lowered its exposure to households in the first half of the year, although this movement began to be reversed in recent months following the greater dynamism of credit. In the period there was an improvement in the quality of the sector portfolio, mainly explained by the performance of consumer lines (see Chart V.19).

In recent months household payment capacity has been strengthened based on the strong dynamism of the economy that was reflected in a positive performance by the labor market (see Page 34). In addition, consumer confidence has continued to recover, driven by positive expectations regarding coming periods, limiting the probability of any credit risk taken on by banks materializing in the short term.

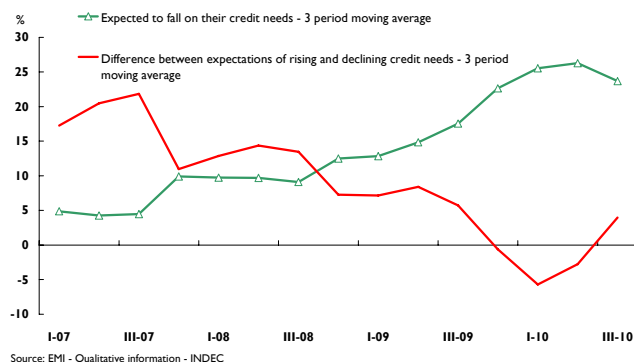


The household non-performance loan ratio declined 0.8 p.p. in early 2010 to 3.9%. This reduction was led by consumer credit lines, in the context of a drop in non-performing loan stocks and greater growth in total loans (see Chart V.20). It is estimated that loans to households granted in recent years to borrowers who took out loans during the height of the international crisis have recorded the highest delinquency rate (see Chart V.21).

It is expected that household payment capacity will continue to show some signs of improvement

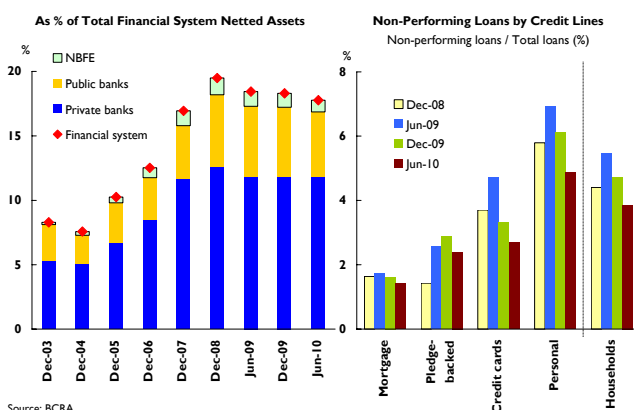
Household income is likely to maintain the improvement seen in recent periods as a result of the improved situation in the labor market and the increase

Chart V.18
Financing Needs Expected for Manufacturing Sector
Variation compared to same quarter last year



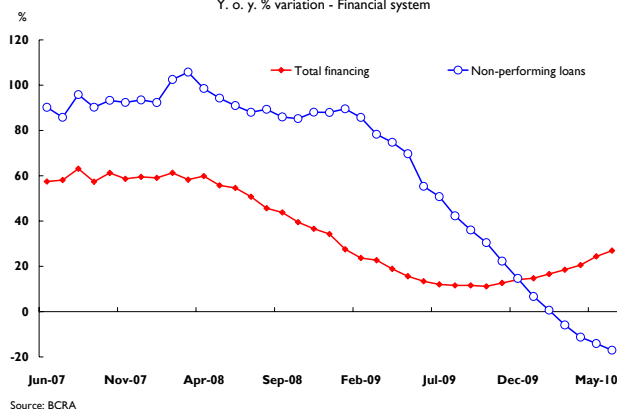
Source: EMI - Qualitative information - INDEC

Chart V.19
Households Financing



Source: BCRA

Chart V.20
Total and Non-Performing Loans - Consumer Loans
Y. o. y. % variation - Financial system



Source: BCRA

in transfers from the government, in line with the sustained economic expansion. Households are likely to maintain their rising consumption levels, with an impact on the performance of bank lending, at the same time as payment capacity will continue to improve.

V.2.2 Public sector

Financial system exposure to the public sector fell, within a framework of positive expectations for the sector following the public debt swap and the continued recording of fiscal account surpluses

Financial system exposure to the public sector fell slightly at the start of 2010 (see Chart V.22), mainly from public banks performance, in the context of a greater relative increase in total assets. As a result, towards the middle of 2010 exposure of financial system to this sector was almost one third of that corresponding to companies and households. Taking into account public sector deposit stocks, the Government continues to be a net creditor of the banking system (10% of total assets).

The National Public Sector has continued to record a primary surplus in its fiscal accounts, and the outlook is positive following the public debt swap and the improved economic indicators (see Page 35). It is expected that the public sector will preserve its payment capacity, and that the financial system exposure to this sector will remain at the current low level.

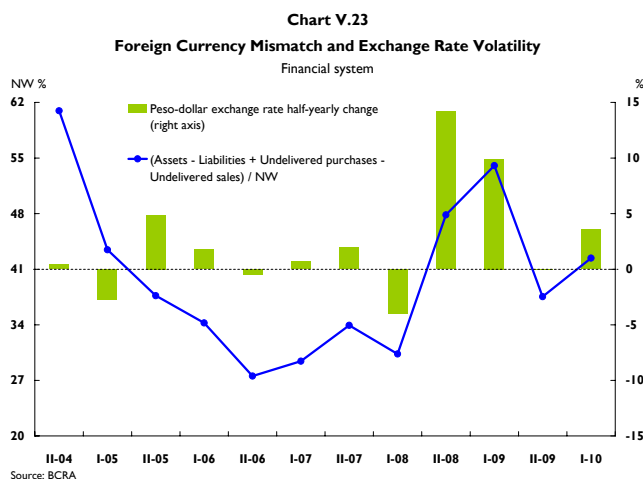
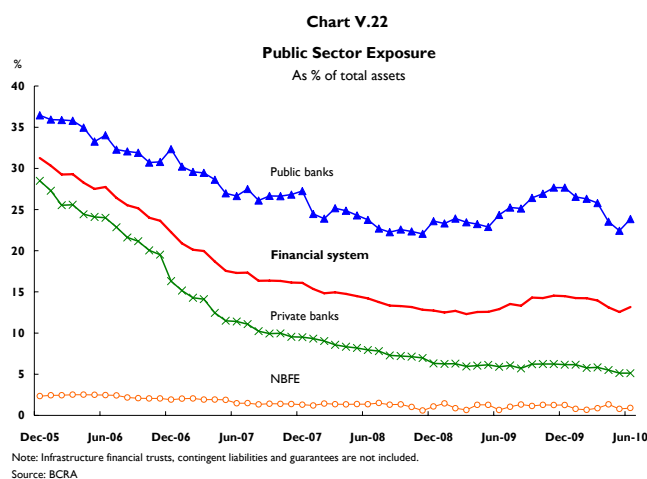
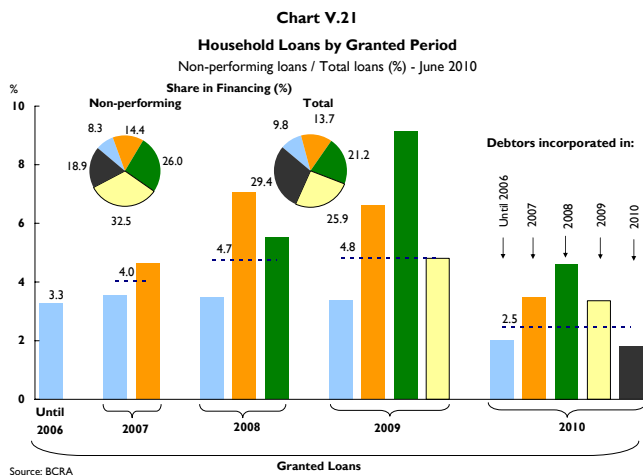
V.3 Currency risk

There has been a slight increase from its very low levels in financial system exposure to currency risk

Within the context of limited exchange rate volatility, the increase recorded in financial system foreign currency mismatching led to a modest increase in balance sheet exposure to currency risk. In the first half of 2010 bank foreign currency mismatching, taking into asset and liability items as well as net undelivered forward purchases of foreign currency⁷⁶, rose by almost 5 p.p. of net worth to slightly over 42% (see Chart V.23).

The increase of financial system foreign currency liabilities (a change mainly associated with public sector deposits) exceeded the rise in foreign currency assets (mainly liquidity). This movement was more than offset by the increase in net undelivered forward purchases of foreign currency by banks during the period. Private

⁷⁶ In memorandum accounts.



financial entities led the way with this increase in foreign currency mismatching recorded in 2010 (see Chart V.24).

Approximately three-quarters of the foreign currency mismatching recorded in June 2010 arose from the difference between assets and liabilities in foreign currency, while the rest was caused by net undelivered forward purchases of foreign currency. Public banks accounted for the largest portion of the aggregate difference between assets and liabilities, while private sector financial entities recorded most of the net undelivered forward purchases of foreign currency (see Chart V.25).

In the first half of the year there was a moderate increase in the nominal peso-dollar exchange rate, with very limited volatility. This rise in the exchange rate on the spot market generated book profits for the financial system from the restatement of the positive difference between foreign currency assets and liabilities (see Page 49). In addition, given the long position of banks on foreign currency futures term market, further small book profits were recorded in the first half of the year. These profits were lower than those accrued during the same period of 2009, in part due to the fact that contracts for recent periods incorporated an exchange rate higher, on average, than that actually recorded when the positions were closed, in a framework in which the net supply of foreign currency tended to exceed market expectations.

Net global foreign currency position (PGNME) for the system stood at approximately 41% of adjusted stockholders' equity (RPC) in mid 2010, having risen slightly over the course of the year.

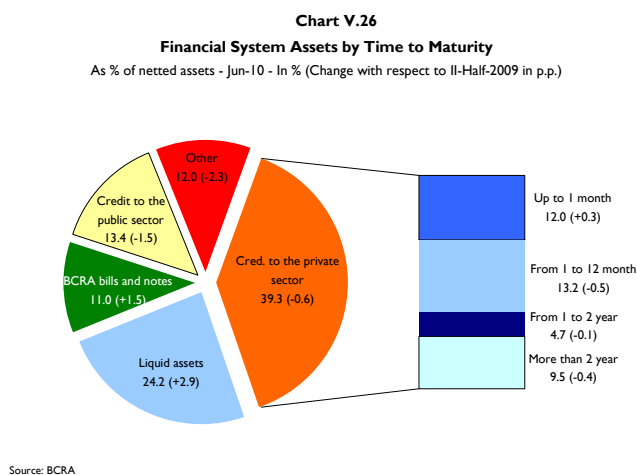
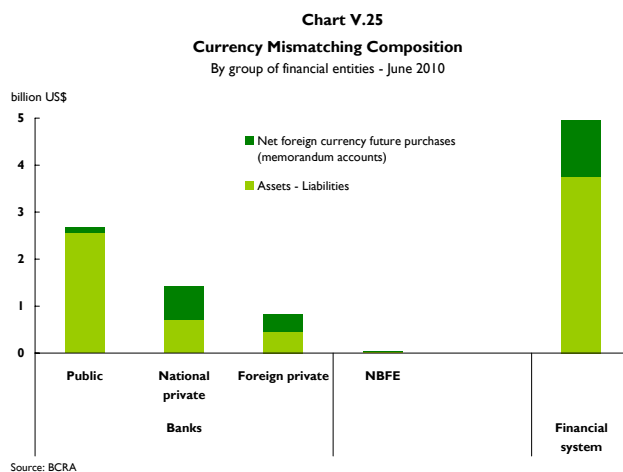
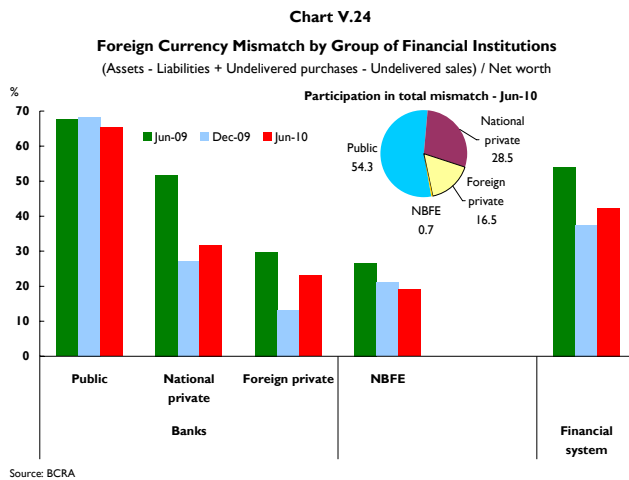
Currency risk is expected to remain at a reduced level

Foreign currency mismatching is expected to continue at low levels for the rest of the year, in a scenario of reduced volatility in the nominal exchange rate, so that exposure to currency risk will remain moderate.

V.4 Interest rate risk

Bank exposure to interest rate risk has remained at a low level

In 2010 there has been a slight shortening of the residual term of bank assets and liabilities, so that there has been no significant change in the maturity mismatching faced by the financial system. The drop in asset maturity was



mainly caused by the reduction in exposure to the public and private sectors, in addition to a moderate shortening of the residual loan term in the case of lending to companies and households (see Chart V.26). There was an increase in liquid assets and holdings of Central Bank bills. The reduction in the duration of total funding for the financial system has reflected the impact of shortening deposit terms at the same time as such deposits continued to gradually increase its participation in the total (see Chart V.27). Funding sources with relatively longer durations (outstanding bonds –ON-, subordinated debt –OS- and foreign lines of credit) have continued to see a decline in their share of funding sources.

During the first part of 2010 leading interest rates continued to decline steadily, at the same time as volatility decreased, reducing the probability of any materialization of the interest rate risk faced by the financial system.

Bank exposure to real interest rate risk has remained at a low level

Following the reduction in CER-adjusted items mismatching seen last year, mainly as a result of the swaps of Préstamos Garantizados Nacionales and Bocon bonds organized by the Government, the financial system significantly lowered its exposure to real interest rate risk. By mid-2010 the difference between CER-adjusted assets and liabilities was below 60% of financial system net worth (see Chart V.28), a level slightly lower than at the end of 2009, and close to half that recorded four years ago.

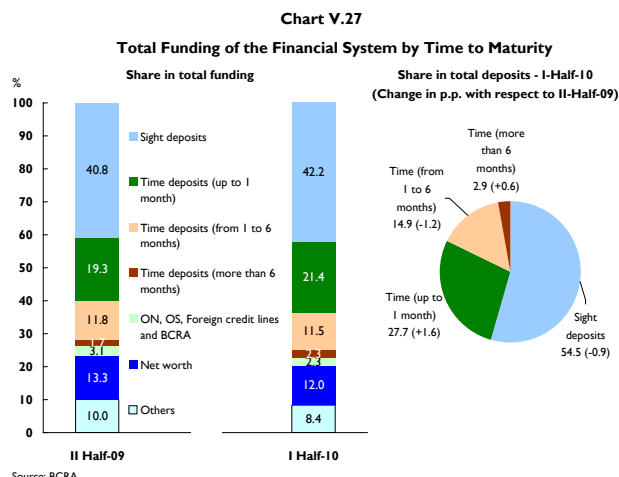
Banks experienced an increase in the capital requirement for interest rate risk in the first half of 2010 that affected both public and private banks, in a context of greater exposure in national currency items.

It is foreseen that the likelihood of materialization of interest rate risk will remain low over the rest of 2010

The positive outlook for the local economy in coming periods leads to forecasts for reduced interest rate volatility. As a result, the probability of materialization of interest rate risk faced by banks will remain low. It should be noted that the Central Bank continues to participate in the interest rates' future market by means of the "función giro", assisting in the generation of new tools to help manage this risk.

V.5 Market risk

From a low level, financial system exposure to market risk rose slightly in 2010

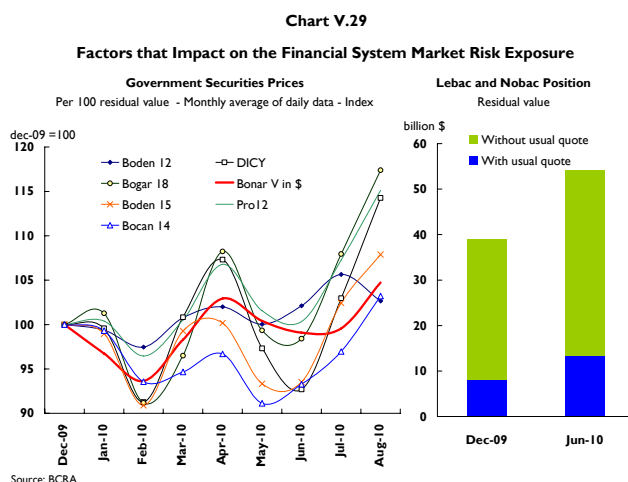
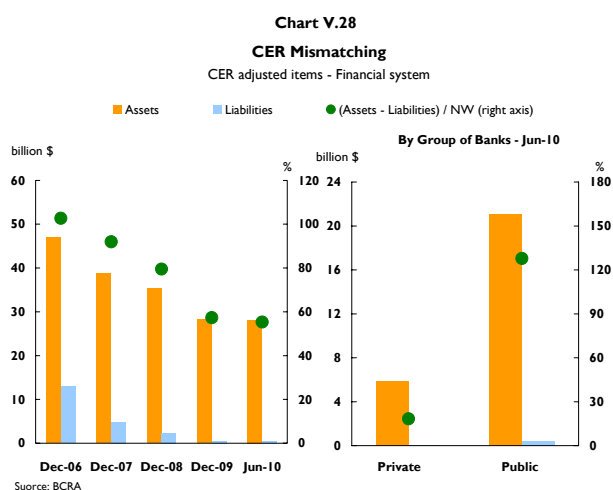


The increased bank portfolio share accounted for by holdings of marked-to-market Lebac and Nobac, during a period in which the prices of leading government securities have improved (see Chart V.29), contributed to explain the gradual rise in the exposure of the financial system to market risk in the first part of 2010. This development was partly offset by the declining volatility of leading securities at the start of the year (see Chart V.30), with an impact on the position of banks in the face of market risk. As a result, over 2010 to date, financial system exposure to market risk in terms of regulatory capital has remained stable (see Chart V.31).

It should be noted that in the face of the financial volatility experienced since the outbreak of the international crisis, the Central Bank has in the last years implemented a series of valuation alternatives for government securities that contributed to prevent short-term price swings for leading financial assets from generating excessive fluctuations in bank net worth.

Market risk faced by the financial system is expected to remain at low levels, while government securities volatility would be moderate, following the positive impact from the public debt swap

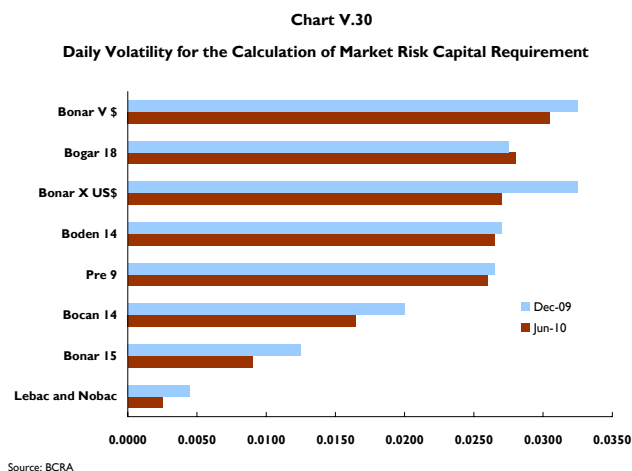
In an international scenario in which further turbulence cannot be ruled out, the local context would remain positive through to the end of 2010. Fixed income security prices are expected to show only moderate volatility in coming months, and financial system exposure to market risk will remain limited.



V.6 Risk balance

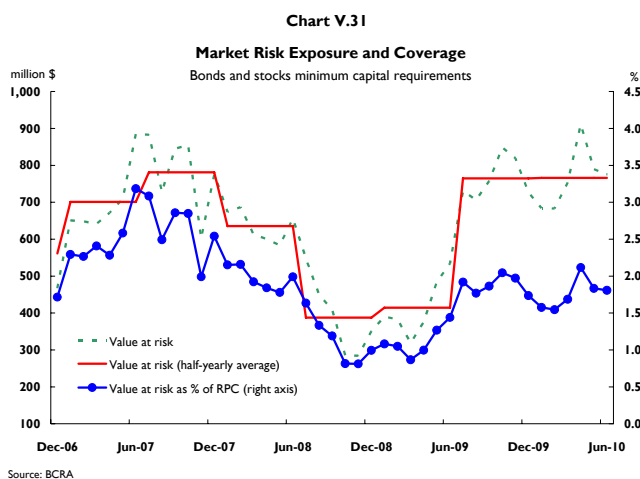
The risk balance has shown signs of improvement, with a good outlook for the rest of the year

Financial system liquid assets have been kept at high levels in recent periods, consolidating improvements in terms of bank funding following the notable growth by private sector deposits. As a result, the liquidity risk faced by the financial system has remained at a reduced level. Household consumer loan non-performance rates fell, while the level of coverage by provisions has risen, resulting in a further drop in banks' exposure to credit risk.



Both interest rate risk and market risk faced by banks remained relatively unchanged, at a time when local financial markets have seen a gradual decline in their volatility. Financial system exposure to foreign currency risk increased slightly in the first part of 2010 as a consequence of a moderate increase in balance sheet mismatching.

It is expected that there will be no significant change in the risk map through to the end of 2010, as the anticipated macroeconomic improvement will give rise to greater development of banking activity, while the main attributes of banking sector soundness will remain at satisfactory levels.



Box 7 / Outline of the Financial Reform in the United States

The financial crisis has shown the need for strengthening the US regulatory and supervision framework of its financial system. Existing mechanisms were not sufficiently adequate in terms of flexibility, coordination or overall vision to preventively identify the build-up of excessive risk or act ex post in an appropriate manner. In this situation, the recently-approved reform has been intended to limit and reduce the risks assumed by the financial system. A supervision scheme has been created to help prevent new crises, limiting bank activities, strengthening bank risk management policies and generating greater transparency for over-the-counter operations⁷⁷

In recent decades the financial system in the United States underwent a significant deregulatory process, with the gradual elimination of limits on geographical expansion of financial entities, restrictions on prices and products, and the blurring of the distinction between activities performed by the various types of financial entities, insurance companies and capital market intermediaries. As a result, greater competition was allowed in the loan market between commercial banks and savings and loans entities, in particular, and between banks from various US states in general⁷⁸. Changing market conditions, the introduction of financial innovation, and progress in technology helped deepen and accelerate this process, leading to the repeal by means of the Financial Services Modernization Act (the Gramm-Leach-Bliley Act, 1999) of the Glass-Steagall Act⁷⁹ that established the separation of banking activity into commercial and investment banks.

These developments gave rise to structural changes in the organization of the financial services sector, with the appearance of new combinations of financial products that were more opaque, and the concentration of financial activities⁸⁰, events that were to lead to a context noted for excessive risk-taking. However, these trends on their own do not completely explain the origins of

the financial crisis that broke out in 2008. Unbalanced global financial flows, the Fed's monetary policy between 2001 and 2004, and the absence of strict macro-prudential banking and capital market supervision were important factors in its development.

The size of the crisis made it clear that the sustainability of the US financial system was at risk (and some large banks failed), leading to the need to strengthen the regulatory framework to confront economic shocks, the effects of financial innovation, the existence of regulatory arbitrage and the increase in financial asset volatility. Faced by this situation the administration of President Obama proposed new reforms with five main aims: (i) to improve the supervision and regulation of financial institutions; (ii) to achieve comprehensive monitoring of financial markets; (iii) to protect the consumers of financial services and investors; (iv) to equip the Government with better tools for crisis resolution in specific institutions, with an emphasis on systemically significant institutions; and (v) to encourage internationally-coordinated efforts on matters of financial regulation. Although these measures were partly in line with those submitted by the Bush administration (2008), they differed mainly regarding the new structure of supervision proposed (institutions) and the terms for implementation.

The Obama Administration bill was passed by Congress in July 2010 under the title of the "Dodd-Frank Wall Street Reform and Consumer Protection Act". This reform seeks to improve financial service consumer protection in a broad sense, covering not only bank operations but also those on capital markets. An independent office has been set up within the Fed⁸¹ that will be dedicated to the protection of financial product consumers, being empowered to issue regulations on the matter. In addition, the mortgage loan segment will be redesigned to limit abusive and risky practices such as those that originated the subprime mortgage market crisis (see Box 1, FSR II-07).

The new law has created a Financial Stability Oversight Council (FSOC) to prevent and manage systemic risks, whatever the type of financial institution that might originate them (commercial banks, financial conglomerates, non-bank financial entities, insurance companies, etc.). Measures have included the power to place limits on leverage in the case of larger entities, stricter capital requirements, limits on loan

⁷⁷ On Over the Counter (OTC) markets, financial instruments (shares, bonds, commodities, swaps and credit derivatives) are traded directly between two parties. This type of trading is performed outside the environment of organized markets.

⁷⁸ The Riegle-Neal Act (1994) did away with the Mac Fadden Act (1927) that restricted the expansion of banks into other states.

⁷⁹ This 1933 law introduced changes to the banking system with the aim of combating the financial system speculation that led to the crisis in 1930.

⁸⁰ Banks provide a greater number of services, leading to universal banking.

⁸¹ Bureau of Consumer Financial Protection

concentration, as well as requirements for increased information on their activities and the drawing up of an *ex ante* liquidation plan in the event of insolvency. At the same time, a mechanism has been defined for the orderly winding up of systemically-important banks that could place financial stability at risk, granting the FDIC the necessary authority to act in relation to banks, insurance companies and clearing houses (payment systems and capital markets) showing solvency problems. Limitations on banks identified as “too big to fail” include restrictions on carrying out certain operations for their own account (known as the Volcker Rule), as well as on developing links with hedge funds and private equity funds when their deposits are insured by the FDIC.

In addition to the setting up of the mentioned Council to deal with systemic matters, the Fed has been given greater powers, some regulators have been unified⁸² and an effort has been made to fill some of the regulatory vacuums (in the areas of hedge funds, private equity funds, derivatives, over-the-counter transactions, etc.), among others. It has been established that the Securities and Exchange Commission (SEC) will be responsible for carrying a register of hedge funds and private equity funds, requesting them to provide information so that it can evaluate the systemic risk represented by the sector. Furthermore, the SEC has been given responsibility for redefining the role and regulation of credit rating agencies, with the setting up of a department to be in charge of supervising them.

With the aim of improving transparency in relation to the risks associated with financial derivatives, the scopes of the SEC's supervision and regulatory roles and those of the Commodity Futures Trading Commission (CFTC) have been broadened to cover derivatives transactions traded on over-the-counter markets and those participating in such markets. The SEC has been assigned new responsibilities, such as the registering, monitoring and periodic inspection of private equity and hedge funds financial advisors managing asset in excess of US\$150 million. Furthermore, the SEC will have the power to set guarantee margins for dealers and the larger operators in the swaps market. Centralized clearing will be required for such financial assets, and standards of conduct will be set for market participants. The new law allows banks to trade in derivatives to hedge risks and to participate as market makers for swaps involving interest rates, exchange rates, precious

metals and CDS traded on regulated markets (initially was intended to be forbidden). In the case of trading with derivatives involving shares, other commodities and CDS not traded on regulated markets, such entities must do so through a subsidiary within a period not longer than 2 years.

In general, the technical press and academic circles have viewed the reforms as a positive contribution to the creation of a sounder financial system for coming years, especially because of the increased scope of supervision following the setting up of the Financial Stability Oversight Council, the development of an instrument to break too-big-to-fail entities, and the search for greater transparency for financial entity trading in derivatives on unregulated markets. The challenges facing this new framework will be to improve the administration of the segmented regulatory framework that exists in the United States, and to fully implement all the reforms that have been proposed.

These measures have been designed to improve the regulatory and supervisory structures, and to strengthen the prudential role of the Federal Reserve, although without fully changing the existence of multiple supervisors on the same financial intermediation segment, among other dimensions. It is for this reason that progress should continue to be made on proposals for new macro-prudential supervision measures to anticipate and prevent new vulnerability scenarios, within the framework of the continued discussions at international level within the sphere of the G-20 and the Financial Stability Board to achieve coordinated global financial reform to ensure overall financial stability.

⁸² The Office of Thrift Supervision (OTS) responsible for Savings and Loans has been merged with the Office of the Comptroller of the Currency (OCC), although its thrift charter (legal framework) has been maintained.

VI. Payments System

Summary

The non-financial private sector gradually increased the use of electronic means of payment, in a scenario of certain efficiency improvements in transactions achieved in recent years. Currency held by the public continued to be a major means of payment in the economy, noting higher levels of use compared to other countries of the region.

The number of credit and debit cards verified a further expansion, in line with the greater momentum of financial intermediation to the private sector. The amount of cleared checks continued the upward trend that began in early 2009, while the number of bounced documents by nonsufficient funds declined. The amount of truncated checks reached 79% of the total cleared documents. The local use of these payment instruments (debit cards, and documents compensated) still has a wide range for growth when compared with the levels observed in developed economies

During the first half of 2010 a gradual increase was observed in the use of direct debits (related to payment of services) and in retail transfers. Also, the use of Electronic Means of Payment for transactions in pesos (high value payment system) showed an improvement in terms of GDP in recent months.

The Central Bank continues boosting measures that contribute to the deepening of the National Payment System, and that would lead to greater agility and

efficiency in transactions. Under the implemented Uniform Federal Clearing (CFU) new advances were produced in order to standardize all documents submitted for clearing.

Continuing with its aim of promoting banking services access, the BCRA established that since October 2010, financial entities should provide to the entire population a no-charge savings bank account ("Cuenta Gratuita Universal", Free Bank Account) and a debit card associated with that account. This contributes to the use of Electronic Means of Payment provide greater security to individuals who perform transactions in relation to the operative by cash. Additionally, also with the goal of increasing safety in the transactions of businesses and families in the banking subsidiaries, the use of settlement checks for payments and the reduction of bank transfers costs is being favored. Thus, inter-bank transfers not exceeding \$10,000 per day will be free of charge for both home banking (internet) and through ATMs. Transfers charges on banking branches operations will be limited based on the amount of the operation: up to \$50,000 the maximum fee is \$5, between \$50,000 and \$100,000 the limit will be \$10, and for operations greater than \$100,000 the cap will be \$300. These limits will serve as a reference for home banking and ATM's operations exceeding \$10,000, where the costs in no case would exceed 50% of that operations ordered in banking branches.

Chart VI.1

Number of Cards Issued by the Financial System

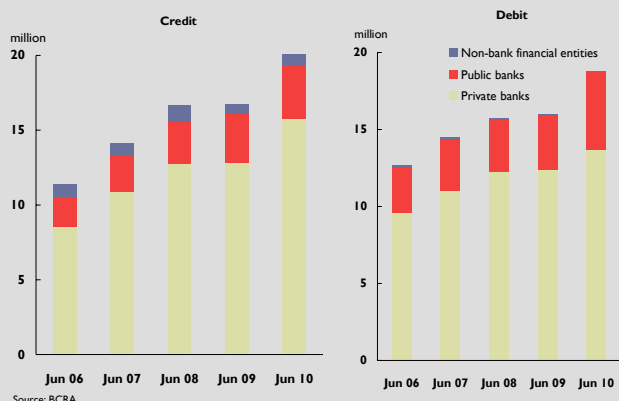
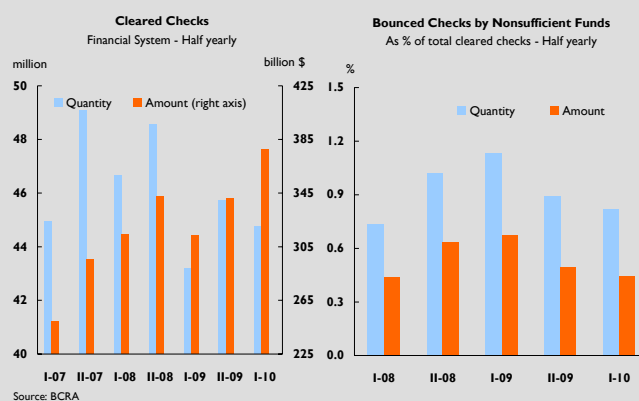


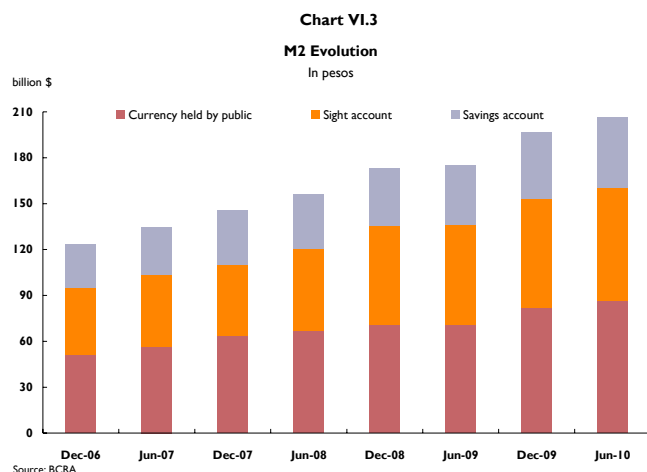
Chart VI.2

Cleared Checks



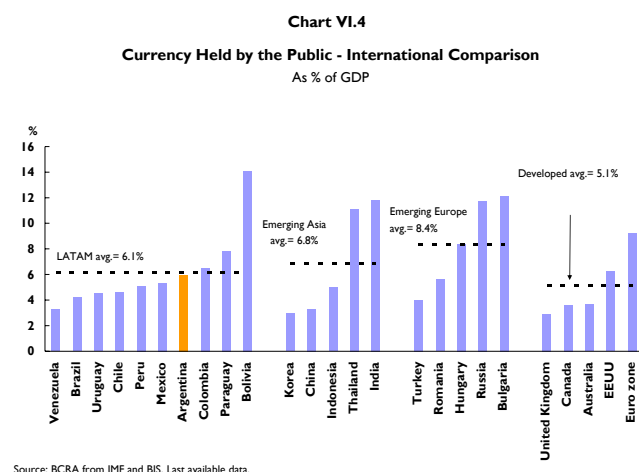
VI.1 National Payments System

The role of cleared checks as well as credit and debit cards deepened as means of payment in the economy, although still have a high development potential



The National Payment System (NPS) continued showing a gradual development, with some increases in scope, efficiency and diversification in terms of payment instruments used, a scenario that helps to provide greater safety for the economy's payment process.

Cash continued ranking among the principal means of payment in daily operations of the economy (see Chart VI.3), with currency held by the public around 6% of GDP. The use of this means of payment in our country is in line with the average of other economies in the region, and above that of some developed countries (see Chart VI.4).



During the first half of 2010 the amount of checks⁸³ cleared in national currency amounted to 44.7 million, reflecting a 3.6% year on year (y.o.y.) increase (see Chart VI.2). Truncated checks⁸⁴ reached, on average, 79% of all cleared documents. In this period the number of bounced checks for various reasons accounted for 2.1% of the total amount of checks presented for clearing, verifying a decrease of 0.6 pp in relation to the same quarter of 2009. The checks bounced for nonsufficient funds in particular were at 0.8% of the amount of checks cleared (equivalent to 0.4% of total), continuing the downward trend that began in late 2009.

Another sign of the gradual development of the payment system is the increase in the amount of credit and debit cards in the domestic market (see Chart VI.1). In late June 2010 the number of credit cards was 21% above the same period in 2009, reaching a total of 20 million. In this evolution non bank financial entities and private banks gained greater participation, where three quarters of plastic in circulation were issued by private financial institutions. Also, the number of debit cards increased 17% during the same period, totaling 19 million.

The growth shown in the use of credit cards as a means of payment in recent years has led to a relatively greater insertion in our country compared to other economies in the region. However, this payment instrument still has a broaden range for growth when compared with the

⁸³ The concepts checks and documents in this section of the chapter are synonyms.

⁸⁴ Those that do not require sending the image to the drawee bank, in amounts up to \$ 5,000.

more advanced economies (see Chart VI.5). This margin is larger when considering the case of cleared documents.

On the other hand, a gradual increase in the use of electronic payments is observed driven both by direct debit (associated to the payment of electricity, telephone and cable TV, etc.) as well as by retail transfers. Direct debits increased against last year, reaching 3.3% of GDP in the first half of 2010 (see Chart VI.6). Retail transfers reported an increase in the number of transactions in the same period, although the transaction values verified a reduction in terms of GDP over 2009.

The amount of operations channeled in pesos through the Electronic Means of Payment -MEP- (high-value payment system) increased during the first half of 2010, resulting in greater weight in terms of GDP (see Chart VI.7).

VI.2. Modernization of the payment system

The BCRA continued working on instruments to help modernize and strengthen the local Payment System, in a context of implementing new measures to improve the safety of household and corporate transactions

The Central Bank continued to design and implement measures that tend to achieve greater depth and scope of the local Payment System as well as contribute to greater efficiency and effectiveness in operations, while providing alternatives to the population to conduct transactions more securely.

On the one hand, some progress is reported in the standardization of all documents in order to achieve an optimal monitoring and control of them by the depository institutions. In this context, the Central bank is currently working, setting minimum safety standards and standardizing documents designs in order to facilitate the truncation of these instruments. Similar procedures design for nominal certificates of deposit is under analysis within the framework of the Interbank Commission for Payment Systems (CIMPRA).

Additionally, the BCRA launched a series of measures aimed at increasing security in public transactions in banking subsidiaries, encouraging the use of bank transfers and discouraging the use of cash. With these objectives, a reduction in costs for bank transfers, which will become free (November) in those cases not exceeding \$10,000 per day for transactions both conducted through home banking (internet) and

Chart VI.5
Payment System - International Comparison

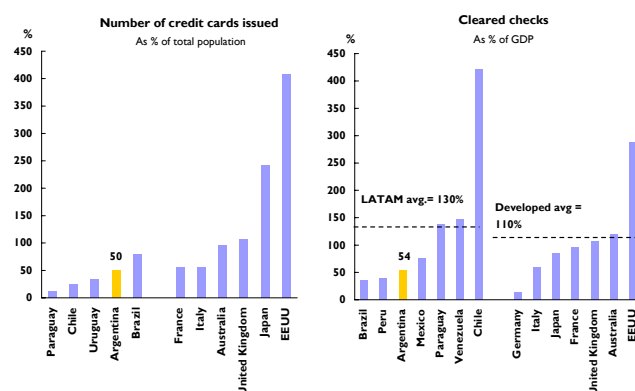
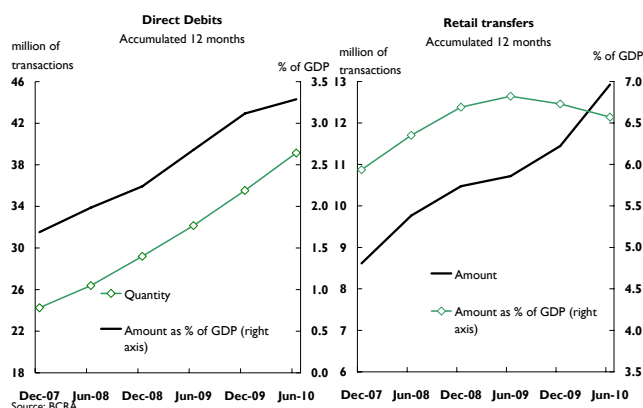
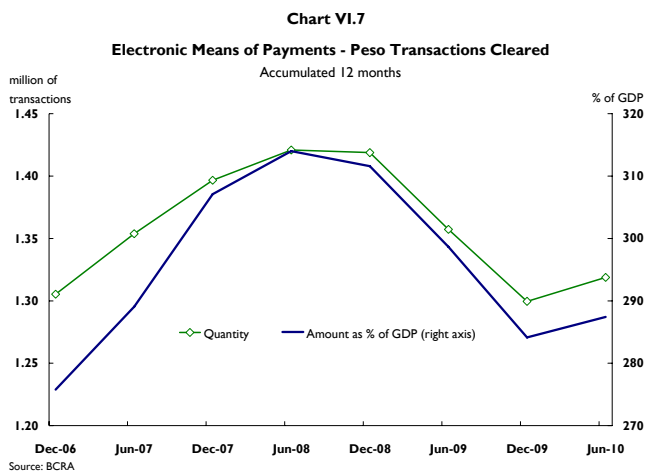


Chart VI.6
Electronic Means of Payments





through ATMs, is being implemented. Service charges for inter-bank transfers⁸⁵ ordered in banks branches' will have a limit based on the amount of the operation: up to \$50,000 the maximum fee will be \$5, between \$50,000 and \$100,000 the maximum cost will be \$10, and for operations greater than \$100,000 there will be a cap of \$300. These limits will serve as a reference for home banking and ATMs operations in excess of \$10,000, and can not in any case exceed 50% of the cost established for transfers ordered in a bank branch.

On the other hand, banks⁸⁶ should make available to households, since October, a "Cuenta Gratuita Universal" (Universal Free Bank Account) (with a maximum balance amounting to \$10,000), denominated in pesos and without service charge, with the presentation of the National Identity Document (DNI) as the only requirement for the transaction. It will include a debit card, service-free operations in the ATMs of the entities that issued the card and have a maximum balance of \$10,000, in order to avoid illegal transactions.

At the same time, the use of settlement checks issued by the Central Bank will be promoted for peso and dollar payments, the latter being only intended for real estate operations. They may be requested by all those who have account and a registered signature in the bank that manages their operations.

⁸⁵ Communication "A" 5127

⁸⁶ Banks with more than 10 ATMs.

Statistics Annex – Financial System

Chart 1 | Financial Soundness Indicators

As %	1996	1997	1998	1999	2000	2001	2002	2003	2004	2005	2006	2007	2008	Jun 09	2009	Jun 10
1- Liquidity	22.3	26.1	23.1	25.0	23.4	19.6	22.8	29.1	29.6	20.1	22.5	23.0	27.9	30.1	28.6	31.0
2- Lending to the public sector	16.9	16.2	16.2	18.0	17.3	23.0	48.5	47.0	40.9	31.5	22.5	16.3	12.7	12.9	14.5	13.2
3- Lending to the private sector	50.8	47.7	48.4	44.9	39.9	42.7	20.8	18.1	19.6	25.8	31.0	38.2	39.4	38.6	38.3	37.5
4- Private non-performing loans	16.2	13.8	12.2	14.0	16.0	19.1	38.6	33.5	18.6	7.6	4.5	3.2	3.1	3.7	3.5	2.9
5- Net worth exposure to private sector	24.9	22.5	20.6	24.7	26.2	21.9	17.3	12.4	-1.0	-4.1	-3.3	-3.0	-3.3	-2.2	-2.8	-3.8
6- ROA	0.6	1.0	0.5	0.2	0.0	0.0	-8.9	-2.9	-0.5	0.9	1.9	1.5	1.6	2.0	2.3	2.3
7- ROE	4.1	6.3	3.9	1.7	0.0	-0.2	-59.2	-22.7	-4.2	7.0	14.3	11.0	13.4	16.7	19.2	19.0
8- Efficiency	142	136	138	142	147	143	189	69	125	151	167	160	167	182	185	164
9- Capital compliance	23.8	20.8	20.3	21.0	20.1	21.4	-	14.5	14.0	15.3	16.9	16.9	16.9	16.9	18.8	17.6
10- Excess capital compliance	64	73	49	54	58	54	-	116	185	173	134	93	90	81	100	84

Source: BCRA

Chart 2 | Balance Sheet

In millions of current pesos	Dec 02	Dec 03	Dec 04	Dec 05	Dec 06	Dec 07	Dec 08	Jun 09	Dec 09	Jun 10	Change (in%)	
											Half-yearly	Annual
Assets	187,532	186,873	212,562	221,962	258,384	297,963	346,762	366,409	387,381	442,616	14.3	20.8
Liquid assets ¹	17,138	27,575	29,154	20,819	37,991	46,320	58,676	62,576	71,067	87,384	23.0	39.6
Public bonds	31,418	45,062	55,382	66,733	64,592	62,678	65,255	76,262	86,318	100,556	16.5	31.9
Lebac/Nozac	-	-	17,755	28,340	29,289	36,022	37,093	41,030	43,867	61,227	39.6	49.2
Portfolio	-	-	11,803	21,067	25,767	31,598	25,652	26,464	34,748	45,951	32.2	73.6
Repo	-	-	5,953	7,273	3,521	4,424	11,442	14,566	9,119	15,275	67.5	4.9
Private bonds	332	198	387	389	813	382	203	270	307	256	-16.8	-5.4
Loans	84,792	68,042	73,617	84,171	103,668	132,157	154,719	157,071	169,868	191,200	12.6	21.7
Public sector	44,337	33,228	30,866	25,836	20,874	16,772	17,083	15,066	20,570	23,701	15.2	57.3
Private sector	38,470	33,398	41,054	55,885	77,832	110,355	132,844	138,171	145,247	163,186	12.4	18.1
Financial sector	1,985	1,417	1,697	2,450	4,962	5,030	4,793	3,834	4,052	4,313	6.4	12.5
Provisions over loans	-11,952	-9,374	-7,500	-4,930	-3,728	-4,089	-4,744	-5,482	-5,824	-5,868	0.8	7.0
Other netted credits due to financial intermediation	39,089	27,030	32,554	26,721	26,039	29,712	38,152	41,072	33,498	37,183	11.0	-9.5
Corporate bonds and subordinated debt	1,708	1,569	1,018	873	773	606	912	1,197	1,146	1,360	18.7	13.6
Unquoted trusts	6,698	4,133	3,145	3,883	4,881	5,023	5,714	6,255	5,942	5,985	0.7	-4.3
Compensation receivable	17,111	14,937	15,467	5,841	763	377	357	17	16	15	-3.9	-10.5
Other	13,572	6,392	12,924	16,124	19,622	23,706	31,169	33,604	26,395	29,824	13.0	-11.2
Leasing	567	397	611	1,384	2,262	3,469	3,935	3,260	2,933	2,969	1.2	-8.9
Shares in other companies	4,653	4,591	3,871	4,532	6,392	6,430	7,236	7,792	6,711	7,081	5.5	-9.1
Fixed assets and miscellaneous	8,636	8,164	7,782	7,546	7,619	7,643	7,903	8,132	8,239	8,510	3.3	4.7
Foreign branches	3,522	3,144	3,524	3,647	2,782	2,912	3,153	4,075	3,926	3,158	-19.6	-22.5
Other assets	9,338	12,043	13,180	10,950	9,953	10,347	12,275	11,380	10,337	10,185	-1.5	-10.5
Liabilities	161,446	164,923	188,683	195,044	225,369	261,143	305,382	321,619	339,047	392,593	15.8	22.1
Deposits	75,001	94,635	116,655	136,492	170,898	205,550	236,217	250,083	271,853	325,484	19.7	30.2
Public sector ²	8,381	16,040	31,649	34,019	45,410	48,340	67,151	67,268	69,143	101,910	47.4	51.5
Private sector ²	59,698	74,951	83,000	100,809	123,431	155,048	166,378	179,232	199,278	220,041	10.4	22.8
Current account	11,462	15,071	18,219	23,487	26,900	35,245	39,619	40,259	45,752	52,371	14.5	30.1
Savings account	10,523	16,809	23,866	29,078	36,442	47,109	50,966	56,649	62,807	68,753	9.5	21.4
Time deposit	19,080	33,285	34,944	42,822	54,338	65,952	69,484	75,068	83,967	90,216	7.4	20.2
CEDRO	12,328	3,217	1,046	17	13	0	0	0	0	0	-	-
Other netted liabilities due to financial intermediation	75,737	61,690	64,928	52,072	46,037	46,225	57,662	58,638	52,114	54,231	4.1	-7.5
Interbanking obligations	1,649	1,317	1,461	2,164	4,578	4,310	3,895	3,087	3,251	3,530	8.6	14.4
BCRA lines	27,837	27,491	27,726	17,005	7,686	2,362	1,885	1,002	270	268	-0.6	-73.2
Outstanding bonds	9,096	6,675	7,922	6,548	6,603	6,938	5,984	5,670	5,033	4,059	-19.4	-28.4
Foreign lines of credit	25,199	15,196	8,884	4,684	4,240	3,864	4,541	3,608	3,369	3,272	-2.9	-9.3
Other	11,955	11,012	18,934	21,671	22,930	28,752	41,357	45,272	40,191	43,102	7.2	-4.8
Subordinated debts	3,712	2,028	1,415	1,381	1,642	1,672	1,763	1,914	1,922	1,973	2.7	3.1
Other liabilities	6,997	6,569	5,685	5,099	6,792	7,695	9,740	10,984	13,159	10,904	-17.1	-0.7
Net worth	26,086	21,950	23,879	26,918	33,014	36,819	41,380	44,790	48,335	50,023	3.5	11.7
Memo												
Netted assets	185,356	184,371	202,447	208,275	244,791	280,336	321,075	338,235	364,726	416,336	14.2	23.1
Consolidated netted assets	181,253	181,077	198,462	203,286	235,845	271,652	312,002	329,779	357,118	407,752	14.2	23.6

(1) Includes margin accounts with the BCRA; (2) Does not include accrual on interest or CER.

Source: BCRA

Methodological note (chart 1)

1.- (Cash compliance according to BCRA + Other cash holdings + Central Bank repos) / 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 non-performing loans - 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; **9.-** Capital compliance (Responsabilidad Patrimonial Computable) / Risk - adjusted assets according to the regulation of BCRA about Minimum Capital Compliance; **10.-** (Capital compliance minus requirements, included forbearances) / Capital requirements.

Statistics Annex – Financial System (cont.)

Chart 3 | Profitability Structure

In millions of current pesos	Annual								Half-yearly			Change (in %)	
	2002 ¹	2003	2004	2005	2006	2007	2008	2009	I-09	II-09	I-10	I-10 / II-09	I-10 / I-09
Financial margin	13,991	1,965	6,075	9,475	13,262	15,134	20,462	28,858	13,614	15,244	14,557	-5	7
Net interest income	-3,624	-943	1,753	3,069	4,150	5,744	9,573	13,917	6,655	7,263	8,057	11	21
CER and CVS adjustments	8,298	2,315	1,944	3,051	3,012	2,624	2,822	1,196	515	681	1,043	53	103
Foreign exchange rate adjustments	5,977	-890	866	751	944	1,357	2,307	2,278	1,516	761	1,042	37	-31
Gains on securities	3,639	1,962	1,887	2,371	4,923	5,144	4,398	11,004	4,178	6,827	4,363	-36	4
Other financial income	-299	-480	-375	233	235	264	1,362	463	751	-288	51	-118	-93
Service income margin	4,011	3,415	3,904	4,781	6,243	8,248	10,870	13,052	6,139	6,913	7,449	8	21
Loan loss provisions	-10,007	-2,089	-1,511	-1,173	-1,198	-1,894	-2,839	-3,814	-1,993	-1,821	-1,515	-17	-24
Operating costs	-9,520	-7,760	-7,998	-9,437	-11,655	-14,634	-18,767	-22,710	-10,878	-11,833	-13,400	13	23
Tax charges	-691	-473	-584	-737	-1,090	-1,537	-2,318	-3,272	-1,561	-1,711	-1,821	6	17
Income tax	-509	-305	-275	-581	-595	-1,032	-1,342	-4,226	-1,684	-2,542	-1,434	-44	-15
Adjustments to the valuation of government securities ²	0	-701	-320	-410	-752	-837	-1,757	-184	-110	-74	-151	105	37
Amortization payments for court-ordered releases	0	-1,124	-1,686	-1,867	-2,573	-1,922	-994	-471	-127	-344	-342	0	168
Other	-3,880	1,738	1,497	1,729	2,664	2,380	1,441	686	-137	823	1,061	29	-876
Monetary results	-12,558	69	0	0	0	0	0	0	0	0	0	0	0
Total results	-19,162	-5,265	-898	1,780	4,306	3,905	4,757	7,920	3,263	4,656	4,405	-5	35
Adjusted results ³	-	-3,440	1,337	4,057	7,631	6,665	7,508	8,575	3,501	5,074	4,897	-3	40
Annualized indicators - As % of netted assets												cambio en p.p.	
Financial margin	6.5	1.1	3.1	4.6	5.8	5.7	6.7	8.5	8.3	8.8	7.5	-1.3	-0.9
Net interest income	-1.7	-0.5	0.9	1.5	1.8	2.2	3.1	4.1	4.1	4.2	4.1	0.0	0.1
CER and CVS adjustments	3.9	1.3	1.0	1.5	1.3	1.0	0.9	0.4	0.3	0.4	0.5	0.1	0.2
Foreign exchange rate adjustments	2.8	-0.5	0.4	0.4	0.4	0.5	0.8	0.7	0.9	0.4	0.5	0.1	-0.4
Gains on securities	1.7	1.1	1.0	1.2	2.2	1.9	1.4	3.3	2.6	3.9	2.2	-1.7	-0.3
Other financial income	-0.1	-0.3	-0.2	0.1	0.1	0.1	0.4	0.1	0.5	-0.2	0.0	0.2	-0.4
Service income margin	1.9	1.9	2.0	2.3	2.7	3.1	3.6	3.9	3.7	4.0	3.8	-0.2	0.1
Loan loss provisions	-4.7	-1.1	-0.8	-0.6	-0.5	-0.7	-0.9	-1.1	-1.2	-1.0	-0.8	0.3	0.4
Operating costs	-4.4	-4.2	-4.1	-4.6	-5.1	-5.5	-6.1	-6.7	-6.6	-6.8	-6.9	-0.1	-0.2
Tax charges	-0.3	-0.3	-0.3	-0.4	-0.5	-0.6	-0.8	-1.0	-1.0	-1.0	-0.9	0.0	0.0
Income tax	-0.2	-0.2	-0.1	-0.3	-0.3	-0.4	-0.4	-1.3	-1.0	-1.5	-0.7	0.7	0.3
Adjustments to the valuation of government securities ²	0.0	-0.4	-0.2	-0.2	-0.3	-0.3	-0.6	-0.1	-0.1	0.0	-0.1	0.0	0.0
Amortization payments for court-ordered releases	0.0	-0.6	-0.9	-0.9	-1.1	-0.7	-0.3	-0.1	-0.1	-0.2	-0.2	0.0	-0.1
Other	-1.8	0.9	0.8	0.8	1.2	0.9	0.5	0.2	-0.1	0.5	0.5	0.1	0.6
Monetary results	-5.8	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
ROA	-8.9	-2.9	-0.5	0.9	1.9	1.5	1.6	2.3	2.0	2.7	2.3	-0.4	0.3
ROA adjusted ³	-	-1.9	0.7	2.0	3.4	2.5	2.5	2.5	2.1	2.9	2.5	-0.4	0.4
ROE	-59.2	-22.7	-4.2	7.0	14.3	11.0	13.4	19.2	16.7	21.6	19.0	-2.5	2.4

(1) Information in currency of december 2002. (2) Com. "A" 3911. Adjustments to the valuation of government unlisted securities according to Com. "A" 4084 are included under the "gains on securities" heading.

(3) Excluding amortization of payments for court-ordered releases and the effects of Com. "A" 3911 and 4084.

Source: BCRA

Chart 4 | Portfolio Quality

As percentage	Dec 02	Dec 03	Dec 04	Dec 05	Dec 06	Dec 07	Dec 08	Jun 09	Dec 09	Jun 10
Non-performing loans (overall)	18.1	17.7	10.7	5.2	3.4	2.7	2.7	3.3	3.0	2.5
Non-performing loans to the non-financial private sector	38.6	33.5	18.6	7.6	4.5	3.2	3.1	3.7	3.5	2.9
Provisions / Non-performing loans	73.8	79.2	102.9	124.5	129.9	129.6	131.4	118.0	125.7	139.0
(Total non-performing - Provisions) / Overall financing	4.7	3.7	-0.3	-1.3	-1.0	-0.8	-0.8	-0.6	-0.8	-1.0
(Total non-performing - Provisions) / Net worth	17.2	11.9	-1.0	-4.1	-3.3	-3.0	-3.3	-2.2	-2.8	-3.8

(*) Include commercial loans treated as consumer loans for classification purposes.

Source: BCRA

Statistics Annex – Private Banks

Chart 5 | Financial Soundness Indicators

As %	1996	1997	1998	1999	2000	2001	2002	2003	2004	2005	2006	2007	2008	Jun 09	2009	Jun 10
1- Liquidity	23.6	26.9	22.8	24.3	24.1	23.6	24.8	27.6	29.2	21.5	23.7	25.7	34.1	32.7	29.8	29.3
2- Lending to the public sector	13.5	13.7	13.6	16.1	14.7	20.8	49.4	47.7	41.6	28.5	16.3	9.5	6.3	5.9	6.2	5.1
3- Lending to the private sector	51.0	46.7	47.6	44.6	38.4	45.4	22.4	19.9	22.5	31.1	37.9	46.6	44.0	42.9	43.3	46.8
4- Private non-performing loans	11.1	8.5	7.7	8.9	9.8	14.0	37.4	30.4	15.3	6.3	3.6	2.5	2.8	3.6	3.3	2.7
5- Net worth exposure to private sector	21.6	14.3	13.2	11.5	13.4	11.4	18.6	11.2	1.9	-2.2	-3.0	-3.6	-3.4	-2.2	-3.1	-3.9
6- ROA	0.6	0.7	0.5	0.3	0.1	0.2	-11.3	-2.5	-1.0	0.5	2.2	1.6	1.9	2.5	3.0	2.6
7- ROE	4.1	6.3	4.3	2.3	0.8	1.4	-79.0	-19.1	-8.1	4.1	15.3	10.9	15.2	20.1	22.9	19.6
8- Efficiency	144	135	139	146	152	151	168	93	115	136	158	152	166	193	195	169
9- Capital compliance	15.9	15.4	14.6	18.9	18.0	17.6	-	14.0	15.1	17.8	18.6	19.2	18.3	19.1	22.5	20.6
10- Excess capital compliance	33	47	27	60	49	43	-	88	157	155	116	87	86	87	120	102

Source: BCRA

Chart 6 | Balance Sheet

In millions of current pesos	Dec 02	Dec 03	Dec 04	Dec 05	Dec 06	Dec 07	Dec 08	Jun 09	Dec 09	Jun 10	Change (in%)	
											Half-yearly	Annual
Assets	118,906	116,633	128,065	129,680	152,414	175,509	208,888	218,950	229,549	245,082	6.8	11.9
Liquid assets ¹	11,044	14,500	15,893	14,074	22,226	29,418	37,044	40,376	43,562	45,305	4.0	12.2
Public bonds	19,751	22,260	24,817	29,966	27,663	24,444	29,552	38,736	47,949	46,393	-3.2	19.8
Lebac/Nobac	-	-	8,359	15,227	15,952	17,684	23,457	25,784	31,575	32,157	1.8	24.7
Portfolio	-	-	5,611	12,899	14,220	15,639	12,858	18,274	27,413	26,348	-3.9	44.2
Repo	-	-	2,749	2,328	1,732	2,045	10,598	7,510	4,161	5,809	39.6	-22.7
Private bonds	273	172	333	307	683	310	127	135	233	153	-34.4	13.4
Loans	51,774	47,017	50,741	56,565	69,294	88,898	98,529	96,017	101,722	117,151	15.2	22.0
Public sector	25,056	23,571	21,420	15,954	10,036	6,413	6,249	1,820	1,694	1,622	-4.2	-10.9
Private sector	26,074	22,816	28,213	39,031	55,632	78,587	88,426	91,151	96,790	112,123	15.8	23.0
Financial sector	644	630	1,107	1,580	3,626	3,898	3,854	3,046	3,238	3,406	5.2	11.8
Provisions over loans	-7,463	-5,225	-3,717	-2,482	-2,227	-2,365	-2,871	-3,425	-3,653	-3,767	3.1	10.0
Other netted credits due to financial intermediation	27,212	22,148	25,753	16,873	18,387	17,084	25,265	26,447	21,258	21,278	0.1	-19.5
Corporate bonds and subordinated debt	1,514	1,394	829	675	618	430	699	840	734	821	11.8	-2.3
Unquoted trusts	6,205	3,571	2,362	2,444	2,982	3,456	3,869	4,424	4,198	4,348	3.6	-1.7
Compensation receivable	15,971	13,812	14,657	5,575	760	377	357	17	16	15	-3.9	-10.5
Other	3,523	3,370	7,905	8,179	14,027	12,822	20,339	21,167	16,311	16,093	-1.3	-24.0
Leasing	553	387	592	1,356	2,126	3,149	3,451	2,842	2,569	2,610	1.6	-8.2
Shares in other companies	3,123	2,791	1,892	2,416	4,042	3,762	4,538	5,084	4,067	4,258	4.7	-16.2
Fixed assets and miscellaneous	5,198	4,902	4,678	4,575	4,677	4,685	4,926	5,062	5,096	5,290	3.8	4.5
Foreign branches	-109	-136	-53	-148	-139	-154	-178	-199	-202	-213	5.2	6.9
Other assets	7,549	7,816	7,137	6,178	5,682	6,277	8,505	7,873	6,946	6,623	-4.7	-15.9
Liabilities	103,079	101,732	113,285	112,600	131,476	152,153	182,596	190,219	198,438	213,673	7.7	12.3
Deposits	44,445	52,625	62,685	75,668	94,095	116,719	135,711	142,901	154,387	171,258	10.9	19.8
Public sector ²	1,636	3,077	6,039	6,966	7,029	7,564	19,600	20,528	17,757	23,318	31.3	13.6
Private sector ²	38,289	47,097	55,384	67,859	85,714	107,671	114,176	120,170	134,426	146,126	8.7	21.6
Current account	8,905	11,588	13,966	17,946	20,604	27,132	30,188	30,337	35,127	39,489	12.4	30.2
Savings account	6,309	10,547	14,842	18,362	23,165	30,169	32,778	36,265	40,999	43,654	6.5	20.4
Time deposit	11,083	18,710	22,729	27,736	38,043	45,770	46,990	48,974	54,058	57,290	6.0	17.0
CEDRO	9,016	2,409	798	3	1	0	0	0	0	0	-	-
Other netted liabilities due to financial intermediation	49,341	42,367	45,083	32,349	31,750	29,323	39,298	38,817	34,235	33,704	-1.5	-13.2
Interbanking obligations	836	726	1,070	1,488	3,383	1,979	1,160	1,163	1,668	1,845	10.6	58.7
BCRA lines	16,624	17,030	17,768	10,088	3,689	675	649	91	41	37	-11.2	-59.7
Outstanding bonds	9,073	6,674	7,922	6,548	6,413	6,686	5,672	5,317	4,626	3,750	-18.9	-29.5
Foreign lines of credit	15,434	9,998	5,444	2,696	2,249	1,833	2,261	1,231	1,262	1,182	-6.4	-4.0
Other	7,374	7,939	12,878	11,530	16,015	18,150	29,555	31,016	26,638	26,891	1.0	-13.3
Subordinated debts	3,622	1,850	1,304	1,319	1,642	1,668	1,759	1,910	1,918	1,970	2.7	3.2
Other liabilities	5,671	4,890	4,213	3,264	3,989	4,443	5,828	6,591	7,897	6,741	-14.6	2.3
Net worth	15,827	14,900	14,780	17,080	20,938	23,356	26,292	28,731	31,111	31,409	1.0	9.3
Memo												
Netted assets	117,928	115,091	121,889	123,271	143,807	166,231	192,074	201,838	216,100	231,852	7.3	14.9

(1) Includes margin accounts with the BCRA; (2) Does not include accrual on interest or CER.

Source: BCRA

Methodological note (chart 5)

1.- (Cash compliance according to BCRA + Other cash holdings + Central Bank repos) / 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 non-performing loans - 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; **9.-** Capital compliance (Responsabilidad Patrimonial Computable) / Risk - adjusted assets according to the regulation of BCRA about Minimum Capital Compliance; **10.-** (Capital compliance minus requirements, included forbearances) / Capital requirements.

Statistics Annex – Private Banks (cont.)

Chart 7 | Profitability Structure

In millions of current pesos	Annual								Half-yearly			Change (in%)	
	2002 ¹	2003	2004	2005	2006	2007	2008	2009	I-09	II-09	I-10	I-10 / II-09	I-10 / I-09
Financial margin	10,628	2,575	3,415	5,253	7,778	8,960	12,964	19,720	9,359	10,361	9,585	-7	2
Net interest income	-304	107	1,214	2,069	2,826	4,191	7,727	10,068	5,003	5,065	5,646	11	13
CER and CVS adjustments	1,476	1,082	900	1,215	858	662	651	185	84	101	108	8	29
Foreign exchange rate adjustments	6,189	-312	666	576	740	990	1,620	1,509	908	601	718	19	-21
Gains on securities	3,464	1,892	959	1,259	3,154	2,888	1,637	7,343	2,599	4,744	2,948	-38	13
Other financial income	-197	-195	-322	134	199	229	1,329	616	764	-149	164	-211	-78
Service income margin	2,782	2,341	2,774	3,350	4,459	5,881	7,632	9,198	4,322	4,876	5,291	8	22
Loan loss provisions	-6,923	-1,461	-1,036	-714	-737	-1,174	-1,863	-2,751	-1,400	-1,351	-1,050	-22	-25
Operating costs	-6,726	-5,310	-5,382	-6,303	-7,741	-9,735	-12,401	-14,807	-7,097	-7,710	-8,799	14	24
Tax charges	-512	-366	-393	-509	-769	-1,105	-1,715	-2,380	-1,131	-1,249	-1,317	6	16
Income tax	-337	-295	-202	-217	-365	-380	-1,168	-3,001	-1,453	-1,548	-1,161	-25	-20
Adjustments to the valuation of government securities ²	0	-665	-51	-201	-170	-100	-267	3	-20	24	9	-62	-145
Amortization payments for court-ordered releases	0	-791	-1,147	-1,168	-1,182	-1,466	-688	-233	-52	-181	-241	33	363
Other	-4,164	1,178	846	1,156	1,641	1,576	916	264	-35	300	575	92	-1,723
Monetary results	-10,531	-20	0	0	0	0	0	0	0	0	0	0	0
Total results	-15,784	-2,813	-1,176	648	2,915	2,457	3,412	6,014	2,491	3,522	2,892	-18	16
Adjusted results ³	-	-1,357	252	2,016	4,267	4,023	4,367	6,244	2,564	3,680	3,123	-15	22
Annualized indicators - As % of netted assets												cambio en p.p.	
Financial margin	7.6	2.3	2.9	4.3	5.9	5.8	7.3	9.8	9.6	10.1	8.7	-1.4	-0.9
Net interest income	-0.2	0.1	1.0	1.7	2.1	2.7	4.4	5.0	5.1	4.9	5.1	0.2	0.0
CER and CVS adjustments	1.1	0.9	0.8	1.0	0.6	0.4	0.4	0.1	0.1	0.1	0.1	0.0	0.0
Foreign exchange rate adjustments	4.4	-0.3	0.6	0.5	0.6	0.6	0.9	0.8	0.9	0.6	0.6	0.1	-0.3
Gains on securities	2.5	1.7	0.8	1.0	2.4	1.9	0.9	3.7	2.7	4.6	2.7	-2.0	0.0
Other financial income	-0.1	-0.2	-0.3	0.1	0.2	0.1	0.8	0.3	0.8	-0.1	0.1	0.3	-0.6
Service income margin	2.0	2.0	2.4	2.7	3.4	3.8	4.3	4.6	4.4	4.8	4.8	0.0	0.4
Loan loss provisions	-5.0	-1.3	-0.9	-0.6	-0.6	-0.8	-1.1	-1.4	-1.4	-1.3	-1.0	0.4	0.5
Operating costs	-4.8	-4.6	-4.6	-5.1	-5.9	-6.3	-7.0	-7.4	-7.3	-7.5	-8.0	-0.4	-0.7
Tax charges	-0.4	-0.3	-0.3	-0.4	-0.6	-0.7	-1.0	-1.2	-1.2	-1.2	-1.2	0.0	0.0
Income tax	-0.2	-0.3	-0.2	-0.2	-0.3	-0.2	-0.7	-1.5	-1.5	-1.5	-1.1	0.5	0.4
Adjustments to the valuation of government securities ²	0.0	-0.6	0.0	-0.2	-0.1	-0.1	-0.2	0.0	0.0	0.0	0.0	0.0	0.0
Amortization payments for court-ordered releases	0.0	-0.7	-1.0	-1.0	-0.9	-0.9	-0.4	-0.1	-0.1	-0.2	-0.2	0.0	-0.2
Other	-3.0	1.0	0.7	0.9	1.2	1.0	0.5	0.1	0.0	0.3	0.5	0.2	0.6
Monetary results	-7.5	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
ROA	-11.3	-2.5	-1.0	0.5	2.2	1.6	1.9	3.0	2.5	3.4	2.6	-0.8	0.1
ROA adjusted ³	-	-1.2	0.2	1.6	3.2	2.6	2.5	3.1	2.6	3.6	2.8	-0.8	0.2
ROE	-79.0	-19.1	-8.1	4.1	15.3	10.9	15.2	22.9	20.1	25.5	19.6	-5.9	-0.5

(1) Information in currency of december 2002. (2) Com. "A" 391 I. Adjustments to the valuation of government unlisted securities according to Com. "A" 4084 are included under the "gains on securities" heading.

(3) Excluding amortization of payments for court-ordered releases and the effects of Com. "A" 391 I and 4084.

Source: BCRA

Chart 8 | Portfolio Quality

As percentage	Dec 02	Dec 03	Dec 04	Dec 05	Dec 06	Dec 07	Dec 08	Jun 09	Dec 09	Jun 10
Non-performing loans (overall)	19.8	15.7	8.9	4.4	2.9	2.2	2.5	3.4	3.1	2.6
Non-performing loans to the non-financial private sector	37.4	30.4	15.3	6.3	3.6	2.5	2.8	3.6	3.3	2.7
Provisions / Non-performing loans	73.4	79.0	97.0	114.3	129.3	141.3	134.1	118.3	128.9	138.1
(Total non-performing - Provisions) / Overall financing	5.3	3.3	0.4	-0.6	-0.9	-0.9	-0.9	-0.6	-0.9	-1.0
(Total non-performing - Provisions) / Net worth	18.6	11.2	1.3	-2.2	-3.0	-3.6	-3.4	-2.2	-3.1	-3.9

(*) Include commercial loans treated as consumer loans for classification purposes.

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 entities.

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 entities 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 Societies.

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.

NBFE: Non-Bank Financial Entities (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.

Index of Charts and Tables

Index of Charts

1.	Real GDP.....	7
2.	Financial Intermediation with the Private Sector.....	8
3.	Non-Performing Credit to the Private Sector.....	9
4.	Financial System Soundness Indicators.....	10
I.1.	Advanced Economies and BRIC. Leading Indicator of Economic Activity.....	11
I.2.	Stock Indices and Expected Volatility.....	11
I.3.	Real GDP.....	12
I.4.	Developed Economies. Unemployment Rate.....	12
I.5.	World Inflation.....	12
I.6.	Commodity Prices.....	13
I.7.	Benchmark Interest Rates.....	13
I.8.	Implied Probability of a Fed Funds Rate Hike.....	13
I.9.	Long Term Yields and Gold Price.....	14
I.10.	Dollar Exchange Rate Versus Main Currencies.....	14
I.11.	MSCI Indices (Equities).....	14
I.12.	Emerging Debt Spread Indices (CDS).....	15
I.13.	Emerging Market Currencies: Indices and Expected Volatility.....	15
I.14.	Capital Compliance.....	15
I.15.	Liquid Assets.....	16
I.16.	Financial Intermediation. LATAM.....	16
I.17.	Non-Performing Loans and Provisions.....	16
B.1.1	Credit Default Swaps: Debt of Vulnerable Economies in Europe.....	17
B.1.2	Dollar/Euro: Expected Volatility and Non-Commercial Positions of Traders	17
B.1.3	European Financial Institutions Stress Tests.....	18
B.1.4	Interbank Spreads and European Banks' CDS.....	18
II.1.	Real GDP.....	19
II.2.	Issue of Corporate Bonds.....	19
II.3.	Activity. EMAE Index.....	20
II.4.	Consumption Growth.....	20
II.5.	Current Account Balance Evolution.....	20
II.6.	Price Indexes.....	21
II.7.	M2 Explanatory Factors.....	21
II.8.	Private Sector Time Deposits.....	21
II.9.	M2 and Monetary Program Targets	22
II.10.	Expansion due to FX Purchases and Sterilization with LEBAC and NOBAC.....	22
II.11.	International Reserves.....	22
II.12.	Argentina Yield Curves.....	23
II.13.	Relative Value.....	23
II.14.	Outstanding Lebac and Nobac Stock Composition.....	23
B.2.1	Situation Previous to the 2010 Swap Offer.....	24
B.2.2	Issuance due to the 2010 Debt Swap.....	25
B.2.3	Global 17: Secondary Market.....	25
II.15.	Yield Curves of Lebac Auctions.....	26
II.16.	Lebac Secondary Market.....	26
II.17.	Traded Volume of Government Bonds (MAE + BCBA).....	26
II.18.	Issuance of Financial Trusts.....	27
II.19.	Trading of Differed Payment Checks.....	27
II.20.	Local Stock Market Evolution.....	27
II.21.	Equity Trading Volume.....	28
II.22.	Future Dollar.....	28
II.23.	Amount and Maturity of Traded Badlar Interest Rate Futures.....	28
III.1.	Manufacturing Evolution.....	29
III.2.	Household Consumption Indebtedness.....	29
III.3.	Financial System Asset Portfolio.....	30

III.4.	Composition of Corporate Loan Portfolio.....	30
III.5.	GDP. Goods and Services.....	30
III.6.	Corporate Debt.....	31
III.7.	Corporate Debt Burden.....	31
III.8.	Industry. Sectorial Evolution.....	31
III.9.	Manufacturing Sector Debt.....	32
III.10.	Primary Sector Debt.....	32
III.11.	Synthetic Indicator of Public Services.....	33
III.12.	Service Sector Debt.....	33
III.13.	Supermarket and Shopping Malls Centers.....	33
III.14.	Construction Indicators.....	34
III.15.	Labor Market.....	34
III.16.	Consumer Confidence.....	34
III.17.	Household Debt Burden.....	35
III.18.	Share in National Tax Revenue.....	35
III.19.	National Tax Revenue.....	35
III.20.	NFPS Primary Expenditure*.....	36
III.21.	NFPS* Primary Balance.....	36
IV.1.	Financial Intermediation with the Private Sector.....	37
IV.2.	Leverage and Profitability Structure.....	37
IV.3.	Loans to the Private Sector by Type of Line.....	38
IV.4.	Loans to the Private Sector by Group of Banks.....	38
IV.5.	Loans to the Private Sector.....	39
IV.6.	Lending Interest Rates in Pesos.....	39
IV.7.	Loans to the Private Sector by Type of Debtor.....	39
IV.8.	Loans to Companies by Economic Sector.....	40
IV.9.	Loans to Companies by Economic Sector and by Type of Line.....	40
IV.10.	Lending to the Private Sector.....	40
IV.11.	Funding Composition by Group of Financial Entities.....	41
IV.12.	Private Sector Time Deposits in Pesos.....	41
IV.13.	Spread of Lending Interest Rates - Loans to the Private Sector.....	41
B.3.1	Households - Main Results.....	42
B.3.2	Enterprises - Main results.....	42
B.3.3	Bank Services Access - Summary.....	43
B.3.4	Barriers to Banking services access for Households.....	43
B.3.5	Barriers to Banking Services Access for Companies.....	43
B.3.6	Obstacles for Increasing Banking Services to Households.....	44
B.3.7	Obstacles for Increasing Banking Services to Companies.....	44
B.3.8	ATM Distribution.....	44
IV.14.	Financial System Operational Structure.....	45
IV.15.	Financial System Regional Coverage.....	45
IV.16.	Financial System Coverage with Branches and Human Development Index.....	45
B.4.1	Private Sector Financing by Region.....	46
B.4.2	Private Sector Credit Distribution between Households and Companies.....	46
B.4.3	Credit to Companies by Activity and Region.....	47
B.4.4	Household Credit. Regional Distribution by Type of line.....	47
B.4.5	Non-performing Credit to the Private Sector by Region.....	47
IV.17.	Leverage.....	48
IV.18.	Prudential Requirement and Capital Compliance.....	48
IV.19.	Profitability Structure by Group of Banks.....	48
IV.20.	Financial Margin Composition.....	49
IV.21.	Net Interest Income.....	50
IV.22.	Operating Costs and Efficiency.....	50
IV.23.	Loan Loss Provisions.....	50
IV.24.	Institutional Investors in Argentina.....	51
B.5.1	Financial Conglomerates. International Comparison. 2008.....	52
B.5.2	Ownership and Capital Structure of Conglomerates.....	53
IV.25.	Mutual Funds Net Worth Evolution.....	54
IV.26.	Assets. Banks, Insurance Companies and Mutual Funds.....	54

IV.27.	Conglomeration in Financial Intermediaries.....	55
V.1.	Liquidity.....	57
V.2.	Non-Performing Loans to the Private Sector	57
V.3.	Liquidity by Group of Financial Entities.....	58
V.4.	Deposits and Credits to the Private Sector Change.....	58
V.5.	Liquidity in Pesos.....	58
V.6.	Interbank Liquidity Markets.....	61
V.7.	Call Market.....	61
V.8.	Interest Rates.....	61
V.9.	Loans to the Non-Financial Private Sector	62
V.10.	Non-Performing Loans to the Private Sector.....	62
V.11.	Loans to the Private Sector Evolution.....	62
V.12.	Lending to the Private Sector by Granted Period.....	63
V.13.	Loan Loss Provisions.....	63
V.14.	Financial Intermediation with the Private Sector by Currency.....	63
V.15.	Lending to Companies.....	64
V.16.	Non-Performing Lending to Companies by Economic Sector	64
V.17.	Lending to Companies by Granted Period.....	64
V.18.	Financing Needs Expected for Manufacturing Sector.....	65
V.19.	Households Financing.....	65
V.20.	Total and Non-Performing Loans - Consumer Loans	65
V.21.	Household Loans by Granted Period	66
V.22.	Public Sector Exposure.....	66
V.23.	Foreign Currency Mismatch and Exchange Rate Volatility.....	66
V.24.	Foreign Currency Mismatch by Group of Financial Institutions.....	67
V.25.	Currency Mismatching Composition.....	67
V.26.	Financial System Assets by Time to Maturity.....	67
V.27.	Total Funding of the Financial System by Time to Maturity.....	68
V.28.	CER Mismatching.....	68
V.29.	Factors that Impact on the Financial System Market Risk Exposure.....	68
V.30.	Daily Volatility for the Calculation of Market Risk Capital Requirement.....	69
V.31.	Market Risk Exposure and Coverage.....	69
VI.1.	Number of Cards Issued by the Financial System.....	73
VI.2.	Cleared Checks.....	73
VI.3.	M2 Evolution.....	74
VI.4.	Currency Held by the Public - International Comparison.....	74
VI.5.	Payment System - International Comparison.....	75
VI.6.	Electronic Means of Payments.....	75
VI.7.	Electronic Means of Payments - Peso Transactions Cleared.....	76

Index of Tables

III.1.	Grain and Oilseed Production.....	32
IV.1.	Balance Sheet.....	38
IV.2.	Profitability Structure: Financial System.....	49
IV.3.	Profitability Structure by Type of Bank.....	49
IV.4.	Social Security Fund FGS-ANSES Portfolio	51
B.6.1	Phase-in arrangements (shading indicates transition periods).....	60