



Financial Stability Report

Second Half 2008



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, with statistics up to the end of December 2008, will be on March 31, 2009, on the Central Bank website.

Buenos Aires, September 30, 2008

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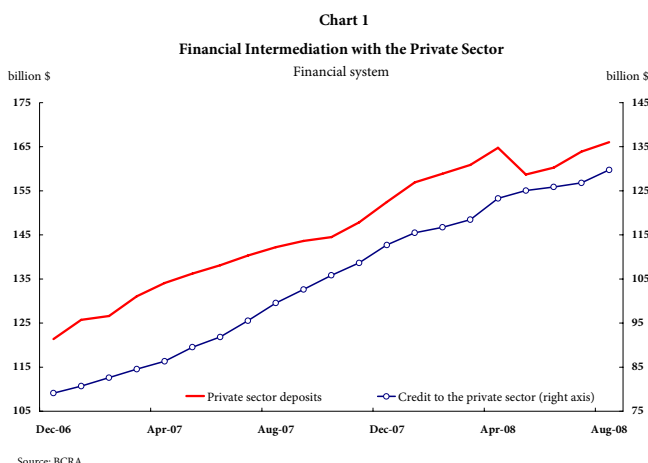
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Central Bank Outlook

The recent episodes of stress in the domestic financial variables have been concrete evidence to assess the efficacy of the overall strategy and the specific measures that the Central Bank is carrying out. Both the impact of an extraordinarily critical period on the international markets and the sharp fall of the private sector deposits during the second quarter of 2008 have been overcome, to restore the monetary and financial stability of the Argentine economy. These developments have enabled it to continue on the economic growth trajectory.

The Central Bank has carried out a set of prudential countercyclical policies during recent years, among which the accumulation of international reserves and building a solid financial system with limited mismatches stand out. On these pillars a number of instruments were set up which have enabled a robust and flexible framework to adequately face possible adverse shocks, all subject to a risk management focus. Specifically, facing the abrupt mismatch in the demand for money exhibited in May, matched by the fall of private sector deposits and an increased demand for foreign currency, the Central Bank decided to use a broad arsenal of measures that successfully targeted both fronts: attacking the expectation of a depreciation of the peso, stabilizing the demand for money, and providing liquidity.

The measures adopted by the Central Bank were thus capable of reversing the May scenario, which was neither in connection with the financial system conditions nor with the fundamental economic variables. Specifically, 10 measures were launched that are listed below: 1. The repo market was adapted, providing liquidity at a fixed interest rate (up to \$3 billion) and variable rate (BADLAR rate); 2. Lebac and Nobac maturities were renewed partially, carrying out repurchases of these securities; 3. Limits for operations on the futures market were extended, for both the Central Bank and the agents associated with some of the counterparties; 4. The reference exchange rate applicable to futures and forward transactions between the Central Bank and its counterparties was allowed to be set by EMTA (Emerging Market Traders Association); 5. The open market operations for trading government bonds by purchases settled in pesos and in dollars on the secondary market was set up (an additional tool to provide liquidity); 6. The minimum cash reserve position for June and July was unified as a two-month period, which enabled better liquidity management; 7. A repo loan mechanism in dollars was created with the purpose of reducing the expectations of a depreciation of the peso; 8. The Central Bank started to operate on the non-deliverable forwards (NDF) market with transactions at up to a one year term, with



counterparties with a credit rating not less than AA-; 9. A new repo window allowing collateral with certain issues (Bogar and Guaranteed Loans) not used for traditional repos was established; 10. The menu of terms for reverse repos was expanded, adjusting their costs.

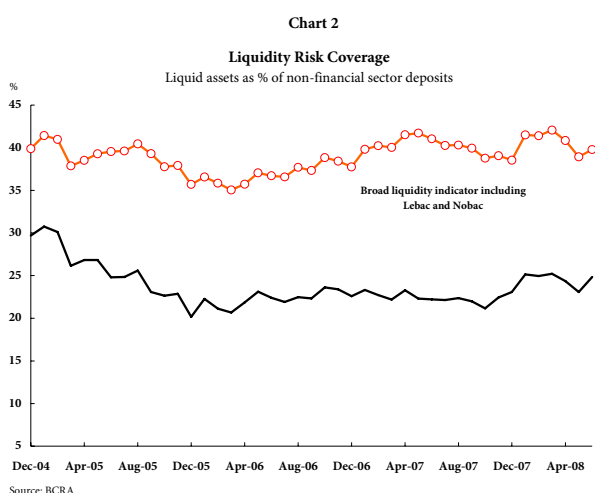
This resulted in a lower volatility of the exchange rate, stabilization of the monetary variables (including the reversal of the outflow of deposits), less pressures on the interest rates, and therefore the preservation of the overall momentum of credit to the private sector.

The world economic situation is still worsening sharply, with no prospect of a reversal in the short term seen, which provides grounds for the perception of facing an almost unprecedented crisis. The stress on the financial markets marks new peaks as time goes by, due to the overall scenario of uncertainty that the combination of the financial crisis, high inflation levels and the strong risk of a recession in the central economies provides. The major central banks in the developed countries are turning towards more flexible strategies like that applied in Argentina. From this sharply negative scenario the emerging economies have in general started to note certain consequences, with the situation of those more dependent on external funding standing out.

Based on the prudent financial policy the Central Bank has adopted, the financial system continues exhibiting a high degree of strength, although it operates in an overall framework dominated by the profound deterioration of the global financial conditions. The local banks, backed by adequate liquidity and solvency levels, continue deepening the funds channeled to firms and households. Bank credit to the private sector maintains its rising trend (30% y.o.y.), despite showing some deceleration after four years of a high and persistent rate of growth. These loans were equivalent to 12% of the GDP in mid 2008, presenting a high growth potential for coming years. The increase of funding by deposits still explains this trend, during a period when the international financial conditions lead to a pause in obtaining funds on the capital markets.

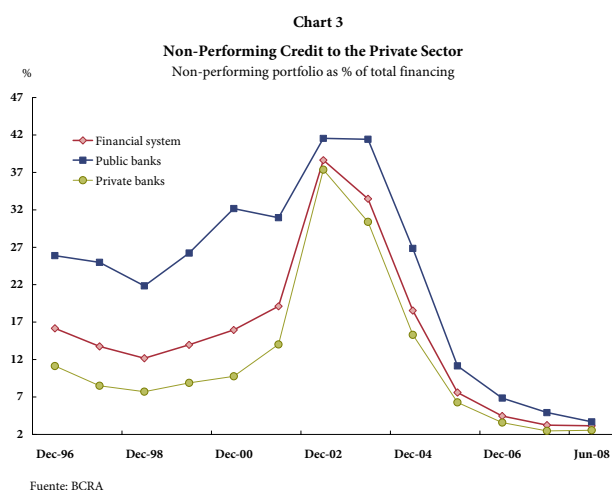
The expansion of bank credit to the private sector continues happening in a framework of solid levels of cautionary liquidity. The liquid assets of the banking system totaled 25% of the deposits in mid 2008, a figure that increases considerably to 40% if broad liquidity that includes the Lebac and Nobac stock in bank portfolios is observed. The Central Bank measures consolidate the liquidity reserve role that these securities have, to become an effective tool in a context of financial turbulences that exert a negative impact on the inter-bank liquidity markets.

The improvements shown by the labor market and the expansion of the economic activity of the different



production sectors, combined with the moderate levels of debt in these sectors, enables the banks to continue increasing their channeling of funds in a limited risk context. As a response to this the share of loans to the private sector in an irregular situation is at a historical minimum (3.1%). Corporate credit continues exhibiting improvements in their performance, while the quality of the household loan portfolio has started to show a slight worsening, mainly by the consumer lines. The falling trend in irregularity of aggregate financing of the private sector may be finding a floor, in a scenario of some moderation of economic growth and of credit, following an extensive period of high expansion of both variables.

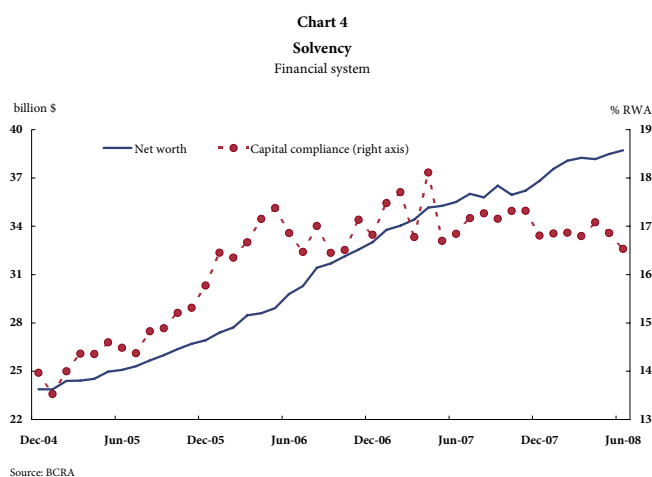
Due to the rules and incentives established by the Central Bank and after four years of persistent and significant reduction, the financial system's exposure to the public sector is 14% of total assets. This development occurs in a context in which the public sector sustains its payment capacity in line with the fiscal surplus and the sources of funding that are available to face financing needs in coming periods.



The financial system persists in a gradual improvement of its position relative to foreign currency risk, a change driven by a smaller mismatch due to the regulations adopted by the monetary authority, in a framework of limited variation in the peso-US dollar exchange rate. The exposure of banks to interest rate risk remains relatively stable, although a fall in public sector assets, a portfolio with longer maturities and fixed interest rates is observed. The market risk exhibited a decline, reflecting the impact of the valuation measures of sovereign bond adopted by the Central Bank, which aim at moderating the impact of the excessive turbulences on banks' net worth.

In line with the Basel Committee sound practices for operating risk management, in April the Central Bank released the minimum standards to manage this risk. The rule calls for the management of this risk to be approached as an integrated discipline separate from other risks, identifying the factors that generate it, and how they are monitored and managed. It also provides the main guidelines that the management process must have. According to the schedule that was set, by the end of 2009 the financial institutions will have to adopt the requirements that were established.

The solvency of the financial system continues its consolidation process as a result of the profits that were obtained and the fresh capitalizations that were received. This process is fundamental in order to strengthen the degree of banking resilience in the face of a possible hostile environment, while it consolidates the foundations to continue with a healthy credit expansion. Capital measured according to the current prudential ruling is 16.5% of risk weighted assets, and thus exceeds



both the domestic requirements and the internationally recommended minimum levels. The profit rate of the banking system was 1.6%a. of assets during the first six months of 2008, with net interest and service revenues that are the main source of funds. The low credit risk assumed enables sustained reductions of the level of loan loss provisions, while operating costs grow together with the wages and operating capacity.

The Central Bank keeps generating measures to achieve a wider scope of the financial system, with the aim of extending the level of banking reach. The categories to establish the minimum capital for each jurisdiction were readjusted and the bureaucratic burden to open new branches was reduced. With the purpose of achieving an offer of a standard product by banks for easier comparison and transparency, a “basic account” is being adopted as part of the rule on savings deposits and wage payments.

The national payments system continues improving its performance, boosted by the ongoing Central Bank efforts to consolidate its efficiency, agility and security. A greater use of electronic instruments for customary transactions is thus observed. In order to make the tasks of managing check transactions even more agile and continue optimizing the uniform federal clearing procedure, there was progress to fully standardize the documents that can be cleared and implement a depository of check images to enable consultations.

Looking ahead, the severe deepening of the uncertainty framework on the international financial markets continues posing a challenge for the adequate development of the economies in the region, and especially for its central bank actions. The preventive strategy that was developed and the possible Central Bank use of the instruments it has available are expected to enable it to protect the domestic economy from the possible threats due to a more hostile international financial scenario. Therefore, an adequate context is expected to sustain the conditions that make for local financial stability.

I. Internacional Context

Summary

The world economic situation continued to deteriorate at a sharp and accelerating pace: tension in the financial markets recorded new peaks, inflationary pressures accentuated along with high prices of raw materials, and the economic slowdown began to show. The weakening of the economic situation became dramatic by September, becoming evident the unprecedented nature of this crisis. With the stability of the financial markets seriously compromised, the US Treasury had to submit a rescue plan by pointing directly to the credit markets. While this helped the prices of the financial assets cease to collapse, the uncertainty surrounding the future evolution of the markets was still critical at the closing of this Report.

In the first half of the year, growth in major economies was higher than originally expected. For US, the wealth effect associated with losses in the real estate and financial markets would be reflected negatively on private consumption. The turbulences originally associated with the subprime mortgages market spilled to the majority of the markets, escalating until critical levels. This became evident in a severe contraction of the stock indexes and in record spreads levels of the interbank markets.

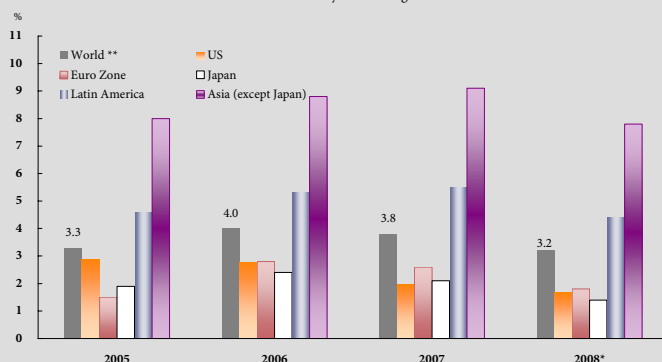
The major Central Banks had to use the tools available to comply with multiple policy goals, prioritizing financial stability. Regarding the Fed, it implemented various measures with the purpose of controlling the problems observed, with special focus on liquidity.

Inflationary pressures intensified at global level, driven by the record prices of raw materials (especially oil and agricultural commodities). Inflation in US reached values around 5%, while in the Euro zone and Japan the hikes of prices achieved levels of 4% and 2% respectively. The core inflation, however, remained controlled in these economies.

The emerging economies, in general, and Latin America in particular exhibited high rates of growth with signs of slowing in recent months. Inflationary pressures became deeper thus increasing the core inflation. This generated Central Bank reactions pointing to more restrictive policies. The stock markets of the emerging economies tended to follow the deterioration observed at global level, albeit with some differentiation by region (with a better performance of the Latin American stock markets which later on diluted). The spreads risk of the emerging economies tended to widen in general, although the decline was greater in those countries most vulnerable to a change in international funding availability.

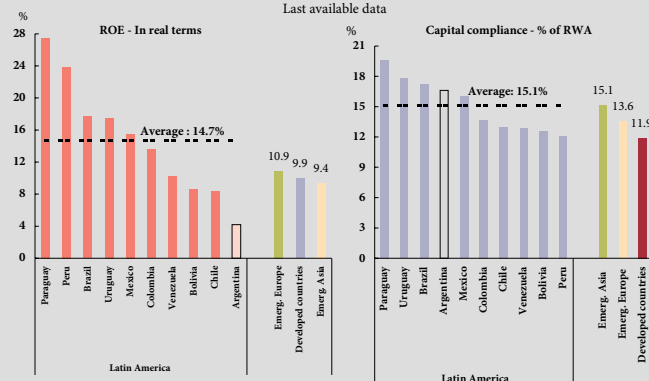
In this scenario, the Latin American banking systems showed some moderation in growth intermediation, while keeping very good indicators of liquidity and solvency. The direct exposure of the banks of the region to assets that are at the eye of the storm is almost zero. Moreover, in the worst of the financial crisis they were profitable, while the solvency levels remain appropriate and exceed international recommendations.

Chart I.1
Real GDP
Year on year % change



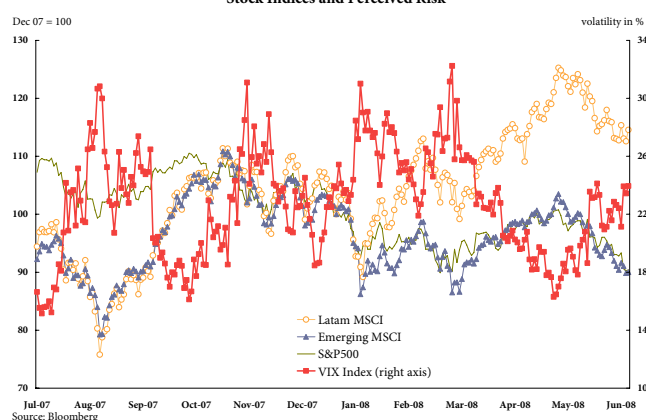
* Forecasted; ** Mentioned rates are calculated using market exchange rates.
Source: Focus Economics

Chart I.2
Profitability and Solvency
Last available data



Note: CPI adjusted
Source: Central Banks, Superintendencias and IMF

Chart I.3
Stock Indices and Perceived Risk



I.1 International Condition

Severe deterioration in the international context, with a slowdown in the economic activity, high inflation and critical situation in financial markets

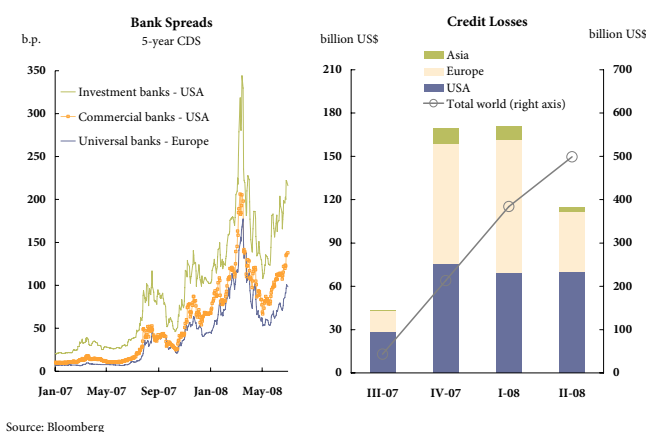
The international context continued worsening, during 2008, deepening the international financial volatility and the disruptions in the credit markets, while inflation increased and the slowdown in the global economic activity intensified (see Chart I.1). In this scenario the prices of raw materials are at historically high levels.

Growth of industrialized countries in the early months of the year was higher than expected, but growth expectations for the remainder of 2008, as well as for 2009, still point to a significant economic slowdown or even, for some countries, the probability of entering a recession. Particularly, the US expansion of the first half of the year responded to the favorable performance of net exports and private consumption which was favored by the tax return that began in May. However, the weakness of the housing market, a weak job market, the loss of wealth from consumers, the transitory nature of tax returns and the more difficult situation of the financial markets would significantly affect private consumption.

The episodes of turbulence on international markets became more frequent and intensified as the year progressed. Thus, the global stock indices reflected concerns about the financial sector problems and the evolution of the activity level, showing significant declines so far this year (see Chart I.3). The S&P 500 index accumulated by September a decline greater than 20% in the year, the expected volatility (measured by the VIX index) was over 20% on average and exceeded the high rates of late 2007 (reaching peaks of 35%). The financial sector (measured by the S&P 500 financials) accumulated a decline of nearly 40% by September.

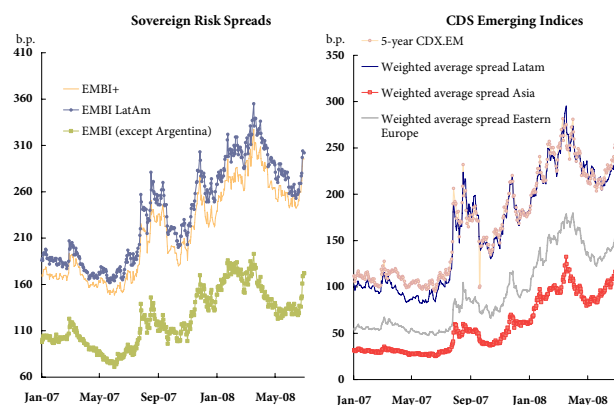
The interbank markets continued to show high spreads, showing a crisis of confidence between the financial institutions (given the uncertainty about the final loss to be recorded by banks) and the precautionary savings (see Chart I.4). This led the Central Banks (with a more aggressive behavior by the Fed) to implement a series of measures to avoid further disruptions in the markets (see Section 1). Despite these measures and given the persistence of various sources of risk (including concerns for bond insurers and the US mortgages agencies Fannie Mae and Freddie Mac), the high risk aversion situation and the deleveraging trend continued.

Chart I.4



Source: Bloomberg

Chart I.5



Source: BCRA from Bloomberg and Markit data

Chart I.6
Emerging Economies Debt Instruments Trading Volume
EMTA - Quarterly

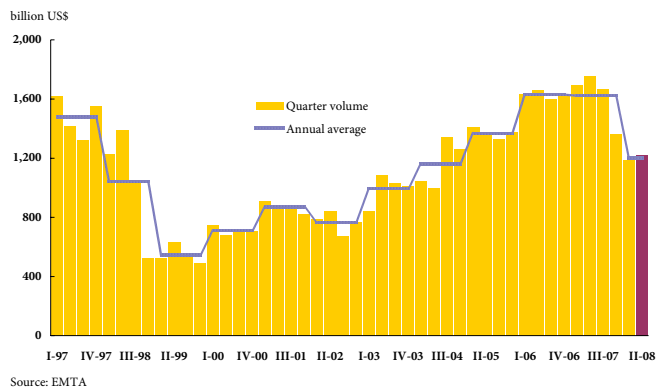


Chart I.7
Commodity Price Index
3-month moving average

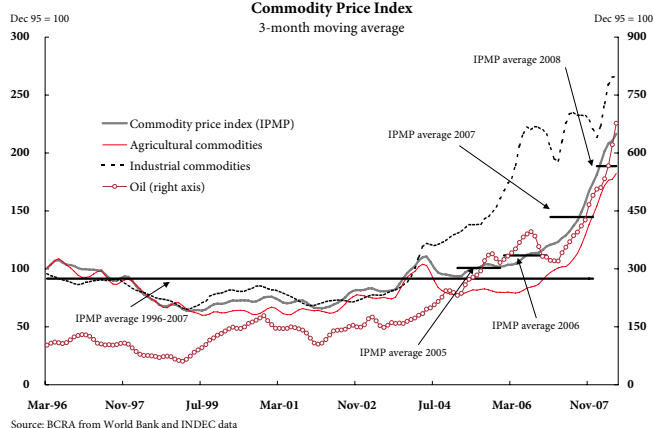
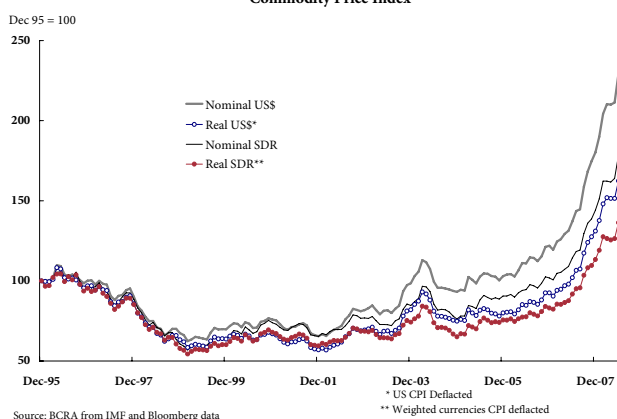


Chart I.8
Commodity Price Index



In this context, the outlook of the US economy is unfavorable reflecting levels of confidence at historical lows. In the Euro zone and Japan the slowdown is also evident despite the positive surprise of the GDP increment in the first three months of the year.

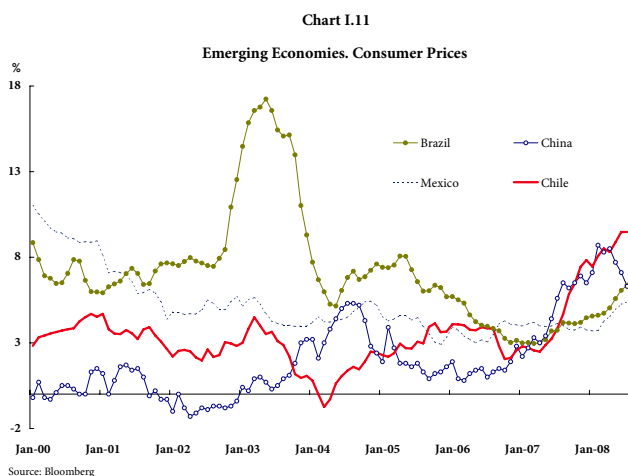
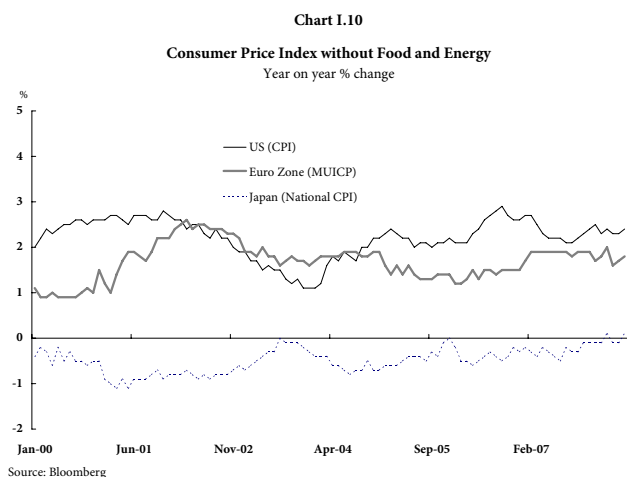
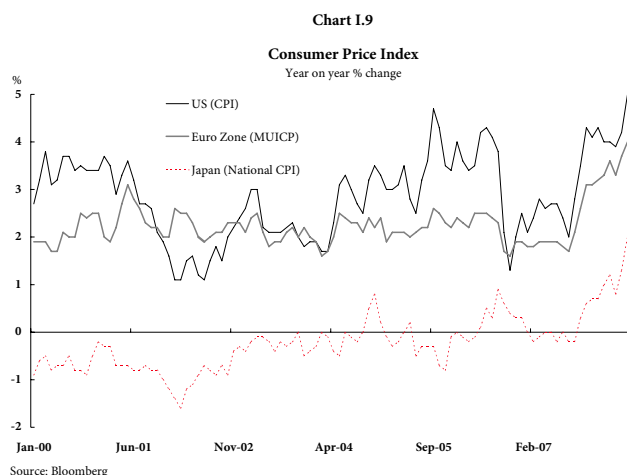
The emerging economies continue to drive global growth, although there are signs of less activity for the coming quarters

Emerging economies continued to be the main drivers of global growth, but would reduce the rate of increase of the economic activity in the remainder of the year. Particularly, emerging Asia would continue to grow steadily, although 0.4 p.p. below the expectation of the beginning of the year, driven by China and India. At the same time, Latin America would expand for the fifth consecutive year at a rate higher than 4%, benefited by the improvement in its fundamentals which contribute to be better prepared than in the past to withstand the current international context and to mitigate the impact on the region of the growth weakness of the industrialized economies.

In the first half of the year, this difference in behavior was reflected in the stock indices. While the MSCI index (in dollars) for the majority of the emerging economies showed a decline of 12.7%; the Latin American stock markets showed an increase of 8%. This demonstrates the concurrence of several factors: low direct exposure in the financial sector of the region to the US subprime mortgages, sound public and foreign finances, credibility in monetary policies and, especially, high commodities prices. However, this relative strength had been losing momentum in recent months.

At the same time, the sovereign debt of emerging economies exhibited a widening of its spreads; whether considering the credit default swap contracts as well as the EMBI+ (see Chart I.5). The spread of the CDX index to 5 years for emerging economies, which in early 2008 was around 180 b.p., was close to 400 b.p. in September. All the regions that make up the universe of emerging economies exhibited similar hikes in spreads, while those countries with larger dependence on foreign capital flows exhibited higher deterioration. Regarding the EMBI+ spread, it recorded peaks above 430 b.p. in recent months from levels around 240 b.p. in early 2008. As regards Latin America, the spread widened 200 b.p. since the beginning of the year, reaching peaks of nearly 480 b.p. in September.

With a more unstable situation and spreads on the rise, the government debt issuance of emerging economies in



international markets tended to shrink. In the secondary markets also decreased the debt trading volume of these economies. According to data from EMTA¹, the trading volume of emerging markets debt stood at US\$2.4 trillion² in the first half of 2008, with a drop of 30% compared to the same semester of 2007 (see Chart I.6).

The raw materials prices remained high, particularly explained by agriculture and crude oil

The prices of the raw materials continued to rise while showing greater volatility (both in agriculture as well as in crude oil). While in mid-July prices reached maximum levels and later on exhibited significant setbacks, the current levels remain high in historical terms and in relation to the already high prices of last year. Thus, the Price Index of Raw Materials (IPMP) developed by the BCRA, which mainly reflects the average evolution of prices in dollars of the most relevant primary commodities in the Argentine exports, in June showed a cumulative rise of 27,2% over December (67.1% y.o.y.) reaching a new record (see Chart I.7). Even when considering the prices in real terms and with a basket of currencies, to avoid the distortions that come from too volatile bilateral exchange rates, commodities prices exhibit a significant cumulative growth in the first half of the year (see Chart I.8).

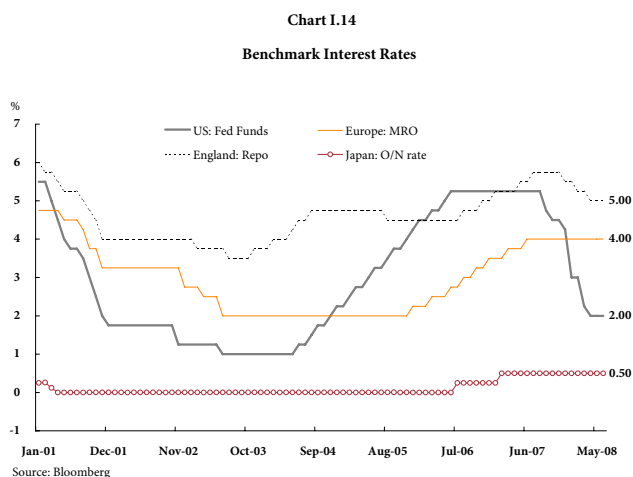
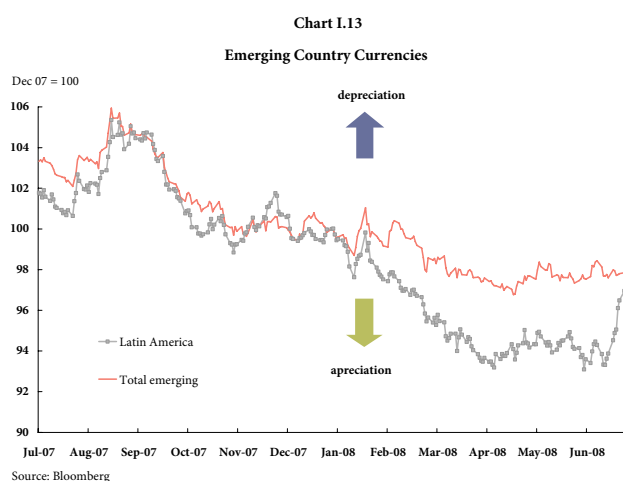
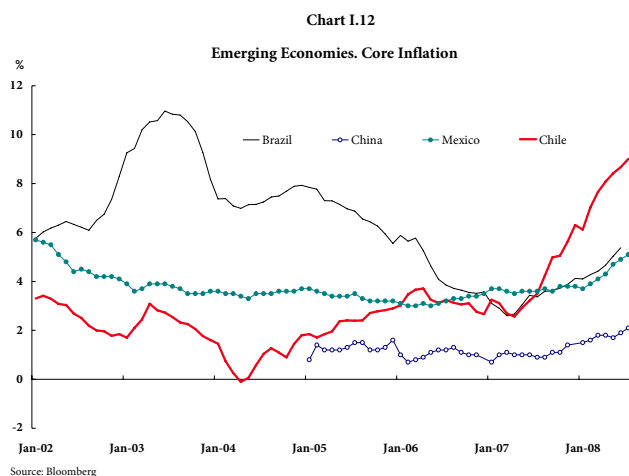
The price evolution of the agricultural products is explained mainly by an increasing demand for food consumption in emerging economies and for biofuels from developed economies, in a context where supply growth was not sufficiently dynamic. Furthermore, the increase in the crude oil price is largely explained by supply problems in key producing areas coupled with a demand that remained on the rise, situation that was magnified by movements of speculative investment. In the coming months, it is expected that the fundamentals continue to give support to prices, mainly in agricultural raw materials, albeit with high volatility.

Global high inflation, driven by raw material prices

The raw materials high prices sustained the increase of the food and energy prices which continued pushing upward the retail inflation both in developed and emerging economies, registering maxima in recent history (see Chart I.9) and being located above the implicit or explicit goal of the monetary authorities. In fact, the increment of the Consumer Price index (CPI) in

¹ Emerging Markets Traders Association

² Million of million



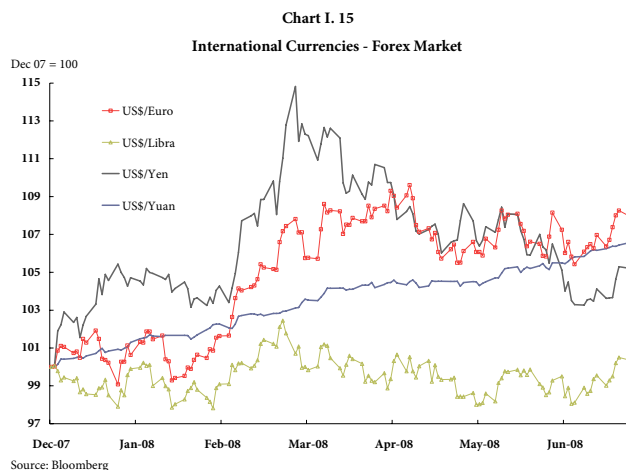
US accelerated during 2008 up to 5% y.o.y. by mid-year, the highest record since May 1991. In the Euro zone inflation also rose so far in 2008 to reach 4% y.o.y., the highest value since 1992, thus doubling the level of the target of the European Central Bank (ECB). Same trend was observed in the retail prices in Japan, registering the biggest hike in the last ten years. However, the inflation measure that excludes food and energy remained relatively contained in these economies (see Chart I.10).

The emerging economies showed an acceleration of both overall as core inflation (see Chart I.11), thus second-round effects would have materialized. In this sense, the inflation in China continued to record high levels, although the rate of increase declined since May, partly due to the decrease in inflation of food by the end of the period. In Brazil, the Enlarged CPI accelerated, registering the biggest change since February 2004, while the core inflation exceeded the levels of the past two years (see Chart I.12). In Chile, both measures of inflation also recorded significant growth, reaching the highest levels of the decade.

The currencies of the emerging economies continued, in general terms, with their appreciation trend though with a remarkable reversal trend towards the last few months. The currencies of the Latin American countries strengthened together with the appreciation of the raw materials (see Chart I.13). It is noticeable that the currencies of the Latin American countries had managed to appraise to 7% by the end of May, but the deterioration of the international context and the moderation in the rise of the prices of the commodities ended up pushing a generalized depreciation.

The high inflation, the lowest levels of growth and the crisis of the financial markets, are particularly challenging in terms of monetary policy

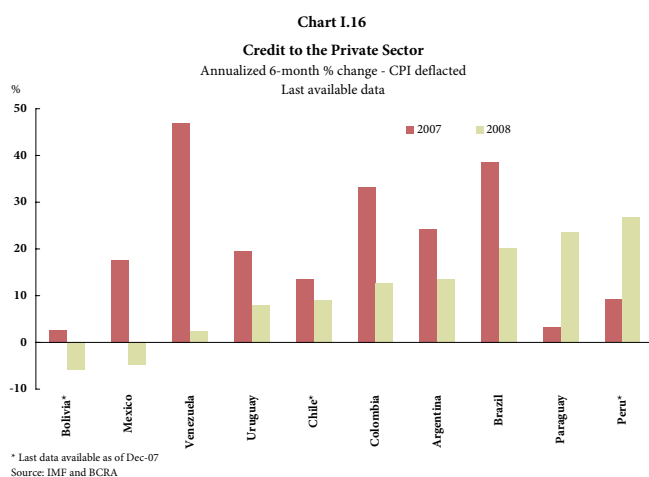
In a global macroeconomic context characterized by the presence of significant fluctuations in the financial markets and in the prices of raw materials, while there are still inflationary pressures and economic slowdown, some Central Banks continued to carry out actions in pursuit of relaxing its monetary policy (see Chart I.14). Faced with the inability to meet several goals simultaneously with limited tools, it is observed up to now that some priority was granted to financial stability over growth. In this sense, the Fed continued the process of cutting the interest rate monetary policy from a level of 4.25% annually, at the beginning of the year, up 2% while additional measures were taken to provide market liquidity and even support to entities of various kinds, not in all cases banking institutions.



The ECB and the Bank of Japan (BOJ) did not change their rates of reference in the first half of 2008, keeping them at 4% and 0.5% annually, respectively. However, facing the financial turmoil, growth in inflation expectations and the reduction of growth expectations, some of the major Central Banks that were decreasing its reference rate discontinued the downward cycle and also implemented measures to provide liquidity and to rescue financial entities.

In this context, it is expected that the Fed does not carry out changes of importance on its reference rates in the coming months, behavior also foreseen for the Euro zone (after the small increase shown in July). Also, supporting the commitment with the financial stability, several monetary agencies would continue carrying out more liquidity injection policies in order to bolster the short term credit markets.

Thus, during the first months of the year, the US currency continued to depreciate, but as the Fed intervened with measures to support the financial system and the risk of slowdown outside of US became more evident, the dollar began to revalue gradually (see Chart I.15).



The monetary authorities of the emerging economies implemented more restrictive policies in response to the acceleration in the pace of price rises. The increase in the respective rates of reference or the requirements of bank reserves constituted some of the measures adopted. Thus, the Central Bank of India increased the repo rate on several occasions, taking it to the maximum of the past six years, while the Central Bank of China raised the reserve requirements ratio five times. The Central Banks of Brazil, Chile and Mexico also increased in several opportunities their interest rate of monetary policy.

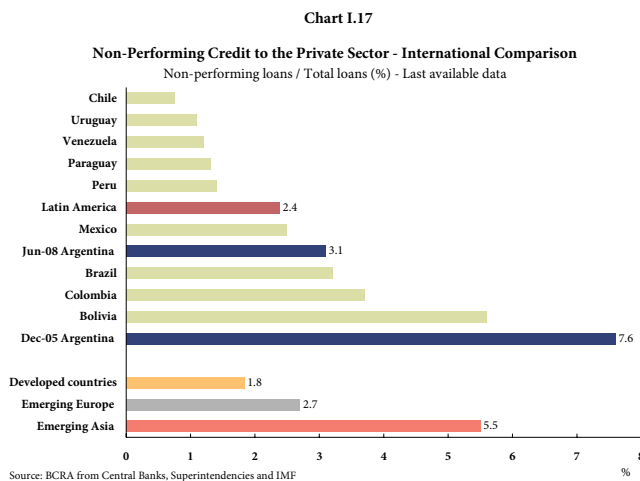
I.2 Latin American banking systems

With some moderation in the growth of financial intermediation, the Latin American banking systems are still solid

The financial systems of the emerging economies continue to show resilience against the effects of turbulence evident in developed economies since mid-2007. This trend is observed particularly in Latin America and, to a lesser extent, in other emerging economies like those in Europe. The latter have an increased relative vulnerability, given their dependence on external resources to increase local funding.

The Latin American banking systems continued to increase its activity with the private sector in the first half, while easing its pace of expansion (see Chart I.16). It is noteworthy that the financial systems in Latin America have an insignificant direct exposure to the assets affected by the crisis in the US. In this context, they are still profitable, with adequate solvency levels that exceed the minimum international recommendations (see Chart I.2).

The scenario of higher inflation was reflected in an increase in interest rates in several countries of the region, which combined with a slowdown in the economic activity, could eventually translate into the capacity of payment of certain sectors and in a higher credit risk assumed by banks. Anyway, the Latin American economies show low levels of irregularities both from a historical perspective and with regard to other emerging regions (see Chart I.17).



An additional consideration comes from the potential negative impact that might have the most unfavorable international scenario on the evolution of the remittances that the region receives in general. In particular, the funding of some financial systems of the region depends partly on such resources, so that the process of intermediation of funds could be affected.

Another potential source of contagion of the economy could be through a contraction of the credit granted by banks that are subsidiaries of international financial institutions of countries whose central economic conditions and/or financials have relatively deteriorated. This situation could be particularly evident in those Latin American economies with greater weighting on foreign financial institutions.

Despite the relative strength of the Latin American banking systems, vulnerabilities still exist on some fronts. The growth of the credit to finance the household consumption in recent years, and the incipient deterioration of the quality of this portfolio have identified the need for a more detailed management by the authorities of the region of such debtors and of the grant funding practices. The inequalities in the access to financial services both geographically and by economic strata continue being one of the challenges faced by banks of the region. The gradual incorporation of these sectors to the financial services constitutes a new source of risk to be managed.

II. Domestic Context

Summary

During the first nine months of the year domestic economic activity exhibited some signs of a deceleration in a scenario of a sharp deepening of the international turbulences. Although economic growth continued at a strong pace, some moderation of the increase in private sector consumption has meant that the rate of economic expansion was slightly lower. Nevertheless, growth during 2008 is expected to be higher than the regional average, for it to be the sixth consecutive year with a sharp increase in the level of economic activity.

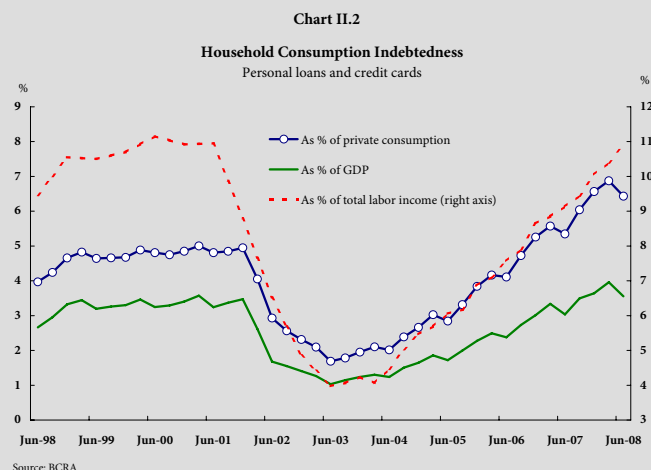
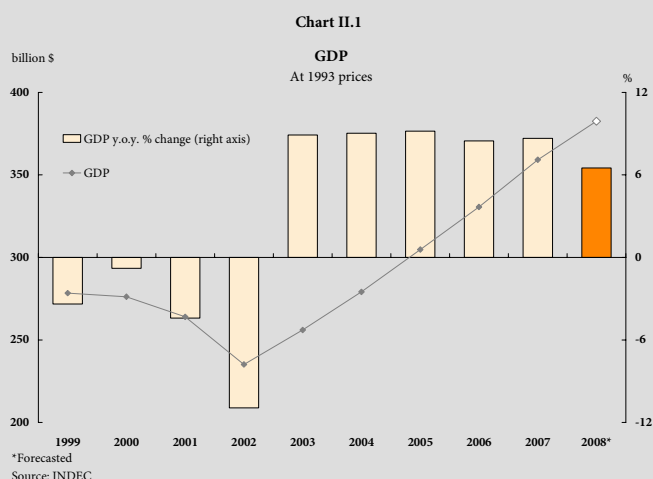
In the early months of the year an episode of a strong and concentrated outflow of private sector deposits was recorded (in May they fell 8%, exceeding what was seen during the worst months of the 1995 and 2001-2002 crises), offsetting a temporary mismatch in the demand for money which led to a significant demand for foreign currency. In this scenario, the Central Bank used different tools, based on the prudential counter-cyclical policies it had undertaken in timely manner (focused on the accumulation of international reserves, building up liquidity cushions and controls of mismatches in the financial system) to achieve a rapid reversal of the outflow of deposits, normalizing the monetary variables and therefore minimizing the impacts on the real economy.

The Central Bank actions were concentrated on two lines particularly. It first attacked the expectations of a depreciation of the peso, stabilizing monetary demand. Then it injected liquidity in order to reduce the pressures on the domestic interest rates and restore credit dynamics. The former target was achieved by providing enough foreign currency to reverse the fears of abrupt exchange rate fluctuations, which would have led to

inflationary pressures and affected the economy severely. The injection of liquidity in pesos was meanwhile carried out by reducing the outstanding stock of Lebac and Nobac, adjusting repo transactions (offering them at fixed and variable interest rates), purchasing sovereign debt securities on the secondary market and authorizing a liquidity window that broadens the acceptable collateral.

For the rest of 2008 the preventive mechanisms that the Central Bank has developed are expected to protect the domestic economy in a very adverse international context (unprecedented in several decades) marked by extreme volatility, a financial crisis and a large risk of a recession in central economies. The capacity and determination exhibited by the Central Bank in managing both domestic episodes of high financial volatility (July-August 2007 and May 2008) are therefore, as such, factors that minimize the possibility that fresh events of excessive caution by economic agents (which as is known, mean the dollarization of portfolios and falling deposits) may appear.

The sector development shows that with some differences all productive segments continue growing in 2008 so far. The corporate sector has a better repayment capacity due to a lower aggregate debt. On the other hand the rate of growth of household consumption is moderating as a consequence of a tighter labor market, as regards both job creation and the changes in real incomes. Household consumer debt remains on an upwards trend. Finally, the national public sector still has sources of funds to face its financial obligations, mainly due to the persistent primary fiscal and financial surplus in recent years, in a scenario of a falling debt in GDP terms.



II.1 Domestic conditions

Some moderation of economic growth is evident

Various indicators exhibited a slower growth during the first half of the year, which is being partly reversed at the end of 2008. The GDP expanded at a 7.8% y.o.y. rate during the first half of 2008 (see Chart II.1). The strong investment performance (particularly during the first quarter), mostly in durable equipment, added to the significant accumulation of inventories, enabled GDP growth to not be as severely affected by the moderation of the rising trend of private sector consumption (see Chart II.3).

The performances of the fiscal and external accounts are still the fundamental pillars to face the changing international scenario and its impacts on expectations at the domestic level (see Chart II.4). The current account may achieve its seventh consecutive year with a surplus in 2008, sustained by the trade surplus in goods (see Chart II.5). The growth of goods exports was 34% y.o.y. during the first half of the year, largely due to the higher prices. The increase in the export volumes of industrial manufactures (18% y.o.y.) also stood out, as it was even larger than the rate seen in 2007.

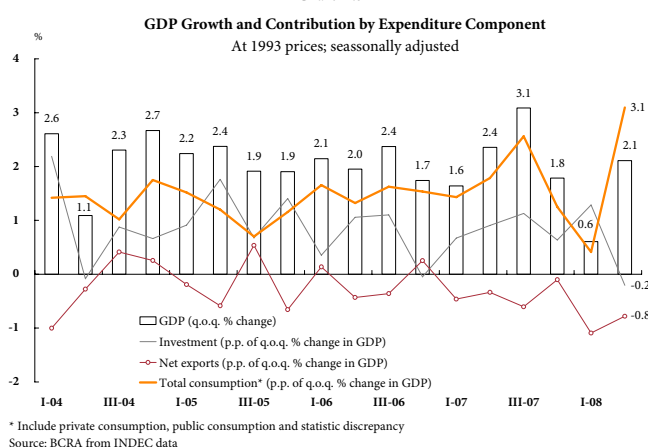
The Central Bank actions enabled the consolidation of systemic liquidity

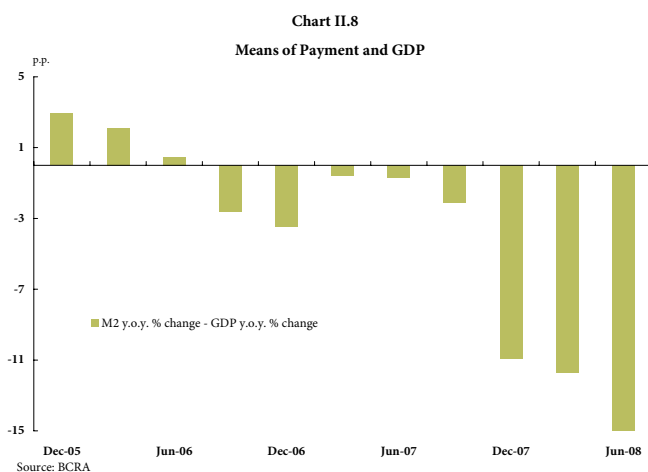
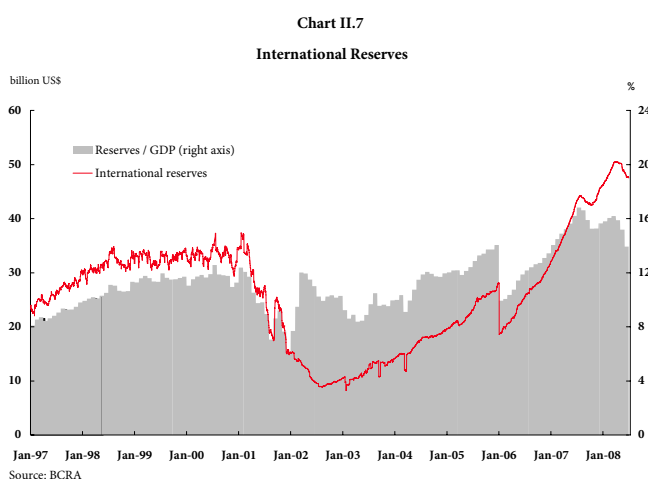
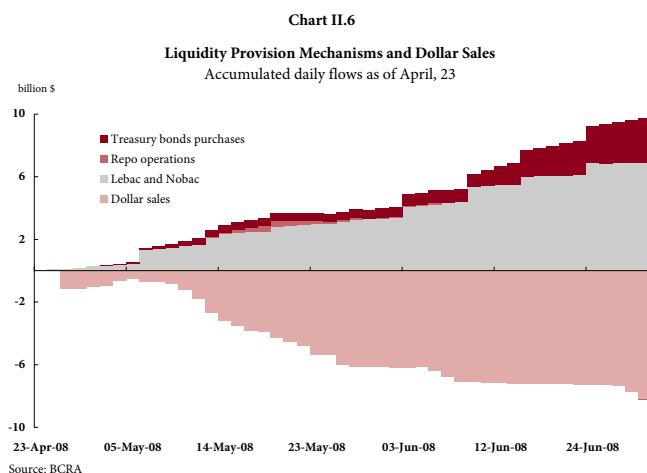
Monetary aggregates kept growing during the first four months of the year without diverging from the trend exhibited in 2007. But between April and June a fall of private sector deposits was recorded, with a simultaneous increase in the demand for foreign currency, events that were not related to the conditions of the financial system nor the economic fundamentals. In this scenario the Central Bank went ahead with a series of actions that allowed the domestic variables to show normal signs again.

To avoid possible negative impacts on the savings and investment decisions of the private sector agents, the Central Bank generated different mechanisms that attacked the expectations of a depreciation of the peso to stabilize the demand for money while they also provided liquidity. As a signal of the willingness and capacity to supply the foreign currency that the market might demand, there was therefore intervention on the spot market, and as from the end of May repo loans in dollars were offered.

On the other hand, of the mechanisms employed to inject liquidity the decline of the outstanding stock of

Chart II.3





Lebac and Nobac (by their redemption on the secondary market and the partial renewal of maturities) and the adjustment of the repo operations schedule stood out. In mid May the fixed rate repo loan lines was reinstated for up to \$3 billion, and additional repo offers were offered at a variable rate (at a fixed margin over the BADLAR interest rate at private sector banks). The Central Bank supplemented these transactions with the purchase of sovereign bonds on the secondary market, as most of the world's central banks carry out through their open market transactions (see Chart II.6).

With the purpose of making it easier to manage the liquid funds the Central Bank decided on a two-month period (June-July) for calculation of minimum cash reserves. Finally, at the end of the first half a liquidity window was opened that allows banks to borrow funds with Guaranteed Loans and/or Bogar 2020 bonds as collateral, and decided that these securities may also be used to guarantee inter-bank loans.

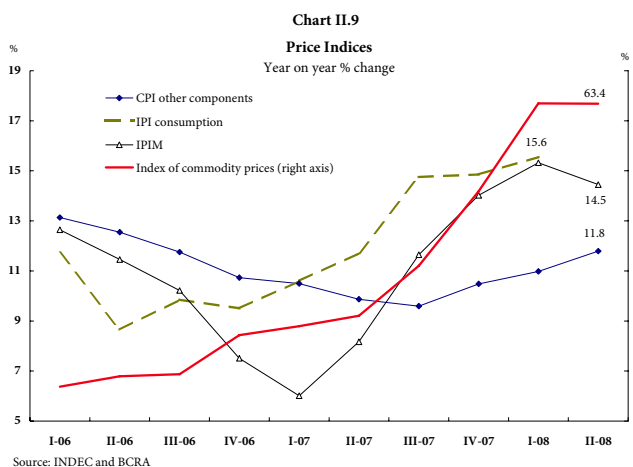
Once the Central Bank intention and capacity to moderate the volatility of domestic markets had been proven the monetary variables henceforth started returning to normal. As from mid June the private sector deposits therefore began their recovery. Likewise, the major interest rates (BADLAR and inter-bank call money) started reversing the rises they had exhibited in previous months.

The tools resulting from the policy of accumulating international reserves enabled to cope with volatility

Therefore, the convenience of a prudential policy of international reserve accumulation driven by the Central Bank as reinsurance to avoid the advance of excessive volatilities that might disturb the economic decisions was once again revealed. This target was achieved while only using a small share of the international reserves (see Chart II.7).

In this framework, the broadest aggregate in pesos (M3), which includes cash held by the public and total deposits in pesos, decelerated to reach a year-on-year (y.o.y.) change of about 17%. Meanwhile M2 exhibited a similar performance, recording growth rates of 18% y.o.y. and 20 consecutive quarters of monetary program compliance were therefore completed, as the means of payment continued growing less than the nominal GDP (see Chart II.8).

For domestic prices the different indicators available continued exhibiting a diverging trajectory, albeit with a



slight moderation at the margin. If a broad price indicator like the GDP Implicit Price Index (IPI) is considered, more momentum is seen at present, mainly explained by the development of export prices and the IPI of private sector consumption (see Chart II.9).

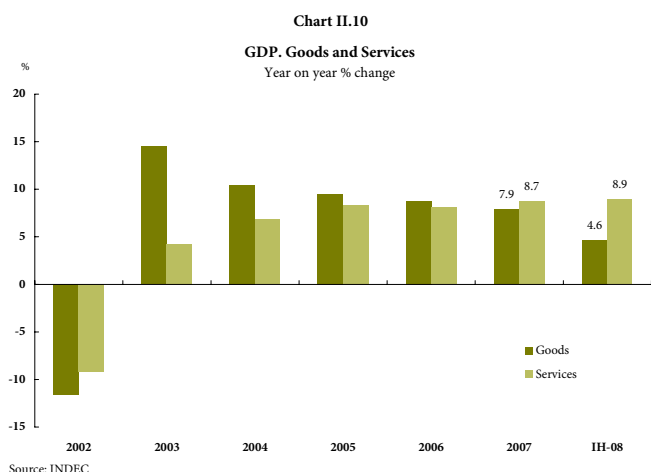
2008 could be the sixth consecutive year of economic growth

During the rest of 2008 credit conditions on the international financial markets are expected to remain rigorous. Facing this scenario the positive results of the Argentine fiscal and external accounts, added to the preventive mechanisms developed by the Central Bank in recent years, will allow for the fluctuations of the monetary and financial variables to still be limited, to support the consolidation of the economic growth process. For the rest of the year a larger momentum aggregate activity is forecast, boosted by the recovery of exports and a larger household expenditure, following the stabilization of expectations and financial conditions.

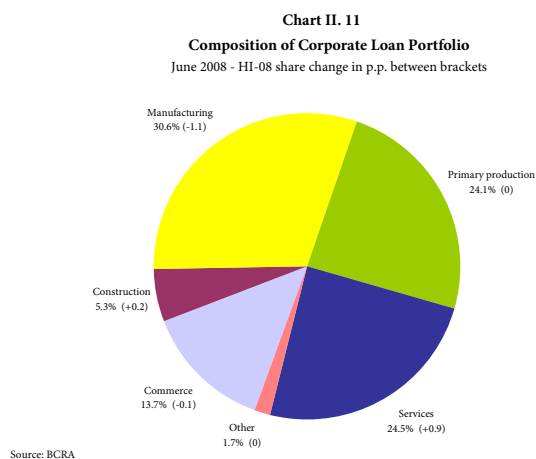
II.2 Financial system debtors

II.2.1 Corporate sector

In a scenario of a smaller external debt level and an increasing use of domestic financing, corporate sector activity levels outline a sound financial position for the sector



The economic expansion seen during the first half of 2008 was led by the service producing sectors, especially by commerce, transport, storage and communications. Meanwhile, goods production recorded a more moderate momentum during the first half of 2008 (see Chart II.10). This performance was affected by the smaller increase of farming output in the last harvest and the greater volatility of construction activity.



During the first half of the year a relative increase of banking finance of the services and construction sectors was recorded. Manufacturing is still the main recipient of bank funds (30.6% of total corporate credit); while services outgrew primary production as the second largest corporate segment borrowing from the financial system (see Chart II.11).

Total corporate debt keeps falling, to stand at levels of about 25% of the GDP (see Chart II.12). This development is led by the persistent fall of foreign debt, although it still accounts for slightly more than two thirds of total liabilities, to become a source of

Chart II.12
Corporate Debt
As % of GDP 4-quarter moving average

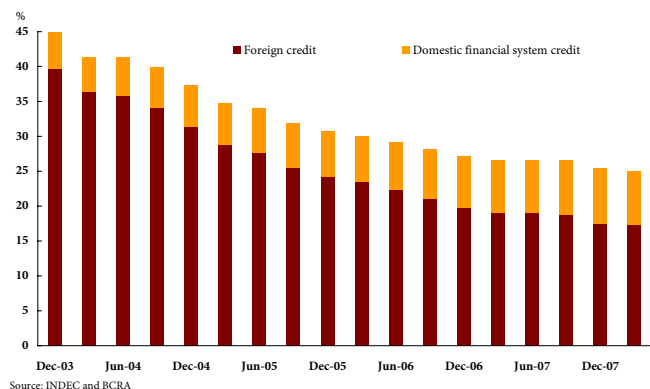


Chart II.13
Corporate Debt Burden
Companies reporting to the BCBA

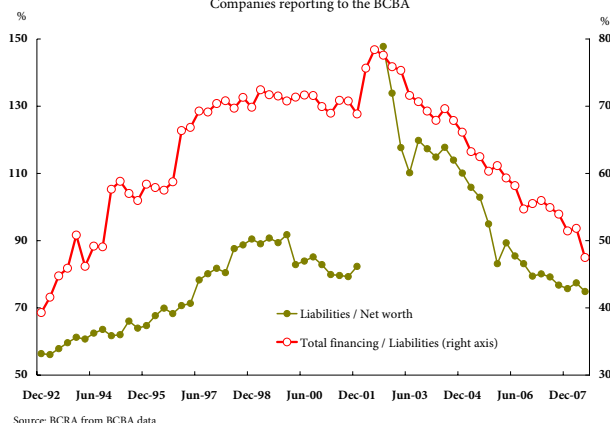
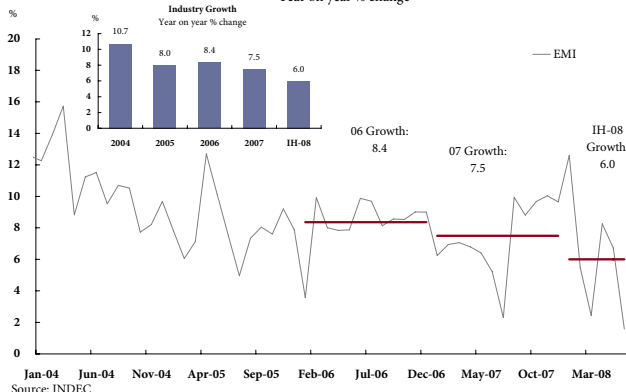


Chart II.14
Industry Evolution
Year on year % change



vulnerabilities in the face of potential changes in the peso-dollar exchange rate, to the extent that the firms do not have enough foreign currency revenues (mainly from exports) in order to service these debts. On the other hand, the share of domestic financing of the corporate sector is gradually increasing.

Apart from the greater international turbulences which are reflected on the local stock exchange, the financial position of the larger listed corporations continued improving in 2008 (see Chart II.13). This trend is partly driven by the falling degree of leverage and the lesser weighting of loans in their liabilities. Therefore, in overall terms these firms exhibit a relative improvement in their financial position in a framework in which the prospects for domestic and export business remain positive.

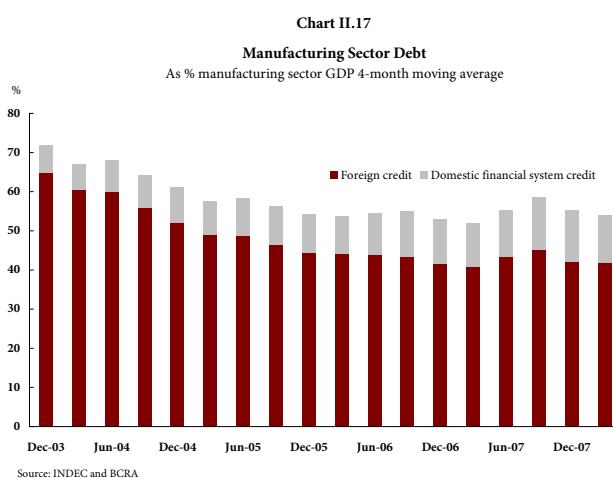
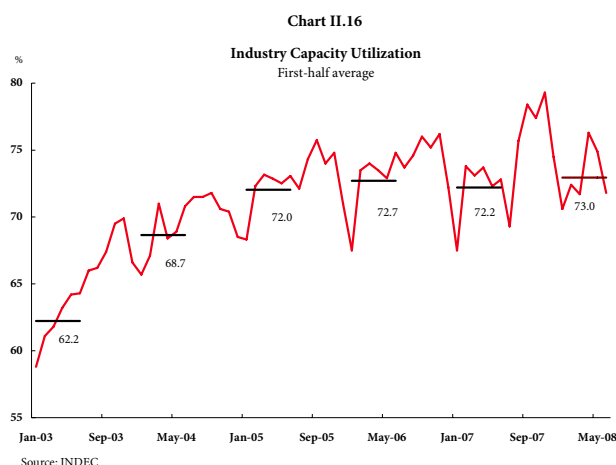
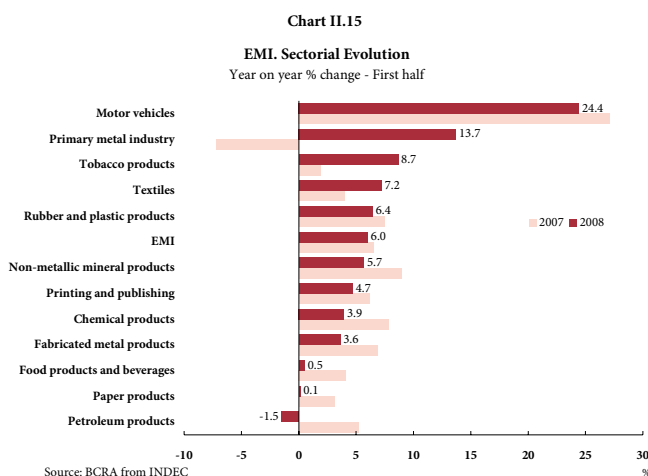
The economy is estimated as maintaining its expansive path. Therefore, for 2008 a GDP rise of around 6.5% is projected, boosted by both firms producing services and goods. This scenario will enable the corporate sector to continue relatively increasing its usage of domestic bank finance.

II.2.1.1 Manufacturing

Manufacturing moderated its rate of growth and maintains a sound economic and financial position

Manufacturing output continued growing, although at a slightly slower pace than observed last year (see Chart II.14). Automobile and base metals output exhibited the largest relative growths (see Chart II.15), given that new production lines resulting from the investments undertaken in recent years started up to operate and from the increased use of existing installations. Meanwhile, food and beverage production developed with a slight increase, largely subject to the fall of red meat output and the smaller growth of dairy products, cereal milling and oilseed crushing. These latter branches were affected by the temporary stoppage of trading in grain and cattle during the second quarter of the year.

The average capacity utilization factor (UCI) of manufacturing during the first half of the year was 73%, which was slightly higher than the same period in 2007 and at similar levels to earlier years (see Chart II.16). The largest rises in UCI were seen in automobiles, base metal industries and for rubber and plastic products.



During the rest of the year manufacturing is expected to record a slightly higher growth than it attained in the first half, to thus end its sixth consecutive growth year with a 6% expansion. Furthermore, the sector will continue reducing its reliance on foreign finance, as during recent periods (see Chart II.17), with an increase of domestic funding utilization. Therefore, this segment of production will consolidate its economic-financial position, which will be reflected by its payment capacity.

II.2.1.2 Primary sector

The primary sector continues increasing its activity, consolidating its already sound capacity to face financial debts

The 2007/2008 harvest ended with an almost 95 million ton crop, which meant that there was only a slight rise from the previous farming cycle (see Table II.1). This change was explained by the expansion of the cultivated area which was partly offset by the climate conditions that had a negative impact on yields.

At the outset of the 2008/2009 harvest cycle prospects differ between the crops. Firstly, the drought that is affecting some Argentine regions has inhibited planting of winter grains, which explains the fall of the area sown with wheat. For the coarse grains the initial estimates suggest a significant progress in soy sowing plans.

The 2008/2009 harvest cycle may therefore be similar to the previous crop, but with a larger share of oilseeds and other non-traditional cereals.

The beef production volume in the first half of 2008 was less (-5.6%)³ than in the same period in 2007, a fall that was due to a smaller number of cattle shipped for slaughter and a lower average weight. The volumes exported by packing plants dropped 18% y.o.y., although the price rises meant the sector's sales exhibited an increase (11.3% y.o.y.). Primary milk output saw a slight growth in volumes, but the outlook for producers remains tighter due to the loss of profitability in the sector (see Chart II.18).

The increase of international prices has allowed for an improvement in the financial position of farmers, after several years of profits and investments. Specifically, the Central Bank's Commodity Price Index (IPMP) exhibited a sharp rise to reach much higher levels than the historical average for the series (see Chart I.7).

³ National Agriculture and Livestock Commerce Control Bureau (ONCCA).

Table II.1

Grain and Oilseed Production

	2006-07		2007-08		Chg. %	Chg. tns
	Thousand tns	Structure %	Thousand tns	Structure %	2007-08 / 2006-07	2007-08 / 2006-07
Cereals	41,731	44.4	42,681	44.9	2.3	950
Corn	21,755.4	23.1	20,400	21.5	-6.2	-1,355
Wheat	14,548.0	15.5	16,067	16.9	10.4	1,519
Grain sorghum	2,795.0	3.0	2,900	3.1	3.8	105
Other	2,632.4	2.8	3,314	3.5	25.9	682
Oilseeds and oleaginous fruits	52,339.5	55.6	52,295	55.1	-0.1	-44
Soybean	47,460.9	50.5	46,500	49.0	-2.0	-961
Sunflower	3,630.2	3.9	4,630	4.9	27.5	1,000
Other	1,248.3	1.3	1,165	1.2	-6.7	-83
Total	94,070	100.0	94,976	100.0	1.0	906

Source: BCRA form SAGPyA and USDA data

USDA estimations: rice, corn, wheat, cotton and soybean production

The moderate debt levels of the primary sector continue without any significant changes (see Chart II.19). The sound prospects for output, exports and prices enable the sector to continue having a sound economic and financial position.

II.2.1.3 Services

The growth of activity and reduced foreign debt of service companies is reflected in a sound financial performance

Firms that provide services maintain a strong rate of expansion (see Chart II.20), even despite the reduced level of transport activity during the second quarter.

In this context services are expected to continue exhibiting more momentum than the goods producing sector during the rest of 2008, to gain share in the GDP. Likewise, during the year the government authorized price increases for a number of utilities, which enabled these firms to improve their cash flows. This scenario, combined with the moderate levels of total debt and the declining foreign debts permitted the economic and financial position of the sector to become more robust.

II.2.1.4 Commerce

Low debt levels and sound economic prospects for coming months define a strong payment capacity

Retail trade continues developing positively, while the investment plans in this segment are maintained. The increase of nominal billing accelerated, while at shopping centers the rate of expansion remained in line with what was seen during the three previous years, albeit with a deceleration of the quantities sold. Sales of household appliances and other durable goods continued exhibiting a considerable growth rate.

In the first half of 2008 the investments carried out by the commercial chains matured, as reflected by an increase in the number of outlets for both supermarkets and shopping centers. This trend should continue in the short term, due to the high occupancy of the available shop locations.

During the next few months a moderate increase of household purchasing power is expected, to provide a dynamic framework for the sector. With debt levels that remain low and stable, with the use of local and foreign funding in equal shares, the sector still has an adequate payment capacity, and therefore access to local banking funds.

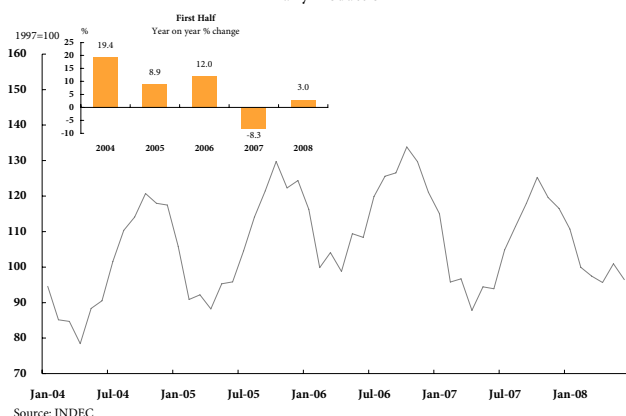
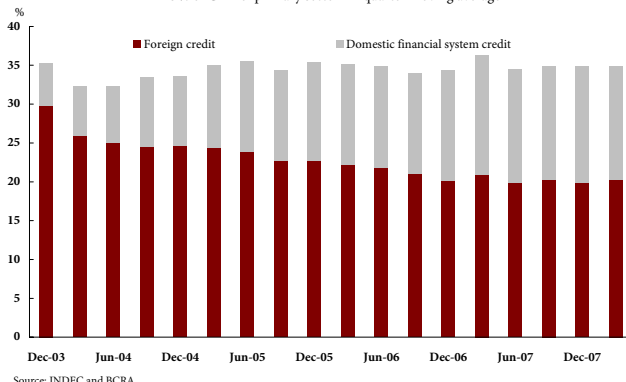
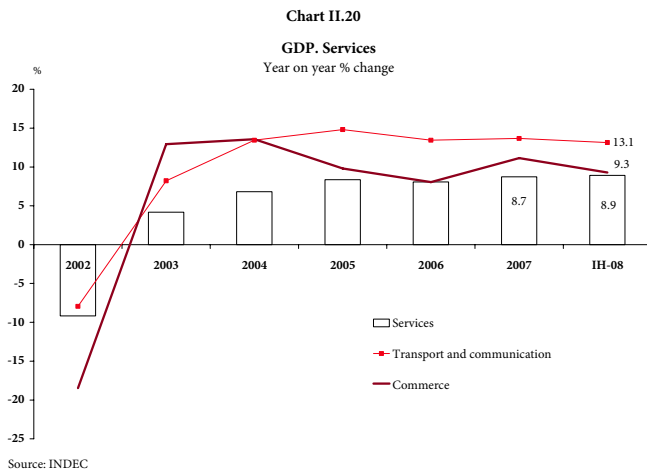
Chart II.18
Dairy Production

Chart II.19

Primary Sector Debt

As % of GDP of primary sector - 4-quarter moving average



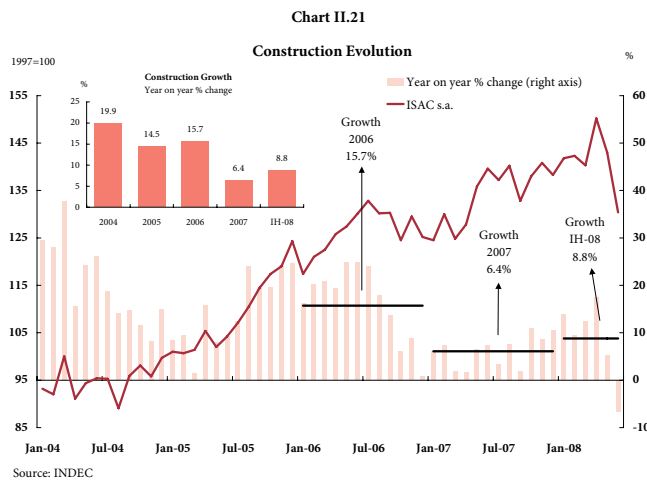


II.2.1.5 Construction

Construction firms consolidate their financial position, in a framework of growth of the activity and low debt levels

The growth of construction activity was higher than recorded in 2007 (see Chart II.21) despite the inconveniences in transport of raw materials shown in the second quarter. The most dynamic segment was home building, while public works recorded a smaller rise.

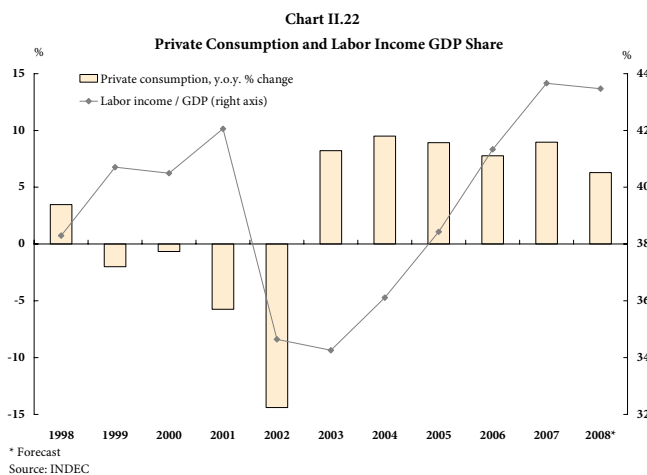
Towards the end of the year a deceleration of the level of activity level in the sector is expected, according to corporate expectations and the maturity of the real estate market. In this manner, in May for the first time in the past five years a fall of registered employment in the sector was observed at a national level⁴, while fewer filings for building permits were seen. Despite this possible deceleration the sector will continue growing, in a context of domestic and external debt levels that are still low, a situation that provides an adequate financial profile.



II.2.2 Households

A narrower labor market poses initial doubts about the repayment capacity of the sector

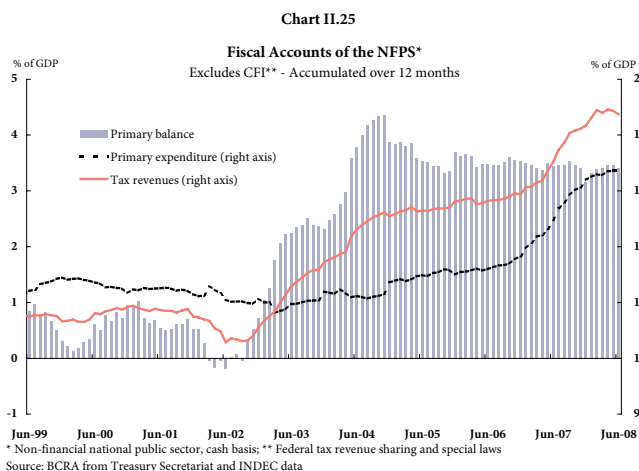
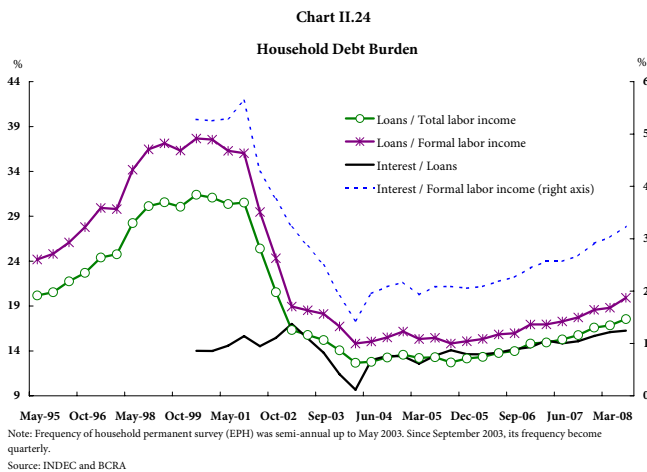
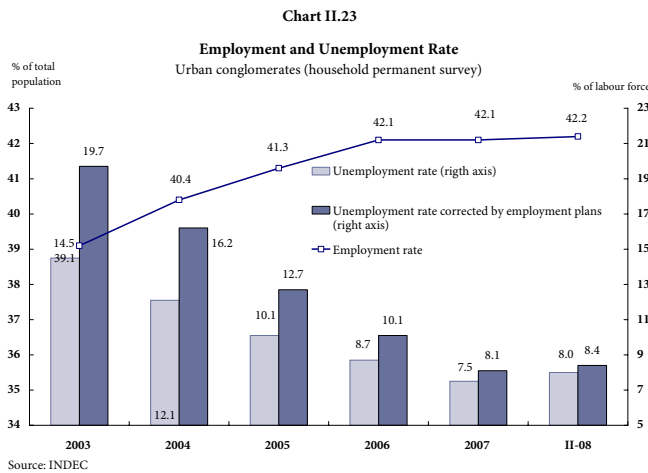
Household spending continued increasing at a similar rate to the average growth of the economy, and slightly less than 2007. The smaller increase originated in an increase of private consumption that was not so steep (see Chart II.22), due to the deceleration of the real aggregate payroll, in a scenario of more debt and some worsening of consumer confidence.



New job creation was weaker, less than population growth, but nevertheless a further y.o.y. fall of unemployment levels was recorded. The unemployment rate was thus 8% of the workforce (PEA) during the second quarter (see Chart II.23) or 0.5 p.p. less than a year ago. Likewise, growth of employment in the formal sector was recorded, to continue with the improvement in the quality of work observed in recent years, which means wages are better and there is less likelihood of being fired.

On the other hand nominal earnings have maintained a rising trend. Collective bargaining in the formal private sector set staggered wage improvements (between 20%

⁴ According to Construction Industry Statistics and Records Institute (IERIC) data.



and 30%), while the workers in the informal segment have exhibited a significant rise in their wages so far this year. The workers in the national public sector received a wage increase in June and another rise in August. Furthermore, families are also favored by the restructuring of pensioner social security earnings during the year. Nevertheless, the development of real wages in the registered private sector has ceased to be positive, and returned to neutral.

In this scenario the degree of debt and the burden of the services on debt that households face still exceeds the expansion of their incomes (see Chart II.24), although the situation remains more comfortable than during the past decade. The lines for financing household consumption are at similar levels to those seen at the end of 2007, in terms of both private sector consumption and the GDP (see Chart II.2). This trend, which is expected to continue being recorded during coming months, will allow for backing the payment capacity of the sector, which has been somewhat weakened.

During the closing months of the year real household incomes are expected to increase slightly, partly due to the wage increases that have already been agreed on and the adoption of new income measures by the national government. On the other hand, in a scenario in which the labor market remains adjusted, the unemployment rate should only exhibit marginal improvements.

II.2.3 Public sector

The positive performance of the public sector accounts persists⁵

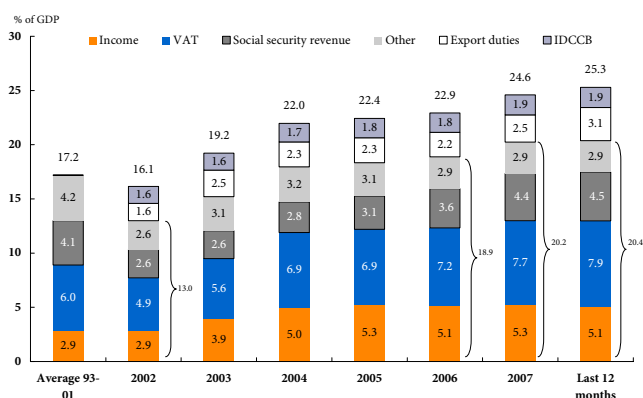
The primary surplus of the national non-financial national public sector (NFPS) increased from 2007 (see Chart II.25). National tax revenues continued growing significantly in nominal terms, mainly boosted by the collection of value added tax (VAT) and export duties and by social security funding. These revenues thus remain at a record level of more than 25% of the GDP (see Chart II.26). If the revenues are considered in real terms a slower rate of growth is evident (see Chart II.27).

The growth of primary spending was mostly explained by the increase of subsidies for the private sector and the social security outlays. This rise was partly offset by the reduced transfers to the provinces. Primary spending therefore recorded a historical record at 24% of the GDP (see Chart II.28).

⁵ For a more detailed analysis of the public sector revenues and expenditure see the Inflation Reports for the first and second quarters of 2008.

Chart II.26

Share in National Tax Revenue

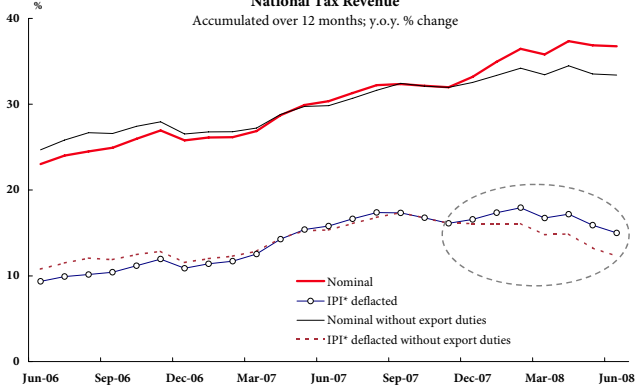


Source: BCRA from Treasury Secretariat data and INDEC

Chart II.27

National Tax Revenue

Accumulated over 12 months; y.o.y. % change

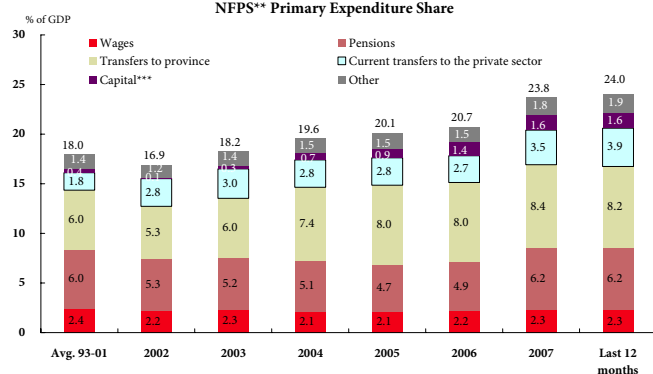


* Implicit Prices Index of GDP

Source: BCRA from Treasury Secretariat data and INDEC

Chart II.28

NFPS** Primary Expenditure Share



*BCRA on previous methodology; includes automatical transferences to provinces; **Non-financial national public sector;

***Excludes capital transfers to provinces

Source: BCRA from Treasury Secretariat and INDEC data

The financial surplus increased significantly during the year to date, despite the increase of interest payments. The fiscal result is thus at values of about 2.5% of the annual GDP.

The public sector debt continues falling in GDP terms, a trend that may deepen during coming months

In June 2008 the National Public Debt (NDP) totaled US\$150 billion, US\$5.12 billion more than at the end of 2007 (a change associated with the appreciation of the peso against the US dollar, adjustment of the debt by the Reference Stabilization Coefficient –CER– and capitalization of interest). The NDP was therefore equivalent to approximately 49% of the GDP and exhibited a fall of around 7 p.p. from December 2007.

Sources of funding are sufficient to face the financial requirements until the end of the year, providing the public sector with a strong repayment capacity

As a result of the expected development of revenues and spending and the measures that the national government has announced, the NFPS primary surplus is expected to exceed the national budget guideline (3.15% of the GDP) this year. If the interest payments are considered the NFPS financial result could be more than 1.5% of the GDP for the full year. At a consolidated level the primary surplus may be more than 3% of the GDP, due to the almost neutral performance recorded by the provinces, while the financial balance would be over 1% of the GDP.

In this framework financial requirements are forecast to be concentrated in the final quarter of 2008 and to be covered by domestic and intra-public sector sources. It is estimated that both the nation and the provinces may cover their financial needs with no major difficulties during the rest of the year.

For 2009 the needs for funds will be larger due to the maturities of principal of the National Guaranteed Loans (PGN), but these services do not seem to be hard to meet due to the multiple alternative financing sources.

III. Capital Markets

Summary

International market turmoil has strongly conditioned the performance of domestic capital markets in 2008 to date. The highly volatile scenario, added to domestic matters (which gradually lost significance as the critical situation at global level worsened) had a negative impact on Argentine financial assets prices. Although the effects of the crisis are expected to continue to be felt during the remainder of 2008 and throughout 2009, there could be some gradual recovery in the demand for local assets as risk aversion begins to give way.

Following declines in some cases exceeding 30% in National Government bond prices so far this year, yield curves in both dollars and in pesos adjusted by CER have shown a sharp upward displacement. As US Treasuries have been gaining in value, Argentine sovereign risk has deteriorated, at the same time as there has been an increase against benchmarks among emerging nations.

In this situation, the Central Bank introduced a series of measures with the aim of lessening the local impact of the international crisis, including the issuance adaptation of debt instruments to investor changing demand and a liquidity injection. As a result, there was a fall in the outstanding stock of Lebac and Nobac, with greater weighting for fixed rate instruments and a reduction in portfolio maturity.

Trading volumes on the MAE continued to rise, because of increased trading of both National Government and Central Bank securities.

The placing of corporate bonds (ON) dropped sharply, totaling \$350 million in the first half of the year following by company issues in the financial, commercial and metallurgical sectors. Bank ONs traded recorded increased yields on the secondary market. Financial trust placements continued to increase during the period, becoming the leading source of financing on capital markets. The trend towards securitization of consumer-linked assets has continued to gain strength.

In the middle of several episodes of high volatility, the Merval index experienced an accelerated decline in recent months, underperforming in comparison to the rest of the stock-markets in the region. Trading volumes held steady, however.

Performance by future exchange rate markets was in line with the increasingly volatile environment, with an expansion in the volumes traded on futures and forwards currency markets.

Chart III.1

Yield of High Liquid Argentine Bonds

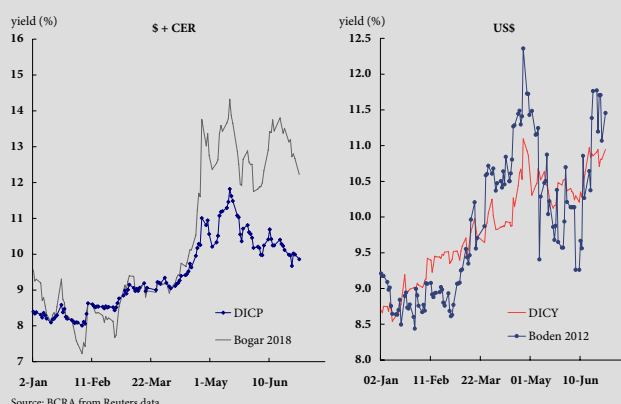


Chart III.2

Dollar Futures
Monthly traded volume

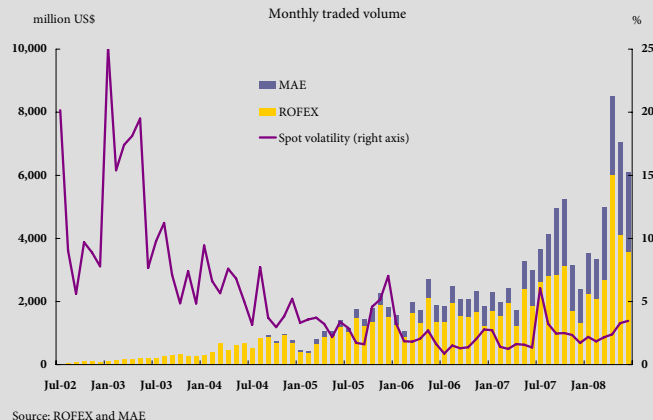


Chart III.3

Argentina Yield Curves

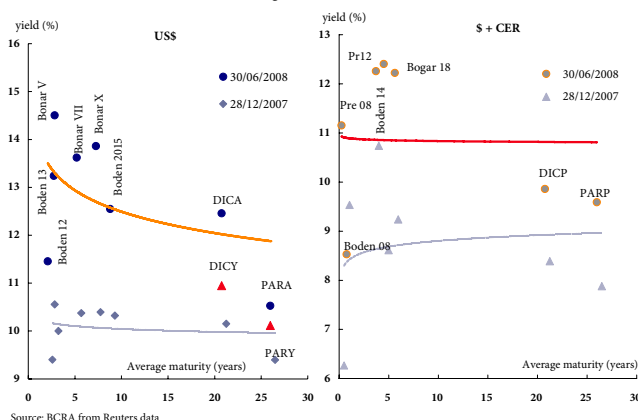


Chart III.4

Relative Value of Argentine Bonds

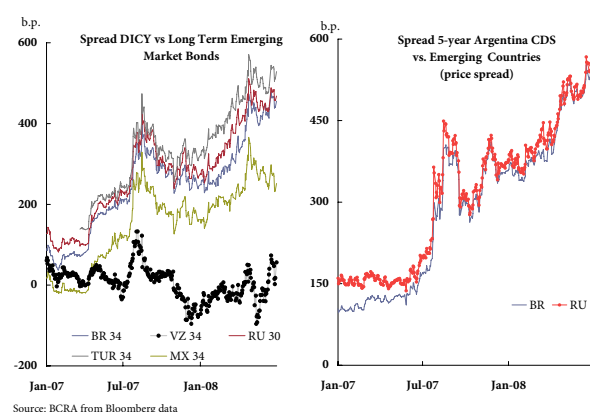
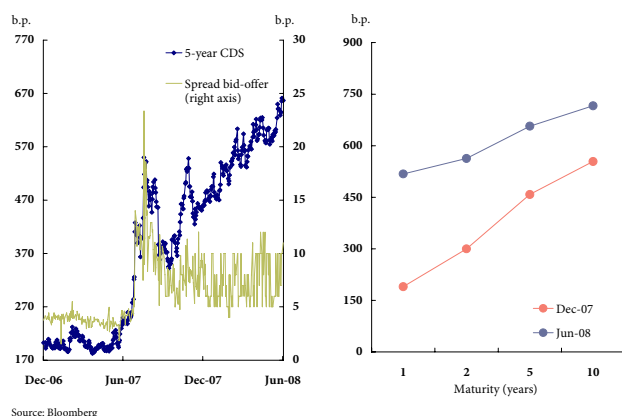


Chart III.5

Credit Default Swaps: Argentina



III.1 Public sector fixed income

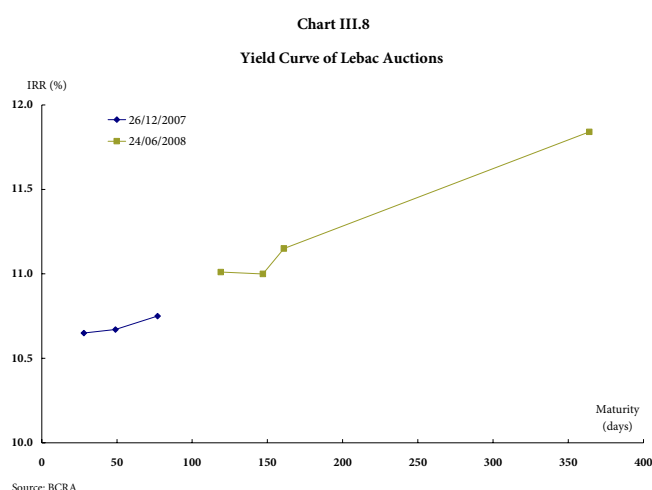
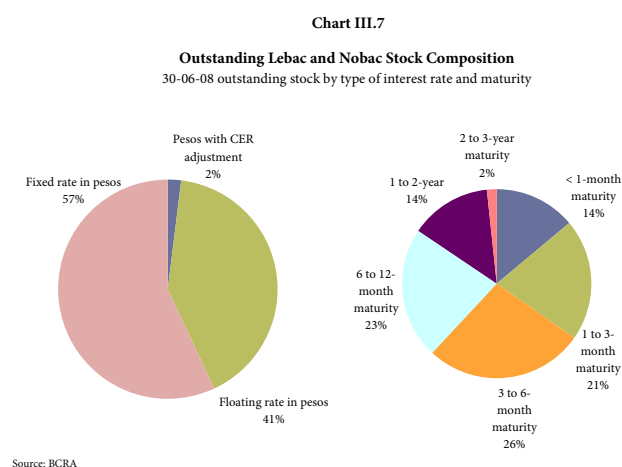
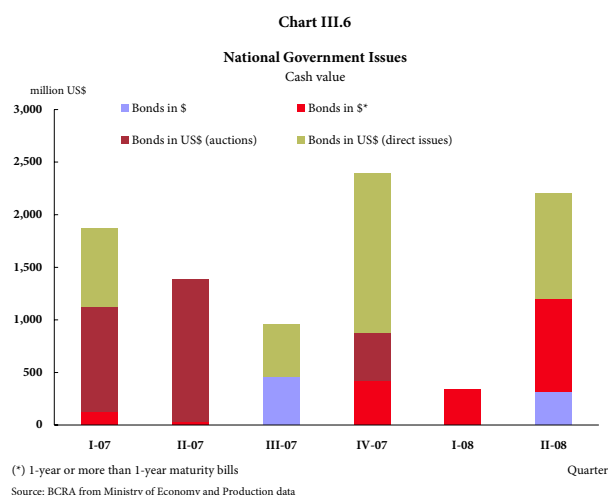
Volatility on international markets, together with certain local factors, exerted strong downward pressure on Argentine sovereign bonds

Argentine National Government bonds have recorded a strong and widespread deterioration in 2008 to date. This behavior can be linked to the highly volatile behavior of international financial markets (see Chapter I), to which can be added certain matters of a local nature. The demand for Government debt instruments was markedly impacted by the significant rise in risk aversion, and was reflected in a falling back of prices and widening yields, which already by May were reaching new heights (see Chart III.1).

Following declines in Government bond prices so far this year that in some cases exceeded 30% compared with the end of 2007, yield curves in both dollars and in pesos adjusted by CER have shown a sharp upward displacement this year. In the case of foreign currency issues, the increase in yield was in excess of 800 b.p. at the time of the recent market turbulence, with sharper increases in the short segment of the curve (leading to the slope becoming negative). In this context, the spread over Treasuries increased, with the largest increases in the short segment of the curve. Lower demand for CER-adjusted securities, which were the most affected by matters of a domestic nature, led the yield curve for index-linked paper to record an upward displacement averaging close to 300 b.p. in the year to date. As a result, the curve flattened towards the middle of the year (see Chart III.3), showing a slightly positive development by the closing date for this Bulletin.

Long-term local bonds recorded a greater depreciation compared to that of benchmark instruments of a similar duration, with an increase in the yield differential when matched against the debt of countries such as Turkey, Russia, Brazil and Mexico (see Chart III.4).

Increasing risk perception in the case of local sovereign bonds was evident from the increasing risk spreads for Argentina, both for credit default swaps (CDS) and EMBI+ spreads (see Chart III.5). Prices of 5-year CDS contracts reached their highest levels for the year (rising above 1,000 b.p. in recent months, whereas at the end of 2007 the level stood at 461 b.p.). The increase was more marked for shorter-term contracts for 1 and 2 years. In the case of the EMBI+ spread for Argentina, the rise totaled over 400 b.p., compared to an increase of over



100 b.p. in the emerging markets index as a whole. The differentials in sovereign risk spreads for Argentina compared with those for other emerging such as Brazil and Mexico have risen above 600 b.p. so far this year.

In April the Government announced its Financial Programme for 2008, which included bond placements (both directly and on the market) and the placement of its entities bills for an amount of approximately US\$6.1 billion, to face up financial commitments through to the end of the year. The Government obtained financing in April by the issuance of a bond in pesos adjusted by BADLAR rate, offering a yield of 13.3%⁶. Since then, because of the unfavorable market context, no further placements were made by means of auctions. In May the Government made a direct placement with Venezuela of Boden 2015 for US\$1 billion (cash value), offering a yield of 12.9% (see Chart III.6). More recently, in July, a similar placement took place, for the same amount, this time yielding 14.81%. Borrowing by means of the placement of bills within the public sector has reached a level of over \$8 billion in the year, with issues for 152 and 365 days, including rollovers. As a result, the stock of intra-public sector bills rose by almost \$2 billion.

The Central Bank lowered the stock of bills and notes, with a reduction in the share of variable rate instruments

The Central Bank introduced a series of measures to deal with the impact locally of the crisis on international financial markets (see Section II.1). Securities issues were adjusted to meet the demand for short-term paper, issues were redeemed in advance of maturity on secondary markets, and liquidity was injected into the market. As a result, on the basis of the figures for the end of June, the stock of Lebac and Nobac stood at a par value of \$50.4 billion, a significant year-on-year drop (from a par value of \$61.5 billion in mid-2007).

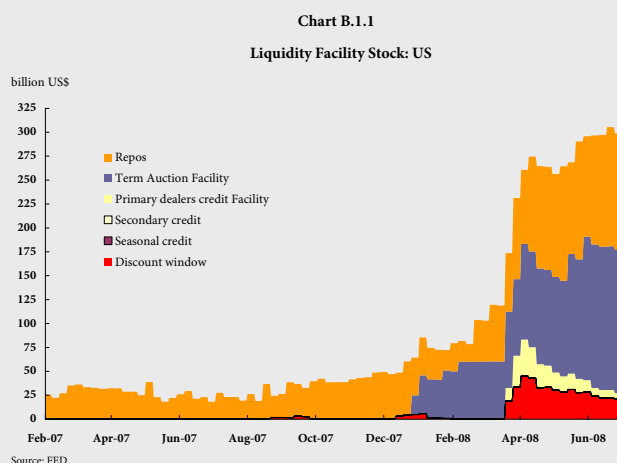
The result of this was that fixed rate securities accounted for a larger proportion of outstanding Central Bank paper, with a decrease in the share of variable rate instruments in particular, and to a lesser extent, in CER-adjusted securities (see Chart III.7). For example, in the middle of the year 57% of the stock of Central Bank Lebac and Nobac consisted of fixed-rate instruments

⁶ The Government raised \$828 million in cash by means of this bond, which accrues interest quarterly at BADLAR rate plus a margin of 350 b.p., principal to be repaid in full at maturity. The amount bid at the auction on April 4 was well in excess of the amount being tendered (with a bid to cover ratio of 2.1).

Box 1 / Turbulence and Measures Taken to Provide Liquidity

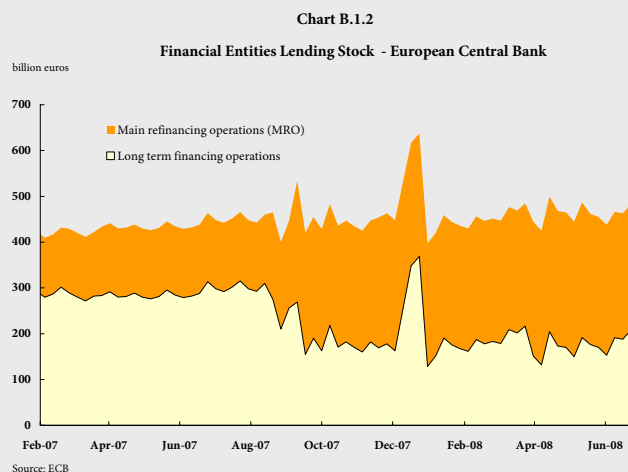
The tension evident in interbank markets since mid-2007 pushed the leading central banks to introduce various different measures to shore up liquidity, performing increasingly significant transactions over the course of 2008 to date. The various monetary authorities (the Federal Reserve in particular) displayed considerable flexibility, succeeding in lowering volatility in short-term interest rates, although interbank markets remain under stress (with further peaks in the second half of the year)

The turmoil observed in financial markets as from the second half of 2007 has been presenting the monetary authorities of the world's leading economies with major challenges. In addition to the problems on financial markets, economic activity levels have been placed under serious threat, in a scenario aggravated by the sharp rise in commodities prices.



The prevailing uncertainty and lack of confidence among the various financial system agents have translated into severe tension on interbank markets. This can be seen from the wide spreads that began to be recorded between Libor and Euribor rates compared with interest rates for transactions with almost no counterpart risk (prior to the turbulence, such margins were insignificant). The central banks of the leading developed economies were obliged to intervene to anchor expectations regarding short-term interest rates, preventing further pressure on the cost of funding and preserving their monetary policy transmission mechanisms. As a result, in addition to changing the bias in monetary policy (the cuts in the Fed's reference rate being a prime example), central banks found it

necessary to implement specific measures to inject liquidity into the market.



As tensions on money-markets worsened, liquidity injections (initially carried out by means of larger amounts in standard transactions) called for increasingly flexible actions. New types of collateral began to be accepted, and the counterpart universe was widened (for example, by allowing primary dealers access to the discount window in the case of the Fed). In addition, terms of transactions were lengthened, and measures of an extraordinary nature were taken (such as the Fed's tenders of TAF and TSLF⁷). Measures were also agreed among the various central banks (such as currency swaps between the Fed, the European Central Bank -ECB- and the Swiss National Bank). In the case of the Bank of England, there was also a change in reserve requirements.

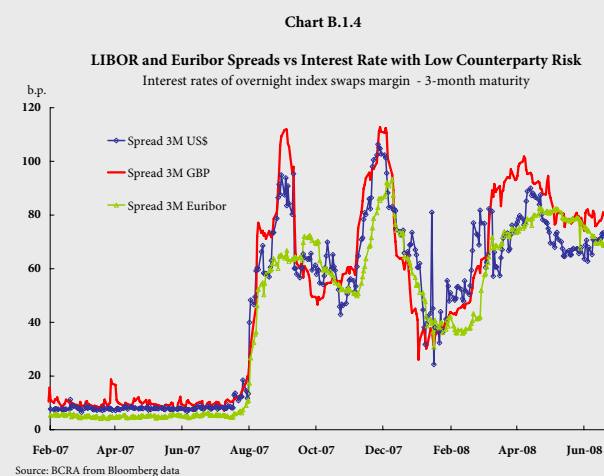
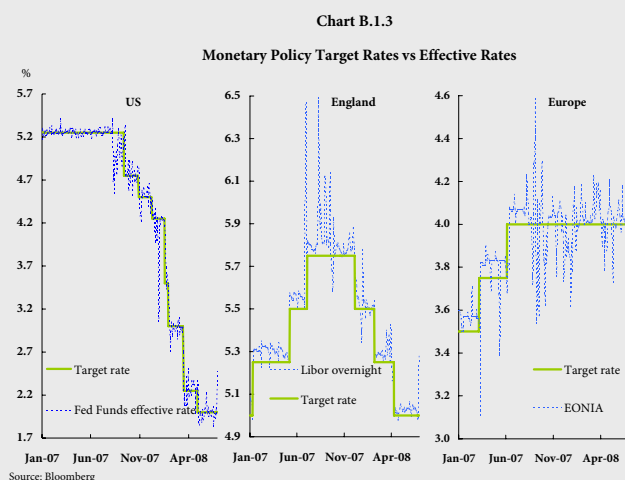
In the United States (Chart B.1.1), there was an increase in repo stocks in the second half of 2007, with a surge in the liquidity provided through the introduction of the TAF mechanism at the end of 2007. The sharpest rise took place in March and April, however, with a substantial increase in amounts involving repos and TAF, together with more intensive use of the discount window, to which was added utilization by primary dealers of the facilities available. For its part, action by

⁷ The Term Auction Facility -TAF- is a temporary procedure that was introduced in December 2007 (involving open market transactions with a wide range of potential counterparts and collateral). The Treasuries Securities Lending Facility -TSLF- (announced in March) represented an asset swap (Treasuries for less liquid assets).

the ECB resulted in a more discreet change in terms of total balances (see Chart B.1.2).

Although the changes made to the conditions for granting liquidity were widespread among central banks, the change made differed, particularly given the divergence that existed in the tools initially available. In the case of the Fed, the central bank making the largest changes, there have been signs of a move towards the model that was already being implemented by the ECB (with its broader operating range).

Although the measures introduced have helped to keep short-term rates close to monetary policy targets (see Chart B.1.3), interest rates recorded on interbank markets have shown wide spreads. Spreads over LIBOR in dollars, pounds and three-month Euribor (market benchmarks) compared with interest rates with low counterparty risk (such as those on overnight index swaps or equivalent items), which before the turbulence were below 10 b.p., widened to over 100 b.p. (see Chart B.1.4), obliging central banks to continue to make efforts to inject liquidity.

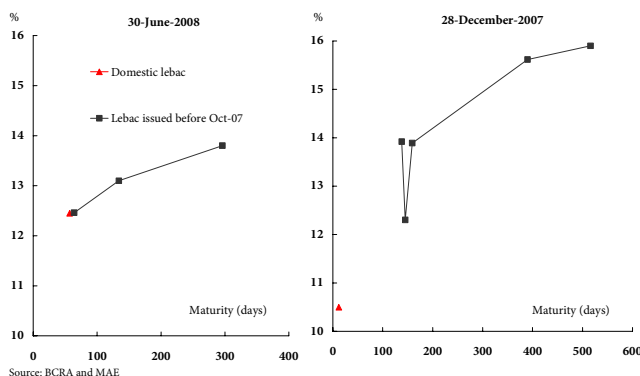


The measures introduced brought to light the need for central banks to be able to count on a flexible operations framework allowing them to adapt to unprecedented circumstances. Nevertheless, this temporary use of novel tools has led to discussion regarding the consequences of such action in terms of moral hazard from the handling each bank gives to its liquidity. Another of the lessons from the turmoil that is still developing arises from the relevance of the stigma associated with the use of facilities that include penalty rates. As the use of such facilities could be interpreted as an indication that the borrower is in difficulties, there is a reputation cost that inhibits their use. Despite the changes that have been made (less punitive rates), banks have avoided making use of the discount window. This stigma problem is not an exclusive attribute of more developed financial systems. At local level, for example, although the problem was more serious in the past (when the Central Bank's ability to assist financial entities was more limited) work continues to reduce its impact.

The persistence of wide spreads on money markets reflects the unwillingness of banks to lend to each other (a confidence crisis) at a time during which liquidity continues being accumulated to be able to confront potential problems. Given the different dimension of current market problems, and in view of the particular nature of the factors in play (slow adjustment in the real estate market, uncertainty as to the total losses derived from market turmoil, lack of transparency regarding the situation of each financial entity) money-market adjustments are expected to take place slowly and progressively. This means that volatility will continue to be high, at least for the remainder of 2008 and much of 2009, forcing developed country central banks to adopt a proactive policy to ensure liquidity. Indeed, the US authorities have already been obliged to draw up even more drastic measures, impacting not solely upon liquidity but also directly on credit market problems

Chart III.9

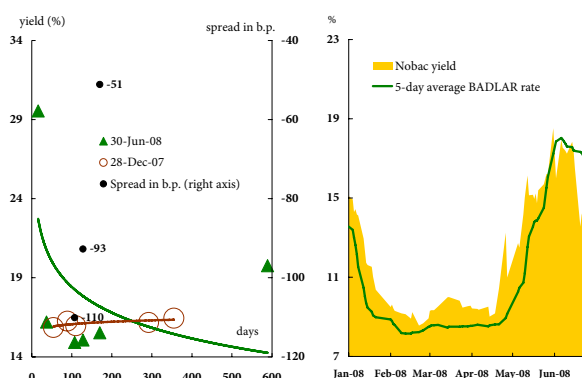
BCRA Securities Secondary Market
Domestic Lebac vs. Lebac issued before October 2007



Source: BCRA and MAE

Chart III.10

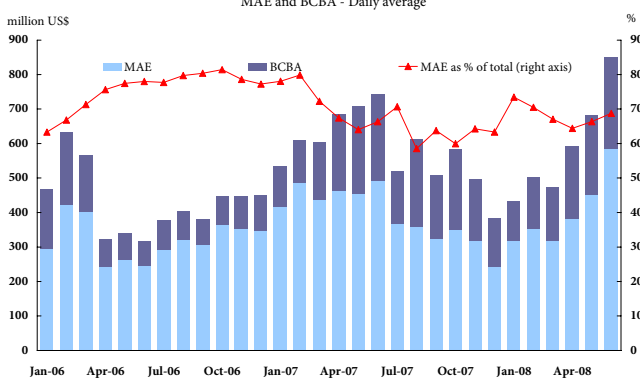
Nobac Secondary Market
Yield curves and most traded Nobac evolution



Source: BCRA from Reuters and MAE data

Chart III. 11

Traded Volume of Government Bonds
MAE and BCBA - Daily average



Source: MAE and BCBA

(mainly Lebac), while 41% was made up of variable rate notes (Nobac carrying a coupon adjusted by BADLAR), compared with weightings of 41% and 55% at the end of 2007, respectively. There was a shortening of the average duration of the securities placed: at mid-year 62% of the outstanding stock of bills and notes had a 6-month residual term or less (10 p.p. more than 2007).

Yields at Lebac auctions have tended to increase. From a range of 10.65%-10.67% at 28-77 days at the last auction in 2007 (see Chart III.8), the yield rose by the middle of this year to 11.0%-11.8% for terms of between 119 and 364 days, rising to 11.75%-12.26% at the end of September (for less than one year term). In the case of Nobac, yields have recorded significant declines on the primary market during the year (matching the performance by BADLAR), with certain volatility⁸.

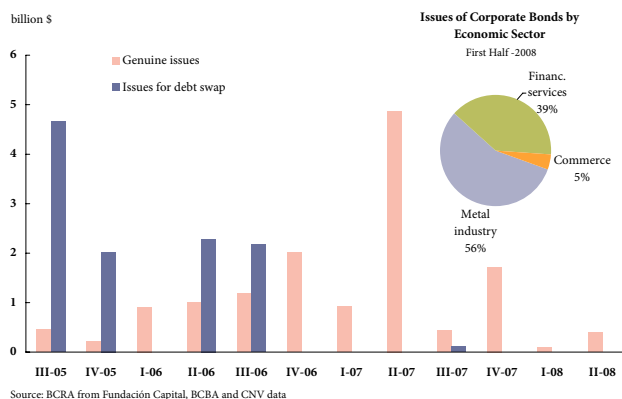
On the secondary market, Lebac issues made prior to October 2007 continued to show the highest trading volumes, compared with the Lebac issued for domestic use only. A decline was noted in the maturity of the instruments traded, while comparable yields recorded a cutback of around 100 b.p. in the case of standard Lebac (see Chart III.9). Prices on secondary markets for Nobac have been rising over the course of the current year. This means that on the basis of comparable periods there has been an average reduction of over 400 b.p. in yields (much of which is explained by the performance in recent months), while transactions have been entered into for longer maturity. This behavior has taken place in a context marked by strong pressure on the BADLAR rate as from the second quarter of the year (see Chart III.10).

Trading volumes on domestic markets for fixed-income securities (including Lebac and Nobac) have shown signs of recovery

Domestic market trading volumes for fixed-income securities (on the BCBA and MAE) have picked up during the year, reaching levels similar to those of the first half of 2007. On the basis of results for the first half of 2008, daily average trading volume reached US\$589 million, 14% higher than in the previous half (see Chart III.11). Trading volume on the MAE continued to gain share; whereas the volume traded on the BCBA fell slightly, on the MAE it rose by over 20%.

⁸ As a reference, whereas at the last auction in 2007 (18 Dec) the yield for a 287-day residual term that was accepted was 15.76% -a spread of 2.20%- , the yield at the auction on May 13, 2008 for a term of 315 days was 11.96% -a spread of 1.50%- . At September 23 the yield on Nobac for a term of almost one year was 13.71% - a spread of 1.35% for almost a year-.

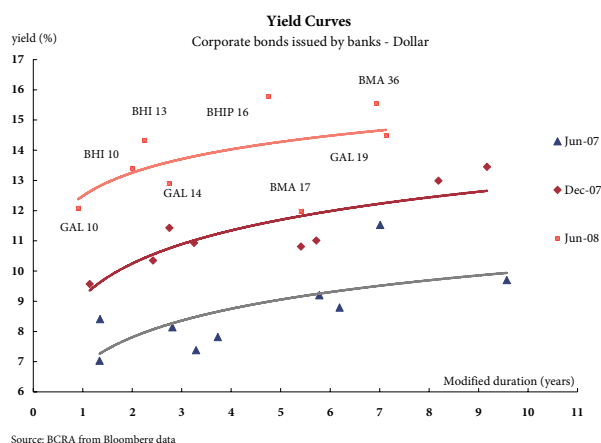
Chart III.12
Issues of Corporate Bonds, Commercial Papers and SMEs Bonds



An increase has taken place in trading volumes of securities issued by the Central Bank. On the basis of performance in the first half of the year, the increase has been 13% compared with the previous half, weighting according to instrument having remained steady: 31% of the average amount traded in the first half has corresponded to Lebac, while the remaining 69% has been in the form of Nobac. Amounts of Government bonds traded on the MAE recorded an average increase of 56% in the first part of 2008 (averaging almost half the total trading volume on the MAE).

As the international situation has shown signs of serious deterioration in August and September, it will continue to condition the possibility of any recovery in Argentine debt prices. It is therefore expected that government securities will continue to show considerable volatility during the rest of the year and in 2009, although given the floors that have been reached to date (particularly in the case of sovereign debt), a gradual recovery in prices as risk aversion declines cannot be ruled out.

Chart III.13

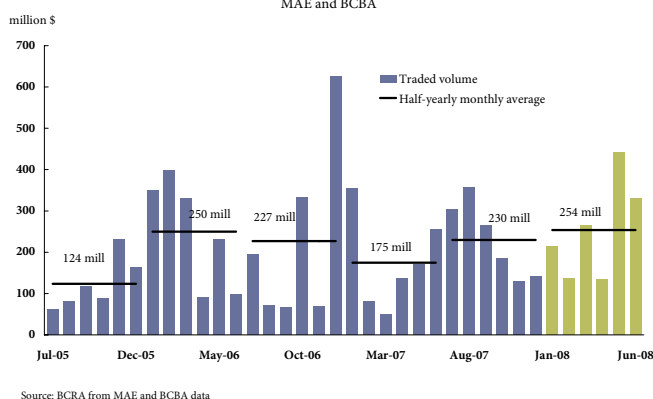


III.2 Other fixed-income instruments

Corporate debt placements declined, at the same time as there was an increase in the volume traded on the secondary market

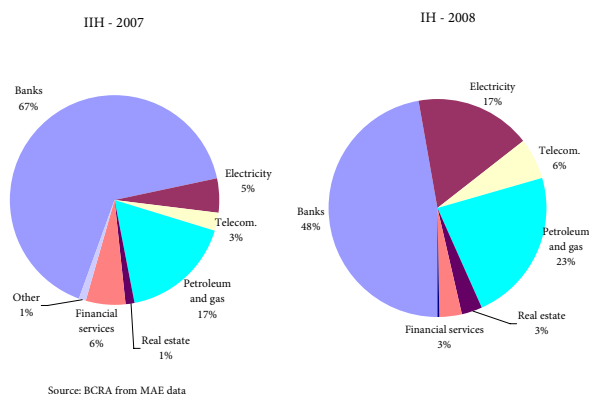
Financing by means of the issue of corporate bonds (ON) has dropped in the year to date as a result of the situation prevailing on domestic and international markets. Whereas in the first half of 2007 approximately \$6.1 billion was placed by means of such instruments, in the same period of 2008 the total fell to \$350 million (a trend that was maintained in subsequent months, despite one large issue). Taking into account all corporate debt issues (ON, SME ONs and short-term issues), financing totaled \$490 million during the first half of 2008, significantly below the total recorded in the same period of 2007 (see Chart III.12). The full amount raised by these issues has corresponded to new funds (rather than debt restructuring), a proportion that had been 96% and 46% in 2007 and 2006, respectively. Mention should be made of the fact that dollar-denominated issues have continued to predominate.

Chart III.14
Trading of Corporate Bonds
MAE and BCBA



In the case of issues classified by sector of the economy, and taking as a basis the ONs placed in the January-June 2008 period, those of the financial, commercial and metallurgical sectors have been predominant. In the same period of 2007 there was a greater presence by the energy and banking sectors. In the banking sector,

Chart III.15
Trading of Corporate Bonds by Economic Sector - MAE

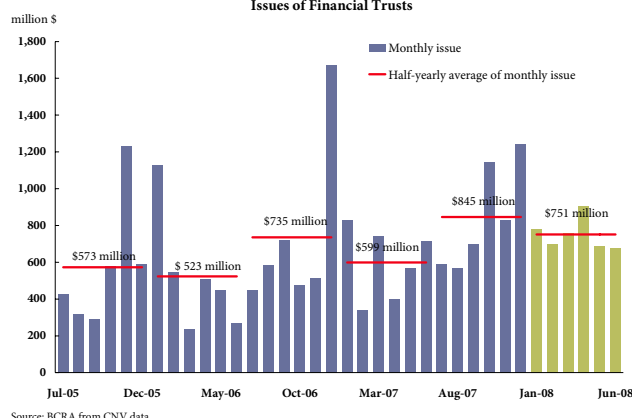


during the first half of 2008 only two placements of short-term paper were made (with a further issue in August). Two bank ONs have been approved by the CNV and await improved conditions to go onto the market.

The current situation on financial markets has also been reflected in the yields on private sector fixed income notes (see Chart III.13). In the case of ONs issued by banks, there has been a parallel upward movement in the yield curve, with a rise of almost 600 b.p. in the year to date (largely explained by the deterioration that has taken place in recent months).

Trading of ONs on secondary markets has increased. Taking the first half of the year (see Chart III.14) there was an increase of over 45% compared with the same period of 2007. Although the MAE has continued to account for the largest trading volume, the share accounted for by the BCBA has risen. In the case of ONs traded by sector, the degree of concentration has declined over the course of 2008 (see Chart III.15). In addition, whereas in the first half of 2008 six ONs accounted for half the deals on the MAE involving these instruments, only four had accounted for half the volume in the immediately preceding half.

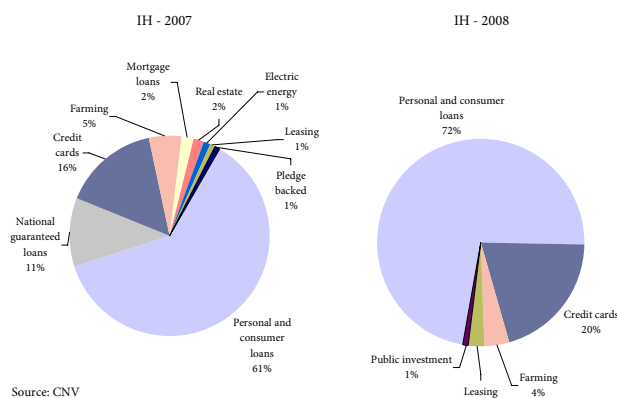
Chart III.16
Issues of Financial Trusts



Financial trusts, with consumer-related issues leading the way, have positioned themselves as the main marking financing instrument

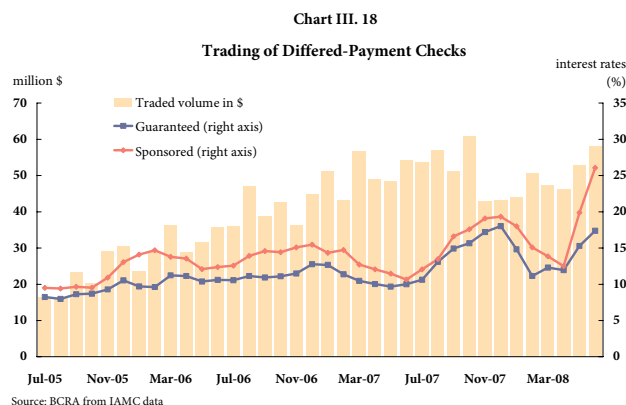
Financing by means of financial trusts has continued to post a sound growth rate in 2008 (see Chart III.16). For example, the amount placed in the first half of the year went up 25% compared with the same period of the previous year. The total amount placed has been in excess of \$4.5 billion, derived from 118 issuances. This trend (which persisted through the fourth quarter⁹) demonstrates the strength of this instrument as a source of finance, even during times of turbulence.

Chart III.17
Issues of Financial Trust - Classified by Underlying Assets



Securitized assets continue to be largely related to consumer finance -personal loans and credit card spending- (see Chart III.17) for an amount of close to \$4 billion (92% of the total amount placed) in the first half of 2008. During the same period of 2007 consumer financing accounted for a lower proportion of the total (77%), as a result of the issues with Guaranteed Loans as underlying assets. Sector activity can be explained by the

⁹ There was some slowing in August following changes made to the tax framework.



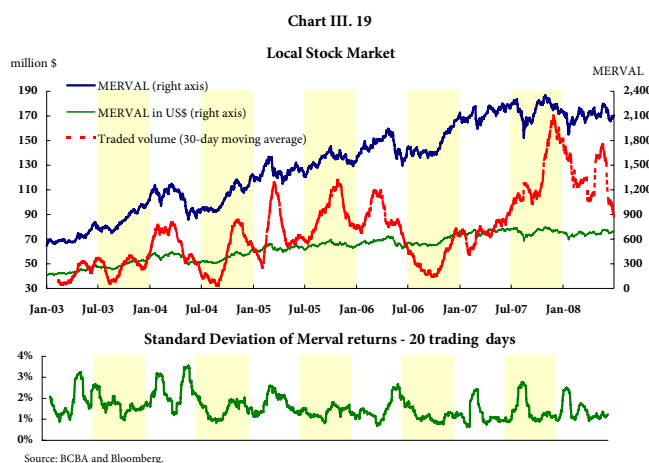
supply (household spending) and investor appetite for short-term instruments with a good risk to return ratio.

Good trading volume levels continued to be recorded by deferred payment checks, with a slight decline compared with 2007 (see Chart III.18). The average discount rate weighted by amount posted a sharp decline in the first two months of the year, returning to pre-turbulence levels. The change in the situation during the second quarter of the year led to a significant increase in rates, despite the fact that the yield being demanded for guaranteed checks was lower than that observed at the end of December. While the average rate at which checks guaranteed by a Mutual Guaranty Companies (SGR) fell back by an average 65 b.p., the rate on so-called sponsored checks increased on average by more than 670 b.p.. Given their greater relative cost, trading in sponsored checks continues to show signs of decline.

III.3 Equities

The local stock-market was affected by the international situation

The Merval has posted a loss of around 20% in the year to date (whether measured in pesos or in dollars) as a result of the crisis on international markets, in addition to matters of a local nature. Performance has been highly volatile (see Chart III.19), with a pronounced drop in January, improvement until May, and a subsequent collapse. The overall decline measured in dollar has been sharper than that seen in countries such as Mexico and Chile. These trends are expected to persist during the rest of the year, in a highly uncertain scenario at both international and regional level.

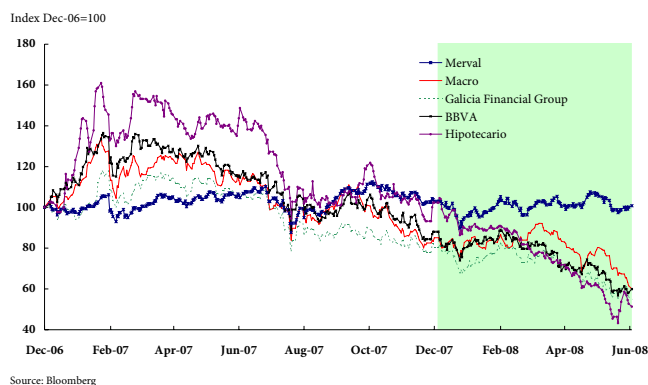


Market turbulence had a significant impact on equities linked to the domestic financial system (see Chart III.20). Shares of financial entities with the greatest participation in the Merval index have dropped close to 30% on average in the year to date. Shares in Tenaris, (the corporation with the greatest weighting in the index) have kept pace with the rise in oil prices over much of the period.

Equity trading volumes have not recorded any significant change. Average daily trading volume in the year to date has been close to \$90 million, within the range seen for 2007 as a whole.

Financing by the private sector by means of share issues was clearly influenced by the increased uncertainty of

Chart III. 20
Bank Stock and Merval Index



the situation. As a result, during the first half of the year this type of financing raised almost \$1.3 billion, including one initial public offering that generated over \$350 million (see Chart III.21). This share subscription total was less than the financing obtained in the two previous half-years (close to \$1.5 billion in each half of 2007).

An increase in the number of listed companies and capital increases for listed companies were only partly able to compensate for the drop in market capitalization as a result of the financial turmoil and growing risk aversion. Stock-market capitalization of local listed companies has dropped by over \$20 billion so far this year. Given the growth of the economy, the value of the local stock market in terms of GDP has fallen from 20% to under 15%.

III.4 Derivatives

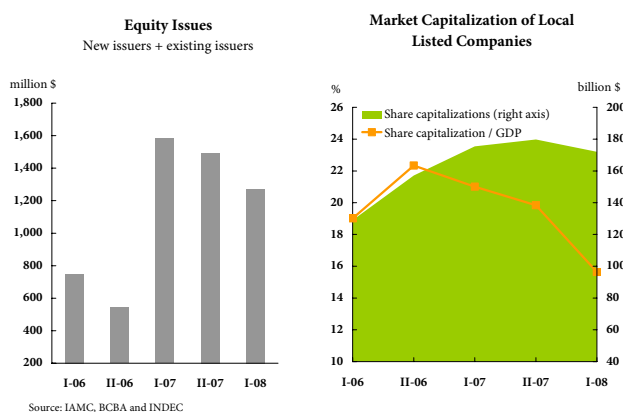
Trading volume in exchange rate futures reaches a new high

Trading in exchange rate derivatives set a new record for the year, reaching a level almost 100% higher than the total for the comparable period of 2007. On average, almost US\$6 billion has been traded per month in the year to date (see Chart III.2). On both the MAE and the ROFEX, trading in derivatives was up 60% on the monthly average for 2007. Activity level peaks were recorded in April and May, coinciding with one of the most significant episodes of turbulence (and more recently, in September, trading levels were also high). Increased trading volumes were in part associated with a greater level of Central Bank activity in forward markets. The Central Bank participated in both the spot market and by means of futures and forward contracts, with the aim of anchoring expectations.

As in 2007, a certain number of transactions were performed using the Discount Bond in pesos. Derivative transactions were also carried out using the BADLAR rate. In both cases, amounts continued to be marginal compared with the volume of exchange rate contracts. No futures were entered into with the CER index.

Looking forward, it is possible that expansion by the dollar futures market will be maintained this year and through 2009, as long as the critical situation in developed economies persists, generating an uncertain outlook at regional level.

Chart III.21



IV. Financial Intermediaries

Summary

The financial sector intermediation process continues on its growth trend led by the performance of the banking sector. Institutional investors (II) recorded a reduced expansion of their assets, mainly because of what happened with the mutual funds (MF) as a result of a more volatile international and domestic scenario.

The volume of pension and retirement fund (PF) assets grew again after the fall exhibited in the second half of 2007, and was boosted by the increase of contributions by workers especially (the contribution rose from 7% to 11% at the beginning of 2008), a change that was partly offset by the voluntary transfer of contributors to the pay-as-you-go regime and worsening profitability in a more volatile financial scenario.

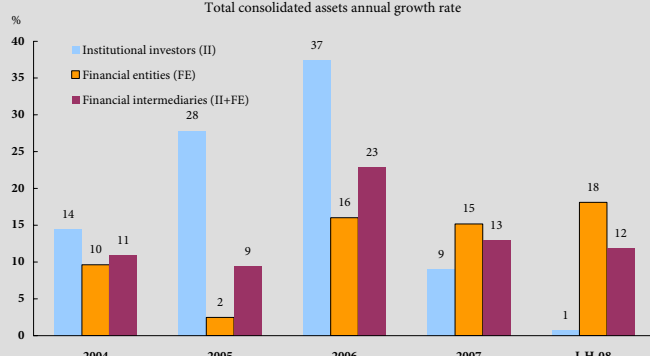
Pension funds increased their exposure to the public sector and to the financial system during the first half of 2008, as their shareholdings worsened and with smaller mutual fund holdings. While the insurance market continued expanding, mainly in general and retirement insurance, the mutual funds saw a fall due to the impacts of the financial turbulence on the equity funds. Institutional

investors are forecast to gradually resume their growth by the end of 2008, in a trend that will remain conditional on a gradual recovery of the financial markets.

In line with the incentives that the Central Bank has established, banks' financial intermediation continued deepening. Loans to the private sector remain on a growth path, although they record a more moderate momentum. The rate of expansion of household credit, especially for consumption, keeps standing out relatively. In the corporate segment, services, construction and the primary sector (excluding the farming sector) are all gaining share of banking finance. In the context of the financial policy carried out by the Central Bank, the financial system has been able to move towards a normal position, reflected by the persistent fall of its exposure to the public sector and the almost entire disappearance of debts for matching funds. Meanwhile the private sector deposits attained a 54% share in total funding of the banking system (netted liabilities plus net worth), while total deposits already account for almost three quarters of these funds.

Chart IV.1

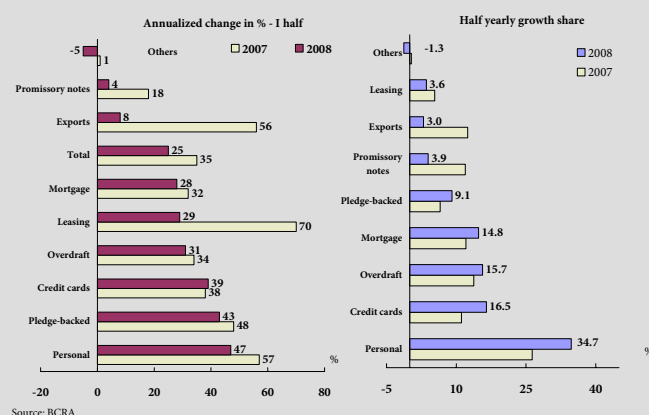
Local Financial Intermediaries Growth
Total consolidated assets annual growth rate



Note: Deposits in the local financial system are netted in order to consolidate investments from institutional investors.
Source: BCRA

Chart IV.2

Credit to the Private Sector by Type of Line



Source: BCRA

IV.1 Financial intermediaries

The local financial intermediaries partly reflect the volatility on the financial markets

Local financial markets continue reflecting the impact of the international turbulences during 2008. Adding to this scenario are domestic factors like the conflict with the farming sector and some deceleration observed in economic growth, although the GDP continues expanding at historically high rates. In this scenario the local financial intermediaries made up by the banks and the institutional investors –II– (pension funds, insurance companies and mutual funds) recorded a slightly more moderate growth of their consolidated assets¹⁰ compared to earlier years (see Chart IV.1), which mainly reflected the fall observed in the net worth of the mutual funds.

Looking ahead at the second half of the year, the estimated growth of the financial intermediaries should still be moderate, mainly explained by the persistence of a volatile international scenario. Furthermore, the expected increase in the number of contributors to the pension funds (PF) during the rest of 2008 will be relatively small, due to a gradually tighter labor market (see Page 26). Nevertheless, further wage rises in certain sectors and the impact of the increased personal contributions (from 7% to 11%) implemented at the beginning of the year may strengthen the funding sources for this sector. This context will be accompanied by a sustained growth of banking activity, while the mutual funds market should remain tightly linked to international financial conditions and the degree of aversion to domestic risk.

IV.2 Institutional investors

The share of bank deposits in institutional investment portfolios keeps growing

Consolidated assets under institutional investor management totaled about \$145 billion at the end of the first half of 2008, with an expansion of around 1%a. seen between January and June, and a slight fall in year-on-year (y.o.y.) terms. The increase observed in the first half of 2008 mainly reflects the increase in funds managed by the pension funds and the insurance companies, changes that were almost completely offset by the fall of the mutual funds.

Chart IV.3
Individual Contribution Regime

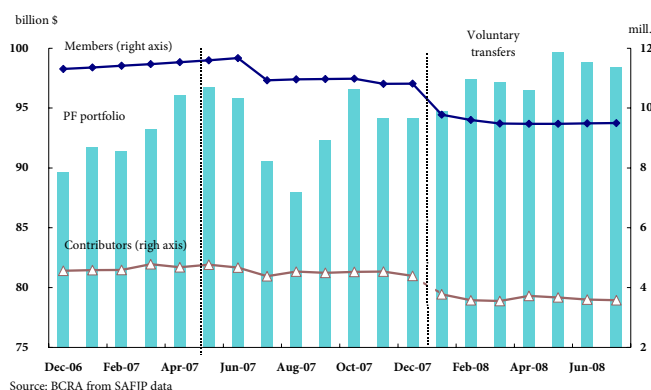
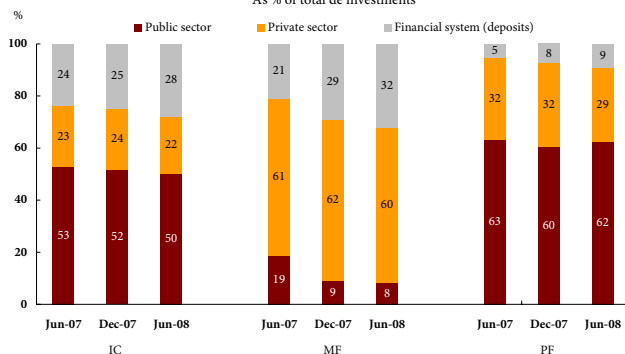


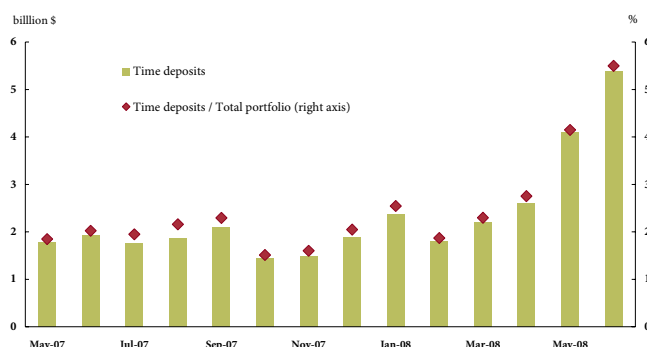
Chart IV.4
Institutional Investors Portfolio Composition
As % of total de investments



Note: Holdings of MF, IC and PF are assigned to sectors as the composition of MF portfolio.
Source: BCRA from SAFJP, Cámara Argentina de FCI and SSN data.

¹⁰ Bank deposits of insurance companies, mutual funds and pension funds are netted out.

Chart IV.5
Time Deposits of Pension Funds
Total stock



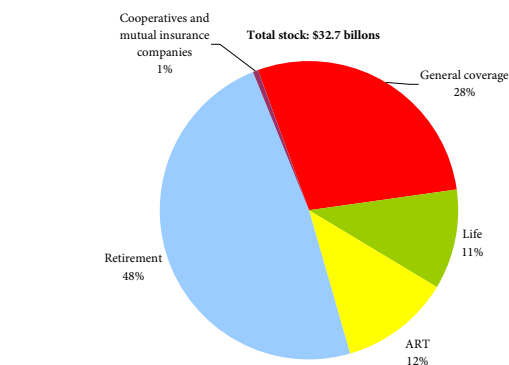
Source: BCRA from SAFJP data

The volume of funds managed by the pension funds resumed their upwards path during these six months, after the fall they recorded towards the end of last year due to transfers of members (and their respective cumulative investments) to the pay-as-you-go regime¹¹ (see Chart IV.3). The investment portfolio of the pension funds totaled approximately \$99 billion¹² at the end of June, with a 10%a. increase during the first six months of the year.

The pension fund performance was mostly explained by the increased revenues, in a framework of the recovery of the personal contributions rate (from 7% to 11%) since the beginning of 2008 and of nominal wages of workers. These effects were partly offset by the decline in the number of contributors during the first six months of the year, which reflected the first window for the voluntary transfer option since the individual capitalization regime started operations in 1994 and the contractive impact of the profitability during the period.

The investment portfolio of the pension funds channeled to financing the private sector saw a semi-annual decline of almost 3 p.p. to 29% (see Chart IV.4), a change that was mainly explained by the impact of volatility on the stock market during the six months period and by the smaller mutual fund holdings¹³. The funds targeted at the public sector continue exhibiting the largest weighting in pension fund portfolios (almost 62%), with a 2 p.p. increase during the first half of the year. The funds deposited in the financial system (mostly as time deposits) recorded a significant increase to reach a 9% weighting in the portfolio. The increase of time deposits at banks was concentrated as from April (see Chart IV.5).

Chart IV.6
Insurance Market Composition
Investments - June 2008



Source: BCRA from SSN data.

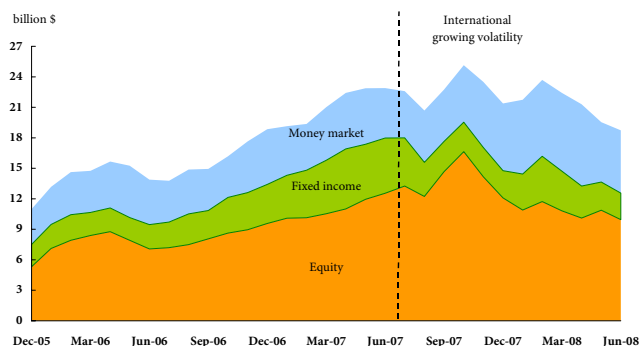
The volume of insurance company assets totaled approximately \$44 billion by mid 2008, exhibiting a 17%a. increase during the first six months of the year, accumulating a slightly lower expansion (16%) in y.o.y. terms. Retirement insurance (with a longer maturity term for its investments) and general insurance still dominated the expansion of the sector (see Chart IV.6). As for the pension funds, the public sector assets amply lead the investment portfolio allocation of the insurance companies (over 50%), followed by deposits in the financial system and by finance to the private sector (of which the mutual fund weighting stands out).

¹¹ Law 26,222. For further details of the changes that were made see FSB I-08, Section IV.1.

¹² Non-consolidated data.

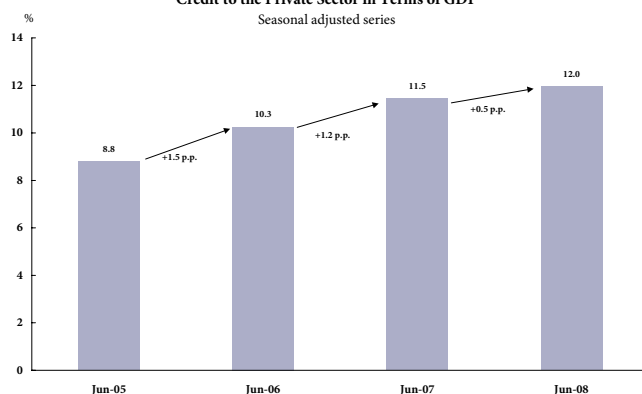
¹³ On this subject, it should be recalled that in October 2007 the Pension Fund Management Superintendent (SAFJP), the Central Bank and the National Securities Commission (CNV) issued a joint resolution that stipulates a cap of 2% of the portfolio for mutual funds with net worth of Mercosur issuer assets.

Chart IV.7
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.

Chart IV.8
Credit to the Private Sector in Terms of GDP
Seasonal adjusted series



Source: BCRA

Table IV.1

Balance Sheet

Financial system - As % of netted assets

	Jun-07	Dec-07	Jun-08	HI-08 variation (p.p.)	Half-yearly HI-08 % change annualized
Assets	100	100	100		18
Liquid assets	16	17	18	1	40
Lebac and Nobac	13	11	11	0	12
Credit to the private sector	34	40	41	1	25
Credit to the public sector	19	17	15	-2	-8
Other assets	17	15	15	0	14
Liabilities + Net Worth	100	100	100		18
Private sector deposits	18	17	20	1	54
Public sector deposits	53	56	54	1	11
Liabilities with the BCRA (1)	1	1	1	-1	-11
ON, OS and foreign lines of credit	5	4	4	-1	3
Other liabilities	9	9	9	0	23
Net worth	13	13	13	-1	11

(1) Includes matching schedule and other liabilities with the BCRA

Source: BCRA

Like the final months of 2007 mutual funds were still affected by the volatility exhibited by the international and domestic financial markets. This scenario impacts on the prices of security and stock portfolio holdings, and to some extent leads to unit share redemptions. At the end of the first half of 2008 the net worth of the mutual funds saw a 23%a. decline from the end of 2007, to reach a total slightly more than \$18.7 billion (see Chart IV.7). The fall was mostly explained by equity funds (which have the most significant volume) that recorded a fall of almost \$2.15 billion (down 32%a.) during the first half, to account for about 80% of the total reduction. The money market funds saw fell almost \$450 million (down 13%a.) in the first half of 2008. In a manner similar to the end of 2007 the more uncertain scenario was reflected by a larger share of liquid assets in the mutual fund portfolios (accounting for about a third of the total). This change was offset by the falling share of finance for the private sector.

IV.3 Financial entities

Credit to the private sector kept growing during the first half of 2007, although it moderated its rate of expansion

Stimulated by the Central Bank's financial policy, the banking system continues supplying the demand for credit by households and firms, despite the volatility seen on the international financial markets and some uncertainty at the local level. Loans to the private sector were thus equivalent to 12% of the GDP in mid 2008. Although this ratio is slightly less than at the end of 2007 due to the momentum of economic activity, it is 0.5 p.p. higher than the same period in 2007 (see Chart IV.8), and exceeds the minimum recorded following the 2001-2002 crisis by almost 5 p.p.. The scope for credit still exhibits a strong growth potential, because it is still below the levels observed in other countries in the region and in developed economies.

In this scenario the financial system maintains the trend to crowd in the private sector, partly offsetting the persistent rescaling of the banking exposure to the public sector (see Table IV.1).

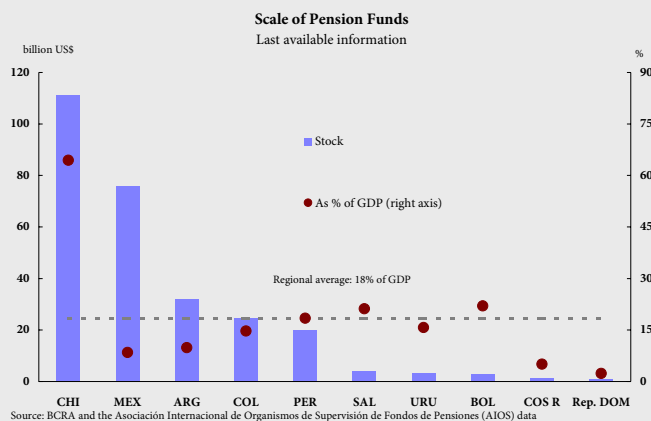
Box 2 / Pension Funds in Domestic Financial Intermediation

In recent years the pension funds have attained a considerable size boosted by the regular contributions from the workers, new members joining them and the profitability of their investments. This trend has not been accompanied by a deepening of their funds being targeted at financing the domestic productive sector, which is one of the pending issues for coming years

During the 1990s several Latin American economies changed their retirement and pension schemes to adopt individual capitalization schemes (SCI)¹⁴. In some cases the SCI started to operate independently from the government pay-as-you-go regimes (RR), while in other countries they replaced the latter entirely. Overall, these changes sought to avoid the financing problems observed in the RR on many occasions and to improve incentives for contributors, because their future earnings would have more correlation with the contributions that they made, and to stimulate deepening the domestic capital markets, a situation that would enable stimulation of financing by the domestic capital markets, mainly for firms. The ultimate purpose of the SCI is to increase the yields for the contributors and their future pension or retirement benefits.

In Argentina, specifically, the SCI started operating in 1994 alongside the RR, in the framework stipulated by the Integrated Retirement and Pension System (Law 24,241). Starting with total funds of approximately \$2.5 billion (1% of the GDP) in 1995, the pension and retirement funds (PF) have by now achieved a volume of around \$98 billion (almost 10% of the GDP), to have intermediate amounts compared to the other SCI in the region (see Chart B.2.1) and still show a large potential for growth and scope in terms of the workforce.

Chart B.2.1



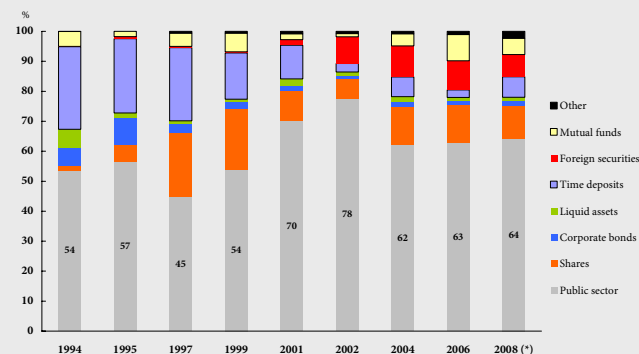
¹⁴ Chile incorporated the system at the beginning of the 1980s.

Locally the PF are the largest institutional investor in terms of the funds available for management, followed in size by the insurance companies and the mutual funds. The considerable development of the Argentine SCI was mainly explained by the increase of both the number of workers contributing, which at present total around 3.6 million persons¹⁵, the increase of revenue from each contributor and the profitability accumulated by the sector (at an almost 14% nominal historical rate or 8% in real terms), in a framework of few pension an retirement outlays granted until now because the system is at an initial stage.

Since the SCI were established in Argentina only a limited share of the funds available has been deployed as investments in the productive sector, with the funds being absorbed especially by the public sector's financial requirements, which throughout the period were more than half the portfolio (except in 1997), peaking at 78% in the 2001-2002 crisis, to exhibit some stabilization in recent years at around 60% (see Chart B.2.2).

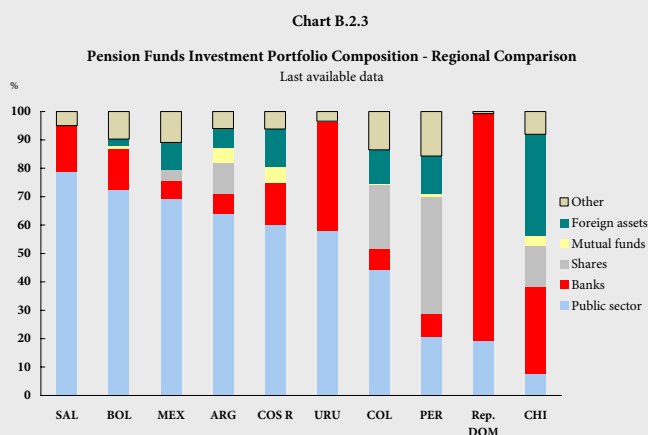
Chart B.2.2

Pension Funds Portfolio Composition, Argentina



It is noteworthy that the large exposure to the public sector is a feature common to most SCI in Latin American countries (see Chart B.2.3), mainly as a result of the financial needs of their governments. Although Chile is an exception, partly due to the low level of its public sector debt, at an early stage of its development (at the beginning of the 1980s) the public sector funds had more weighting in the aggregate portfolio.

¹⁵ As from the changes adopted by Law 26,222 (2007) the capitalization system saw transfers to the RR.

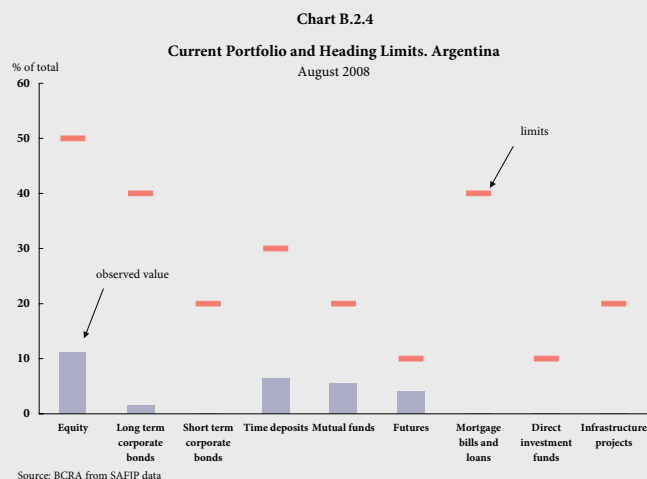


Source: BCRA and the Asociación Internacional de Organismos de Supervisión de Fondos de Pensiones (AIOS) data

Offsetting the considerable exposure to the public sector, only a small share of the domestic PF can be regarded as financing investment directly: long term corporate bonds (ON), direct investment funds (FID), for agriculture or livestock, and the recently included productive and/or investment projects. For this last item a new clause (“q”) was included in the SCI by the 2007 pension reform that considers such investments among the PF investment options, with a minimum of 5% of the total assets of the funds and up to a 20% maximum.

The share of long term corporate bonds in the portfolio is 1.44%, while for FID the weighting is 0.10% and the productive and infrastructure projects only account for 0.02% of the portfolio. These figures are still much smaller than the maximums stipulated in the regulatory framework (almost 70% of the portfolio if the three

headings mentioned are considered). The investments in government bonds and in foreign securities are the only headings that are near their admissible maximum. For the rest of the headings the weightings are far below their caps (see Chart B.2.4), which leaves room to increase financing of the corporate sector.



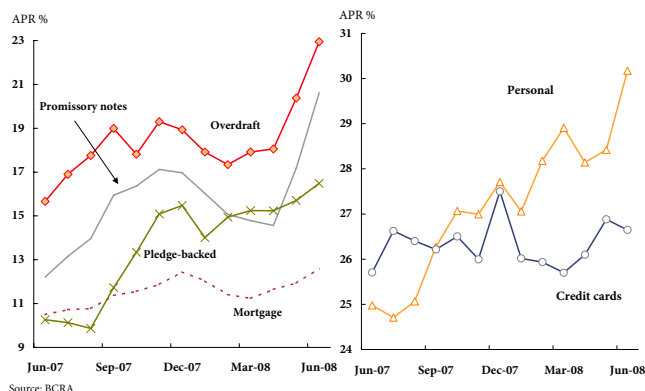
Source: BCRA from SAFJP data

Therefore, until now the local SCI have shown some weaknesses when it came to stimulating finance for the productive sector, as it finds credit for the public sector to be a considerable restriction. Nevertheless, there is room to increase financing of the economy, a trend that has to be supplemented by the presence of adequate investment tools and genuine productive projects that require financing.

Chart IV.9

Lending Interest Rates

Credit to the private sector - Financial system

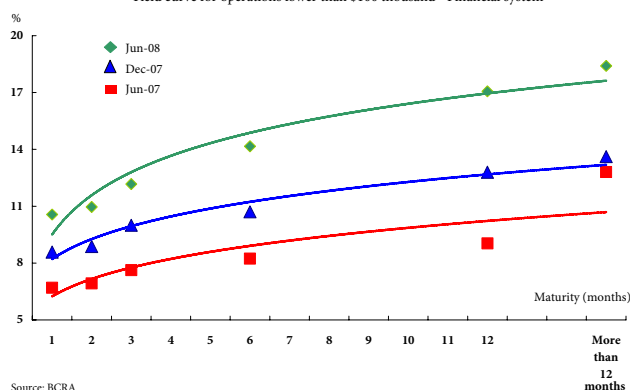


Source: BCRA

Chart IV.10

Private Sector Time Deposits in Pesos

Yield curve for operations lower than \$100 thousand - Financial system

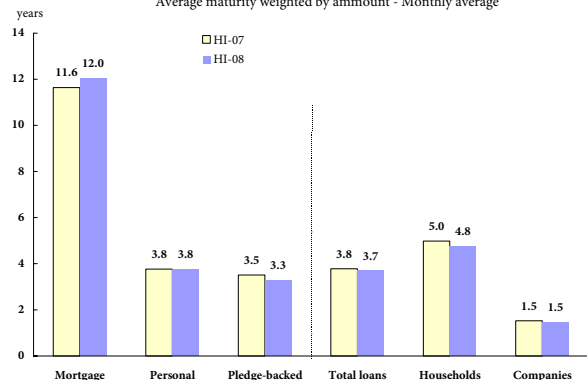


Source: BCRA

Chart IV.11

Lending to the Private Sector

Average maturity weighted by amount - Monthly average



Source: BCRA

Specifically, the exposure of the banking system to the government is dropping by 2 p.p. of netted assets so far in 2008, to accumulate a 4 p.p. fall in the past 12 months. Loans to the private sector¹⁶ continued growing during the first half of 2008 (25%a.) (see Chart IV.2), although they moderated their rate of expansion relative to the same period last year (35%a.). Due to this increase, credit for firms and families in June was 41% of the netted out assets of the financial system, 7 p.p. more than the same period last year.

The decline of the growth rates of credit to the private sector was widespread among loan lines during the first half of 2008, except for credit card finance that exhibited slightly more dynamism. Commercial loans (promissory notes, leasing and export finance) exhibited the most moderation in their rate of expansion. On the other hand, despite recording declines in their performance, overdrafts and leasing exhibited a higher rate of growth than the aggregate.

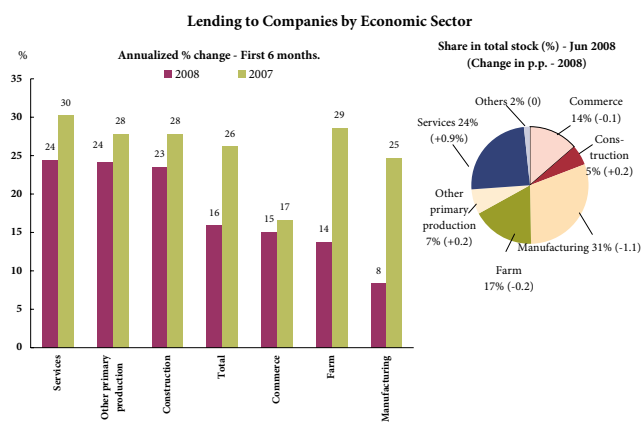
Personal loans are still the most dynamic heading, as they became the credit segment with the largest contribution in the stock of loans to the private sector. Personal loans therefore acquired the largest share of the private sector portfolio (21%), exceeding promissory notes (19%). Personal lending lines, added to the credit cards, exhibited a 44%a. increase, accounting for more than half the growth of loans in the first six months of the year. Meanwhile, loans with real collateral still exhibited an outstanding momentum during the first half of 2008, at a similar pace to that recorded in the same period last year. Therefore, these lines gained weighting in the aggregate growth of credit for the private sector.

Growth of household and corporate loans occurs in a scenario of gradually higher interest rate levels (see Chart IV.9). The most significant rises were recorded by the commercial lines (overdrafts and promissory notes) and for personal loans, while credit card finance was the only segment with a slight decline in its interest rate between the beginning and the end of the six months period. It is worth noting that the increase of the interest rates mainly reflects the impact of the higher interest rates on time deposits (see Chart IV.10), partly because of the scenario of rising financial volatility. Nevertheless, the liquidity measures that the Central Bank adopted (see Page 54) have been able to moderate this growth.

The durations of new loans granted to the private sector remain stable overall so far this year (see Chart IV.11).

¹⁶ Including leasing finance.

Chart IV.12



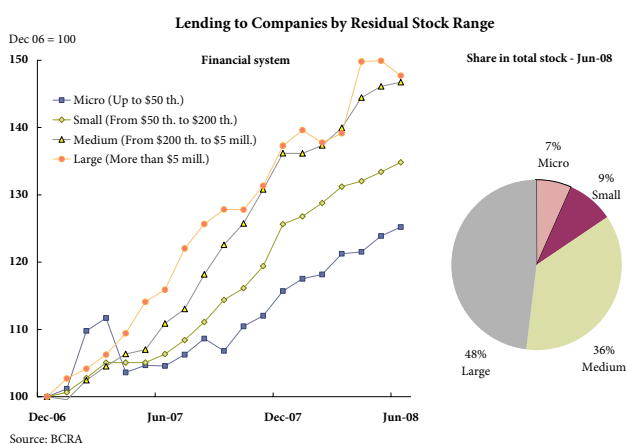
Source: BCRA

Nevertheless, some shortening of the lines for families is observed, except for mortgage loans which at present are for almost 12 year terms. Apart from this behavior, household finance still exhibits longer terms than those channeled to the corporate sector.

Corporate credit keeps growing, mostly driven by services and primary production

Finance to the corporate sector records a deceleration for all sectors in general during the first six months of 2008 (see Chart IV.12). By growing above the average the loans to services, construction and primary production firms (not including the farming sector) are gaining share, although manufacturing still concentrates the largest weighting (a third of the total).

Chart IV.13



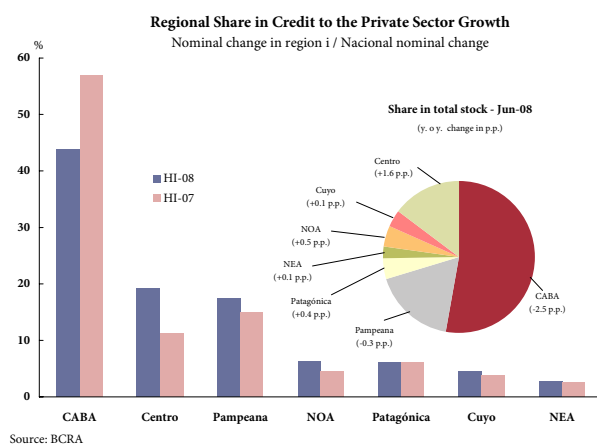
Source: BCRA

The expansion of corporate credit lines is generalized among all outstanding tranches, while a gradual deceleration of the expansion of the largest tranches is seen. Despite still having a small share in financing the corporate sector (see Chart IV.13), the loans with the smallest stocks (less than \$200,000) exhibit some acceleration during the period.

The penetration of credit to the private sector is growing in the geographical regions of Argentina with a lesser relative access

Although credit to the private sector is still concentrated in Buenos Aires city, the growth seen in the first half of 2008 was better distributed among the Argentine regions that have a smaller weighting in the total, such as the North East (NEA). Cuyo and the North West (NOA) (see Chart IV.14). Specifically, the three regions that concentrate three quarters of total credit to the private sector (City of Buenos Aires –CABA–, Pampas and Center) record a smaller share of the aggregate credit growth compared to the first half of 2007, and as a result a gradually greater uniformity in the shares that the different regions have in credit to the private sector is therefore seen. While the City of Buenos Aires and the Pampas region reduced their weighting slightly, the remaining regions increased their share of aggregate credit.

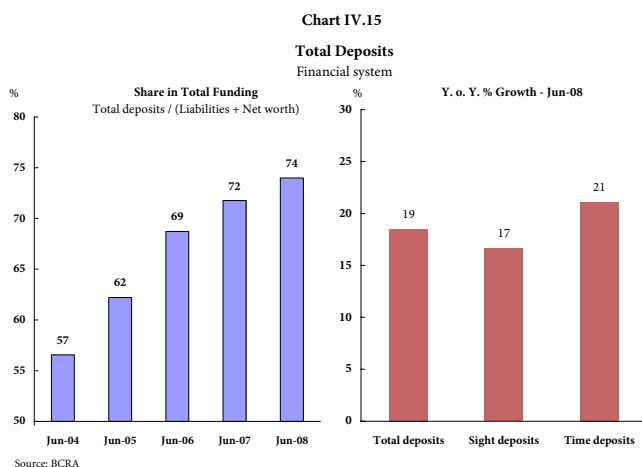
Chart IV.14



Source: BCRA

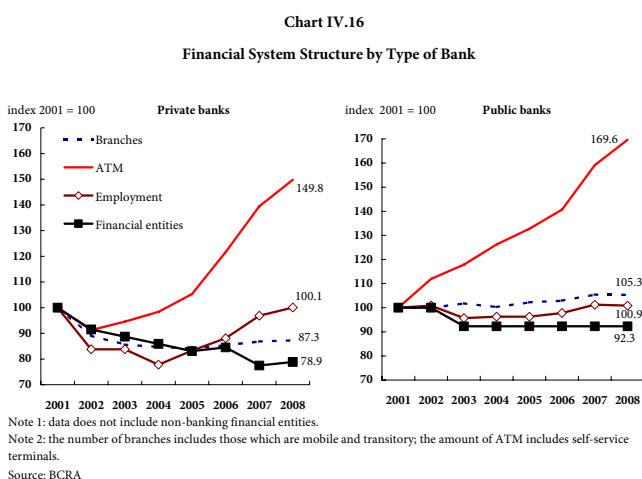
In a scenario of persistent normalization of liabilities, deposits increase their share of bank funding

In line with what was seen in recent years, the stock of total financial system deposits increased 20.4%a. in the first half of 2008, mostly explained by the performance of the public sector deposits (that grew 53.6%a.) and to a



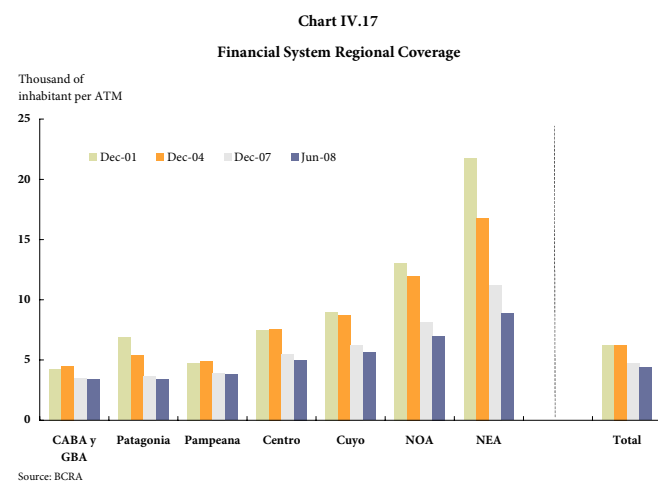
lesser extent by the private sector deposits (10.6%a.). It should be noted that in May private sector deposits recorded a temporary fall, which was not associated with the fundamental variables of the financial system, that was rapidly reversed by the timely Central Bank actions (see Page 7). Total deposits were also boosted by both sight and time deposits, with the latter being more dynamic. Aggregate deposits thus continued gaining share in total funding (netted liabilities plus net worth) of the banking system as they accounted for 74%, 2 p.p. more than in mid 2007 (see Chart IV.15).

The rediscounts for illiquidity that the Central Bank had granted during the 2001-2002 crisis, on the other hand, were reduced during the first half of 2008 until at present they only account for 0.4% of the financial system liabilities, 0.1 p.p. less than at the end of 2007 and 9.8 p.p. lower than at the end of 2004. These liabilities have therefore practically disappeared from bank balance sheets, as only one financial institution of the 24 initial banks still has debts under the matching schedule.

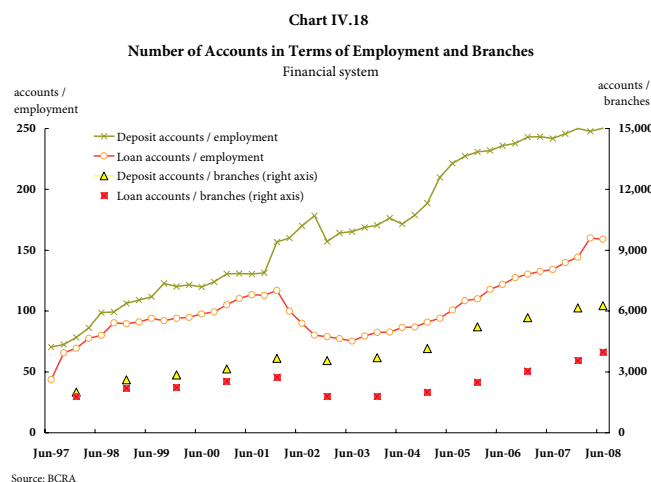


The number of ATMs and branches increased, while the domestic capital private sector banks increased their share in private sector deposits

The persistent increase of financial intermediation activity is still reflected by both the growth of staff and of the number of branches and automatic teller machines (ATM). In the first six months of 2008 bank staff grew 1.8% (1,700 employees) with a cumulative 4.4% (4,100 persons) y.o.y. growth, and therefore surpassed the December 2001 figures at both public and private sector banks (see Chart IV.16). The amount of ATMs rose 7.2% (600 units) during the first half of 2008 and 16.6% (1,300 units) in the past 12 months. The number of ATMs is thus almost 55% more than the stock of 2001, a trend which though showing more momentum at the public sector banks (starting from lower levels) is mainly explained by the private sector financial institutions. The number of branches increased slightly (10 branches) in the first half and 1.7% (66 branches) during the past year, although it still remains below the pre-crisis number in the private sector banks.

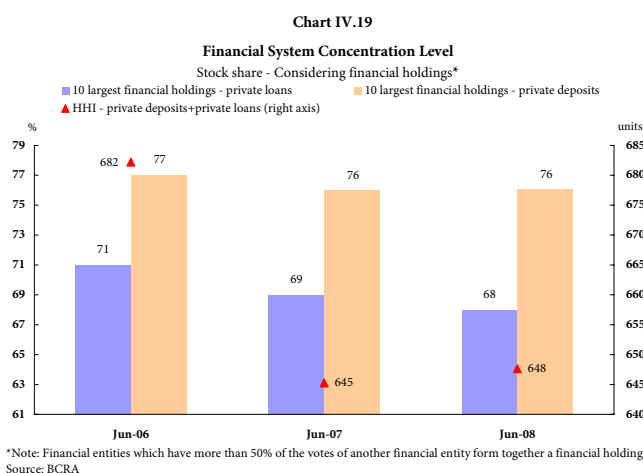


The growth and distribution of ATM behavior seen in recent years has been generating an improvement in the regional access to financial services throughout Argentina. In this context, the number of inhabitants per ATM continues exhibiting significant progress in the regions with less coverage (NEA, NOA and Cuyo) (see Chart IV.17), reducing to 2.6 times the gap between the regions with most and least coverage (4.1 times before the crisis).



The growth of the financial system operating structure mentioned above is happening in a scenario of an expansion of the number of accounts (for deposits and for loans) per employee and per branch, to exceed the figures recorded in 2001 (see Chart IV.18). The banking system thus continues showing progress in its operating efficiency level in terms of these indicators.

It is worth noting that the Central Bank is still increasing the incentives to achieve a greater coverage by the domestic financial system in order to encourage the banking depth, both regionally and by economic strata. Therefore, at the beginning of the year the categories to determine the minimum capital for financial institutions by jurisdictions were readjusted, and the bureaucratic burden to open new branches was also reduced. On the other hand, with the purpose of having the financial institutions offer a standard product to make for easier comparisons, transparency and scope of financial services, a “Basic Account” is being adopted in the rules on savings deposits, wage and special payments, for the banks and mutual credit cooperatives.



The degree of financial system concentration remains stable in the period (see Chart IV.19). On the other hand, deepening the dynamics that began in the post-crisis period, the banking system continues increasing its trend towards a more uniform market distribution by bank class. In the first half of 2008 the domestic capital private sector banks increased their share of private sector banks to 33% at the expense of the foreign banks, although this grouping still has the largest market share (36%).

Box 3 / The Scale of Microfinance in Latin America

Microfinance activity has managed to achieve a growing activity in Latin America in recent years. Although it still has a strong growth potential, this business segment is still at an initial stage in Argentina, while a larger number of financial institutions decide to get involved in providing financial services to the low income sectors of the population

Microfinance activity is usually defined as the supply of financial services to low income individuals, mainly by small loans for commercial or personal use, deposits, money transfers, means of payment and insurance¹⁷. These services are usually marketed by the microfinance institutions (MFI), which include credit unions, small scale commercial banks, non-government organizations (NGO) and credit cooperatives, as institutions that carry out this task of identifying the population to be catered for and design the methodology to allocate funds and then for their repayment.

Microfinance (MF) originated in the 1970s, and was started by Bengali economist Muhammad Yunus who granted his own funds to poor individuals to be used to finance small-scale undertakings that lacked guarantees. These efforts later led to establishing the Grameen Bank, which at the end of 2007 had 7.4 million partners and a loan portfolio of US\$530 million¹⁸.

The MF have characteristics that differ substantially from traditional finance. Firstly, as a substitute for the lack of tangible collaterals, solidarity responsibility guarantees or joint debts are often used, which therefore mitigates the possible adverse selection and moral hazard problems. In addition, the loan portfolio is atomized, in general with a low sector diversity and a high rotation index, while the loans are for short terms, with repayment according to the business cycle of micro-entrepreneurs (weekly or twice a month). The extensive use of staff and of information intensive methods by the MFI is usually reflected as high operating costs, and therefore by higher interest rates on their loans.

¹⁷ Consultative Group to Assist the Poor (CGAP, 2003): "Microfinance Consensus Guidelines: Guiding Principles on regulation and supervision of microfinance"; Delfiner, Pailhé y Perón (2006): "Microfinanzas: un análisis de experiencias y alternativas de regulación" (Microfinance: An analysis of experiences and regulatory choices), BCRA.

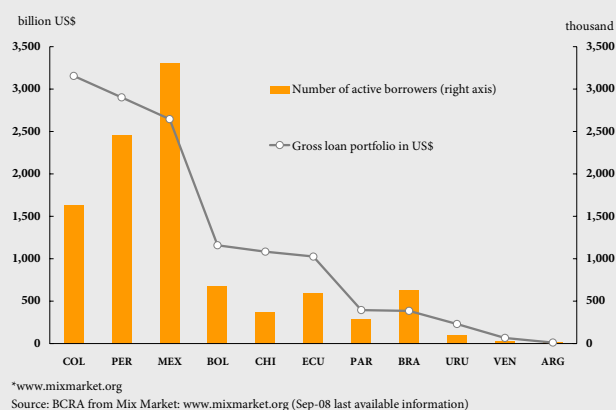
¹⁸ www.grameen-info.org

These intrinsic characteristics of MF activity, in combination with the low yield that the sector was usually understood to have (due to the high unit costs and the little potential demand for these services), meant that historically the commercial banks have not involved themselves in MF activity. This viewpoint has been changing during recent years, together with the proven profitability of the banks that adopted this activity (downscaling¹⁹) –some of these banks being large scale- led to new banks entering into the MF business.

In Latin America MF started with its initial steps in the 1970s, together with a number of NGOs that had the purpose of providing funds to a population segment that the banking system was not catering for. At present, in some countries the MF are part of the traditional financial systems as a result of the NGOs becoming formal financial institutions (upgrading), as happened with BancoSol in Bolivia or MiBanco in Peru, or as a result of the already existing commercial banks starting to provide MF services, like Bancolombia in Colombia or Banco del Trabajo in Peru, for example. As a result, MFIs already have about 11 million clients in the region and a portfolio of over US\$14 billion²⁰ (see Chart B.3.1).

Chart B.3.1

Latin American MIX MARKET* Listed Entity Statistics



This MF development in recent years has led these institutions to gradually become subject to the prudential regulations. As the MFI size achieved larger scales in order to cater for the growing demand for financial services, the need to attract savings from the

¹⁹ Delfiner & Perón (2007): "Los bancos comerciales y las microfinanzas" (Commercial banks and microfinance), BCRA.

²⁰ According to the financial institutions listed in the Mix Market for Latin America and the Caribbean.

public was therefore posed. As a result, the MFI began to enter into the orbit of the sovereign regulators that have a mandate to safeguard the interests of small savers and ensure systemic financial stability.

In Argentina a relatively little microfinance development is still observed. Particularly, among the main legal status that the MFIs have adopted locally are NGOs and joint stock companies (Ltd.), and there are no banks dedicated solely to MF. Although the universe of institutions and programs is heterogeneous, there is a strong concentration in the financial institutions associated in the Argentina Microcredit Institution Network (RADIM)²¹ (see Table B.3.1).

Table B.3.1
Scale of Microfinances in Argentina

MFIs	Type of institution	Gross loan portfolio in \$	Average credit stock in \$	Number of active borrowers	Credit consultants
RADIM associated	Ltd.	43,069,283	2,699	15,956	94
	NGO	10,316,545	960	10,747	60
Other	Ltd.	25,652,054	2,693	9,526	120
	NGO	2,229,537	785	2,841	13
Total		81,267,419	2,080	39,070	287

Note: Total is undervalued because data for smaller MFIs is not available.

Source: BCRA from RADIM (Jun-2008 information), PNUD project (Jul-2008 information) and other.

The Argentine financial institutions who seek to dedicate part of their business to MF can use certain regulatory figures advantageously to channel their transactions. On the one hand, the Central Bank has permitted “low value loans”, which only require the client identification for them to be granted and do not require formal guarantees. On the other hand, the possibility of “temporary customer attention offices” was authorized, by which banks can set them up in towns that do not have branches to enable them to reach possible microfinance clients. Likewise, MF can have shares in the credit union cooperatives, which also have a line for small value loans.

As regards public sector programs supporting MF, in 1997 the “Fondo de Capital Social” (FONCAP) was established, originated as a limited company to manage a fund originally set up with a contribution from the national government. Its mission consists of using money as funding for institutions dedicated to MF, so that it is a second tier organization. On the other hand, the Microcredit Promotion Law issued in 2006 established a new fund to back the MFI activities.

Although commercial bank participation is as yet at an initial stage, there are a number of financial institutions that have entered into MF in Argentina. At present Banco de la Provincia de Buenos Aires and Banco de la Ciudad de Buenos Aires have a second tier role through their “Fuerza Solidaria” and “Ciudad Microfinanzas” programs, respectively. On the other hand, in 2004 Banco de la Nación Argentina started operations of the “Fondo Nacional para la Creación y Consolidación de Microemprendimientos” (FOMICRO), coordinated together with the Small and Medium Enterprise Undersecretariat. Later FONDER was created, a trust fund that provides financial and technical assistance at an intermediate scale for regional development.

Within the private sector banks group in 2006 Banco Columbia entered into a strategic alliance with Acción Internacional to develop a microfinance services arm, which led to Columbia Microcréditos Ltd. On the other hand Banco Supervielle set up Cordial Microfinanzas Ltd., which began operations in 2007. In 2006 Banco Hipotecario decided to channel its efforts towards microfinance through “Fundación Pro Mujer” (in Salta and Jujuy), while in 2007 Banco Santander Río developed the first stage of the microcredit program focused on financial assistance for MFIs organized as NGOs, by providing soft term finance.

Although there is still a broad dispersion between countries, microfinance has exhibited a significant growth of its activity, although there is still a significant path to travel in order to better satisfy the credit needs of the low income segments of the population. These could be supplied with funds from both non-regulated entities (NGOs and Ltd.) and the gradually increasing participation of the commercial banks.

²¹ Alternativa 3, FIE Gran Poder, FIS Empresa Social, Pro Vivienda Social, Entre Todos, Progresar, Fundación Grameen Mendoza, BM de la Mujer / INTIHUACA, Pro Mujer.

V. Risk Management

Summary

Within a context of growing financial volatility and a certain deterioration in the global economic situation, the domestic financial system maintained an appropriate profile for the risks it carries, backed by the measures introduced by the Central Bank.

Banks continue to deepen their financial intermediation with the private sector, at the same time as they reinforce their liquidity levels. This activity benefited from the measures introduced by the Central Bank that promptly corrected the temporary mismatch in the demand for money that took place in May. As a result, banks are in a sound position to confront liquidity risks.

The financial system has further increased its exposure to the private sector, a development that is taking place in the context of moderate improvements in the labor market and growth by the various productive sectors of the economy, ensuring they maintain a sound repayment capacity. One indicator of this scenario is the fact that private sector loan non-performance stands at 3.1%, having fallen over the course of the year. Credits to companies have continued to show an improved performance, while the quality of the portfolio of loans to households has been evidencing some signs of deterioration, driven by consumer lines. In this context, banks continue to record provision levels in excess of their non-performing portfolios.

The position of banks in relation to risk from the public sector remains sound, at a time when fiscal accounts are positive and declining levels of indebtedness underscore the good payment capacity of the sector.

Facing certain volatility in the nominal peso-dollar exchange rate, the financial system has gradually been reducing its exposure to foreign currency risk. At the same time banks are holding their exposure to interest rate risk relatively stable, with mismatching between CER-adjusted assets and liabilities items that have not changed significantly in 2008. Security valuation regulations introduced by the Central Bank in the second half of 2007 succeeded in preventing volatility in financial asset yields from generating any excessive impact on financial system net worth.

At the beginning of 2008 minimum standards were introduced for financial entities operational risk management, establishing that it should be treated as a comprehensive discipline, distinct from the management of other risks, identifying the factors that give rise to it, their monitoring and management methods. Full implementation is planned for the end of 2009.

For the rest of the year, the local impact of deepening turmoil on financial markets represents the main factor to be monitored, to prevent any materialization of the risks faced.

Chart V.1

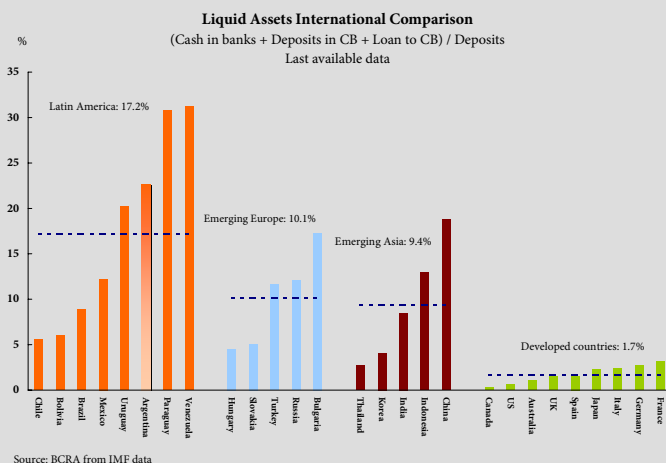
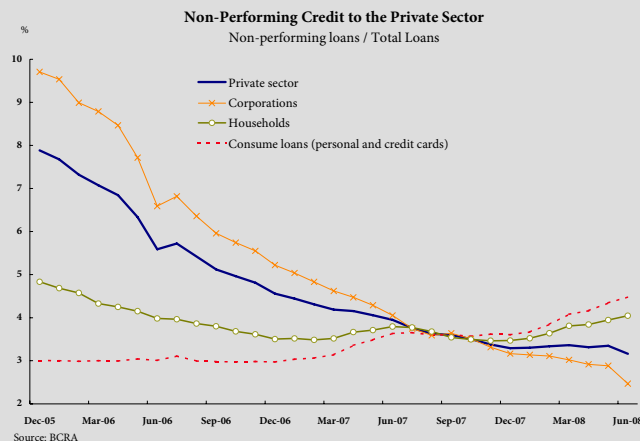


Chart V.2



V.1 Liquidity risk

Banks continue to show a sound position in the face of liquidity risk, a situation encouraged by the timely actions of the Central Bank

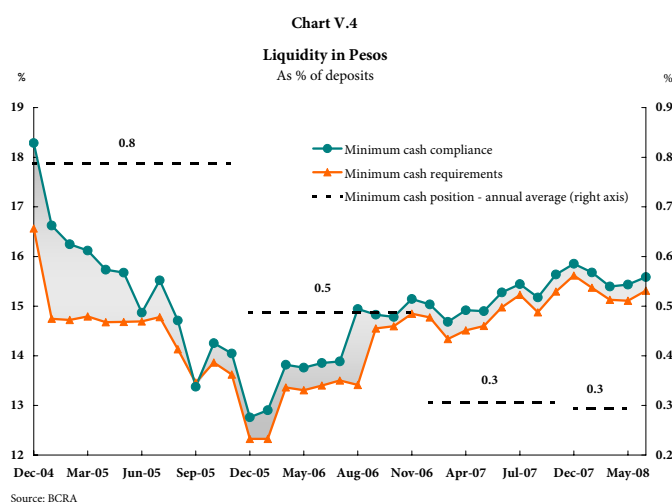
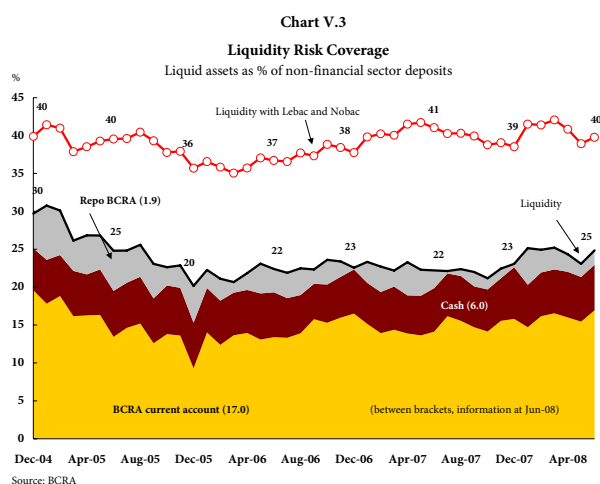
Encouraged by the measures implemented by the Central Bank during the first half of 2008, banks have continued to deepen their financial intermediation with the private sector, at the same time as ensuring adequate liquidity levels. As a result, it has been possible to reduce the impact of the scenario of greater financial volatility on banking activity.

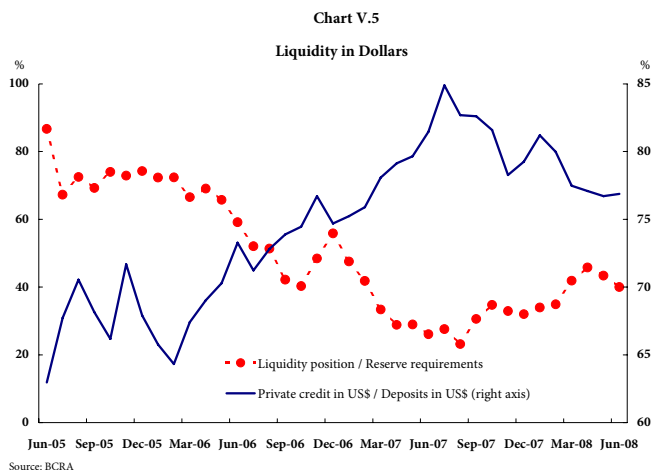
Private sector deposits posted an increase (11%a.) in 2008 to date, after recording a temporary decline in May unrelated to the situation of the financial system or the fundamentals of the economy. In this context, the Central Bank implemented a series of measures that ensured the situation was rapidly corrected. Specifically, liquidity was injected by means of a reduction in the outstanding stock of Lebac and Nobac, and the repo mechanism was overhauled: in mid-May reverse repos at fixed rates for up to a total of \$3 billion were reintroduced, and reverse repos at variable interest rates were also made available (with a fixed margin over the private bank BADLAR rate).

These transactions were complemented by the purchase by the Central Bank of Government securities on the secondary market, at the same time as a two-month period was set for the cash reserve requirement calculations (covering June and July). Together with these measures, since mid-year a liquidity window has been opened to enable banks to take funds using National Guaranteed Loans and/or BOGAR 2020 as collateral (these securities are now available to be used as collateral of loans between banks).

As a result, by the middle of the year private sector deposits accounted for 54% of total financial system funding (netted assets plus net worth), a slight year-on-year increase. In recent months there has been a sharper rise in wholesale deposits, particularly those by Pension Funds (PF), a development that has taken place in a scenario of a certain degree of volatility in interest rates on time deposits.

In this situation, during recent months banks have succeeded in strengthening their position in the face of liquidity risk. The more liquid assets held by banks (made up of cash, current accounts at the Central Bank and repos with the Central Bank) reached almost 25% of total deposits in mid-year (see Chart V.3), a higher level





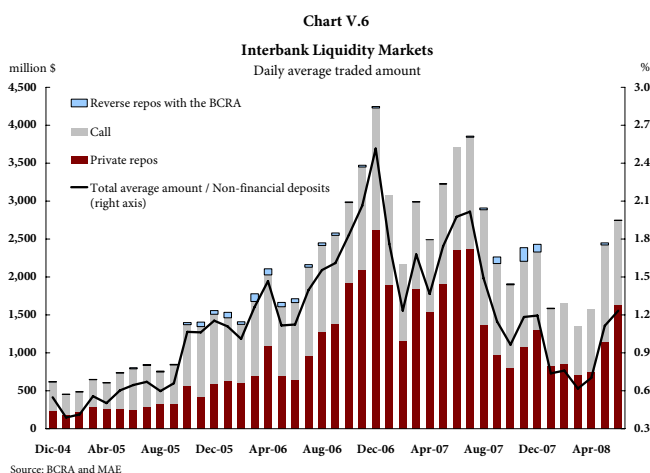
than that of financial systems in other emerging and developed countries (see Chart V.1). This level was also higher than that seen at the middle and end of 2007, a signal of the strategy by banks for expanding their lending capacity without neglecting to create a liquid asset cushion to provide cover at times of sudden deposit withdrawals. The broad measure of liquidity, which takes into account the position in Lebac and Nobac, reached almost 40% of total deposits in mid-2008, also slightly higher than the levels recorded in recent periods.

Banking liquidity continues to be in excess of the Central Bank's requirements in pesos (see Chart V.4). Foreign currency deposits continue to register an upward trend (up 25%a. in the first half of 2008), a development that has taken place in the context of rising lending in that currency. As a result, the foreign currency position represented 40% of the total requirement (see Chart V.5), with a rising trend.

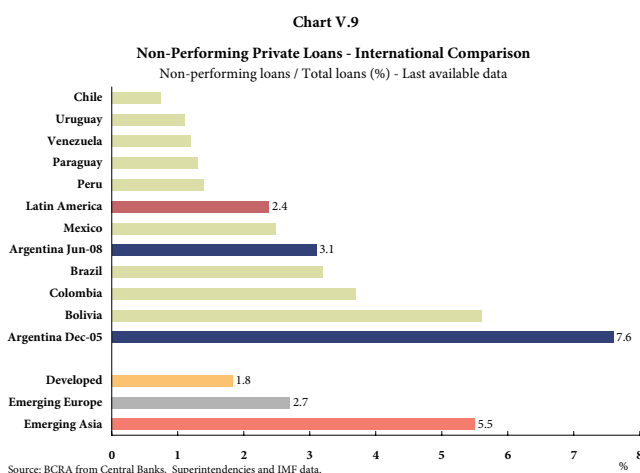
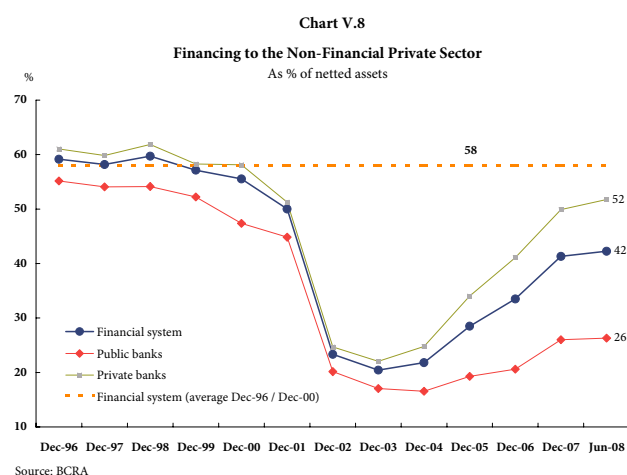
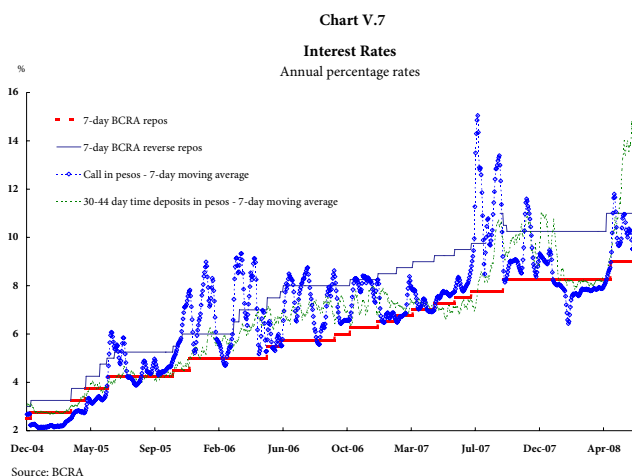
Interbank liquidity markets reflected the impact of greater financial volatility

In recent months interbank liquidity markets have continued to be effected by increasing financial volatility. Over 2008 some reduction in amounts traded on the call market and in interbank repos has been recorded (see Chart V.6). This situation is also reflected in larger variations in leading interest rates (see Chart V.7), although this trend has been contained by the effectiveness of the liquidity measures introduced by the Central Bank.

In a situation in which volatility will persist in coming months, bank liquidity levels, added to measures implemented by the Central Bank, will enable the financial system to strengthen its position in the face of this risk



Financial entities continue to record liquidity levels placing them in a sound position to confront shocks, at a time when the Central Bank constitutes an extra safeguard, consolidating the conditions that contribute to financial stability. In this context, in addition to the liquidity sources made available by the Central Bank in recent months, it can play the role of a lender of last resort, enabling further cover to be provided in the event of deposit withdrawals unconnected with the fundamentals of the financial system and the economy.



V.2 Credit risk

V.2.1 Private sector

Within the context of a reduced credit risk, during 2008 the exposure of the financial system to the private sector has continued to increase

In 2008, bank exposure to the private sector has continued to climb, although at a slower rate than in previous years. This performance has taken place in the context of moderate improvements in the labor market and growth by the productive sectors of the economy, although at aggregate level growth has been lower than in previous periods. These conditions, together with still moderate indebtedness levels for households and companies (see Chapter II), help to ensure that the financial system continues to face a limited credit risk from the private sector.

By mid-2008 lending to companies and households²² stood at 39% of total assets (over 42% of netted assets) (see Chart V.8). Although still below the levels recorded prior to the crisis in 2001-2002, loans to households and the corporate sector continue to increase their share of financial system assets, with a rise of 21 p.p. in the last four years. As in previous periods, the rise for the half-year was largely accounted for by private banks, with a weighting of lending to the private sector totaling over half their asset portfolios.

Increased lending to the private sector is taking place within the context of low non-performance levels

At the end of the first half of the year private sector lending non-performance stood at 3.1% of the portfolio, showing a slight drop over the course of 2008. Consequently, private sector loan non-performance stands at its lowest level in historical terms, and is in line with levels recorded in other economies in the region (see Chart V.9).

Improvement in the quality of the private sector portfolio recorded during 2008 was largely explained by public banks, with a reduction of 1.2 p.p. in their loan non-performance ratio to 3.7% (see Chart V.10). Private bank non-performance levels are slightly lower, holding steady at around 2.6% of loans to the private sector.

Credit to companies continued to show improved performance during the first half of 2008, leading the

²² Including loans to residents abroad

Chart V.10
Non-Performing Credit to the Private Sector
Non-performing loans / Total loans

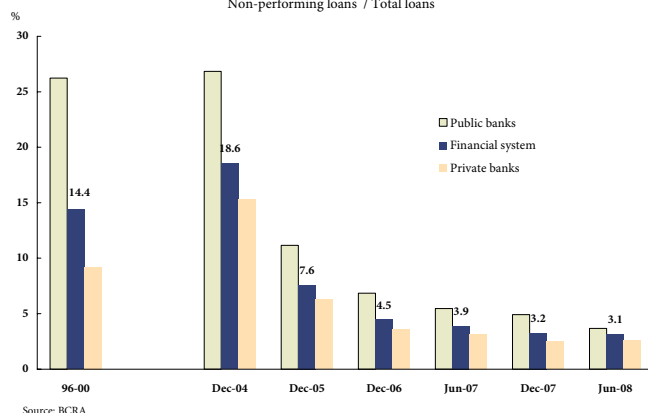


Table V.1
Transition Matrix December 2007 / June 2008
As % of non-financial private sector financing

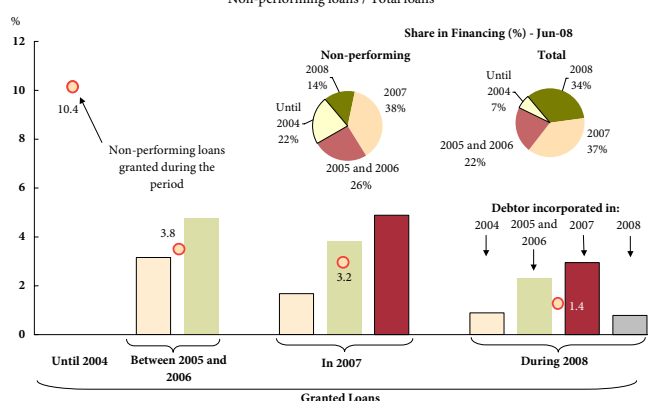
		June 2008							
		Performing		Non-Performing				Write off (*)	TOTAL
		1	2	3	4	5	6		
December 2007	1	93.0	1.2	0.6	0.2	0.0	0.0	5.0	94.9
	2	31.6	40.8	8.2	12.8	0.6	0.0	5.9	1.8
	3	9.6	3.9	51.4	25.0	1.5	0.0	8.5	1.1
	4	6.0	1.2	2.8	46.8	30.2	0.0	13.0	1.1
	5	1.6	0.2	0.8	1.1	43.2	0.0	53.0	1.0
	6	4.7	0.2	0.2	0.1	0.5	87.7	6.7	0.1
TOTAL		89.0	1.9	1.3	1.2	0.8	0.1	5.6	100.0

Figures based on debtor information at the start of the exercise

(*) Includes both repaid financing and that charged-off from balance-sheet

Source: BCRA

Chart V.11
Lend to Private Sector by Granted Period
Non-performing loans / Total loans



reduction in private sector non-performance. Non-performing corporate loans declined in the first half of the year, to 2.5% of loans²³. The household loan portfolio has shown some signs of deterioration, as non-performance reached 4% of the total, 0.5 p.p. more than at the end of 2007. This performance has been driven mainly by household consumer loans (personal and credit card), for which non-performance rose to a level of 4.5% (see Chart V.2).

Credit to the private sector outstanding at the end of the previous year experienced a slight deterioration. While 90.5% of the lines maintained their credit rating during the six-month period, 3% recorded a worsening situation, and 0.9% improved their grade²⁴. Loans rated in situation 1 in December 2007, almost 95% of the total, recorded a mild 2 p.p. deterioration in their quality, of which 0.8 p.p. became non-performing (see Table V.1). In turn, loans classified as non-performing at the end of 2007 also deteriorated slightly, as 19% of the loans in the non-performance segments at the end of last year posted a deterioration in their situation, whereas only 9.2% showed an improvement (7.7% returned to making regular payments, and the rest remained in non-performing categories) while almost half²⁵ maintained their category.

Debtors incorporated to the financial system in more recent periods tend to show higher relative levels of non-performance within all segments of loans grouped according to the period in which they were generated (see Chart V.11), a sign of the gradually increasing risk being assumed in credit origination. This behavior is mainly associated with household consumer credit lines.

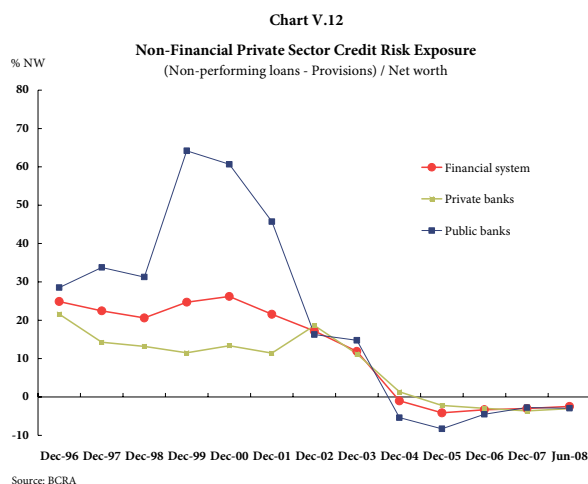
It is estimated that credits generated in the first half of 2008 (somewhat more than one third of the total) present low levels of non-performance (just 1.4%), while loans granted in 2007 (37% of the total) register a slightly higher non-performance (3.2%). Loans granted in 2005 and 2006 show a moderately higher non-performance rate (3.8%), although it is below the level for those loans granted until 2004 (which have a non-performance rate of 10.4%, although with a low weighting in the overall total).

Banks continue to show provision levels that are in excess of their non-performing portfolio

²³ This performance reflects the impact of non-performing loans on which payment begins to be made, that are settled, or that are definitively transferred to memorandum accounts in accordance with current regulations.

²⁴ The balance is explained by repayments.

²⁵ The balance is explained by repayments.



The financial system continues to maintain a good level of cover against the possibility of credit risk materializing. In mid-2008 provisions stood at 124% of non-performing loans to the private sector, with similar levels in both private and official banks. As a result, the ratio for non-performing loans not covered by provisions in terms of net worth has remained negative for the financial system as a whole (see Chart V.12), a sign of the sound position of banks to be able to confront the repayment risk of the private sector.

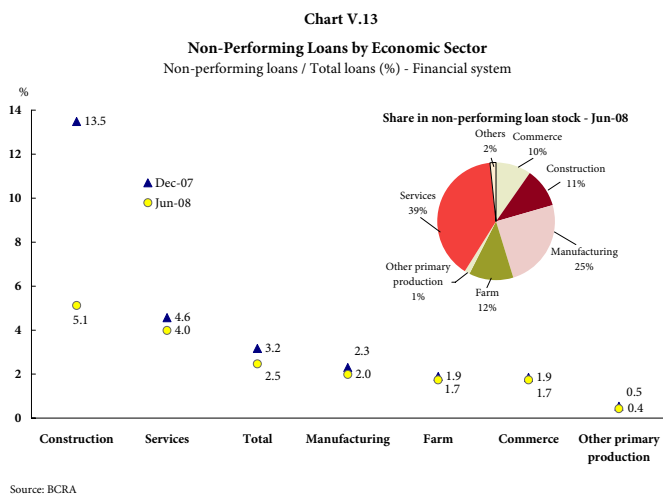
Within the framework of financial volatility and more moderate economic growth, it is estimated that banks could gradually increase their exposure to private sector credit risk in coming periods

The turbulence on financial markets presents new challenges for financial entity risk management. This volatility could impact on lending interest rates, affecting the repayment capacity of certain debtors. In addition, the expected slowing in the rate of domestic economic and credit growth, in the context of a more modest improvement in labor market indicators, could generate a certain increase in the credit risk faced by the financial system, although it will nevertheless remain well within bounds.

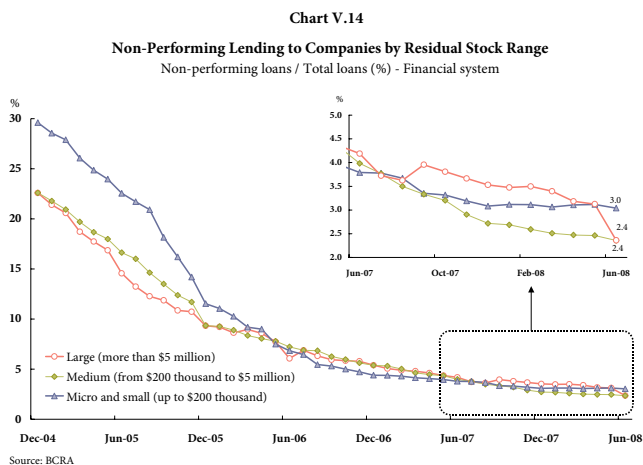
Corporations

Credit to corporate sector has stabilized its share in bank's assets, with signs that the sector's payment capacity is improving

During the course of 2008 the financial system has held its exposure to the corporate sector relatively unchanged at 23% of netted assets. This performance has taken place in the context of volatile interest rate spreads, as a consequence of the turmoil on financial markets. In the first part of 2008, companies have recorded some improvement in their economic and financial position, given the economic growth rate and their still moderate indebtedness levels (see Page 22).



On the basis of this performance, the situation of the financial system in the face of the credit risk of the corporate sector continues to show progress. Corporate loan non-performance is still falling, dropping 0.7 p.p. in the first half of the year to 2.5% of loans. All productive sectors have posted declines in their non-performance in the half, the largest drops being seen in construction and service company credit lines (see Chart V.13). The farm sector, other primary goods producers and commerce stand out as the sectors with the lowest non-performance ratios. The outlook for primary sector



production (for both the local and export markets) explains the relatively sound economic and financial situation of this particular sector, as evident from low and declining non-performance levels, despite the local turbulence seen in the second quarter of the year.

In 2008 non-performance in lending to companies dropped for all segments²⁶ (see Chart V.14). In particular, loans in the relatively larger segments showed the most important drop in non-performance for the year, while loans for up to \$200 thousand (mainly associated with micro and small undertakings) continue to perform well, although their share of the total is still relatively low.

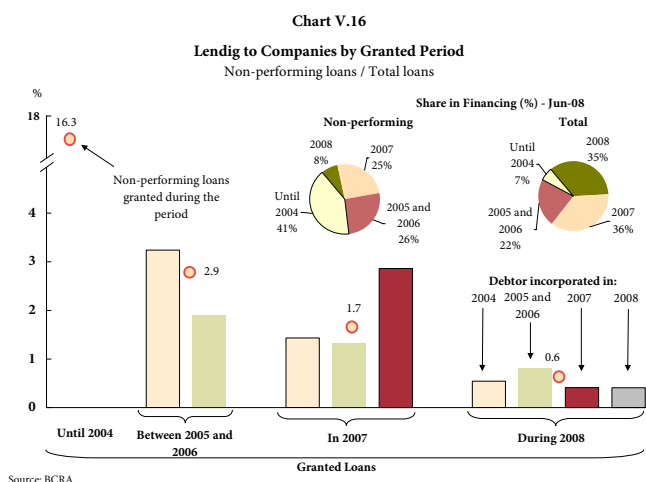
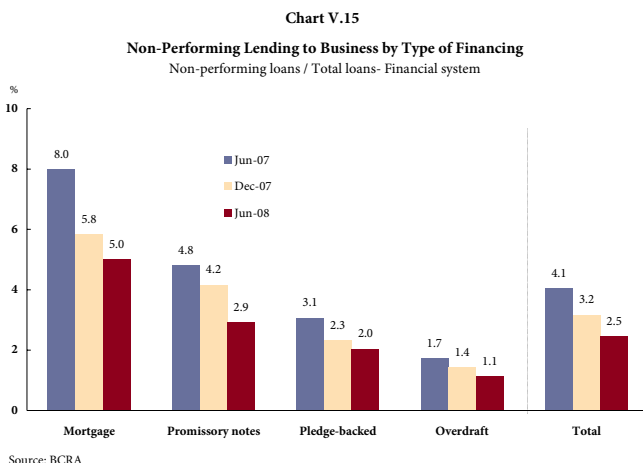
Corporate portfolio quality improvement is widespread across all credit lines. Although still showing the highest non-performance ratios, promissory notes and mortgage loans have recorded the greatest reductions in their non-performance ratios in the first half of the year, reaching levels of 2.9% and 5% in mid-2008 (see Chart V.15). Overdrafts continue to show the best relative performance, with a non-performance ratio of 1.1%.

Corporate loan non-performance is centered on lines granted until 2004

It is estimated that corporate sector loan non-performance is mainly explained by lines dating back more than three-and-a-half years, while those granted subsequently have performed better (see Chart V.16). In the middle of 2008 lines generated until 2004 recorded non-performance greater than 16%. Although they represent only a small portion of total loans to corporations (6%), these lines account for over 40% of the total non-performing credit stock for companies at June 2008.

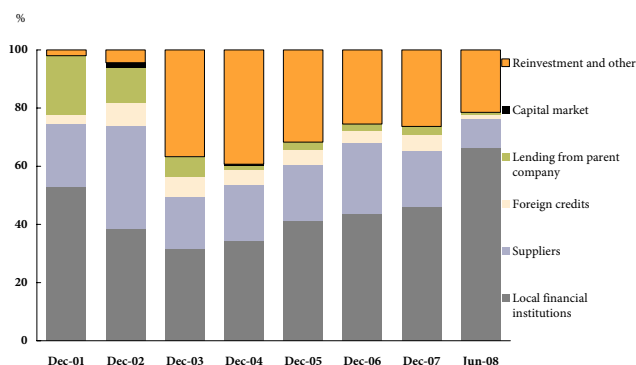
The financial situation of the corporate sector leads to predictions that credit risk to which financial system is exposed will remain low, although the impact of the increase in financial volatility will need to be monitored

During the remainder of the year the corporate sector will continue to increase its demand for bank credit. Signs of this can be seen in the manufacturing sector (see Chart V.17), with the largest relative share of total bank loans to corporations. Nevertheless, if turbulence on financial markets is to worsen, the potential impact on domestic lending interest rates could generate an increase in financial difficulties for certain debtors. In



²⁶ Based on residual balance stocks.

Chart V.17
Expected Sources of Funds for Manufacturing Sector
Outlook for the third quarter of 2008



Source: EMI - Qualitative information - INDEC

addition, the current slowing rate of economic growth and the possibility of an impact from lower global expansion on certain domestic exporting sectors could have a similar effect. Therefore, although it is expected that the credit risk represented by companies will continue to be limited, there are new factors that present challenges for the rest of 2008, and these could be reflected in a reversal of the current trend towards a decline in non-performance.

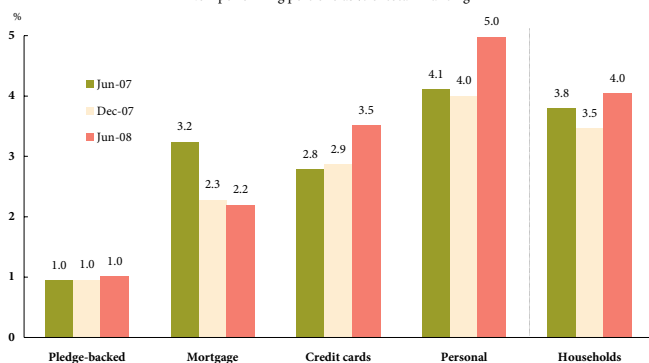
Households

Some deterioration is being noted in the quality of household financing, although the credit risk from this sector remains low

Lending to households continues to gain share of bank asset portfolios. Loans to households rose above 19% of financial system netted assets in the middle of the year, higher than the level at the end of 2007.

On the basis of some improvement in labor market indicators and still low levels of household indebtedness, the sector's payment capacity has remained relatively stable (see Page 26). Nevertheless, a slight deterioration in the household credit portfolio can be noted, although rising from levels that were low in historical terms. This increase in non-performance has mainly taken place in consumer credit lines (personal loans and credit cards) (see Chart V.18), whereas performance by collateralized loans (mortgages and pledge-backed) has remained unchanged.

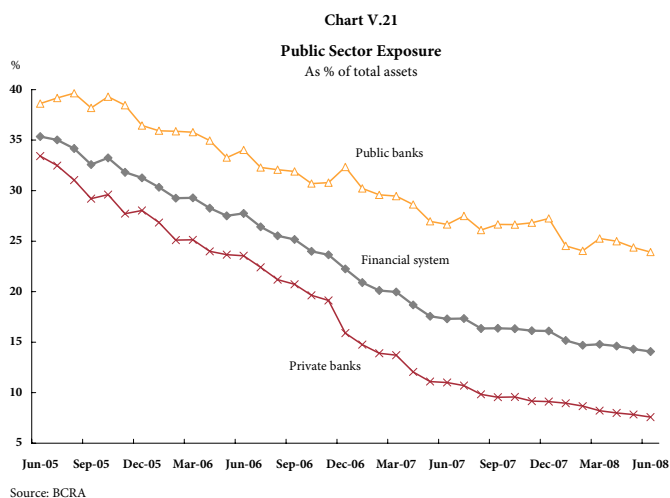
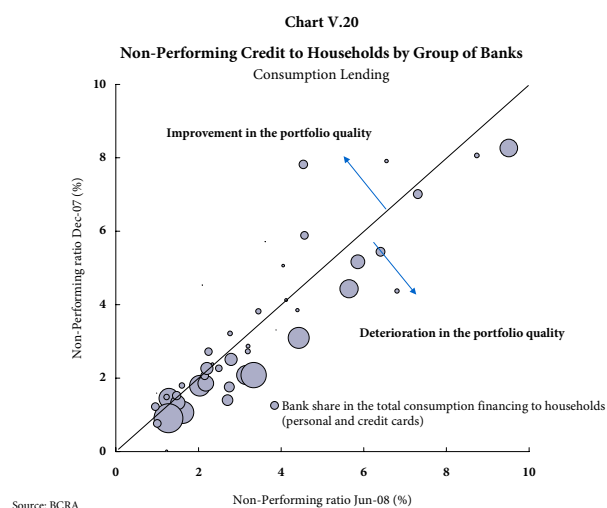
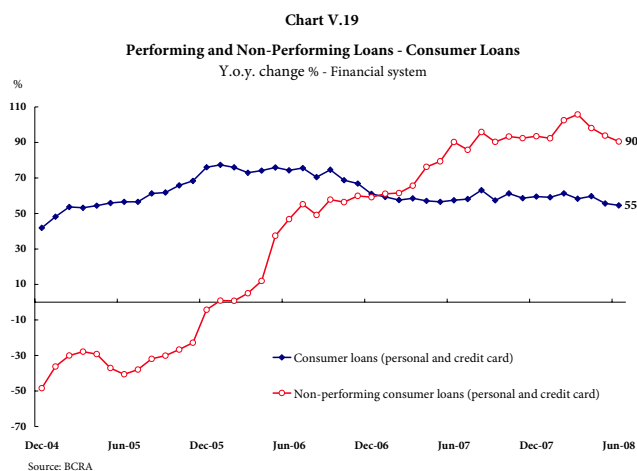
Chart V.18
Non-Performing Lending to Households by Type of Line
Non-performing portfolio as % of total financing



Source: BCRA

The increase in the non-performance ratio in the case of consumer loans is the result of the greater dynamism shown by non-performing loan stock compared with growth levels for this portfolio as a whole (see Chart V.19), and has been widespread among the financial entities participating in this business segment (see Chart V.20). The moderate deterioration in this portfolio, added to its increased weighting within bank lending to the private sector (29% in mid-2008, 3 p.p. more than in the same period of 2007), have caused a rise of the credit risk from households faced by the financial system. This development is in line with the trend seen in most of the region's economies, and represents an area that is increasingly being monitored by the respective supervisory authorities.

Within the consumer loan segment of household lending, it is estimated that a significant portion of the non-performing balance is centered on lines originated in the last few years, as a result of the considerable dynamism observed in this segment of the credit market.



In addition, it can be noted that those households added most recently to the financial system and that took out consumer loans have shown a relatively weaker performance.

Within the framework of a gradual slowing in bank lending to household growth rates, the financial system will continue to face a limited credit risk from this sector

Banks are expected to continue to expand their lending to households, although the more moderate growth rates seen in recent months will be maintained. Over the rest of the year household income is expected to continue to rise in nominal terms, in a context in which there will be only marginal improvements in the labor market, preserving the sector's payment capacity. Nevertheless, any increase in financial market volatility with an impact on lending interest rates could have an effect on the financial position of some households, raising the probability of a gradual increase in non-performance.

V.2.2 Public sector

The financial system is improving its position in relation to the public sector credit risk, based on the record of positive fiscal results and declining levels of indebtedness of this sector

The financial system has continued to lower its exposure to the public sector in 2008. This sector accounted for 14% of bank assets in mid-year (15% of netted assets), almost 2 p.p. below the level at the end of 2007 and less than one third of the level recorded four years earlier. This development during the year has taken place in both public and private banks, with the latter showing lower levels of exposure to the Government (see Chart V.21). The reduction in this exposure is explained by the gradual amortization and sale of securities, and the rise in financial system assets, in a context in which the public sector has maintained its payment capacity.

The setting of a global cap of 35% of bank assets since July 2007, as well as maximum limits based on financial entity capital and on area of jurisdiction, the elimination of the bias in minimum capital requirements (with unification of the requirement for lending to the private and public sectors), among other measures introduced by the Central Bank, have encourage a reduction in the share of the public sector in the financial system portfolio. As a result, this exposure is now in line with levels recorded in other economies in the region (see Chart V.22).

The sound position of banks in the face of public sector credit risk will persist during the remainder of 2008

The gradual reduction in banking sector exposure to the public sector, added to recent announcements on the regularization of Government liabilities, helped to continue strengthening the position of the financial system in the face of the risk to credit represented by this sector. In addition, surpluses in national public sector accounts and lower levels of indebtedness will contribute to this development (see Page 27). For the rest of the year, the expected fiscal surplus, in a context of adequate sources of funding to meet financial needs, will provide the public sector with good repayment capacity, ensuring the financial system is in a sound position with regard to this credit risk. However, rising levels of market volatility could lead to new challenges.

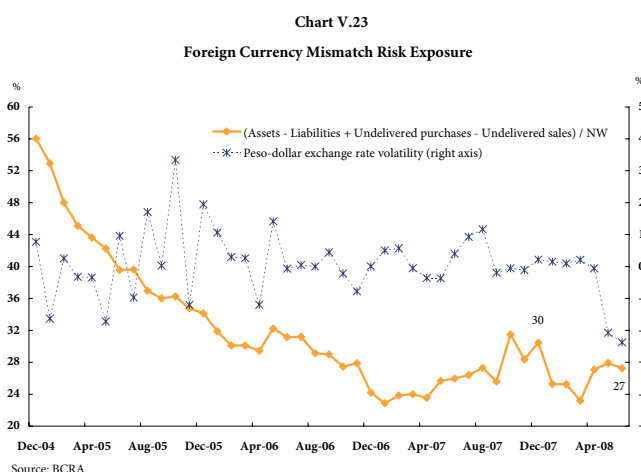
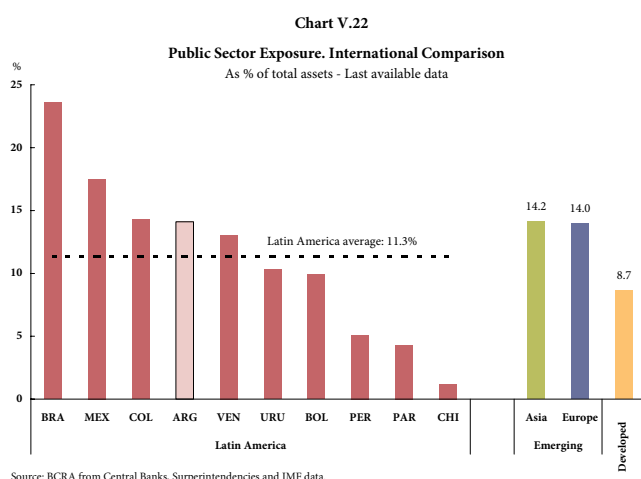
V.3 Currency risk

The financial system faces only a limited exposure to currency risk

In a situation showing some degree of volatility in the nominal peso-dollar exchange rate, the financial system cut back its exposure to the risk from foreign currency over the course of 2008. This trend was backed by the financial policy implemented by the Central Bank to avoid excessive balance sheet foreign currency mismatching. In particular, foreign currency loans can only be granted to borrowers with foreign currency income, and such lines must be funded out of deposits in the same currency.

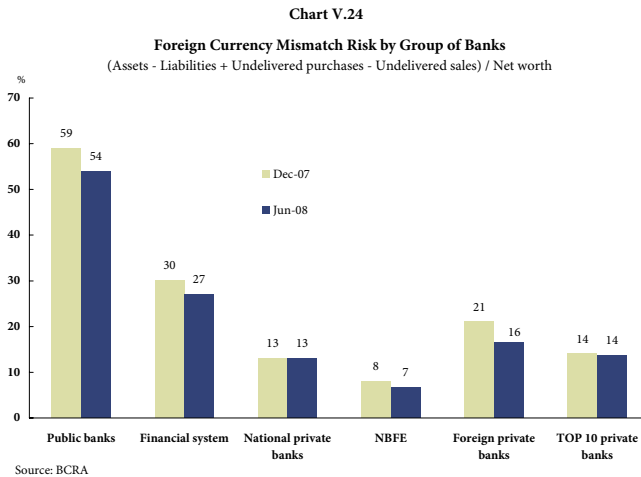
The foreign currency position of the banking sector²⁷ fell slightly in the first half of the year, during a period in which the increase in liabilities exceeded that of assets. Deposits, and to a lesser extent foreign lines of credit, were behind the rise in bank liabilities in foreign currency. Increased liquidity and export finance explained the growth in foreign currency assets. In addition, during a time of growing financial turbulence, banks increased their net purchases of currency on futures markets (without delivery) moderating the drop in foreign currency position, which reached 27.3% of net worth by mid-year (see Chart V.23), less than at the end of 2007.

During the first part of the year there was an increase in the demand for foreign currency unrelated to either the situation of the financial system or the fundamentals of



²⁷ Includes foreign currency assets, liabilities and forward purchases of foreign currency in memorandum accounts.

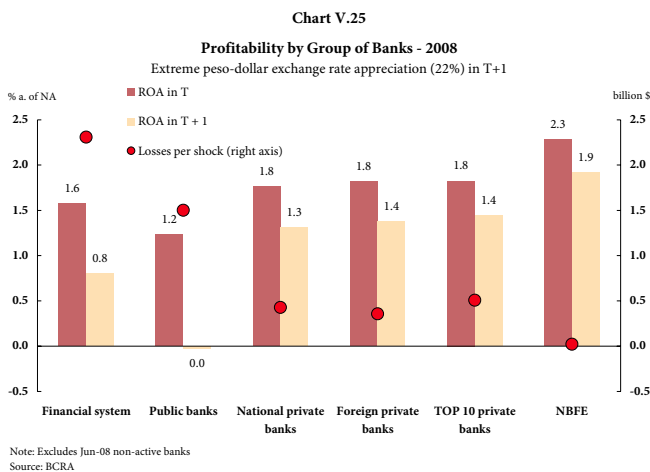
the economy. This situation led to a slight increase in peso-dollar exchange rate volatility during the period, which was moderated by the timely action of the Central Bank (see Page 7).



All groups of financial entity recorded a reduction in their foreign currency positions in the first part of the year, except for domestic private banks, which held their positions relatively stable. The largest falls in foreign currency position were registered by public banks and foreign private banks (see Chart V.24), groups with the greatest exposure to this risk.

Stress-test exercises continue to show satisfactory results in scenarios of high peso-dollar exchange rate volatility. As the financial system records an active position in foreign currency items, the sensitivity of their accounting results and their solvency indicators is evaluated in situations of extreme appreciation of the domestic currency²⁸. Analysis is also performed for the different types of financial entities, given the difference in size of balance sheet mismatching that exists. Public banks in particular, being the group with the greatest foreign currency exposure, would experience the greatest relative impact from such a shock, which could absorb all the profits earned in 2008 (see Chart V.25), although their capital compliance would remain above 10% of their risk-weighted assets (see Chart V.26).

At a time of increasing turbulence on financial markets, it is expected that the measures already introduced by the Central Bank will help to ensure the financial system can maintain an adequate level of exposure to foreign currency risk.

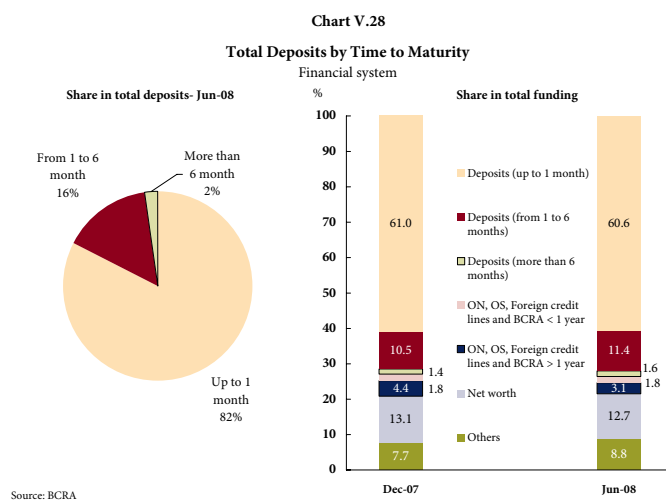
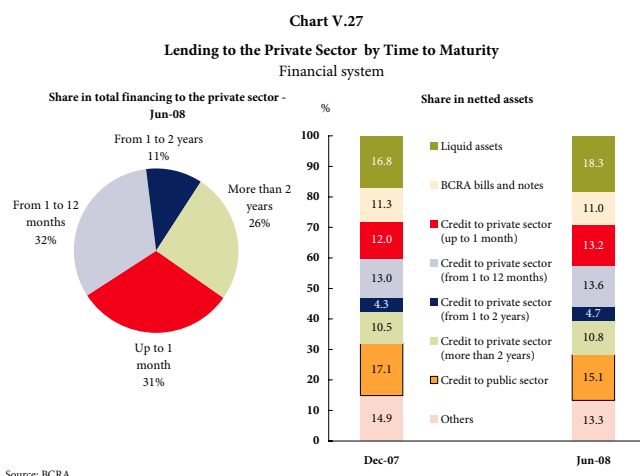
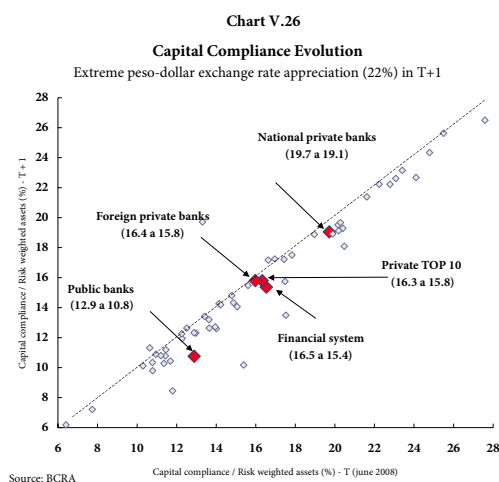


V.4 Interest rate risk

Financial system exposure to interest rate risk has remained relatively steady

Over the course of the first half of 2008, the banking system held interest rate exposure steady, with an uneven performance among the different bank groups. It is estimated that in recent months bank asset maturities have remained at levels similar to those of the end of 2007. Although the share of portfolios accounted for by certain long-term assets at fixed interest rates, such as those of the public sector, has continued to decline, loans to the private sector with a greater relative maturity have also been gaining ground (see Chart V.27). In the case of bank funding, a slight increase took place in the proportion of deposits with a lower residual

²⁸ Equivalent to a fall of 22% in the value of the nominal exchange rate.



term, to the detriment of other liabilities with longer durations (see Chart V.28). The gradually deteriorating conditions on financial markets recorded since mid-2007 led some financial entities to postpone the issuance of ONs, so such liabilities have seen a reduction in their significance as a source of financial system funding.

Bank exposure to real interest rate risk, derived from the balance-sheet mismatching of CER-adjusted items (at fixed interest rates), has not changed significantly in 2008. At a time when the items adjusted according to this coefficient are declining, both in the case of assets (from the amortization and sale of public sector securities) and liabilities (from a reduction in adjusted time deposits), there has been a moderate increase in the size of this mismatching, which stood at three-quarters of net worth in mid-2008 (see Chart V.29), slightly under the level at the end of last year, as a result of the improvement in the solvency of the sector. Private banks accounted for the gradual reduction in mismatching of CER-adjusted items in terms of net worth, while official banks continue to record a higher level of mismatching.

In a scenario of increasing financial turbulence, some materialization of interest rate risk can be expected in coming months

As current financial market volatility is expected to persist in the second half of 2008, its impact on domestic interest rates could lead to some materialization of this risk. In this context, the Central Bank continues to evaluate alternatives for the development of market solutions that will allow banks to improve their position in the face of this risk, such as the introduction of interest rate swap mechanisms.

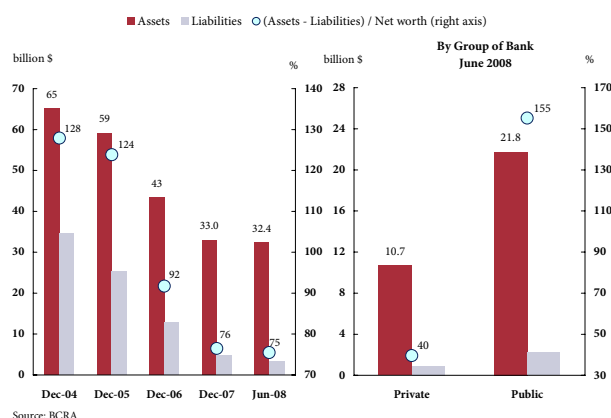
V.5 Market risk²⁹

In the midst of the turbulence being seen on financial markets, measures introduced by the Central Bank assist banks to avoid excessive balance sheet fluctuations

Faced by the surge recorded in financial volatility, the measures introduced by the Central Bank in 2007 succeeded in preventing short-term variations in the prices of leading financial assets from causing excessive fluctuations in bank net worth. In particular, Lebac and Nobac to be held until maturity were allowed to be recorded in investment accounts, as well as allowing such assets and Government securities to be recorded in "trading accounts". This dampened the impact of

²⁹ This section includes the balance sheet impact of price volatility in relation to both bonds and shares

Chart V.29
CER Mismatching



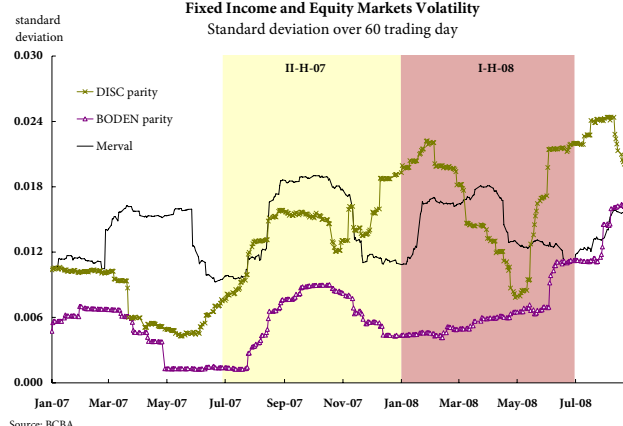
financial asset yield (and thus price) volatility on this risk borne by banks (see Chart V.30).

In this context market risk exposure in terms of financial system regulatory capital (consisting mainly of domestic fixed-income assets) has shown a moderate decline in 2008 (see Chart V.31).

Some manifestation of market risk is expected in the latter part of the year, in line with the resurgence of financial volatility

Although the measures implemented by the Central Bank in relation to the valuation of securities should moderate the balance sheet impact for banks, growing international uncertainty will increase price volatility for such assets, leading to some materialization of this risk.

Chart V.30
Fixed Income and Equity Markets Volatility
Standard deviation over 60 trading day



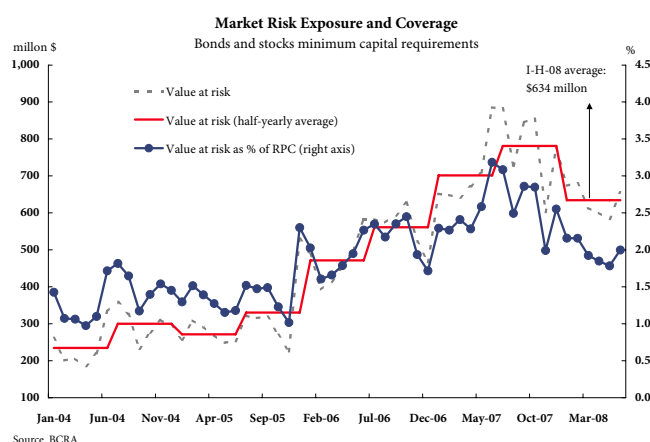
V.6 Operational risk

The Central Bank's prudential policies include a time-table for falling into line with international practices

In line with the Basel Committee's sound practices for operational risk management, in April this year minimum standards were announced for financial entity operational risk management, understood as the risk of losses from misalignments or failures in internal control, or actions by personnel or the failure of information technology systems.

These standards require this risk to be dealt with as an integrated discipline, separate from other risks, with identification of the factors that lead to it, its monitoring and effective management methods. The main guidelines and elements for each stage of the management process have been laid down, and an "Operational Risk Unit" is required to be set up, consistent with the size of the financial institution, the nature and complexity of its products and processes. On the basis of the schedule that has been announced, by the end of 2009 banks should have implemented the requirements in this area.

Chart V.31



VI. Solvency

Summary

The financial system continues showing progress in its solvency, fundamentally due to the profits emerging from an intermediation process that maintains its rate of expansion. This performance, which is widespread among financial entities, improves the sector's position to face possible adverse shocks and to maintain a sustained credit growth path.

In line with the growth of the more stable sources of revenue, the banking system saw an increasing profitability during the first half of 2008. The expansion of the volume of financial intermediation with the private sector, particularly, boosts the expansion of the net interest and service income margins. Meanwhile, by assuming a limited credit risk, financial entities are facing small loan loss provisions.

Since mid 2007, the more volatile scenario affects gains on securities. Operating costs, another line with negative impact on profits, maintain their upwards trend resulting from the growth of employment and also of wages in the sector. This trend is not an impediment for some efficiency gains, although progress must still be achieved.

Adjustments to valuations of public sector assets and the amortization of court ordered releases continue losing weight in the profitability structure of the banking system, to accompany the process of normalizing balance sheets. It is expected that these headings will lose importance in coming periods.

The recovery of profitability was evident at both public and private sector financial entities. However, among the latter a heterogeneous performance was observed, as the banks with a regional scope exhibited a slight decline in their profitability while those operating nationwide (which have more weighting in assets) showed an increase of their profits.

The book profits earned by the banks during this period, and, to a lesser extent, the fresh capitalizations they received, enable the financial system to strengthen its solvency. Therefore, the net worth of the banking system continue growing, in a context of qualitative improvements mainly due to the absorption of results from previous accounting years.

The financial system capital, as measured by the current prudential rules, is 16.5% of risk-weighted assets, which exceeds both local requirements and minimum levels recommended internationally. This pattern that sustains the perception of a solid banking system is evident in all financial entity sub-groups in the sector.

Looking ahead, the solvency of the financial system is estimated to continue consolidating, especially as a result of the new accounting profits, although this process is expected to be accompanied by fresh capital contributions. This scenario may be slightly restrained due to a possible impact of a more volatile international context.

Chart VI.1
Half-Yearly ROA

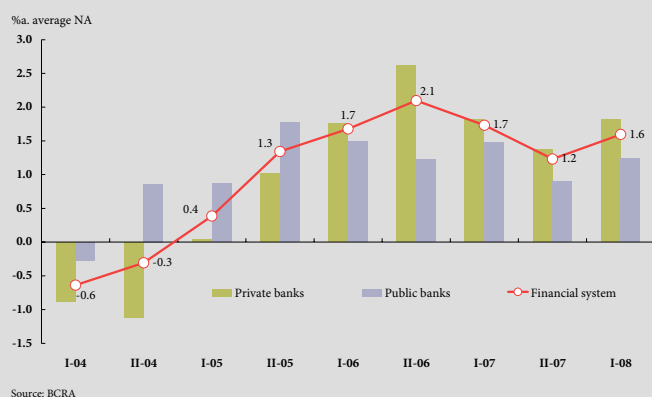
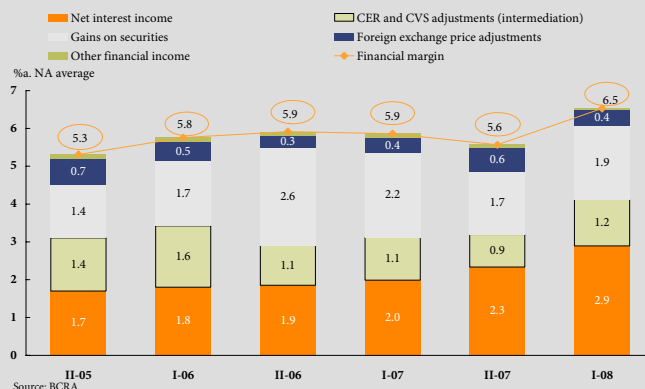


Chart VI.2
Financial Margin Composition



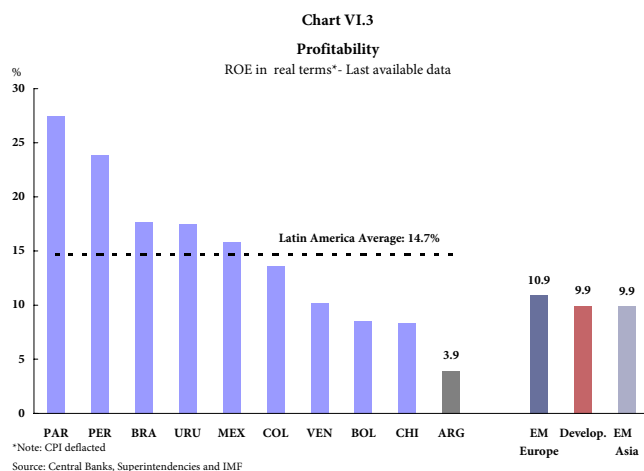


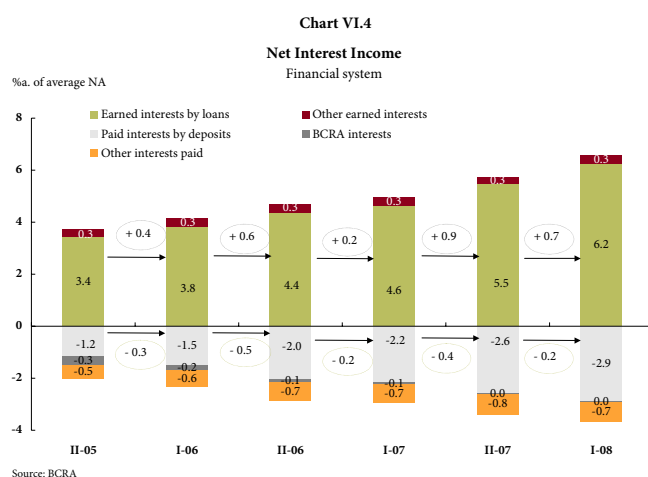
Table VI.1

Profitability Structure: Financial System
In annualized terms - As % of average netted assets

	93-00	2005	2006	2007	I-07	II-07	I-08
Financial margin	6.1	4.6	5.8	5.7	5.9	5.6	6.5
Net interest income	4.9	1.5	1.8	2.2	2.0	2.3	2.9
CER y CVS adjustments	0.0	1.5	1.3	1.0	1.1	0.9	1.2
Gains on securities	0.8	1.2	2.2	1.9	2.2	1.7	1.9
Foreign exchange price adjustments	0.0	0.4	0.4	0.5	0.4	0.6	0.4
Other financial income	0.3	0.1	0.1	0.1	0.1	0.1	0.0
Service income margin	3.5	2.3	2.7	3.1	2.9	3.3	3.4
Operating costs	-6.7	-4.6	-5.1	-5.5	-5.2	-5.8	-6.0
Loan loss provisions	-2.2	-0.6	-0.5	-0.7	-0.6	-0.8	-0.8
Adjustments to the valuation of gov. securities (*)	-	-0.2	-0.3	-0.3	0.0	-0.6	-0.5
Tax charges	-0.5	-0.4	-0.5	-0.6	-0.5	-0.6	-0.7
Amortization payments for court-ordered releases	-	-0.9	-1.1	-0.7	-0.8	-0.7	-0.4
Other	0.7	0.8	1.2	0.9	0.6	1.2	0.5
Monetary results	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Income tax	-0.3	-0.3	-0.3	-0.4	-0.5	-0.3	-0.5
ROA	0.5	0.9	1.9	1.5	1.7	1.2	1.6
ROE	3.4	7.0	14.3	11.0	12.8	9.3	13.6
Adjusted ROA (**)	-	2.0	3.4	2.5	2.5	2.5	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



VI.1 Profitability

Boosted by the deepening of the financial intermediation process, the banking system ended its seventh consecutive half year with profits

The financial system continues increasing its solvency by posting profits, and thus completes three and a half years of uninterrupted positive earnings. Specifically, the banking system accrued profits of \$2.35 billion during the first half of 2008, equivalent to 1.6%a. ROA (see Chart VI.1). This performance was widespread among the banks: 71 of the 85 financial entities earned positive results during the period (accounting for 99% of aggregate assets). The domestic financial system profits are still less than those recorded by financial systems in the region and in developed countries (see Chart VI.3).

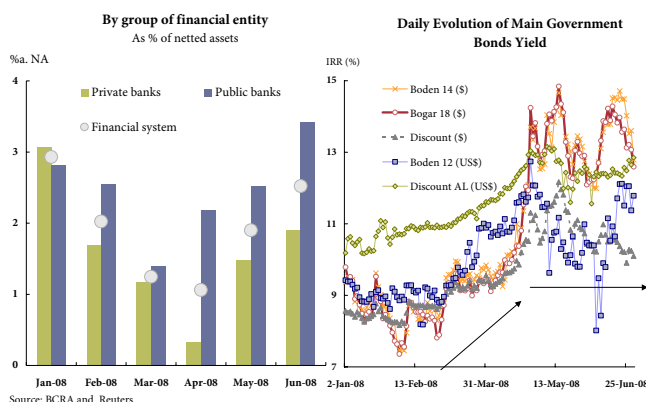
Banking system profitability remains in line with that accrued in the same period last year, although it is 0.4 p.p. on assets higher than in the second half of 2007 (see Table VI.1). Underlying this performance is the positive momentum of the more stable sources of revenues, the interest and service income margins, while the results on securities remain depressed and the operating costs continue to grow.

Net interest income drives the growth of the banking system's financial margin

The financial margin of the banking system reached a maximum amount, even when the pre-crisis period is considered, as it increased by 0.9 p.p. of assets to 6.5%a. in the first half of 2008 (see Chart VI.2). The moderate increase in the lending and borrowing interest rates during the period in a framework of a greater relative momentum of credit to private sector (with low levels of non – performing loans) than term funding, was reflected by a growth of the interest income margin (see Chart VI.4). It is worth noting that these results are especially significant for the private sector financial entities, while the official banking sector still has progress to show on this matter. A slight increase in the adjustments by the Reference Stabilization Coefficient (CER) is also seen, which reflects the performance of this coefficient.

The gains on securities continued exhibiting large variations during the first half of 2008 (see Chart VI.5), which reflected the impacts of a scenario of greater international financial turbulence and some volatility at the local level. The amount of net revenues in this line remains below the amount accrued in earlier periods,

Chart VI.5
Gains on Securities

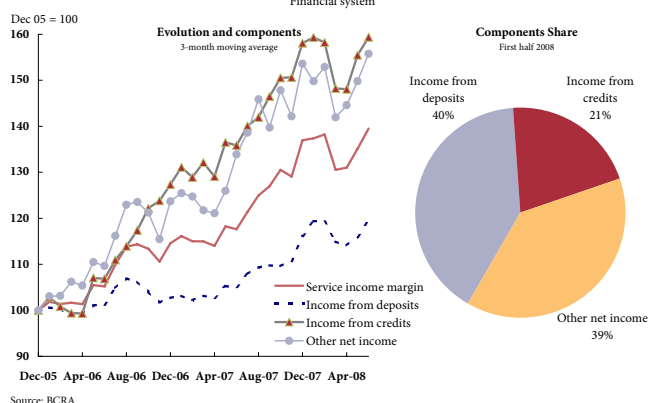


although some recovery from the end of last year is recorded.

Service income margin is consolidating as the main source of revenues for the sector

Boosted by the growth of economic activity and of financial intermediation framework the net service revenues remained on their expansion path, reaching a level that is in line with the pre-crisis average. The revenues from collecting deposits still exhibit the largest weight in this heading of the profitability structure, while the funds associated with granting loans are the most dynamic (see Chart VI.6). The trend towards consolidation of this component of banking profits is happening at both public and private banks.

Chart VI.6
Service Income Margin



The growth of lending to households and corporations is still happening in a context of limited credit risk, which is reflected by small loan loss provisions. The reduced weight of these charges is maintained despite the increased share of credit to the private sector in total assets.

In the context of expansion of financial intermediation, the recovery of employment levels (which expanded 1.8% in six months or 4.4% y.o.y.) and of sector wages maintain the upwards trend of the operating costs. Despite this trend, the relatively more stable revenues are enough to exceed these costs.

The banks with a regional scope record the highest profitability, while investment banks still show losses

Table VI.2
Profitability Structure: Private Banks
In annualized terms - As % of average netted assets

	93-00	2005	2006	2007	I-07	II-07	I-08
Financial margin	6.6	4.3	5.9	5.8	5.9	5.7	7.0
Net interest income	5.1	1.7	2.1	2.7	2.3	3.1	4.0
CER y CVS adjustments	0.0	1.0	0.6	0.4	0.5	0.3	0.5
Gains on securities	1.1	1.0	2.4	1.9	2.3	1.4	1.6
Foreign exchange price adjustments	0.0	0.5	0.6	0.6	0.5	0.8	0.8
Other financial income	0.5	0.1	0.2	0.1	0.2	0.1	0.1
Service income margin	3.9	2.7	3.4	3.8	3.6	3.9	4.1
Operating costs	-7.3	-5.1	-5.9	-6.3	-6.0	-6.6	-6.8
Loan loss provisions	-2.1	-0.6	-0.6	-0.8	-0.7	-0.8	-1.0
Adjustments to the valuation of gov. securities (*)	-	-0.2	-0.1	-0.1	0.0	-0.1	-0.2
Tax charges	-0.6	-0.4	-0.6	-0.7	-0.7	-0.8	-0.9
Amortization payments of court-ordered releases	-	-1.0	-0.9	-0.9	-1.1	-0.9	-0.4
Other	0.6	0.9	1.2	1.0	0.9	1.1	0.5
Monetary results	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Income tax	-0.4	-0.2	-0.3	-0.2	-0.3	-0.2	-0.5
ROA	0.7	0.5	2.2	1.6	1.8	1.4	1.8
ROE	5.0	4.1	15.3	10.9	12.3	9.6	14.2
Adjusted ROA (**)	-	1.6	3.2	2.6	2.8	2.4	2.4

(*) 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

Private sector banks recorded profits of \$1.55 billion in the first half of 2008, equivalent to 1.8%a. on assets, a similar figure to that seen during the first half of last year, but with some recovery from the immediately preceding period (see Table VI.2). The drivers of this performance were mostly the interest results, and to a lesser extent, those generated by services and the smaller charges accrued as amortization of court ordered releases.

While private sector retail banks exhibited profits equivalent to 2%a. of their assets in the first half of the year (see Table VI.3), those usually known as investment banks posted losses for the second consecutive six month period. In the first sub-group the profitable performance of the banks with a national scope (with a larger share in asset terms) stands out, based on the growth of interest results.

Table VI.3
Profitability Structure by Type of Bank
In annualized terms - As % of average netted assets

	Private						
	Retail					Investment (***)	
	II-07		I-08			II-07	I-08
	Total	Total	National coverage	Regional coverage	Specialized		
Financial margin	5.7	6.9	6.4	8.9	14.1	5.3	7.7
Net interest income	3.2	4.1	3.8	4.9	11.9	0.4	2.4
CER y CVS adjustments	0.4	0.5	0.6	0.3	-0.1	0.0	-0.2
Gains on securities	1.3	1.4	1.1	2.6	1.5	3.6	5.6
Foreign exchange price adjustments	0.7	0.8	0.8	0.7	1.5	2.0	0.6
Other financial income	0.2	0.1	0.0	0.4	-0.6	-0.7	-0.7
Service income margin	4.0	4.2	4.2	3.8	7.9	3.7	2.6
Operating costs	-6.5	-6.8	-6.5	-7.3	-14.1	-7.1	-7.6
Loan loss provisions	-0.9	-1.0	-1.0	-0.6	-6.0	-0.2	-0.4
Adjustments to the valuation of gov. securities (*)	-0.2	-0.2	-0.1	-0.3	0.0	-0.1	-0.1
Tax charges	-0.8	-0.9	-0.9	-0.7	-1.0	-0.6	-0.5
Amortization payments of court-ordered releases	-0.8	-0.3	-0.4	-0.1	-0.1	0.0	-1.7
Other	1.1	0.5	0.6	-0.1	1.2	-0.6	0.2
Monetary results	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Income tax	-0.2	-0.5	-0.4	-0.8	-0.5	-0.7	-1.2
ROA	1.6	2.0	1.8	2.7	1.4	-0.3	-0.8
ROE	11.6	16.5	15.8	21.1	7.5	-1.1	-2.8
Adjusted ROA (**)	2.5	2.5	2.3	3.1	1.6	-0.1	0.9
Weight in total assets (%)	55.5	55.1	45.4	8.8	0.9	2.6	3.0

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

(***) Excluding an investment bank (by I-07 merged and by book adjustments during II-07).

Source: BCRA

Table VI.4
Profitability Structure: Public Banks
In annualized terms - As % of average netted assets

	93-00	2005	2006	2007	I-07	II-07	I-08
Financial margin	4.9	4.9	5.4	5.2	5.4	5.0	5.5
Net interest income	4.4	0.9	1.0	0.9	1.0	0.8	0.8
CER and CVS adjustments	0.0	2.3	2.3	1.8	2.0	1.7	2.3
Gains on securities	0.4	1.3	1.8	2.1	2.1	2.0	2.5
Foreign exchange price adjustments	0.0	0.2	0.2	0.3	0.2	0.4	-0.1
Other financial income	0.1	0.1	0.0	0.0	0.0	0.0	0.0
Service income margin	2.9	1.6	1.7	2.0	1.8	2.1	2.2
Operating costs	-5.8	-3.5	-3.8	-4.1	-3.9	-4.4	-4.5
Loans loss provisions (*)	-2.0	-0.5	-0.4	-0.5	-0.3	-0.7	-0.5
Adjustments to the valuation of gov. securities (*)	-	-0.3	-0.6	-0.7	-0.1	-1.2	-1.1
Tax charges	-0.4	-0.3	-0.3	-0.3	-0.3	-0.4	-0.4
Amortization payments for court-ordered releases	-	-0.9	-1.5	-0.4	-0.4	-0.5	-0.3
Other	0.8	0.6	1.0	0.7	0.1	1.3	0.6
Monetary results	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Income tax	-0.1	-0.4	-0.2	-0.6	-0.8	-0.4	-0.3
ROA	0.3	1.3	1.4	1.2	1.5	0.9	1.2
ROE	1.8	12.4	12.3	10.7	13.3	8.2	13.0
Adjusted ROA (**)	-	2.4	3.5	2.3	2.0	2.6	2.7

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

Source: BCRA

Public sector banks recorded an increase in their profitability in the first half of 2008, to reach a 1.2%a. level (see Table VI.4), a development that was associated especially with the larger accruals of CER adjustments and the growth of the results earned by holding securities.

At the end of 2008 net interest income and service margin are estimated to continue exhibiting more dynamism than operating costs

Looking forward to the second half of 2008 the banking system is forecast to continue strengthening its solvency, mainly by consolidating its flow of book profits. In a scenario of growing financial intermediation with households and enterprises (although probably in a more moderate pace than previous periods), further increases of interest and service results are foreseen.

The developments of results originated by holding and trading securities will be subject, at least in part, to the development of the international and local volatility context. Nevertheless some recovery of these net revenues is expected. It is worth mentioning that the measures adopted by the Central Bank during the second half of 2007, which aim at avoiding short term fluctuations having a significant impact on the normal financial intermediation of the banks³⁰, should continue to have an effect in the next few months.

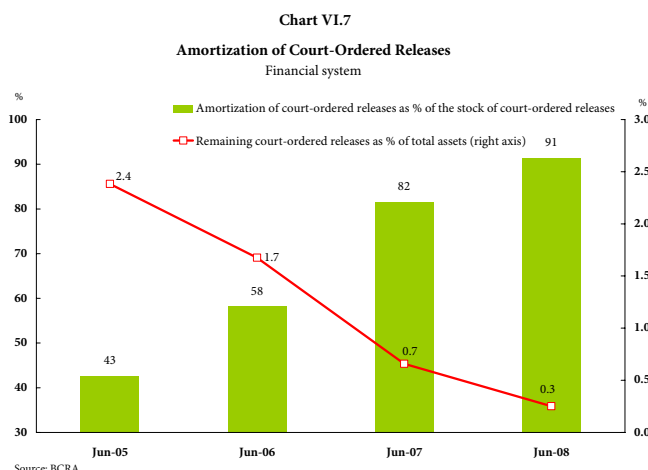
Further increases in the loan loss provisions are also forecast, mainly driven by the dynamic inherent in the expansion of loans to the private sector. Meanwhile, the sector's employment level is about to be at similar levels to those recorded before the crisis, a situation that added to the possible recuperation of wages will be reflected by increases in operating costs the next periods. This behavior poses a challenge for the sector to achieve greater operating efficiency in order to remain on the path to restore profitability.

Finally, the negative effects of the amortization of court ordered releases and the adjustment of government bond values are expected to no longer be part of the banking profitability structure, in a trend aligned with the process of the return to normality of the sector's balance sheet observed during recent years (see Chart VI.7).

³⁰ Alternative valuations of the security portfolios of Lebac and Nobac held in investment accounts and in trading accounts, and Government securities classified under trading accounts.

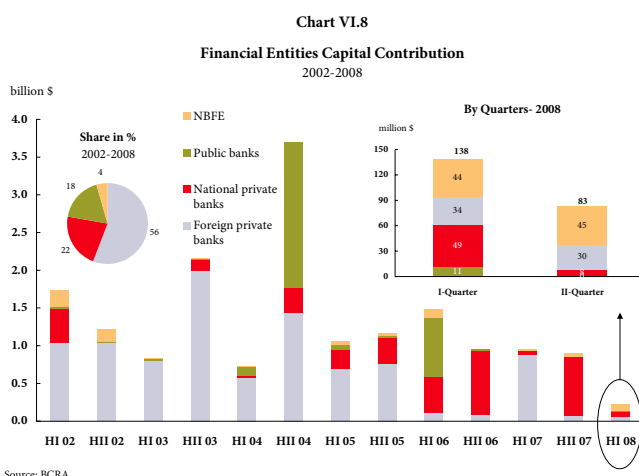
VI.2 Capital position

Accounting profits and, to a lesser extent, the fresh capital injections, strengthen the solvency of the banking system



The financial system continues exhibiting progress in terms of its soundness, in a trend reflected by both the private sector financial entities (of domestic and foreign capital) and the public banks. During the first half of the year the financial system thus received capital contributions of \$220 million, mostly channeled to the non-bank financial entities (40%) and to foreign owned banks (29%). Since 2002 capitalizations of \$17.1 billion were received, especially by the foreign capital private sector banks (see Chart VI.8), with capitalizations pending for almost \$200 million in coming periods, concentrated particularly in the public sector banks.

The net worth of the financial system accelerated its growth during the first half of 2008, a trend that was mainly in connection with the profits from the financial intermediation activity. The private sector banks led the net worth increase accounting for 70% of the expansion. The boost to growth of the sector's net worth from profits was partly offset due to the dividend payments recorded at the beginning of the year by some of the banks that trade on the Buenos Aires Stock Exchange, in the framework of the rules the Central Bank has adopted, and consistent with the balance sheet normalization process that is seen.

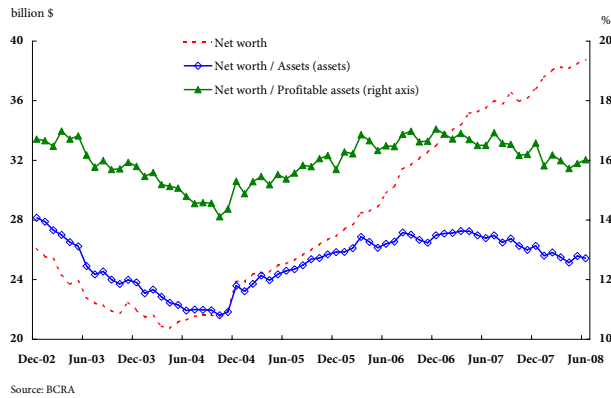


In asset terms the financial system net worth was reduced 0.4 p.p. to 12.7%, continuing on the gradual trend towards more leverage exhibited during the past 3 half year periods (see Chart VI.9). It is worth mentioning that the progress in net worth that was observed occurs together with an improvement of its composition, in terms of both capital growth and the absorption of unallocated results (losses in previous accounting years) and the increase of capital reserves.

Capital compliance levels are a clear sign of banking solvency, to enable the banks to overcome the current more volatile scenario with no major upsets

The capital compliance of the financial system was 16.5% of the risk weighted assets in June 2008, exceeding the minimum levels recommended internationally and the domestic requirements. During the first half of the year a slight fall in the level of the capital compliance ratio was seen (see Chart VI.10) associated with the greater momentum exhibited by assets at risk in a

Chart VI.9
Leverage

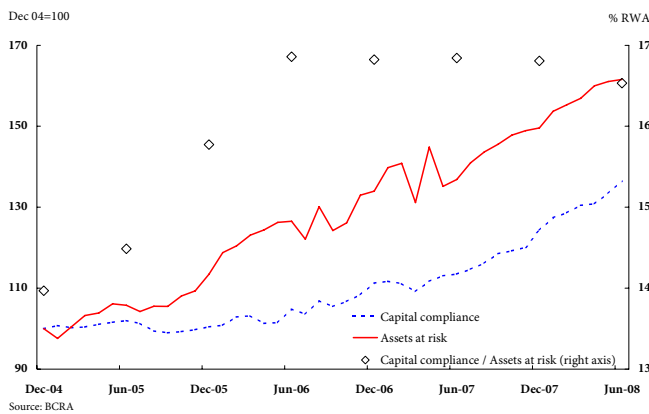


scenario of an expansion of loans. The capital position of the banking system, which indicates the capital compliance surplus over the requirement, therefore remained at slightly more than 80% of the latter.

Both the private sector financial entities and the public sector banks continued exhibiting adequate solvency levels. While the former attained a capital compliance ratio of 18.1% of the risk weighted assets, with a slightly downwards trend in recent periods in connection with the momentum of credit to the private sector, the public sector financial entities recorded a recovery of their capital compliance level to 12.9% of the risk weighted assets.

Looking ahead at the end of 2008, the deepening of the corporate and household financial intermediation activity is forecast to be reflected by a gradually stronger banking solvency, mainly associated with earning profits. Nevertheless, this scenario could be partly moderated by the possible influence on the domestic intermediation process of a scenario of more uncertainty on the financial markets.

Chart VI.10
Composition of the Capital Compliance Ratio



VII. Payments System

Summary

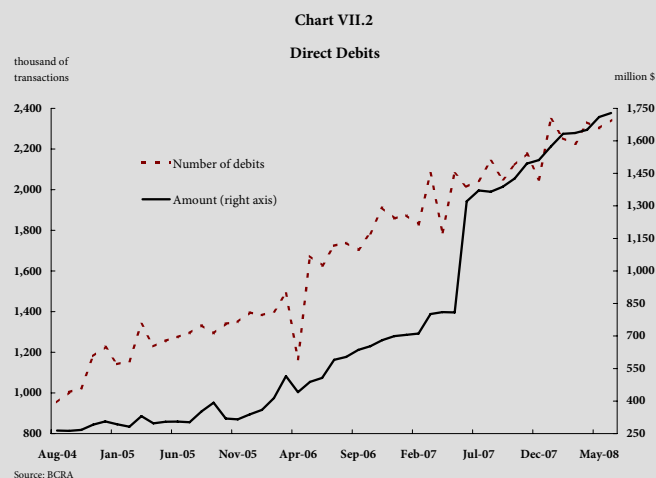
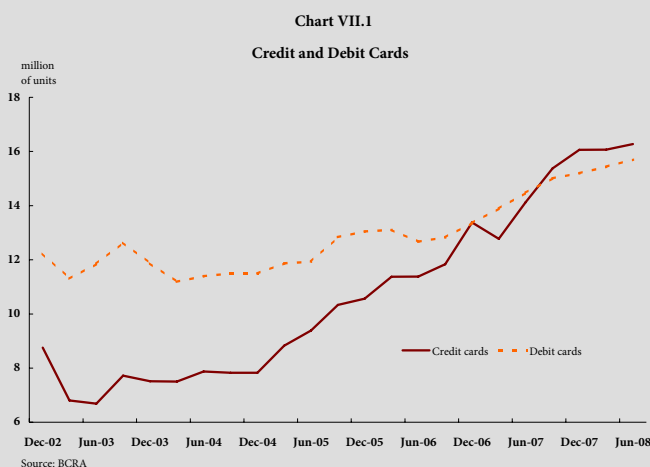
The private sector is gradually making a greater use of electronic payment instruments when carrying out transactions, although they still have a high potential for improvement. This development is still mainly led by local economic growth and by certain existing tax incentives. In this context, the National Payments System (NPS) continues to improve its performance and depth.

While cash remains being the main mean of payment of the economy, cards (credit and debit), direct debits and interbank transfers achieve greater participation in the transactions of households and companies, providing incentives to increase the degree of financial depth of the economy.

The check clearing continued to expand in the past two semesters, both in terms of quantity and volume. At the end of 2007, the rejection of documents verified an increase linked to cases of superior force (bank strikes), which was normalized in the first part of 2008. The transactions carried out with the payments system of high-value MEP (Electronic Means of Payment) also continued to increase its scope.

In line with the growth of the economy, the BCRA continues to make efforts with the aim of reaching an NPS more efficient, flexible and secure. In this context, it is assessing the implementation of actions to update the NPS and the Securities Clearance System, as well as the reformulation of the Central of Registration and Payment of Public Debt Instruments (CRYL).

Likewise, it is still present the purpose of the standardization of all the existing clearing documents or future implementation, in order to enhance the electronic clearing of payments. Also, within the scope of the Interbank Committee for Payment Means (CIMPRA), it is under analysis the implementation of a file of images of all the cleared available documents for checking by the financial drawn-on institutions while it is also useful for depository institutions. This will speed up the tasks associated with the checks processing operations and continue to promote the development of the operations of the Uniform Federal Clearing (UFC).



VII.1 National Payment System

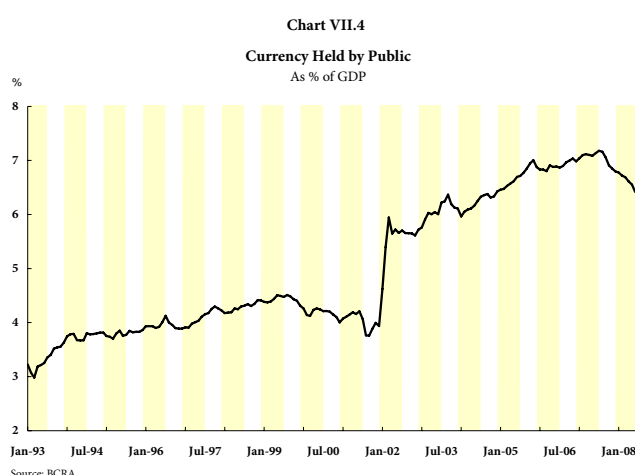
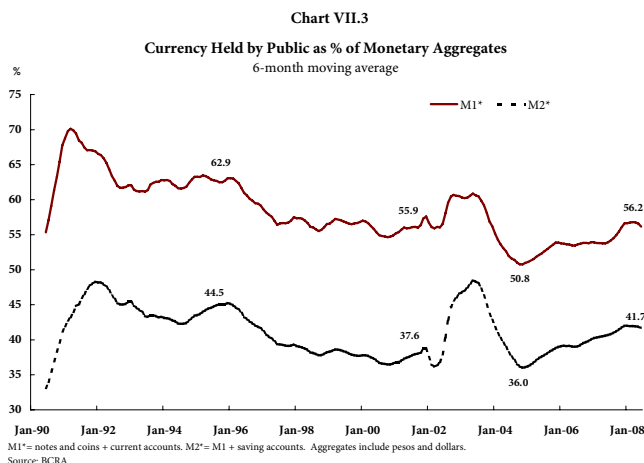
The role of the electronic means of payment in the economy deepens, while they still exhibit a high potential for development

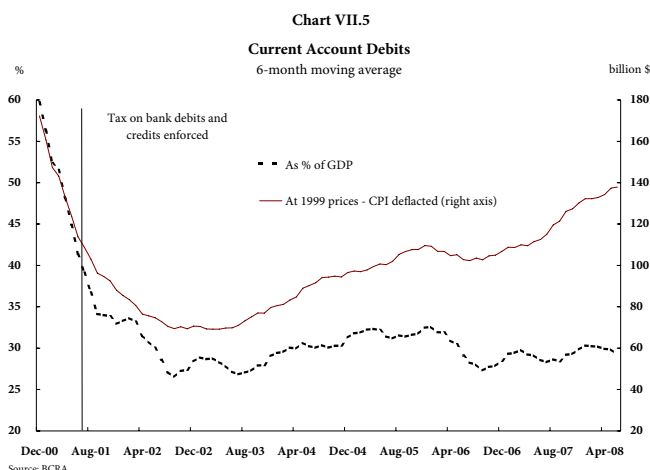
Households and companies gradually turn toward greater use of electronic payment instruments when carrying out their usual transactions, trend that continues to be driven by local economic growth. This evolution will allow achieving new improvements in terms of the financial depth of the agents, while reaching improvements in safety and efficiency in the transactions of the economy. In this context, the National Payments System (NPS) continues to boost its performance.

Currency held by public showed a growing pattern in the last year in terms of the total monetary aggregates M1 and M2 (see Chart VII.3), in line with the economic expansion path and the increase of the price levels. Thus, the banknotes and coins held by public totaled \$65.6 billion in average in the first part of 2008, 9% and 22% more than in the previous six months and during the same period of 2007, respectively. This evolution was more than compensated by the increase of the GDP, generating a decline of nearly 0.7 y.o.y., in the currency weight in the economy to a level 6.4% in June 2008 (see Chart VII.4).

The amounts of debit transactions in current account rose on average 11% and 33% compared with the closing of 2007 and with the first half of the previous year, though it remains virtually unchanged in terms of GDP (see Chart VII.5). The evolution of the use of these means is still being influenced by the effect of the Tax on Current Accounts Debits and Credits (IDCCB), affecting the decisions of the agents at the time of making fund transfers.

Credit and debit cards expanded its scope into the economy although still have plenty of room to grow, especially in the locations more distant from major urban centers. Some of the barriers of these instruments in achieving greater depth are associated with the informality that exists in certain sectors of the economy and with the operating costs (both fixed and variable) associated with its implementation in commercial premises. These factors are somewhat tempered by the benefits associated with its use, both tax (percentage of VAT refund of the transaction) and of increased security on the transport of cash, among others. Thus, the number of debit cards reached almost 15.7 million by the end of the first part of 2008 (see Chart VII.1), rising

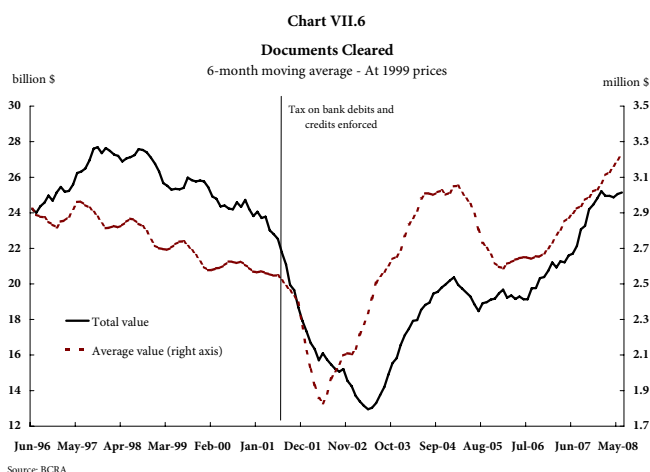




more than 3% and 8% over 2008 and in the past 12 months, respectively. Meanwhile, the number of credit cards rose slightly more than 15% since mid-2007, to almost 16.3 million, registering the lowest interannual momentum of the last years.

The electronic clearing system processed nearly 46.6 million documents in pesos between January and June 2008, exhibiting a growth of 3.8% over the same period of 2007, while showing a decrease regarding the closing of the previous year. In 2008, a total of \$314 billion of cleared checks were accumulated exhibiting an increase of 6% over the second half of 2007 and 26% in interannual terms (1.4% and 16% if deflated by CPI GBA) (see Chart VII.6). This trend continues to be accompanied by an increment in the average value of transactions. The average clearing of checks in the first half reached 4.7% of GDP, slightly below the previous semesters, while the monthly average of truncated checks that have revealed no document image -with amounts of up to \$5,000- was 84% of all the cleared documents.

Throughout the year, the number of rejected documents (on the whole) was 2% of the amount of checks cleared (see Chart VII.7). While this value was located slightly above the same period of 2007, it represents a significant drop of 0.9 y.o.y. regarding the second half of 2007, period in which there were employees stoppages (mostly in a public bank of importance) which generated an increase in the rejection due to circumstances beyond control. As in previous years, the interannual comparison shows that both the quantity as well as the total amount of rejected checks recorded slight increases.



The use of retail transfers continue to grow persistently: in the first six months of 2008 they accumulated nearly 5.1 million transactions, almost one third more than in the same period of 2007. Besides, the total amounts exhibited an increase of just over 52% (value which is located at 40% if deflated by CPI GBA) (see Chart VII.8), gradually growing in terms of GDP.

Direct debits, mainly designated for the payment of services (electricity, gas, health care fees, and credit cards, among others) continue to gain share. In particular, in the accumulated of 2008, the number of direct debits from operations totaled approximately 13.8 million, recording increases of 9.7% and 18.3% regarding the closing and over the same period of 2007, respectively. These transactions reached a volume of about \$9.9 billion in the first six months of 2008 (see Chart VII.2) almost doubling the value of the first half of

the previous year. This trend reflected, to some extent, the incorporation of the Federal Revenue Administration (AFIP) since mid-2007 in the clearing of direct debits through the clearing houses.

Transactions using the Electronic Means of Payment (MEP) (high-value payment system) accumulated nearly 701 thousand in the first half of 2008, for a total value of \$1.550 billion. Thus, these transactions represented an increase of approximately 4% in quantity and 39% in volume (27% deflated by CPI GBA) (see Chart VII.9) when compared to the first half of 2007.

VII.2 Modernization of the payments system

The BCRA continues to work on the modernization and expansion of the National Payments System

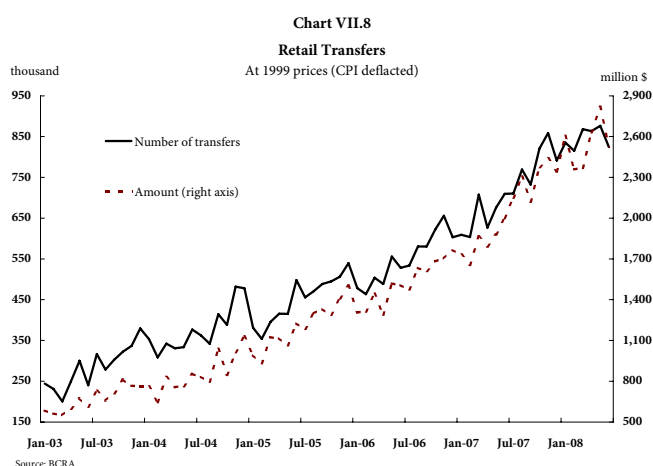
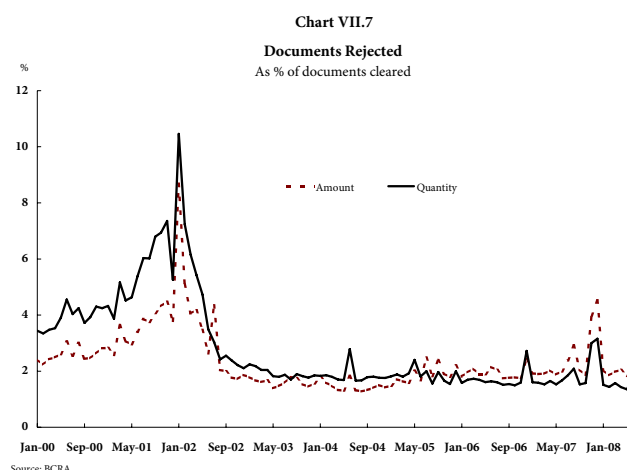
Accompanying the general growth of the economy, the BCRA continues to make efforts with the aim of achieving an NPS more efficient, flexible and secure. In this context, this Institution continues to focus on its responsibilities of monitoring and updating the NPS, promoting its deepening.

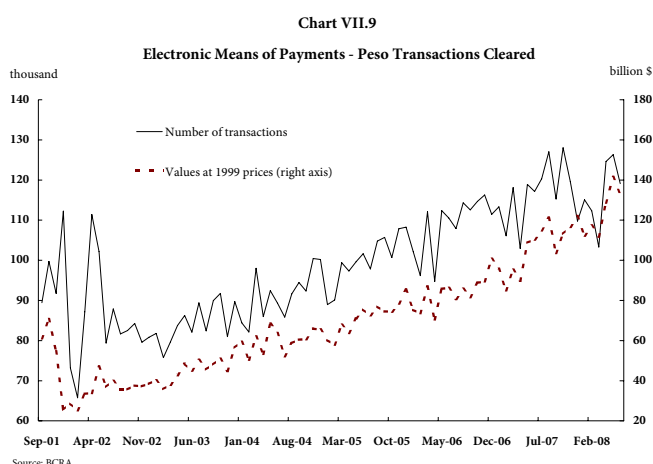
By means of a combined work with the World Bank, a survey and an analysis of the NPS has been carried out with the intention of having a clear picture of its current situation. In the coming periods, the BCRA will elaborate an action plan to further promote the development of the NPS, as well as to be able to adapt it appropriately to future challenges.

In this context, the Central Bank is evaluating the necessary actions to modernize the NPS and the Securities Settlement System. Under study, there are improvements in the legal framework in order to achieve a comprehensive scheme that supports the functioning of the payment system. Furthermore, it is being considered a possible revision of the Central of Registration and Payment of Government Debt (CRYL) to incorporate technological and functional improvements.

Since November 2006, the final stage of the Uniform Federal Clearing (UFC) is completed which is mainly based on the transmission of images of checks and other documents suitable for clearing, thus implying the total elimination of the physical movement of the mentioned documents.

In perspective, the UFC has helped to improve the efficiency of processes, while resulting in a significant





reduction in operational risk and operational costs, enabling simultaneous interconnection of all the financial centers of the country in one single daily video session. The UFC allows customers of the system to receive the funds in the same single run, regardless the place the checks are deposited or their amount.

Since the beginning of the UFC project, the purpose of optimizing the electronic clearing of payments have given rise to a standardization need of all existing clearing documents or of future implementation. This standardization that began with checks allows unifying designs and measures of security with the purpose of offering depository banks more tools for verification and control of documents. This tends to minimize operational risks associated with potential fraud.

As a result, the BCRA has developed and disseminated guidelines to be attuned to the bills of exchange that are feasible of clearing and that can be cleared against accounts opened in Credit Cooperatives (Law No. 26,173 and regulations issued by the BCRA). This process of standardization is supplemented by an approval procedure of document clearing carried out by the BCRA, as the preliminary step to final printing of them by the financial entities.

In turn, within the scope of the Interbank Committee for Payment Means (CIMPRA), the implementation of a file in which images of all the cleared documents are available for checking by all financial entities is being analyzed. The assessment includes both technological aspects and those related to the feasibility of including this file directly on the current clearing mechanism. It is considered that the widespread use and introduction into the clearing mechanism of this file would facilitate, in the future, expediting the tasks arising from the management of checks and continue enhancing the process of UFC optimization.

The proposal outlined by the BCRA to rewrite the law of checks, including the procedure for truncated checks, is currently located as Bill in the Ministry of Economy and Production for appropriate consideration.

Balance of Risks

In a context of worsening, almost unprecedented in international financial markets and some slowdown in local economic growth, the financial system continues to show a significant degree of strength, carrying out a consistent administration of the inherent risks it assumes. The timely action of the BCRA in the exchange market and its systemic liquidity injections help to ensure the conditions of monetary and financial stability, sustaining the process of financial intermediation with the private sector without neglecting the precautionary level of bank liquidity. Consequently, the risks assumed by the financial system remain limited, with no significant changes in recent months.

Credit to companies and households deepen while banks show a good position in the face of liquidity risk, in part driven by the tools developed by the BCRA (thanks to the anti-cyclical prudential policies built on recent years). This helped to attack successfully the mismatch in the demand for money verified in the second quarter of 2008 that was reflected in a transitory decrease of private deposits. Currently, financial intermediaries have a greater range of mechanisms to consolidate their levels of preventive liquidity.

Banks maintain a good position against the repayment risk of the private sector. The moderate levels of indebtedness of households and companies, added to certain improvements in the labor market and to the verified growth and foreseen growth of the different sectors, strengthen its payment capacity. Provisioning outperforms the irregular loans, while these remain at historically low values, although they could be at a minimum in a context of certain deceleration of credit dynamism. While the performance of credit to companies improves, the quality of households financing exhibits a decline driven by the consumer lines, representing one of the factors to monitor. Banks improve its profile when facing the public sector credit risk, due to low exposure to this sector and to the fiscal surplus and declining debt levels of the National Government of recent years.

Due to the lower balance sheet mismatch of foreign currency, the financial system shows an improvement in its position against the fluctuations in the exchange rate peso-dollar. While there is some volatility in the exchange rate peso-dollar, by mid-year this was moderated by the intervention of the BCRA that reversed the expectations, avoiding a negative impact on the level of the economic activity. This also had its

consequence in a volatility reduction of the banks net worth.

The interest rate risk assumed by the financial system continues at moderate levels, in view that mismatches in maturity and in adjustment by CER items do not show changes of magnitude. BCRA has been driving market solutions for the hedging of those mismatches, as the implementation of the swap mechanism of interest rates. On the other hand, the securities valuation rules established by the Central Bank managed to avoid that the volatility in the financial assets yield generate an excessive impact on the balance sheet of the banks, in view of the market risk assumed.

In this scenario, the more volatile international context continues to represent the main factor that could trigger the materialization of the risks the financial system confronts. Faced with this situation, banks currently have a good balance sheet position, reflecting the strong levels of solvency derived from accounting benefits and capital contributions, setting up a more resilient position to confront *shocks* episodes.

For the remainder of the year, it is expected that the strategy pursued by the BCRA will consolidate the degree of resilience of the financial system, protecting the local economy in a context of turbulence. The ability and determination shown by the BCRA in the two episodes of high financial volatility (July-August 2007 and May 2008) are factors that should temper the levels of uncertainty, minimizing the possibility of new episodes of excessive caution of the economic agents that eventually can represent challenges for maintaining a monetary and financial stability.

Statistics Annex – Financial System

Chart 1 | Financial Soundness Indicators

As %	1996	1997	1998	1999	2000	2001	2002	2003	2004	2005	2006	Jun 07	2007	Jun 08
1- Liquidity	22.3	26.1	23.1	25.0	23.4	19.6	22.8	29.1	29.6	20.1	22.5	22.1	23.0	24.7
2- Lending to the public sector	16.9	16.2	16.2	18.0	17.3	23.0	48.5	46.5	40.6	31.3	22.3	17.3	16.1	14.0
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	32.1	38.2	38.7
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	3.9	3.2	3.1
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	-3.1	-3.0	-2.5
6- ROA	0.6	1.0	0.5	0.2	0.0	0.0	-8.9	-2.9	-0.5	0.9	1.9	1.7	1.5	1.6
7- ROE	4.1	6.3	3.9	1.7	0.0	-0.2	-59.2	-22.7	-4.2	7.0	14.3	12.8	11.0	13.6
8- Efficiency	142	136	138	142	147	143	189	69	125	151	167	168	160	165
9- Capital compliance	23.8	20.8	20.3	21.0	20.1	21.4	-	14.5	14.0	15.3	16.8	16.8	16.8	16.5
10- Excess capital compliance	64	73	49	54	58	54	-	116	185	173	134	92	92	82

Source: BCRA

Chart 2 | Balance Sheet

In millions of current pesos	Dec 00	Dec 01	Dec 02	Dec 03	Dec 04	Dec 05	Dec 06	Jun 07	Dec 07	Jun 08	Change (%)	
											Half-yearly	Inter annual
Assets	163,550	123,743	187,532	186,873	212,562	221,962	258,384	289,316	297,963	328,125	10.1	13.4
Liquid assets ¹	20,278	13,005	17,138	27,575	29,154	20,819	37,991	37,595	46,320	51,492	11.2	37.0
Public bonds	10,474	3,694	31,418	45,062	55,382	66,733	64,592	77,284	62,678	65,980	5.3	-14.6
Lebac/Nobac	0	0	-	-	17,755	28,340	29,289	44,913	36,022	40,712	13.0	-9.4
Portfolio	0	0	-	-	11,803	21,067	25,725	35,598	31,598	33,499	6.0	-5.9
Repo	0	0	-	-	5,953	7,273	3,563	9,315	4,424	7,213	63.0	-22.6
Private bonds	633	543	332	198	387	389	813	795	382	753	97.0	-5.3
Loans	83,277	77,351	84,792	68,042	73,617	84,171	103,668	112,083	132,157	146,282	10.7	30.5
Public sector	15,164	22,694	44,337	33,228	30,866	25,836	20,874	16,734	16,772	17,387	3.7	3.9
Private sector	64,464	52,039	38,470	33,398	41,054	55,885	77,832	89,922	110,355	123,095	11.5	36.9
Financial sector	3,649	2,617	1,985	1,417	1,697	2,450	4,962	5,427	5,030	5,800	15.3	6.9
Provisions over loans	-6,907	-6,987	-11,952	-9,374	-7,500	-4,930	-3,728	-3,748	-4,089	-4,261	4.2	13.7
Other netted credits due to financial intermediation	42,361	21,485	39,089	27,030	32,554	26,721	26,039	35,711	29,712	37,003	24.5	3.6
Corporate bonds and subordinated debt	794	751	1,708	1,569	1,018	873	773	724	606	688	13.6	-5.0
Unquoted trusts	2,053	2,065	6,698	4,133	3,145	3,883	4,881	4,754	5,023	5,654	12.6	18.9
Compensation receivable	0	0	17,111	14,937	15,467	5,841	763	367	377	314	-16.8	-14.4
Other	39,514	18,669	13,572	6,392	12,924	16,124	19,622	29,866	23,706	30,347	28.0	1.6
Leasing	786	771	567	397	611	1,384	2,262	2,945	3,469	3,936	13.5	33.7
Shares in other companies	2,645	2,688	4,653	4,591	3,871	4,532	6,392	6,842	6,430	6,735	4.7	-1.6
Fixed assets and miscellaneous	4,939	4,804	8,636	8,164	7,782	7,546	7,619	7,606	7,643	7,699	0.7	1.2
Foreign branches	1,115	1,057	3,522	3,144	3,524	3,647	2,782	2,880	2,912	2,869	-1.5	-0.4
Other assets	3,950	5,334	9,338	12,043	13,180	10,950	9,953	9,322	10,347	9,637	-6.9	3.4
Liabilities	146,267	107,261	161,446	164,923	188,683	195,044	225,369	253,811	261,143	289,412	10.8	14.0
Deposits	86,506	66,458	75,001	94,635	116,655	136,492	170,898	190,281	205,550	225,505	9.7	18.5
Public sector ²	7,204	950	8,381	16,040	31,649	34,019	45,410	47,805	48,340	59,911	23.9	25.3
Private sector ²	78,397	43,270	59,698	74,951	83,000	100,809	123,431	139,935	155,048	163,036	5.2	16.5
Current account	6,438	7,158	11,462	15,071	18,219	23,487	26,900	32,054	35,245	36,702	4.1	14.5
Savings account	13,008	14,757	10,523	16,809	23,866	29,078	36,442	40,654	47,109	48,699	3.4	19.8
Time deposit	53,915	18,012	19,080	33,285	34,944	42,822	54,338	60,515	65,952	70,048	6.2	15.8
CEDRO	0	0	12,328	3,217	1,046	17	13	13	0	0	-	-
Other netted liabilities due to financial intermediation	55,297	36,019	75,737	61,690	64,928	52,072	46,037	54,992	46,225	54,050	16.9	-1.7
Interbanking obligations	3,545	2,550	1,649	1,317	1,461	2,164	4,578	4,864	4,310	5,071	17.7	4.3
BCRA lines	102	4,470	27,837	27,491	27,726	17,005	7,686	3,585	2,362	2,223	-5.9	-38.0
Outstanding bonds	4,954	3,777	9,096	6,675	7,922	6,548	6,603	8,003	6,938	6,376	-8.1	-20.3
Foreign lines of credit	8,813	7,927	25,199	15,196	8,884	4,684	4,240	3,255	3,864	4,681	21.2	43.8
Other	37,883	17,295	11,955	11,012	18,934	21,671	22,930	35,285	28,752	35,699	24.2	1.2
Subordinated debts	2,255	2,260	3,712	2,028	1,415	1,381	1,642	1,657	1,672	1,589	-5.0	-4.1
Other liabilities	2,210	2,524	6,997	6,569	5,685	5,099	6,792	6,880	7,695	8,267	7.4	20.2
Net worth	17,283	16,483	26,086	21,950	23,879	26,918	33,014	35,506	36,819	38,713	5.1	9.0
Memo												
Netted assets	129,815	110,275	185,356	184,371	202,447	208,275	244,791	265,130	280,336	304,797	8.7	15.0
Consolidated netted assets	125,093	106,576	181,253	181,077	198,462	203,286	235,845	255,334	271,652	295,211	8.7	15.6

(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

	Annual									Half year			Change (%)		
<i>In millions of current pesos</i>	1999	2000	2001	2002 ¹	2003	2004	2005	2006	2007	I-07	II-07	I-08	I-08 / II-07	II-08 / I-07	
Financial margin	6,967	7,291	6,943	13,991	1,965	6,075	9,475	13,262	15,134	7,510	7,624	9,668	27	29	
Net interest income	5,396	5,106	4,625	-3,624	-943	1,753	3,069	4,150	5,744	2,545	3,199	4,287	34	68	
CER and CVS adjustments	0	0	0	8,298	2,315	1,944	3,051	3,012	2,624	1,449	1,175	1,814	54	25	
Foreign exchange rate adjustments	227	185	268	5,977	-890	866	751	944	1,357	499	858	622	-28	25	
Gains on securities	1,112	1,481	1,490	3,639	1,962	1,887	2,371	4,923	5,144	2,872	2,272	2,877	27	0	
Other financial income	232	519	559	-299	-480	-375	233	235	264	144	120	68	-43	-53	
Service income margin	3,623	3,582	3,604	4,011	3,415	3,904	4,781	6,243	8,248	3,752	4,496	5,033	12	34	
Loan loss provisions	-2,565	-3,056	-3,096	-10,007	-2,089	-1,511	-1,173	-1,198	-1,894	-732	-1,161	-1,244	7	70	
Operating costs	-7,432	-7,375	-7,362	-9,520	-7,760	-7,998	-9,437	-11,655	-14,634	-6,721	-7,912	-8,884	12	32	
Tax charges	-497	-528	-571	-691	-473	-584	-737	-1,090	-1,537	-681	-856	-1,011	18	49	
Income tax	-421	-446	-262	-509	-305	-275	-581	-595	-1,032	-619	-413	-669	62	8	
Adjustments to the valuation of government securities ²	0	0	0	0	-701	-320	-410	-752	-837	-49	-788	-791	0	1,500	
Amortization payments for court-ordered releases	0	0	0	0	-1,124	-1,686	-1,867	-2,573	-1,922	-975	-947	-541	-43	-44	
Other	617	535	702	-3,880	1,738	1,497	1,729	2,664	2,380	736	1,644	802	-51	9	
Monetary results	0	0	0	-12,558	69	0	0	0	0	0	0	0	0	0	
Total results	291	3	-42	-19,162	-5,265	-898	1,780	4,306	3,905	2,220	1,685	2,362	40	6	
Adjusted results ³	-	-	-	-	-3,440	1,337	4,057	7,631	6,665	3,244	3,421	3,695	8	14	
<i>Annualized indicators - As % of netted assets</i>											<i>change in p.p</i>				
Financial margin	5.6	5.7	5.7	6.5	1.1	3.1	4.6	5.8	5.7	5.9	5.6	6.6	1.0	0.7	
Net interest income	4.3	4.0	3.8	-1.7	-0.5	0.9	1.5	1.8	2.2	2.0	2.3	2.9	0.6	0.9	
CER and CVS adjustments	0.0	0.0	0.0	3.9	1.3	1.0	1.5	1.3	1.0	1.1	0.9	1.2	0.4	0.1	
Foreign exchange rate adjustments	0.2	0.1	0.2	2.8	-0.5	0.4	0.4	0.4	0.5	0.4	0.6	0.4	-0.2	0.0	
Gains on securities	0.9	1.2	1.2	1.7	1.1	1.0	1.2	2.2	1.9	2.2	1.7	2.0	0.3	-0.3	
Other financial income	0.2	0.4	0.5	-0.1	-0.3	-0.2	0.1	0.1	0.1	0.1	0.1	0.0	0.0	-0.1	
Service income margin	2.9	2.8	3.0	1.9	1.9	2.0	2.3	2.7	3.1	2.9	3.3	3.4	0.1	0.5	
Loan loss provisions	-2.1	-2.4	-2.6	-4.7	-1.1	-0.8	-0.6	-0.5	-0.7	-0.6	-0.8	-0.8	0.0	-0.3	
Operating costs	-5.9	-5.8	-6.1	-4.4	-4.2	-4.1	-4.6	-5.1	-5.5	-5.2	-5.8	-6.0	-0.2	-0.8	
Tax charges	-0.4	-0.4	-0.5	-0.3	-0.3	-0.3	-0.4	-0.5	-0.6	-0.5	-0.6	-0.7	-0.1	-0.2	
Income tax	-0.3	-0.3	-0.2	-0.2	-0.2	-0.1	-0.3	-0.3	-0.4	-0.5	-0.3	-0.5	-0.2	0.0	
Adjustments to the valuation of government securities ²	0.0	0.0	0.0	0.0	-0.4	-0.2	-0.2	-0.3	-0.3	0.0	-0.6	-0.5	0.0	-0.5	
Amortization payments for court-ordered releases	0.0	0.0	0.0	0.0	-0.6	-0.9	-0.9	-1.1	-0.7	-0.8	-0.7	-0.4	0.3	0.4	
Other	0.5	0.4	0.6	-1.8	0.9	0.8	0.8	1.2	0.9	0.6	1.2	0.5	-0.7	0.0	
Monetary results	0.0	0.0	0.0	-5.8	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	
ROA	0.2	0.0	0.0	-8.9	-2.9	-0.5	0.9	1.9	1.5	1.7	1.2	1.6	0.4	-0.1	
ROA adjusted ³	-	-	-	-	-1.9	0.7	2.0	3.4	2.5	2.5	2.5	2.5	0.0	0.0	
ROE	1.7	0.0	-0.2	-59.2	-22.7	-4.2	7.0	14.3	11.0	12.8	9.3	13.6	4.3	0.9	

(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

<i>As percentage</i>	Dec 00	Dec 01	Dec 02	Dec 03	Dec 04	Dec 05	Dec 06	Jun 07	Dec 07	Jun 08
Non-performing loans (overall)	12.9	13.1	18.1	17.7	10.7	5.2	3.4	3.1	2.7	2.7
Non-performing loans to the non-financial private sector	16.0	19.1	38.6	33.5	18.6	7.6	4.5	3.9	3.2	3.1
Provisions / Non-performing loans	61.1	66.4	73.8	79.2	102.9	124.5	129.9	129.9	129.6	123.5
(Total non-performing - Provisions) / Overall financing	5.0	4.4	4.7	3.7	-0.3	-1.3	-1.0	-0.9	-0.8	-0.6
(Total non-performing - Provisions) / Net worth	26.2	21.6	17.2	11.9	-1.0	-4.1	-3.3	-3.1	-3.0	-2.5

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

Source: BCRA

Chart 5 | International Indicators

	GDP	Liquid assets / Private deposits	Private loans / Total assets	Non-performing loans to the private sector	Provisions / Non-performing loans	ROA	ROE	ROE (in real terms)	Capital compliance / Risk weighted assets
<i>2007/2008: Last available data</i>	(1)	(2)	(3)	(4)	(5)	(6)	(7)	(8)	(9)
Argentina	343	24.7	38	3.1	124	1.6	13.6	4.0	16.5
Australia	966	0.8	84	0.2	189	1.6	28.1	25.5	10.3
Brazil	1,445	9.2	42	3.2	182	2.7	27.8	22.9	18.4
Chile	173	3.7	85	0.8	211	1.1	16.2	8.4	12.0
Spain	1,544	1.4	80	0.9	273	1.0	19.9	16.9	11.9
United States	13,841	0.6	55	1.1	105	1.1	10.5	8.0	12.8
Japan	4,524	1.6	53	1.5	29	0.2	3.2	3.3	12.9
Mexico	1,025	13.0	26	2.5	195	2.8	20.2	15.6	15.9
United Kingdom	2,770	1.5	43	0.9	55	0.5	8.9	4.7	12.9

Source: BCRA; International Financial Statistics (August 2008) and Global Financial Stability Report (April 2008) - International Monetary Fund.

Methodological note (chart 5)

1.- GDP – in billion of US\$; 2.- Cash in banks plus deposits in the monetary authority / Private deposits (%); 3.- Loans to the private sector / Total assets (%); 4.- Non-performing loans to the private sector / Total loans to the private sector (%); 5.- Provisions / Non-performing loans (%); 6.- Total results / Netted assets (%); 7.- Total results / Net worth (%); 8.- Total results / Net worth (%) (deflated by CPI); 9.- Capital compliance / Risk - adjusted assets (%).

Statistics Annex – Private Banks

Chart 6 | Financial Soundness Indicators

As %	1996	1997	1998	1999	2000	2001	2002	2003	2004	2005	2006	Jun 07	2007	Jun 08
1- Liquidity	23.6	26.9	22.8	24.3	24.1	23.6	24.8	27.6	29.2	21.5	23.7	23.8	25.7	26.6
2- Lending to the public sector	13.5	13.7	13.6	16.1	14.7	20.8	49.4	47.1	41.2	28.0	15.9	11.0	9.1	7.5
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	40.3	46.6	47.4
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	3.2	2.5	2.6
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	-2.9	-3.6	-3.1
6- ROA	0.6	0.7	0.5	0.3	0.1	0.2	-11.3	-2.5	-1.0	0.5	2.2	1.8	1.6	1.8
7- ROE	4.1	6.3	4.3	2.3	0.8	1.4	-79.0	-19.1	-8.1	4.1	15.3	12.3	10.9	14.2
8- Efficiency	144	135	139	146	152	151	168	93	115	136	158	159	152	163
9- Capital compliance	15.9	15.4	14.6	18.9	18.0	17.6	-	14.0	15.1	17.8	18.6	20.0	19.2	18.1
10- Excess capital compliance	33	47	27	60	49	43	-	88	157	155	116	93	87	77

Source: BCRA

Chart 7 | Balance Sheet

In millions of current pesos	Dec 00	Dec 01	Dec 02	Dec 03	Dec 04	Dec 05	Dec 06	Jun 07	Dec 07	Jun 08	Change (%)	
											Half-yearly	Inter annual
Assets	119,371	82,344	118,906	116,633	128,065	129,680	152,414	166,408	175,509	188,766	7.6	13.4
Liquid assets ¹	13,920	10,576	11,044	14,500	15,893	14,074	22,226	23,293	29,418	30,542	3.8	31.1
Public bonds	7,583	1,627	19,751	22,260	24,817	29,966	27,663	32,298	24,444	21,974	-10.1	-32.0
Lebac/Nobac	0	0	-	-	8,359	15,227	15,952	22,229	17,684	15,626	-11.6	-29.7
Portfolio	0	0	-	-	5,611	12,899	14,220	18,668	15,639	12,596	-19.5	-32.5
Repo	0	0	-	-	2,749	2,328	1,732	3,561	2,045	3,030	48.2	-14.9
Private bonds	563	451	273	172	333	307	683	639	310	578	86.2	-9.6
Loans	56,035	52,319	51,774	47,017	50,741	56,565	69,294	74,876	88,898	96,583	8.6	29.0
Public sector	8,172	13,803	25,056	23,571	21,420	15,954	10,036	6,461	6,413	6,186	-3.5	-4.3
Private sector	45,103	36,636	26,074	22,816	28,213	39,031	55,632	64,311	78,587	85,943	9.4	33.6
Financial sector	2,760	1,880	644	630	1,107	1,580	3,626	4,104	3,898	4,454	14.3	8.5
Provisions over loans	-3,248	-3,957	-7,463	-5,225	-3,717	-2,482	-2,227	-2,293	-2,365	-2,626	11.1	14.5
Other netted credits due to financial intermediation	36,600	13,037	27,212	22,148	25,753	16,873	18,387	20,136	17,084	22,963	34.4	14.0
Corporate bonds and subordinated debt	724	665	1,514	1,394	829	675	618	583	430	506	17.7	-13.2
Unquoted trusts	1,609	1,637	6,205	3,571	2,362	2,444	2,982	3,403	3,456	4,105	18.8	20.6
Compensation receivable	0	0	15,971	13,812	14,657	5,575	760	366	377	314	-16.8	-14.4
Other	34,267	10,735	3,523	3,370	7,905	8,179	14,027	15,783	12,822	18,038	40.7	14.3
Leasing	776	752	553	387	592	1,356	2,126	2,743	3,149	3,519	11.8	28.3
Shares in other companies	1,651	1,703	3,123	2,791	1,892	2,416	4,042	4,433	3,762	4,129	9.8	-6.8
Fixed assets and miscellaneous	3,225	3,150	5,198	4,902	4,678	4,575	4,677	4,676	4,685	4,750	1.4	1.6
Foreign branches	75	112	-109	-136	-53	-148	-139	-145	-154	-152	-1.2	4.6
Other assets	2,190	2,574	7,549	7,816	7,137	6,178	5,682	5,753	6,277	6,506	3.6	13.1
Liabilities	107,193	70,829	103,079	101,732	113,285	112,600	131,476	143,830	152,153	164,082	7.8	14.1
Deposits	57,833	44,863	44,445	52,625	62,685	75,668	94,095	105,833	116,719	122,751	5.2	16.0
Public sector ²	1,276	950	1,636	3,077	6,039	6,946	7,029	7,730	7,564	9,450	24.9	22.3
Private sector ²	55,917	43,270	38,289	47,097	55,384	67,859	85,714	96,668	107,671	111,642	3.7	15.5
Current account	4,960	7,158	8,905	11,588	13,966	17,946	20,604	24,317	27,132	27,875	2.7	14.6
Savings account	9,409	14,757	6,309	10,547	14,842	18,362	23,165	25,485	30,169	29,850	-1.1	17.1
Time deposit	39,030	18,012	11,083	18,710	22,729	27,736	38,043	42,582	45,770	48,802	6.6	14.6
CEDRO	0	0	9,016	2,409	798	3	1	1	0	0	-	-
Other netted liabilities due to financial intermediation	46,271	22,629	49,341	42,367	45,083	32,349	31,750	32,598	29,323	35,123	19.8	7.7
Interbanking obligations	2,293	1,514	836	726	1,070	1,488	3,383	3,204	1,979	2,135	7.9	-33.4
BCRA lines	83	1,758	16,624	17,030	17,768	10,088	3,689	730	675	711	5.4	-2.6
Outstanding bonds	4,939	3,703	9,073	6,674	7,922	6,548	6,413	7,813	6,686	6,129	-8.3	-21.6
Foreign lines of credit	5,491	4,644	15,434	9,998	5,444	2,696	1,286	1,833	2,706	2,407	47.6	110.4
Other	33,466	11,010	7,374	7,939	12,878	11,530	16,015	19,564	18,150	23,441	29.2	19.8
Subordinated debts	1,668	1,700	3,622	1,850	1,304	1,319	1,642	1,653	1,668	1,585	-5.0	-4.1
Other liabilities	1,420	1,637	5,671	4,890	4,213	3,264	3,989	3,745	4,443	4,624	4.1	23.5
Net worth	12,178	11,515	15,827	14,900	14,780	17,080	20,938	22,578	23,356	24,683	5.7	9.3
Memo												
Netted assets	88,501	73,796	117,928	115,091	121,889	123,271	143,807	154,184	166,231	174,957	5.2	13.5

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

Source: BCRA

Methodological note (chart 6)

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 8 | Profitability Structure

	Annual									Half year			Change (%)	
<i>In millions of current pesos</i>	1999	2000	2001	2002 ¹	2003	2004	2005	2006	2007	I-07	II-07	I-08	I-08 / II-07	II-08 / I-07
Financial margin	5,176	5,441	5,282	10,628	2,575	3,415	5,253	7,778	8,960	4,407	4,553	6,006	32	36
Net interest income	3,819	3,598	3,519	-304	107	1,214	2,069	2,826	4,191	1,742	2,449	3,463	41	99
CER and CVS adjustments	0	0	0	1,476	1,082	900	1,215	858	662	401	261	429	64	7
Foreign exchange rate adjustments	213	160	256	6,189	-312	666	576	740	990	387	602	694	15	79
Gains on securities	908	1,232	962	3,464	1,892	959	1,259	3,154	2,888	1,747	1,141	1,374	20	-21
Other financial income	236	450	546	-197	-195	-322	134	199	229	131	98	47	-52	-64
Service income margin	2,598	2,554	2,598	2,782	2,341	2,774	3,350	4,459	5,881	2,713	3,168	3,549	12	31
Loan loss provisions	-1,872	-2,173	-2,464	-6,923	-1,461	-1,036	-714	-737	-1,174	-518	-656	-820	25	58
Operating costs	-5,326	-5,263	-5,224	-6,726	-5,310	-5,382	-6,303	-7,741	-9,735	-4,475	-5,260	-5,877	12	31
Tax charges	-368	-379	-418	-512	-366	-393	-509	-769	-1,105	-486	-619	-754	22	55
Income tax	-386	-393	-216	-337	-295	-202	-217	-365	-380	-192	-188	-460	145	140
Adjustments to the valuation of government securities ²	0	0	0	0	-665	-51	-201	-170	-100	20	-120	-132	10	-768
Amortization payments for court-ordered releases	0	0	0	0	-791	-1,147	-1,168	-1,182	-1,466	-781	-684	-356	-48	-54
Other	447	307	615	-4,164	1,178	846	1,156	1,641	1,576	666	910	404	-56	-39
Monetary results	0	0	0	-10,531	-20	0	0	0	0	0	0	0	0	0
Total results	269	93	174	-15,784	-2,813	-1,176	648	2,915	2,457	1,353	1,104	1,560	41	15
Adjusted results ³	-	-	-	-	-1,357	252	2,016	4,267	4,023	2,115	1,908	2,048	7	-3
<i>Annualized indicators - As % of netted assets</i>													<i>change in p.p.</i>	
Financial margin	6.1	6.2	6.4	7.6	2.3	2.9	4.3	5.9	5.8	5.9	5.7	7.0	1.3	1.1
Net interest income	4.5	4.1	4.3	-0.2	0.1	1.0	1.7	2.1	2.7	2.3	3.1	4.0	1.0	1.7
CER and CVS adjustments	0.0	0.0	0.0	1.1	0.9	0.8	1.0	0.6	0.4	0.5	0.3	0.5	0.2	0.0
Foreign exchange rate adjustments	0.3	0.2	0.3	4.4	-0.3	0.6	0.5	0.6	0.6	0.5	0.8	0.8	0.1	0.3
Gains on securities	1.1	1.4	1.2	2.5	1.7	0.8	1.0	2.4	1.9	2.3	1.4	1.6	0.2	-0.8
Other financial income	0.3	0.5	0.7	-0.1	-0.2	-0.3	0.1	0.2	0.1	0.2	0.1	0.1	-0.1	-0.1
Service income margin	3.1	2.9	3.2	2.0	2.0	2.4	2.7	3.4	3.8	3.6	3.9	4.1	0.2	0.5
Loan loss provisions	-2.2	-2.5	-3.0	-5.0	-1.3	-0.9	-0.6	-0.6	-0.8	-0.7	-0.8	-1.0	-0.1	-0.3
Operating costs	-6.3	-6.0	-6.4	-4.8	-4.6	-4.6	-5.1	-5.9	-6.3	-6.0	-6.6	-6.8	-0.3	-0.8
Tax charges	-0.4	-0.4	-0.5	-0.4	-0.3	-0.3	-0.4	-0.6	-0.7	-0.7	-0.8	-0.9	-0.1	-0.2
Income tax	-0.5	-0.4	-0.3	-0.2	-0.3	-0.2	-0.2	-0.3	-0.2	-0.3	-0.2	-0.5	-0.3	-0.3
Adjustments to the valuation of government securities ²	0.0	0.0	0.0	0.0	-0.6	0.0	-0.2	-0.1	-0.1	0.0	-0.1	-0.2	0.0	-0.2
Amortization payments for court-ordered releases	0.0	0.0	0.0	0.0	-0.7	-1.0	-1.0	-0.9	-0.9	-1.1	-0.9	-0.4	0.4	0.6
Other	0.5	0.4	0.7	-3.0	1.0	0.7	0.9	1.2	1.0	0.9	1.1	0.5	-0.7	-0.4
Monetary results	0.0	0.0	0.0	-7.5	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
ROA	0.3	0.1	0.2	-11.3	-2.5	-1.0	0.5	2.2	1.6	1.8	1.4	1.8	0.4	0.0
ROA adjusted ³	-	-	-	-	-1.2	0.2	1.6	3.2	2.6	2.8	2.4	2.4	0.0	-0.5
<i>ROE</i>	<i>2.3</i>	<i>0.8</i>	<i>1.4</i>	<i>-79.0</i>	<i>-19.1</i>	<i>-8.1</i>	<i>4.1</i>	<i>15.3</i>	<i>10.9</i>	<i>12.3</i>	<i>9.6</i>	<i>14.2</i>	<i>4.6</i>	<i>1.9</i>

(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 9 | Portfolio Quality

<i>As percentage</i>	Dec 00	Dec 01	Dec 02	Dec 03	Dec 04	Dec 05	Dec 06	Jun 07	Dec 07	Jun 08
Non-performing loans (overall)	8.3	9.9	19.8	15.7	8.9	4.4	2.9	2.8	2.2	2.3
Non-performing loans to the non-financial private sector	9.8	14.0	37.4	30.4	15.3	6.3	3.6	3.2	2.5	2.6
Provisions / Non-performing loans	67.7	75.7	73.4	79.0	97.0	114.3	129.3	130.1	141.3	132.4
(Total non-performing - Provisions) / Overall financing	2.7	2.4	5.3	3.3	0.4	-0.6	-0.9	-0.8	-0.9	-0.7
(Total non-performing - Provisions) / Net worth	13.4	11.4	18.6	11.2	1.3	-2.2	-3.0	-2.9	-3.6	-3.1

(*) 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.

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