Report on Banks

May 2020

BANCO CENTRAL
DE LA REPÚBLICA ARGENTINA

Executive Summary

- To mitigate the social and economic effects of the adverse context deepened by the COVID-19 pandemic, the BCRA together with the National Government has been implementing a broad set of policy actions that seek, among other objectives, for the ensemble of financial institutions to increase credit flow to the most vulnerable households and businesses, while protecting their savings, and preserve, in turn, the necessary conditions to sustain financial system's resilience.

- It is worth noting that, even before the shock caused by the pandemic, the BCRA had implemented a set of policies with new priorities, seeking to address the downturn the Argentine economy has been experiencing since mid-2018. Since late 2019, the BCRA has been subsequently cutting the monetary policy interest rate -from 63% in December to 38% as of March 2020- and has implemented new tools that are allowing to expand private sector's access to credit in more favorable financial conditions, with a focus on MSMEs. These actions have been enhanced since the end of first quarter, significantly extending financing at interest rates below those observed in the market, reversing the usual pro-cyclical dynamics of credit, while implementing minimum interest rates that protect the real value of time deposits.

- In May, the financial system's stock of loans to private sector in pesos increased by 2.6% in real terms (month end). This positive performance has been observed for three consecutive months, an unprecedented dynamic in the last 2 years. Furthermore, after 20 months, a year-on-year increase in the stock of loans to private sector in pesos in real terms was recorded once again in May. This performance was influenced by the special credit line for MSMEs, accumulating disbursements for $218 billion as of May, totaling $325 billion at the time this Report was published. Given the positive results obtained, the BCRA decided in late June to expand its scope and incorporate loans to non-MSMEs, provided these funds are used to purchase machines and equipment produced by local MSMEs. Likewise, the BCRA launched in early May the so-called MSME Plus (*MiPyME Plus)*, totaling disbursements for approximately $1.6 billion at the end of July, including about 3,300 MSMEs into bank financing.

- Zero-rate loans for workers registered with the simplified tax regime (*monotributistas*) and for self-employed totaled almost $57 billion in the last days of July, of which about $44 billion had been disbursed -representing more than 7% of credit card financing in pesos- through more than 472,000 loans as of the same date. This new line promoted by the National Government together with the BCRA favored greater bancarization, through the issuance of 154,000 new credit cards.

- As to the measures designed to protect households and businesses' savings in pesos, the BCRA established a minimum interest rate for natural persons' time deposits of up to $4 million since early May (until April this rate applied to deposits below $1 million). This regulation was extended to all private sector time deposits in pesos, without limit of amount by mid-month. The BCRA decided to rise these minimum rates in early June, and more recently in August. Hence, the average interest rate on time deposits in pesos climbed about 7 p.p. compared to the April 2020 average. Following this, time deposits gained an outstanding dynamism, growing by 7.3% in real terms, largely explaining the larger stock of total private sector deposits in pesos (+3.3% in real terms).

- The financial system is showing liquidity and solvency margins significantly above local prudential regulation requirements, which is in line with international standards. In May, the system's compliance with regulatory capital stood at 22.9% of risk-weighted assets. Regulatory capital slack is underpinned by prudential measures aimed at setting the conditions to face potential negative effects from the pandemic, based on requirements for additional capital conservation margins and dividends distribution limitation, until the end of 2020.

Published on July 31, 2020.
The data reported are provisional and subject to changes. Information corresponds to end-of-month data. Data of charts and **Latest Regulations** of this issue. Statistics Annexes for the financial system and the ensemble of financial institutions. **Glossary** of abbreviations and acronyms.

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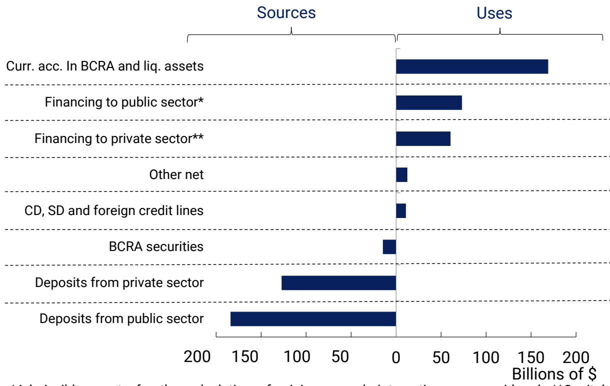
I. Financial Intermediation Activity

In May, the ensemble of financial institutions continued to develop its activities under the measures adopted to face the COVID-19 pandemic.[1] In recent months, the BCRA has been taking actions to face the shock, mitigating thus its negative effects on households and businesses, and it should be pointed out that there were increases in time deposits in pesos and in private sector loans in pesos -especially to MSMEs- in May (for further details, see "Section II. Credit and portfolio quality").

Figure 1 | Estimated monthly cash flow (May-20)
Items in pesos (in $ from May-20) - Financial system

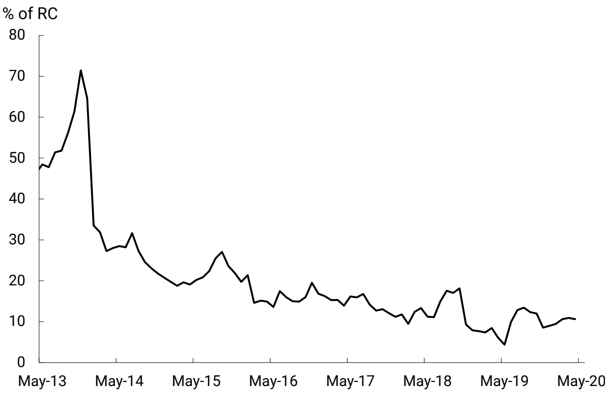


*Admissible assets for the calculation of minimum cash integration are considered. **Capital adjustments and accrued interest are excluded. Source: BCRA

In this regard, and based on the estimated monthly flow of funds for items in national currency,[2] the increase in (public and private sector) deposits in May was the most prominent source of funds for the financial system (see Figure 1). These resources were applied to increase both institutions' balance of current accounts at the BCRA and the stock of loans (to private and public sectors).[3]

In the context of this flow of funds, total assets of the financial system grew 3.1% in real terms (+ 4.6% in nominal terms) in May, mainly driven by the performance of public institutions.

Figure 2 | Foreign currency assets - Foreign currency liabilities + Foreign currency forward position
Financial System



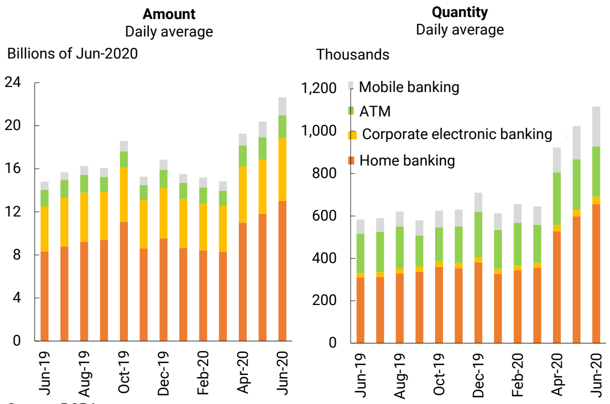
RC: Regulatory Capital. Source: BCRA

The share of items in foreign currency continued to lose weight in the balance sheet of the financial system during May. Assets in foreign currency totaled 21% of total assets in the month, down 1.4 p.p. against April. Liabilities in the same currency stood at 19.8% of total funding (liabilities plus net worth), down 1.3 p.p. against last month. When including off-balance sheet foreign currency forward purchase and sale transactions, the spread between assets and liabilities in said currency totaled 10.6% of the Adjusted Stockholders' Equity (ASE) in May, slightly below April's level (see Figure 2).

1 It should be noted that during May, there have been changes to the preventive and compulsory social lockdown (ASPO), with a greater number of productive branches partially resuming their activity. For further details see Executive Order 459/2020.
2 Prepared with differences in balance sheet stock expressed in uniform currency.
3 Considering monthly changes in foreign currency denominated items in the aggregate balance sheet, the main sources of funding for financial institutions in May came from lower credit to private sector and liquidity. Resources in foreign currency were mainly used to provide for the monthly decrease in private sector deposits.

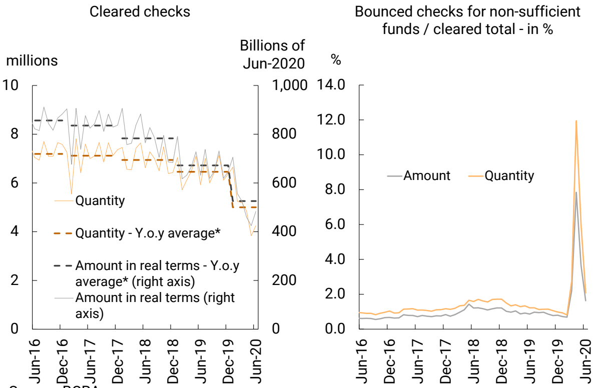
Regarding Payment System transactions, like in April and May, the number and amount of instant transfers grew significantly in June (latest available information) (see Figure 3). In particular, the daily average of instant transfers in pesos climbed 11.1% in real terms and 9% in number compared to May. Among the different channels through which these transfers are made, mobile banking and internet banking dynamics stand out. In turn, cleared checks increased in June (though the level is still below the annual average) and the ratio of bounced checks for insufficient funds fell significantly in terms of the total cleared (see Figure 4). This ratio totaled 1.6% in amount in June (-2 p.p., m.o.m.) and 2% in number (-4 p.p., m.o.m.).

Figure 3 | Instant transfers in domestic currency



Source: BCRA

Figure 4 | Cleared and bounced checks



Source: BCRA

II. Credit and portfolio quality

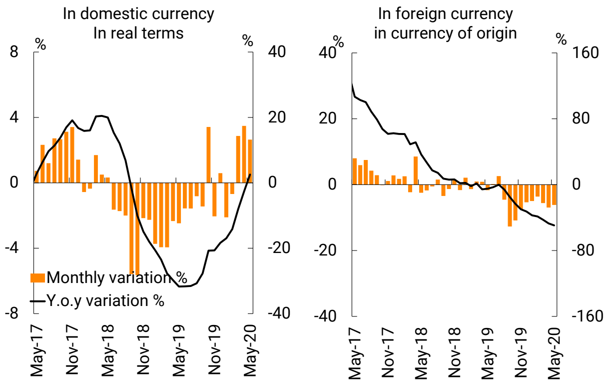
In the context of measures implemented by the BCRA throughout 2020, the stock of loansto private sector in pesos grew 2.6% in real terms (+4.2% in nominal terms) during May in the financial system as a whole (see Figure 5).[4] Loans in pesos expanded thus in real terms for the third consecutive month, a performance that has not been observed since early 2018. Promissory notes and credit cards led the evolution in May.

In this sense, the special line for MSMEs with a 24% interest rate (ANR) launched by this Institution at the end of March (with an interest rate below the market),[5] accumulated disbursements for $218 billion (equivalent to more than 10% of loans to companies) as of May. This amount totaled approximately $325 billion upon the publication of this Report -end of July- (almost $8 billion correspond to health service providers, see Figure 6), with almost 200,000 loans granted under this scheme. Additionally, $11.1 billion, not yet disbursed, have been approved, with additional applications in process for almost $10,5 billion. Following the positive results of this initiative, the BCRA decided to expand its scope by approximately $100 billion in late June, adding the possibility

4 Including adjustments of principal and interest accrued.
5 See Communication "A" 6937 and amendments.

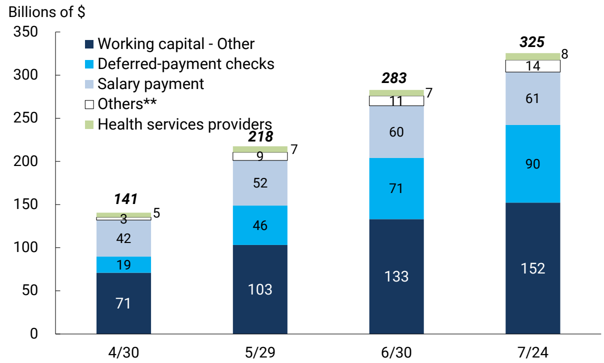
of financing non-MSMEs, provided those funds are used to acquire machines and equipment produced by local MSMEs.[6]

Figure 5 | Stock of loans to the private sector by currency*



*Not seasonally adjusted.

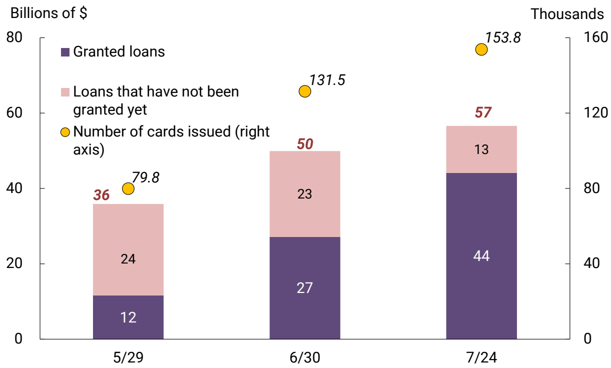
Figure 6 | Special credit lines for MSMEs and health service providers* - Cumulative disbursements by destination



In early May, the BCRA decided to launch an additional credit line, called *MiPyME Plus* (MSME Plus), seeking to channel loans at preferential interest rates to those companies without bank financing.[7] This new tool totaled disbursements for approximately $1.6 billion by the end of July, allowing some 3,300 MSMEs access to bank financing (of which just over 2,400 did so with FoGar sureties). Additionally, some $300 million have already been approved under the umbrella of this credit line, with pending disbursement.

The 0% interest credit line for workers registered with the simplified tax regime (*monotributistas*) and for self-employed, another initiative implemented by the National Government together with the BCRA to mitigate the economic effects of the pandemic, accumulated a total amount of almost $57 billion by the end of July, of which almost $44 billion had already been disbursed through some 472,000 loans (see Figure 7). This new credit line promoted by the National Government together with the BCRA allowed greater financial inclusion through the issuance of 154,000 credit cards for customers who did not have one with the grantor.

Figure 7 | Total loans granted to self-employed workers and members of the simplified tax regime - *monotributistas*- at 0%*



These initiatives taken by the BCRA were partially reflected in the results of the 2020 second quarterly Survey on Credit Conditions -conducted at the end of June-. Thus, the surveyed institutions showed a reduction in the spreads on the cost of funding and commission fees in the second quarter of the year compared to the first, both in household and corporate loans.

6 See Communication "A" 7054. Furthermore, The BCRA established that financial institutions are obliged to grant this credit assistance to MSMEs with FoGar sureties and, in the case of MSMEs that have already been granted this loan, they will be able to access it again for the amount of their entire payroll.
7 See Communication "A" 7006.

The sum of the disbursements made until the end of July in the context of the aforementioned official initiatives, allowing households and businesses to access loans at interest rates much lower than those observed at the end of 2019, was equivalent to over 16% of the total financing in pesos channeled through the financial system on the same date.

In year-on-year terms, the stock of loans to private sector in domestic currency showed a 2.5% rise in real terms in May. It is worth noting that credit lines in pesos have not grown year-on-year in real terms for almost two (2) years, partly as a result of the set of initiatives that the BCRA has been implementing since the beginning of the year, in line with National Government actions.

On the other hand, the stock of loans to private sector in foreign currency fell 6.2% in May and 49.5% y.o.y. -in currency of origin-.

Total loans to private sector represented 35% of the financial system's total assets at the end of May, slightly below last month (-0.7 p.p.) (see Figure 8). Loans in pesos reached 28.5% in May, remaining stable so far this year.

Figure 8 | Stock of loans to the private sector/ Total assets

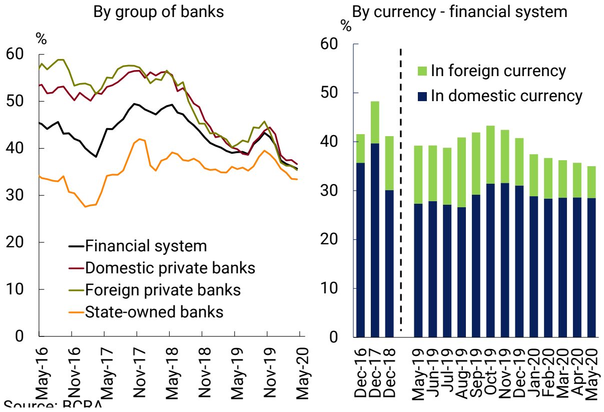
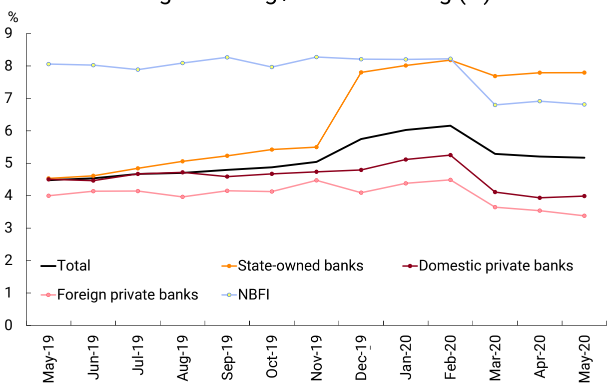


Figure 9 | Non-Performing loans to the private sector
Non-Performing financing / total financing (%)



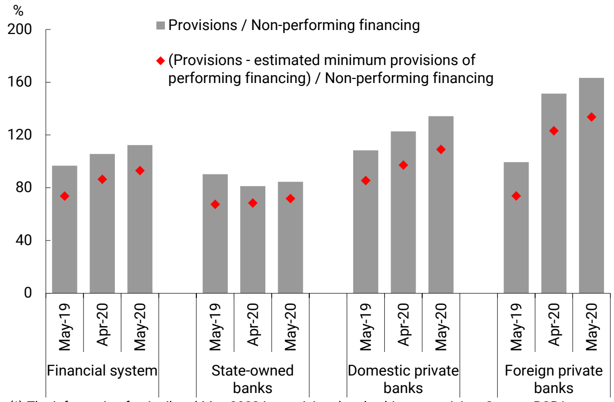
(*) The information for April and May 2020 is provisional and subject to revision. NBFI: Non-banking financial institutions. Source: BCRA

In May, the ratio of non-performing loans to private sector stood at 5.2% of the total portfolio[8], in line with the records of the two previous months (see Figure 9). This ratio did not present significant changes from April when considering the different groups of financial institutions. It is worth noting that the BCRA introduced in March changes to debtor classification parameters, as part of the measures implemented to temper the impact of the pandemic on the financial situation of households and businesses.[9]

8 Provisional information.
9 See Communication "A" 6938.

It should be noted that, among the dimensions that make the financial system resilient against challenging macroeconomic scenarios like the current one, the stock of accounting provisions (originated by both the performing and non-performing portfolio) represented 112.4% of the financial system's non-performing loans to the private sector in the month, up 6.7 p.p. against April (see Figure 10).[10] On the other hand, the estimated stock of provisions for the non-performing portfolio[11] stood at 93% of said portfolio in the month, up 6.6 p.p. against April. Non-performing loans not covered by provisions for this portfolio are estimated at only 1% of the ASE in May (1.6% of the regulatory capital surplus).

Figure 10 | Provisioning and non-performing portfolio
By group of institutions (*)



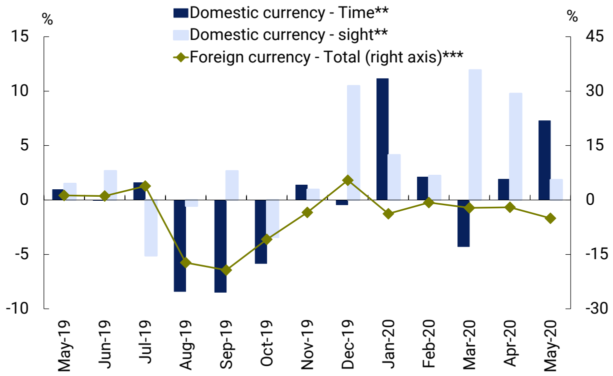
(*) The information for April and May 2020 is provisional and subject to revision. Source: BCRA

In May, the financial system's exposure to public sector represented 9.7% of total assets, up 0.6 p.p. against April, although slightly lower than the level observed 12 months ago. The financial system's exposure to this sector, net of the stock of public sector deposits, continued to be negative, equivalent to 2.5% of total assets in the month.

III. Deposits and liquidity

In May, private sector deposits in pesos grew 3.3% in real terms (4.9% in nominal terms), with a 7.3% rise in time deposits (8.9% in nominal terms, see Figure 11) and 1.9% in sight deposits (3.4% in nominal terms). The boost in term deposits mainly reflected the effect of the measures adopted by the BCRA to protect the population's savings in pesos. In particular, the BCRA established in early May a minimum interest rate for natural persons' time deposits of up to $4 million (affecting deposits under $1 million until the end of April)[12]. This regulation was extended to all private sector time deposits in pesos, with no limit on the amount by mid-month. Furthermore, the BCRA decided to increase these minimum rates in early June, and August[13]. The monthly performance of sight deposits was influenced by the collection of the Emergency

Figure 11 | Stock of private sector deposits
Monthly % change - By currency*



**Not seasonally adjusted. **In real terms. ***In currency of origin. Source: BCRA

10 Provisional information.
11 Pursuant to minimum loss loan provision (IFRS criteria for Group A institutions are not used).
12 For further details see Communication "A" 7000.
13 For further details, see Communication "A" 7018. The minimum interest rate was set at 26.6% ANR -30% EAR- (equivalent to 70% of the LELIQ interest rate) in May. Following this, the minimum rate for time deposits in pesos in Group A institutions and GSIBs not included in this group was set at 30.02% ANR -34.5% EAR- (79% of the LELIQ rate, see Communication "A" 7027) since June, except for debtors of the special credit lines defined by the BCRA; the remaining

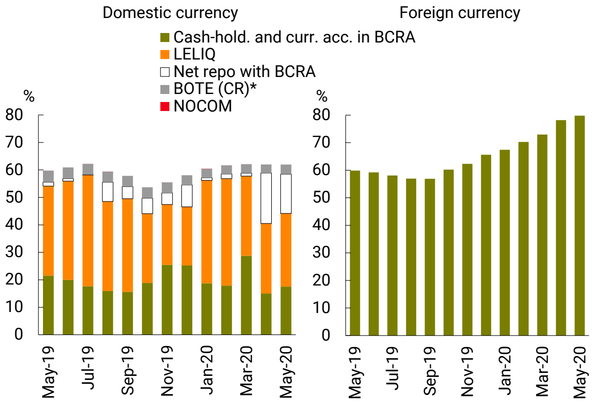
Household Income (IFE),[14] added to a higher precautionary demand for more liquid assets in the context of a health emergency (COVID-19 outbreak). On the other hand, private sector deposits in foreign currency fell by 5% (in currency of origin) in May. Total public sector deposits climbed 20.7% in real terms compared to April (22.6% in nominal terms).[15] Thus, the stock of total deposits rose 4.1% in real terms in the month (5.7% in nominal terms).

In the last 12 months to May, the stock of private sector deposits in pesos increased 18.7% in real terms (70.2% y.o.y. in nominal terms), with a 42.8% rise in sight deposits (104.8% y.o.y. in nominal terms) and a 3.9% drop in time deposits (+37.8% y.o.y. in nominal terms). On the other hand, private sector deposits in foreign currency -in currency of origin- accumulated a 44.7% fall from May 2019. Public sector deposits decreased by 4.7% y.o.y. in real terms (+36.6% y.o.y. in nominal terms). Thus, the total stock of deposits in the financial system fell 4.3% in real terms in the last 12 months (+37.3% y.o.y. in nominal terms).

The financial system's relative share of private sector deposits in pesos in total funding (liabilities plus net worth) climbed in the month, accumulating a 7.9 p.p. rise in the last year, reaching 46% in May. Furthermore, following the measures introduced by the BCRA to encourage people's savings in domestic currency, detailed above, the weighting of households and businesses' time deposits in the total funding of the financial system increased once again.

The liquidity of all financial institutions remained at high levels. In May, the broad liquidity ratio[16] represented 65.8% of total deposits (62% for the segment in pesos and 79.8% for items in foreign currency), plus 0.1 p.p. against April (without changes in the ratio in pesos and +1.6 p.p. in the indicator in foreign currency). In the context of the health emergency, there were movements in the different components of liquid assets throughout the month, with effects on broad liquidity composition.[17] There was a growing relative share of financial institutions' current accounts at the BCRA and of LELIQ holdings between ends of month, offset by a lower weighting

Figure 12 | Financial system liquidity
In % of deposits



*CR=Cash reserves. Source: BCRA

financial institutions may choose to pay that interest rate to depositors. Since August, the minimum interest rate on natural persons' time deposits of up to $1,000,000 in Group A institutions and G-SIBs not included in this group was set at 33.06% ANR -38.5% EAR- (87% of the LELIQ rate, see Communication "A" 7078).

14 For further details see Executive order 310/2020.

15 Performance explained, in part, by transfers from the BCRA to the National Treasury (temporary advances and profits) in the context of the health emergency.

16 Considering liquid assets, compliance with minimum cash requirements and BCRA's instruments, both in domestic and foreign currency, in terms of total deposits.

17 The BCRA introduced a number of measures during the month. The minimum cash requirement compliance for Money Market Mutual Funds sight deposits was eliminated in late April (see Communication "A" 6992). The BCRA established a new minimum cash requirement franchise for 40% of the loans granted to MSMEs at a rate of up to 24% provided they are not included in the "Financial System's Central Debtors Database" (see Communication "A" 7006). Finally, the Institution introduced changes to the LELIQ holding (either to comply with minimum cash requirement or surplus). Regarding the latter, the BCRA established, on the one hand, that financial institutions may comply with through LELIQ the full minimum cash requirement time deposits in pesos since mid-month (see Communication "A" 7018). On the other hand, institutions must reduce since May 11 their LELIQ surplus position by an additional 1% compared to their position as of March 19.

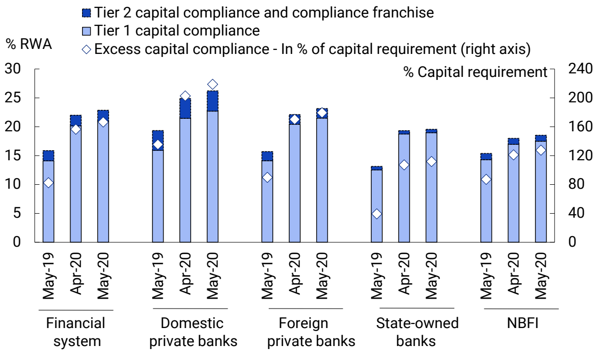
of net repos with the BCRA (see Figure 12). In the last twelve months, the broad liquidity ratio increased 6 p.p. of deposits (+2.3 p.p., y.o.y. for the segment in pesos and +20 p.p., y.o.y, for items in foreign currency).

IV. Solvency

Financial system' solvency ratios increased in May. The Regulatory Capital (RC) reached 22.9% of risk-weighted assets (RWA), up 0.9 p.p. against April and 7 p.p., y.o.y.), with a surplus capital adequacy climbing to 167% of the minimum regulatory requirement. This performance is partly supported by the implementation of local macroprudential regulations that limit, since last March until the end of 2020, dividends' distribution.[18] Through this action, the BCRA aims for financial institutions to continue providing credit to the economy and temper the pro-cyclical nature typical of all financial systems, in line with the measures taken by other Central Banks and regulatory bodies in the context of the COVID-19 shock.[19]

Regarding capital composition, almost 92% of its total compliance responds to Tier 1 capital, with a greater capacity to absorb potential losses.[20] Furthermore, the capital slack concerning regulatory requirements was maintained in all the ensemble of financial institutions (see Figure 13). Besides, the capital conservation buffer continued to be wide and widespread among institutions (including the additional one for systemic institutions).

Figure 13 | Compliance with regulatory capital



Tier 1 capital compliance: Basic Net Worth.
Tier 2 capital compliance: Complementary Net Worth.
NBFI: Non-Banking Financial Institutions. Source: BCRA

It is worth mentioning here that the financial system's solvency and profitability performance during 2020 happens in a scenario different from the year before. During 2019, although the system proved to be resilient in terms of liquidity and solvency to different episodes of financial and exchange rate stress, it did so amidst a significant fall of credit in pesos in real terms (-18% between ends of year) and private sector deposits in pesos (-11% in the same period, especially time deposits, falling -19%). In contrast, in the context of new BCRA policy guidelines, there has been a credit recovery in real terms and a sustained increase in deposits in domestic currency, with ongoing efforts to financially include a large group of households and small enterprises that had no access to bank financing. These developments are reversing the system's typical pro-cyclical behavior, contributing positively to financial stability conditions.

18 Communications "A"6939 and "A" 7035.
19 For further details, see "COVID-19 Pandemic: Financial Stability Implications and Policy Measures Taken", FSB, July 2020.
20 Consisting mainly of ordinary shares and income.

The financial margin of the ensemble of institutions represented 11.2% a. of assets in May (down 0.2 p.p. against April), leading to 11.8% a. of assets in the first 5 months of 2020. Overall, there has been a reduction in interest income in pesos in terms of financial system assets in the last few months, totaling 9.4% a. throughout the year. This performance reflects, in part, the effects of the monetary and financial policy guidelines the BCRA has been implementing since late 2019 (marked reduction in policy interest rates, new incentives and tools to improve access to financing, among others). In turn, income from securities represented a relevant source of net income for institutions so far in 2020. These are partly explained by the accrual of yields and changes in prices of public securities (particularly in April and May), from income derived from BCRA portfolio holdings, as well as from repo transactions with this Institution.[21] The performance of these last two concepts is also influenced by the monetary and financial policy management of this Institution (see sections II and III for further development).

Regarding financial system's interest expenses in terms of assets, although there is a certain reduction in May compared to April, it was much lower than the significant fall observed during the previous month. It is worth mentioning here that, since mid-April, the BCRA established a minimum interest rates for depositors, seeking to create a context that prevents losses in relative performance of their savings.[22] The effects of these measures began to show on this line of institutions' expenditures, and they are expected to be fully reflected since mid-year (see Section III for further development). In this regard, the financial system interest expenses stood at 8.7% a. of its total assets throughout 2020.

Financial system's income from services represented 1.8% a. of assets in May, leading to 1.9% a. of assets in the aggregate of the first five months of 2020.

Loss loan provisions for the ensemble of financial institutions grew 0.6 p.p. of assets in the month, to 2.5% a. of assets. Thus, these expenditures totaled 1.9% a. of assets accumulated between January and May 2020 for the financial system. On the other hand, administrative expenses fell slightly in May compared to April, to 6.7% a. of assets throughout 2020.

Financial system's OCI was positive in May, although lower than in April (when it showed an extraordinarily high level[23]). In the aggregate of the five months of 2020, the financial system accrued negative OCI, of around 0.3% a. of assets.

21 These last transactions are reflected in repo premiums in financial institutions' income statement.
22 Communication "A" 6980, Communication "A" 7000 and Communication "A" 7018. Communication "A" 7027 will become effective in June 2020.
23 For further details, see Report on Banks/April 2020.