

Argentina at a glance

Political structure **Elections:** Argentina's president, Néstor Kirchner, was sworn in on May 25th 2003 with a relatively weak mandate and without a strong base within the ruling, but divided, Justice (Peronist) party. The next election is scheduled for October 2007.

Government: Argentina has a presidential political system with a bicameral Congress. The president is elected to a four-year term that is renewable once. The lower house is the 257-seat Chamber of Deputies. Members are elected for four-year terms, with half the chamber coming up for re-election every two years. The Senate has 72 members who are elected for six-year terms—three senators are elected per state, two from the leading party and one from the runner-up; one-third of the Senate stands for re-election every two years.

Major parties: Partido Justicialista (PJ, the Peronist party), Unión Cívica Radical (UCR), Frente del País Solidario (FrepaSo); minor parties include Afirmación para una República Igualitaria (ARI), Propuesta Republicana (PRO)—an alliance comprising the Movimiento Federal Recrear (MFR) and Compromiso por el Cambio—and several provincial parties.

Fiscal year: January 1st–December 31st.

Sovereign debt ratings* **Standard & Poor's:** B+
Moody's Investors Service: B2
Fitch: DDD

*Senior unsecured long-term foreign-currency debt ratings.

Economist Intelligence Unit country risk rating

Sovereign risk	Currency risk	Banking sector risk	Political risk	Economic structure risk
B	BB	B	B	B

* To make it easier for clients to compare our ratings with those of the three main international ratings agencies, we have adjusted the rating-band system in our ratings model. The scale will still run from 0 to 100, but it will be divided into ten bands of ten points each rather than five bands of 20 points, as previously. These new bands provide a closer match with those used by Standard & Poor's, Moody's and Fitch IBCA. Letter grades have also been changed to conform with those used by the other main rating agencies. Thus, a score of 0–10 would rate AAA; 11–20, AA; 21–30, A; 31–40, BBB; 41–50, BB; 51–60, B; 61–70, CCC; 71–80, CC; 81–90, C; and 91–100, D.

Economic assessment

	2005 ^a	2006 ^b	2007 ^b
GDP (US\$ bn at current market prices)	183.2	207.2	233.0
GDP growth (%)	9.2	7.8	5.6
Private consumption (% growth)	8.9	6.7	5.1
Government consumption (% growth)	6.1	4.8	4.0
Gross fixed investment (% growth)	22.7	11.0	7.0
Exports of goods & services (% growth)	13.5	6.6	10.1
Imports of goods & services (% growth)	20.1	12.0	9.2
Consumer prices (% av)	9.6 ^c	11.0	10.6
Exports fob (US\$ bn)	40.1	45.2	50.9
Imports fob (US\$ bn)	-27.3	-30.7	-35.3
Current-account balance (US\$ bn)	5.7	5.7	6.4
Budget balance (% of GDP)	1.8	2.1	1.8
Government debt (% of GDP)	72.8	62.1	55.4
Exchange rate (Ps:US\$1 av)	2.90	3.06	3.14

(a) Actual. (b) Economist Intelligence Unit forecasts. (c) Economist Intelligence Unit estimate.

Source: Economist Intelligence Unit, *Country Forecast Argentina*, October 2006.

Executive summary

President Néstor Kirchner will continue to emphasise his government's departure from the free-market orthodox policies of the 1990s, stressing a more active role for the state in the economy. The long-lasting recession triggered by the country's decision in late 2001 to default on its sovereign debt and devalue its currency began to abate in 2003, and macroeconomic indicators have improved substantially in 2004-06. However, increased rates of poverty and unemployment have stressed the fabric of society, and social conditions remain well below pre-crisis levels. International financial institutions and overseas governments have been reluctant to provide assistance, as the country has a poor record of carrying out promised political and economic reforms.

The private financial sector—which includes many foreign banks and fund managers—is still recovering from the run on deposits of late 2001. Lending remains very limited. The authorities have provided some funds to bolster the decimated banking sector, and big domestic financial institutions have been the main beneficiaries. Several foreign banks decided to close their operations in the country in the aftermath of the crisis, and many financial firms, both foreign and domestic, have retreated from Argentina's now much-reduced markets for commercial and investment banking, brokerage, insurance and fund management.

The government ended the convertibility programme, the 11-year-old link of the peso to the dollar, in early 2002. Since then, the peso has found its value in trading in the markets, though the Central Bank intervenes regularly to keep the peso from appreciating above a certain level. In doing so, it hopes to spur exports and domestic production—and strong increases in export sales have been in evidence of late. Capital controls, imposed in late 2001 and early 2002 to limit capital flight, were eased in 2003, and only limited minimum-stay requirements now remain in place.

Capital markets have failed to live up to their potential in Argentina. The once-important stockmarket remains small and does not provide much financing for domestic firms; no firm has launched an initial public offering since 2004. The corporate bond market, however, has experienced something of a resurgence in recent months. Local banks and companies are familiar with a range of derivative instruments, and currency-related markets have grown more important since the switch to a floating peso.

Corporate funds are available only at short terms, if at all. The government default effectively closed off most avenues for private financing in Argentina. In the past, local companies were able to use sophisticated financial techniques seldom found in emerging markets, such as private equity and securitised bond issues.

Banks

Overview The banking sector has made impressive gains since mid-2003. According to figures from the Banco Central de la República Argentina (the Central Bank), loans to the private sector grew by 39% in the year to July 2006 and continued increasing at the same rate in the following months, according to preliminary statistics. Deposits grew by 15% in the year to July 2006, supported by public-sector deposits, which soared by more than 23%. Banks continued to shed public-sector assets, which comprised only 25.6% of their total assets. This means that nearly all institutions are in compliance with the Central Bank regulation that limits government assets to 40% of their portfolios. This limit will be reduced to 35% as of July 2007. The increase in the price of government bonds following the debt restructuring of 2005 and the overall good momentum of emerging markets enabled banks to unload government paper and thus minimise losses.

Lending activity had been non-existent until late 2003, when some consumer loans (mostly credit-card lines) and short-term revolving corporate lines emerged. Since then, all lines except for mortgages have been increasing rapidly. Total lending to the private sector, which used to be 25% of GDP in 1998 and 8% at the trough of the crisis in 2002, is now approaching 11% of GDP.

Non-performing loans in the corporate sector were 5.6% in July 2006, down from 12.3% a year earlier. In June 2006 bad loans had reached a decade-low of 5.4%, but the improving trend stopped the following month. Private banks are

doing much better in this field, with bad debts amounting to only 4.6%, compared with 8.1% in state-owned banks, where risk practices are often looser than in the private banking sector. Two factors have contributed to the systemic reduction of delinquency: 17 quarters of economic growth and the completion of debt restructuring in the private sector. In addition, banks have focused on consumer financing—which was increasing twice as fast as corporate lending over the first seven months of 2006. Consumers have traditionally been better borrowers than firms.

After reporting losses of Ps17bn in 2002, Ps5bn in 2003 and Ps1bn in 2004, the system as a whole returned Ps1.8bn in profits in 2005, and twice as much in the first seven months of 2006 on an annualised basis (Ps2.3bn). The return on equity jumped from 7.2% in 2005 to 13.6% in the first seven months of 2006, with private banks doing slightly better than state-owned institutions.

Bank margins—the spread between average interest earned and paid—while still low, have been increasing year after year. In 2003 they amounted to 1.1% of assets, 3.1% the year after and 4.6% in 2005. In the first seven months of 2006 financial margins reached 5.7%, which is closely related to both the decline in government assets and the surge in private lending. The persistence of negative real interest rates for depositors is perhaps the largest contributor to the recovery of profits in the banking system. On the cost side, banks have reduced head count and other administration costs. However, in the last year rising salaries began to be felt again, as the bank employees' union (Asociación Bancaria) managed to obtain significant increases. But overall, administration costs are lower than before the crisis. According to Econviews, a local consultancy specialising in banks, the financial industry will have to invest in IT and marketing, as the system becomes more competitive and the low-cost structure less sustainable.

Banks were among the worst affected institutions in the economic crisis of 2001–02. The sovereign default, the devaluation of the peso and a run on deposits all contributed to the banking sector's dramatic losses in 2002 and 2003. The asymmetric conversion of dollar-denominated debts to pesos, coupled with court rulings obliging banks to return deposits in dollars, further added to the sector's decline. As a result, the banking sector is now smaller, with fewer international players, and is still struggling to regain the confidence of investors and depositors.

The government has not yet fully compensated banks for the asymmetric conversion of assets and liabilities—assets were converted at a rate of Ps1:US\$1 while liabilities were converted at a rate of Ps1.4:US\$1 following the peso's release from its peg to the US dollar. The conversion of dollar-denominated instruments to pesos, as well as the conversion of inflation-indexed instruments to salary-indexed instruments, resulted in great losses for banks. In addition, the banks remain subject to liabilities stemming from court injunctions (known locally as *amparos*) that require banks to return dollar-denominated deposits at their full dollar value despite their conversion to pesos in 2002. Losses have amounted to Ps7bn, according to local analysts—and these have yet to be recognised by the banks on their balance sheets. Given the fear that deposited funds will not be returned in full, as occurred after the crisis,

very few Argentinians now deposit their funds with local banks. Most of the growth in deposits is concentrated in sight deposits, as the average citizen prefers to keep long-term savings out of banks. Some analysts even partially attribute the current construction boom to consumers' desires to avoid banks.

The Central Bank provided regulatory support for this approach by allowing banks to spread out losses over a period of 60 months, rather than in full up front, starting in January 2003. For some banks engaged in long-term lending, the Central Bank stretched this period to 120 months. As part of the arrangement, the banks did not record this effective revaluation of their assets as accounting losses, so they were not required to increase equity by a similar amount to comply with Basle rules stipulating an 8% equity-to-assets ratio.

The Central Bank resumed its powers as lender of last resort following the devaluation. This enabled it to grant large rediscounts to commercial banks to prevent bankruptcy. In May 2002 rediscounts peaked at over Ps22bn. The recovery of deposits since mid-2002 (supported by more stable conditions in the financial and foreign-exchange markets and high deposit rates) increased banks' liquidity and enabled them to start to pay back rediscounts received from the Central Bank. As of September 2006 the banks owed the Central Bank some Ps8.7bn, down from Ps18bn a year earlier. Banco de la Provincia de Buenos Aires and Banco de Galicia are the only institutions with outstanding rediscount lines with the Central Bank, but both of them are paying back principal and interest every month. Financing through the rediscount window is expensive, however, since banks pay three percentage points above inflation; given negative real interest rates most banks have found cheaper money and, thus, decided to pay back to the Central Bank.

Banks have been increasingly funding their operations via deposit-taking rather than other financing options. Most deposits are short-term (the minimum term being 30 days). Since the crisis of 2001-02, sight deposits (which are considered "transactional" funds) have grown twice as much as term deposits, showing that trust in the banking system is not yet fully restored. The average life of term deposits is just 43 days, according to a report issued by the Central Bank in September 2006.

As of end-July 2006, total deposits in pesos amounted to Ps135bn, and some US\$5bn (about Ps15bn) was deposited in dollars. The private sector held over Ps97bn and the public sector (federal government, provinces, municipalities and agencies) a bit more than Ps37bn. Total M-3 in circulation at this time was less than Ps200bn, or less than one-third of GDP.

Financial market indicators**Demand for financial services**

Population, mid-2005 ^a (m)	39.08
Age 65 and above (%)	10.47
Between ages 15 and 64 (%)	63.87
Under 15 (%)	25.67
Gross domestic product, 2005 ^a (US\$ bn)	183.20
Gross domestic savings, 2005 ^a (US\$ bn)	44.33
Gross domestic product per person, 2005 ^a (US\$)	4,690
Personal disposable income per person, 2005 ^a (US\$)	2,160
Private consumption per person, 2005 ^a (US\$)	2,880

Financial intermediaries

Domestic credit provided by the banking sector, 2005 ^b (% of GDP)	38.08
Domestic credit to the private sector, 2005 ^b (% of GDP)	11.66
Insurance company premiums, 2005 ^c (% of GDP)	2.52
of which life insurers, 2005 ^c (% of GDP)	0.76
Pension-fund assets, end-June 2006 ^d (% of GDP)	11.79
Mutual-fund company assets, end-July 2006 ^e (% of GDP)	2.17
Factoring company turnover, 2005 ^f (% of GDP)	0.18
Leasing assets acquired, September 2006 ^g (% of GDP)	0.28

Capital markets

Equity market capitalisation of shares of domestic companies, end-2005 ^h (% of GDP)	25.98
New equity capital raised by domestic companies, 2005 ^h (% of GDP)	0.64
Domestic corporate debt issues outstanding, end-2005 ⁱ (% of GDP)	8.62
International corporate debt issues outstanding, end-2005 ⁱ (% of GDP)	3.00

Sources: (a) Economist Intelligence Unit, *Market Indicators and Forecasts*. (b) World Bank, *World Development Indicators*. (c) Swiss Re, *Sigma* 5/2006. (d) Superintendency of Pension Funds. (e) Argentine Chamber of Mutual Funds. (f) Factors Chain International. (g) Banco Central de la República Argentina. (h) World Federation of Exchanges. (i) Bank for International Settlements, *Quarterly Review on International Banking and Financial Market Development*.

Bank regulators

Following a devaluation during Argentina's financial crisis in 2002, Banco Central de la República Argentina (the Central Bank) recovered its traditional role of lender of last resort through a new charter passed in early 2002. This function was used extensively in 2002 when, despite official restrictions, money continued to flow out of the financial sector. As of September 2006, outstanding loans from the Central Bank were valued at Ps8.7bn, down from Ps18bn a year earlier. Since early 2005, the Central Bank has encouraged commercial banks to pay back these loans. The deal worked for both parties: the Central Bank could soak up liquidity (sorely needed due to its extensive intervention in the foreign-exchange market), and institutions could pay off their Central Bank financing without being penalised for paying them off ahead of schedule. As a result of this arrangement, as of September 2006 only two institutions had outstanding debts with the Central Bank.

In its Communiqué 3,901 of March 2003, the Central Bank stated new rules about accessing its discount window. Banks can turn to the Central Bank when their liquidity falls below 25%; when their liquidity rises above 35% they must pay back these loans. (Liquidity is defined as the proportion of liquid resources to sight deposits plus 30% of term deposits maturing in the following ten business days.) Rediscounts are allowed for 90 days and may be renewed, but interest should be paid monthly. Rediscounts can exceed 100% of net worth, but shareholders must inject capital for the equivalent of that excess. As of end-June

2006, total liquidity in the banking system, defined in a stricter measure of cash and securities to total deposits, was around 37%.

Since the end of the currency-board system, which maintained the peso at parity with the US dollar, the Central Bank is no longer obliged to back the monetary base in full. The Central Bank reports that the monetary base is, nevertheless, backed by instruments worth some 125% of the actual pesos in circulation as of August 2006—but if other peso liabilities (reverse repurchase agreements and bills) were taken into account, the back-up ratio would fall to 88%.

Law No. 25,780, published in the Official Gazette on September 8th 2003, gives the Central Bank more power in determining which assets and liabilities may be included in the sale or merger of financial institutions. That is, the Central Bank may deem it necessary to exclude some assets or liabilities and have them placed in trust, rather than allow them to be included in a transaction. The law also gives employees of the Central Bank some protection from court proceedings. The law sets out that only “unreasonable” or “arbitrary” decisions may be questioned by the judicial system. The law also stipulates that the Central Bank is the exclusive issuer of national currency—thereby making illegal the issuance of sub-currencies, a practice that had gained popularity in the run-up to the crisis.

Regulations regarding banking supervision have started to adapt to the new financial environment in Argentina. The Central Bank reduced the risk-weighted capital-adequacy ratio that banks are required to maintain from 11.5% to the Basle standard of 8% (Communiqué 3,959, of June 2003). At present, very few banks comply with this rule, which is based on the common standards devised under the aegis of the Basle-based Bank for International Settlements. The Central Bank has extended the deadline for meeting Basle requirements to 2008.

The Central Bank has changed its reserve requirement scheme many times since the abolition of the currency board. The most recent revision took place in July 2006 (Communiqué 4,549), when the Central Bank tightened measures and increased reserve requirements for sight deposits while reducing requirements for long-term deposits. As the former are far greater than the latter, the measure resulted in lower bank liquidity and a subsequent increase in interest rates.

The July communiqué established the following reserve requirements:

- 100% of the deposits of other financial institutions;
- 100% of mutual-fund deposits;
- 19% of current and savings accounts in pesos (35% for dollar accounts);
- 14% of time deposits maturing in 29 days or less (35%);
- 11% of time deposits maturing in more than 30 days but less than 59 days (28%);
- 7% of time deposits maturing in more than 60 days but less than 89 days (20%);

- 2% of deposits maturing in less than 180 days (10%);
- no obligation for deposits longer than 180 days.

Furthermore, the banks may now count only 67% of the cash kept in their vaults and automatic teller machines towards their reserve requirements, making it harder for institutions with large networks. According to Melconian & Santangelo, a local economic consultancy, the measure, which will be fully phased in by November 2006, will reduce liquidity in the banking system by Ps2bn.

Dollar deposits can be lent to exporters or to suppliers of exporting companies. In addition, banks can invest their dollars in trust funds authorised by the Securities Commission that are listed locally and have special guarantees or finance exports. Otherwise, such funds must be kept at the Central Bank.

The Central Bank's Superintendency of Financial Institutions (Superintendencia de Entidades Financieras y Cambiarias) is Argentina's banking regulator. Though nominally under the Central Bank's control, it is partially autonomous. Two members of the Central Bank's board are appointed as its superintendent and vice-superintendent. When a financial institution declares bankruptcy, the entire board of the Central Bank usually becomes involved, in order to head off system-wide problems.

A deposit insurance scheme was created by the passage of Law 24,485, published in April 1995. The entity that manages the scheme, Seguro de Depósitos Sociedad Anónima (Sedesa), is funded by the banks. The maximum coverage is now Ps30,000 (previously US\$30,000), regardless of the maturity of the deposit. The coverage is valid only when the interest rate on the deposit is less than 2 percentage points above the rate established by the Central Bank. Sedesa's website (www.sedesa.com.ar) provides the reference rates above which deposits are not covered. In 2001-02 Sedesa helped to capitalise banks with solvency concerns. For example, in February 2002 it provided Banco de Galicia with Ps200m to help shore up the bank's accounts. Sedesa is funded through bank contributions worth 0.015% of the average stock of deposits every month. In addition, there is a special contribution that varies according to the risk of each financial institution, as determined by the Central Bank. The last intervention occurred in November 2005, when Sedesa poured Ps56.5m to help bail out Banco Empresario de Tucuman, a small regional institution eventually taken over by Banco Macro, a larger domestically owned institution. As of June 30th 2006, Sedesa had more than Ps1.4bn in cash. The level of banks' contributions to Sedesa has varied, and it is the Central Bank that ultimately decides on the percentage

The government stepped up restrictions on money-laundering under a law published on May 10th 2000 (Law No. 25,246, Decree 370/2000 and Central Bank Communiqué 3,074). For transactions totalling more than US\$10,000, banks must request documentation regarding the origin of the funds. The Central Bank communiqué outlines a framework for catching money-launderers. Congress is analysing a law that would strengthen the investigative function of the Financial Analysis Unit, the federal division responsible for investigating suspected money-laundering activity. A 2005 study by local NGO

(non-governmental organisation) Unidos por la Justicia estimated that some US\$6bn is laundered every year in Argentina.

To reduce tax evasion and address money laundering, the April 2001 Competitiveness Law (No. 25,413) reduced the level of invoices that may be paid with cash to Ps1,000. Any invoice amount higher than Ps1,000 must be paid via a banking instrument—cheque, credit/debit card, or other bank transfer—but not in cash.

Industry groups include the Association of Argentine Banks (Asociación de Bancos Argentinos), which consists mostly of foreign banks; Adeba, which is an organisation of private domestic banks; and the Association of Public and Private Banks of the Argentine Republic (Asociación de Bancos Públicos y Privados de la República Argentina), which is mostly comprised of public and co-operative institutions.

Domestic banks

Top ten domestic banks

Ranked by total assets at end-May 2006—Ps bn

Bank	Assets	Market share (%)
Banco de la Nación de Argentina ^a	57.6	24.1
Banco de la Provincia de Buenos Aires ^b	22.7	9.5
Banco de Galicia	22.7	9.5
Banco de la Ciudad de Buenos Aires ^b	9.5	4.0
Banco Hipotecario ^c	8.9	3.7
Banco Macro-Bansud	7.2	3.0
Banco Credicoop ^d	5.8	2.4
Nuevo Banco de Santa Fé ^b	4.7	2.0
Banco Patagonia	4.4	1.8
Banco de la Provincia de Córdoba ^b	3.6	1.5
Total market	239.2	100.0

(a) State-owned bank. (b) Province-owned bank. (c) Majority state-owned bank through the Banco de la Nación de Argentina. (d) Co-operative bank.

Source: Banco Central de la República Argentina.

Commercial banks. During the 1990s local banks lost their grip on the Argentine banking sector as international financial groups bought up smaller banks and enlarged their networks. But a reversal of fortune began as the financial crisis deepened in 2001–02. The Central Bank has committed itself to helping state-owned and private domestically owned banks stay afloat. Partly because of the Central Bank's commitment, local banks have been able to increase their market share as depositors look for secure institutions.

Banco de la Nación de Argentina, Banco de Galicia and Banco de la Provincia de Buenos Aires—the three largest domestic banks in Argentina—received a total of nearly Ps15bn in discounts from the Central Bank during the crisis period. A reverse flight-to-quality movement set in as depositors began to move their funds to banks that were assured of Central Bank support in 2001–03. Since then, however, other important players have emerged in the market, including Banco Macro-Bansud, Banco Patagonia and, to a lesser extent, Banco Comafi.

Economic stability has allowed domestic banks to gain market share at the expense of international institutions. The unprecedented fiscal surplus

generated by the federal and provincial governments has resulted in increased resources for state-owned banks, particularly for Banco de la Nación de Argentina, which acts as an agent of the federal government. (The bank receives all federal tax revenue and makes revenue-sharing payments to the provincial governments on behalf of the federal government.) In addition, domestic private banks have been able to resume lending faster than their foreign competitors and have participated in auctions for failed banks, thus gaining market share.

Banco de la Nación de Argentina, a wholly state-owned bank, has over 600 branches and is the sole financial institution in many towns in the interior of the country. It plays an important role as a major lender to agribusiness. As a state institution, it has moved to take over the operations of foreign banks that have decided to leave Argentina, notably *Crédit Agricole* (France). It also manages the government's finances. In times when tax revenue rises—as has been the case since the second half of 2002—the bank receives additional funds at no extra cost.

In effect, Banco de la Nación's large holdings of government revenue have enabled the Treasury to buy dollars to avoid an appreciation of the peso. Banco de la Nación is generally an active participant in the weekly auction of short-term paper backed by these funds. However, despite Banco de la Nación's large amount of liquidity, it has not increased its lending activity by much over the past few years. This appears to be the result of previous bad lending practices that resulted in severe losses for the bank—many loans were granted on the basis of political connections rather than on sound financial assessment.

As of end-May 2006, Banco de la Nación had Ps57.6bn in assets. Although it has recently reduced its exposure to the public sector, it still had some Ps24bn lent to the government. Lending to the private sector represents less than 15% of total exposure. It owns a pension fund (Nación AFJP), along with insurance, leasing and factoring companies. It also manages the Provincial Development Trust, the body responsible for negotiating federal government bail-outs for the provinces. The bank will not likely be privatised, at least not under the current administration of Néstor Kirchner.

Banco de la Provincia de Buenos Aires, owned by the province that surrounds but does not include the capital, and Banco de Galicia both trail Banco de la Nación de Argentina. Banco de la Provincia de Buenos Aires is quite different from other financial institutions. The bank was founded in 1824, before the constitution was written, providing it with several advantages over its competitors. Prior to end-2001 it was exempt from paying any taxes and did not have to meet reserve requirements. In addition, it was permitted to own over 12.5% of a non-financial company—which other banks are not allowed to do. However, in 2000, the provincial government signed an agreement according to which the bank was to meet all federal bank regulations by end-2001. Although in theory the bank should have done so, there has been no official account of the situation, leading many to believe the bank has not yet met these rules.

As of end-May 2006, Banco de la Provincia de Buenos Aires had Ps22.7bn in assets. It owns a life insurer, Provincia Vida, and a general insurer, Provincia

Seguros. The bank also holds a large minority stake in Orígenes, Argentina's leading pension-fund manager. Owing to poor management and skyrocketing non-performing-loan ratios, the bank has undertaken a massive clean-up operation that has resulted in fewer loans to the private sector in the last few years. The policy now is to lend to small and medium-sized enterprises (SMEs), along with consumers, but to participate in larger corporate lending only as a minority member of a syndicate of banks. The latter is an effort to show accountability after many loans were granted solely on political grounds over the last decade.

Banco de Galicia, the largest domestically owned private bank, has completed a difficult restructuring process that resulted in the closure of 60 branches and the elimination of 1,900 staff positions. Banco de Galicia was hard hit by the 2001–02 crisis, and a subsequent corporate scandal, and needed rediscount loans totalling Ps5bn from the Central Bank to shore up its operations. However, the bank has begun to experience renewed growth. As of end-May 2006, it had assets totalling Ps22.7bn. Banco de Galicia owns an insurance firm, Galicia Seguros, but has divested its holdings in other financial-sector firms (such as pension funds).

Banco Hipotecario is another important domestic bank. The government is the largest shareholder, but the bank is run by a private company, as the board members representing private shareholders have three votes. Banco Hipotecario specialises in mortgages, but given the weakness of this segment in the aftermath of the 2001–02 crisis, it is now offering all services. In early 2005 Hipotecario attempted to buy the Argentine operations of Banca Nazionale del Lavoro (BNL–Italy), and while it succeeded in the bidding process organised by Citibank (US), the sale was later halted by the federal government. BNL was then re-auctioned, and HSBC (UK) emerged as the winner in early 2006. BNL would have provided a distribution network of some 100 branches in Argentina. Hipotecario now seems to be planning for organic growth, largely by opening new branches. While the government never made public its reasons for vetoing the BNL deal, most analysts suspect it did not want Banco Hipotecario to take on additional liabilities at that time.

There are a number of smaller public-sector banks, most of which are provincial entities. The federal government owns Banco de Inversión y Comercio Exterior (BICE). Provinces own banks such as Banco de la Ciudad de Buenos Aires, Banco de la Provincia de Córdoba and Banco de Neuquén. Banco de la Ciudad is the top performer in this segment. During the crisis, it increased its market share and was one of the few institutions that decided to lift the government-imposed freeze on deposits ahead of the Central Bank ruling on the subject. Several private domestic banks—including Banco Macro-Bansud, Banco Patagonia and Banco Comafi—seized the opportunity to expand their market share during the crisis. Banco Macro bought Bansud in November 2001 from Citibank. Then it bought branches from other banks and took over Banco Empresario del Tucuman in late 2005 in a bail-out organised by the Central Bank. Its last move was to buy Bisel in an auction organised by Banco Nación in March 2006. Bisel belonged to the Crédit Agricole group until the French institution left the country in the aftermath of the crisis, then was run by Banco

Nación until August 2006. Macro, which has been listed on the Buenos Aires Stock Exchange for ten years, is now also listed on the New York Stock Exchange, where it raised capital earlier in 2006.

Patagonia bought Banco Sudameris from the Italian Grupo Intesa in late 2002 and completed the takeover in June 2003. It then took over the local operations of Lloyds Bank (UK) in late 2004. Over the past several years, Banco Comafi has bought many ailing firms. It bought most of the branches of Scotia Bank (Canada), several small local banks, the credit-card portfolio of Meridian Bank and the Capita Corporation, the leading leasing operator.

Savings and co-operative banks. The 1977 Financial Entities Law enforced strict regulations on savings and co-operative banks. They are allowed to finance only housing and other real-estate projects, and therefore are not a major source of corporate financing. Most of their funds are derived from interest-bearing deposits.

After an earlier financial upheaval in 1994–95, many co-operative banks became insolvent and were either shut down or acquired by larger banks. The only remaining relatively large co-operative bank is Banco Credicoop, with Ps5.8bn in assets as of end-May 2006. The advantage of co-operative banks is that they are exempted from income tax.

Foreign banks

Top ten foreign banks

Ranked by total assets at end-May 2006—Ps bn

Bank	Assets	Market share (%)
Banco Francés (BBVA—Spain)	15.7	6.6
Banco Río de la Plata (BSCH—Spain)	13.8	5.8
Bank Boston (South Africa)	7.6	3.2
Citibank (US)	6.6	2.8
HSBC (UK)	6.1	2.6
Banca Nazionale del Lavoro (UK)	3.3	1.4
Itaú-Buen Ayre (Brazil)	2.0	0.8
Deutsche Bank (Germany)	1.5	0.6
ABN AMRO (Netherlands)	1.3	0.5
JP Morgan Chase (US)	0.7	0.3
Total market	239.2	100.0

Source: Banco Central de la República Argentina.

After a previous financial crisis in 1994–95, a number of foreign banks either made initial investments or increased their presence in the country. This enthusiasm for the Argentine market changed dramatically after the 2001–02 financial crisis. Several foreign banks decided to leave Argentina: Bank of Nova Scotia (Canada) and Crédit Agricole (France) left the country in April 2002. Other financial institutions backed out in other ways. After the failure of its ambitious plans for the credit-card business, Provident sold its portfolio (over US\$100m in loans to credit-card holders) to a local private-equity group for only US\$8m in March 2002. Banco Beal, a subsidiary of German bank West LB, announced its decision to close its operations in June 2002. The bank was very active in the syndicated-loan market and other corporate business. In 2003 Banco Patagonia completed its purchase of Sudameris from Grupo Intesa (Italy), and in late 2004 it completed its purchase of Lloyds Bank (UK). Lloyds Bank

had been present in Argentina for over 150 years at the time of the sale. Société Générale was sold to the local group Banex in June 2005. The most recent retreat from Argentina has been BNL (Italy), whose Argentine operations were finally bought by HSBC (UK) in early 2006 after a failed sale to Banco Hipotecario.

Five foreign banks continue to have dominant positions in the Argentine market: BBVA (Spain), BSCH (Spain), Bank Boston (South Africa), Citibank (US) and HSBC (UK). The two Spanish institutions are by far the largest, and both run aggressive marketing campaigns. HSBC has been less active than its Spanish peers but has shown a strong commitment to its Argentine subsidiary. It has capitalised over US\$400m in subordinated debt since 2002 and boosted its network with the BNL acquisition in January 2006. As a group, HSBC, with insurance companies and a pension fund, is deeply involved in the financial industry. The only divestment was the sale of a healthcare company (HSBC Salud), shortly after the 2001–02 crisis, for US\$25m to SMG, a local group. Citibank, which had significantly scaled back after the crisis, is now very active again, particularly in the corporate market and investment banking. For instance, it conducted the debt restructuring for the Province of Buenos Aires and is now helping the Province of Neuquén.

In all cases, foreign banks have posted greater losses than their local counterparts for two reasons. They have been more aggressive in provisioning for bad loans, thus reducing assets and increasing losses. And because they are required to file their accounts using their parent companies' accounting principles (such as US generally accepted accounting principles), they have not been able to take advantage of the more lenient reporting requirements afforded local banks.

In December 2005 Standard Bank agreed to buy Bank Boston (an Argentine institution) from Bank of America (US). Earlier that year Standard Bank had bought the Argentine assets of ING (the Netherlands). As of mid-October 2006, the BankBoston deal was still awaiting clearance from the Central Bank, but Standard's management was already overseeing the bank in order to make a smooth transition. BankBoston expects the handover to be completed by the first quarter of 2007.

The only foreign transaction in the first nine months of 2006 of a foreign player onto the Argentine market involved First Data Corporation of the US, which bought the Master Card licence from Exxel Group, a domestic private equity fund, for US\$250m in August 2006. Although it did not involve a bank, the transaction marked the first takeover of a domestic player by a foreigner in the Argentine financial market since the crisis of 2001–02.

Investment banks and brokerages

Top ten brokerage houses

Ranked by market share at end-June 2006

Company	Market share (%)
Raymond James (US)	9.2
Allaria Ledesma	7.6
Santander Investment (Spain)	6.8
SBS Sociedad de Bolsa	5.6
Rosario Valores	3.6
Mascardi y Cia	2.8
Napoli Sociedad de Bolsa	2.6
Capital Markets Argentina	2.2
Cohen Sociedad de Bolsa	2.1
Intervalores Sociedad de Bolsa	2.0

Source: Buenos Aires Stock Exchange.

Mergers and acquisitions, initial public offerings and bond issues remain limited in Argentina since the financial crisis of 2001-02. Following the crisis, investment-banking activity was mostly related to debt restructuring for private-sector companies, in an effort to mitigate the effects of the crisis and stem the growing tide of bankruptcies. Although activity has slowed somewhat, debt restructuring remains an important activity for these players.

Morgan Stanley (US), JP Morgan Chase (US) and Deutsche Bank (Germany) are some of the international institutions engaged in these activities, whereas MBA Banco de Inversiones is the leading domestic investment bank involved in debt restructuring. The investment-banking arm of Citibank (US) is also active. It runs the debt restructuring of the Province of Buenos Aires and underwrote bonds for Pan American Energy (UK-Argentina), two of the highest-profile deals of 2006. The top tier of local investment bankers is led by MBA and Infupa. A smaller and younger venture named Columbus has also been very active since the middle of 2005.

Small investment boutiques created by former executives of big banks and consultants have flourished over the last few years. These entities—usually not supervised by the Central Bank—have concentrated their operations in servicing the needs of small and medium-sized enterprises.

Although the Argentine stockmarket is small, brokers are still very active. Investors have found that some stocks (oil firms and other large exporters) are stable investments, and a reasonable hedge against currency fluctuation, because they have foreign-currency revenue. In addition, most brokers sell third-party products, such as mutual funds, on behalf of large US and European firms. The proof that broker activity has not plunged is in the price of their operating licences: though these have fallen from their peak of US\$2m in the late 1990s, they have been on the rise of late. In November 2005 a licence to trade on the exchange was sold for US\$800,000.

The most important brokerage houses had traditionally been subsidiaries of the dominant banks, though this has changed somewhat since the recent financial crisis. Raymond James (US) leads in the rankings of brokerage houses and has lately expanded its services to provide private banking and launched a mutual-fund family; it also does some investment banking. Its main shareholder

(Raymond James Financial, based in Tampa) increased its stake in the firm by buying out some local shareholders and now holds around three-quarters of the stake. Santander (of the Spanish group Banco Santander Central Hispano) is another active player.

Development and postal banks

There are no postal banks operating in Argentina. Banco de Inversión y Comercio Exterior (BICE), a state-owned bank, provides funding to small and medium-sized companies. Until 2003 it was a second-storey lender that channelled loans through commercial banks. Those banks bore some of the lending risk. But since then, BICE has become a direct lender. Though the bank claims to be successful via periodic press releases, demand for long-term credit is scarce and BICE's balance sheet shows that it has not grown much in terms of assets. As of end-May 2006, total assets were Ps1.23bn, roughly the same—in nominal terms—as in the last three years. Total loans to the private sector amounted to Ps300m.

Banco Latinoamericano de Exportaciones (BLADEX) focuses on providing trade financing in Latin America and the Caribbean. The Inter-American Development Bank (IDB) and the International Finance Corp (IFC, part of the World Bank) are two multilaterals serving as important sources of funds for government and corporate projects.

The IFC, for instance, has lent money to exporters through export pre-financing mechanisms. Two local firms that have taken advantage of these facilities are the vegetable oil firms Vicentin and Aceitera General Deheza. Banco de Galicia has also accessed loans from the IFC. In April 2005 the bank received a US\$40m facility aimed at providing financing for local small and medium-sized enterprises. The loan to the bank matures in seven years and has a grace period of two years. The IFC also lent money to the Argentine subsidiary of Cencosud (Chile) to acquire rival supermarket chain Disco from Ahold (Netherlands). Loan terms were finalised in early 2005. In early 2006, Capsa, a locally owned oil company, borrowed from the IFC.

The Inter-American Investment Corporation (IIC, an arm of the IDB) lent US\$35m to a locally owned firm called Molinos Cañuelas in July 2006. This company serves the agricultural commodity export market as well as the domestic market with branded products. This was the first deal of the IIC in Argentina in many years.

Offshore banks

Most banks operating in Argentina had branches in centres such as the Cayman Islands, Nassau, Jersey or Uruguay, in order to offer offshore services to their customers. However, since the devaluation and the onset of exchange controls in 2002, all offshore operations—except for debt repayments (which are unrestricted)—are now subject to Central Bank approval.

Despite government barriers, Argentines are still sending money abroad, through informal channels that bypass official controls. Stringent Central Bank controls limiting the movement of capital—that remain in place for this sector though they have been relaxed in other cases—have encouraged many brokers and private banking arms to move their offices to Montevideo. Brokers such as