MONTHLY REPORT

ECONVIEWS

ECONOMÍA Y FINANZAS

March 2022

Issue #213

THE MONTH AT A GLANCE

RECENT DEVELOPMENTS

- Russia's invasion of Ukraine upended world markets, in a way comparable to the outbreak of the Covid pandemic two years before. The S&P 500 (-5.2%), NASDAQ (-10%) and Euro Stoxx 50 (-9.9%) are all down YTD. Commodity prices moderated after the initial shock, but oil (51.6%), natural gas (44.8%) or wheat (40.9%) and soybeans (28%) are still well above December 31st's levels.
- With US inflation at a 40-year high of 7.9% in February and expected to climb higher in coming months, the Fed hiked its policy rate 25 basis points on March 16th, for the first time in 27 months. Euro Area CPI shot to a new record of 5.8%, but the ECB is sitting tight on rates, although it accelerated the cutback of its pandemic emergency purchase program (PEPP).
- On March 18th the Senate approved the IMF deal. Its "light" targets of a 2.5% primary deficit, USD 5.8 billion reserve accumulation and keeping the RER at Dec-21 levels (a crawling peg in line with 4% monthly inflation) appear less light after the spike in natural gas prices, which puts pressure on subsidies. The politics of the deal are also shaky considering the schism between President Fernández and his VP Cristina Kirchner.
- On March 22nd, the BCRA hiked the Leliq reference rate 200 basis points, from 42.5 to 44.5%, its third increase in the year.

FIGURE OF THE MONTH

February's primary deficit reached

ARS 76 bn

quadrupling the same month in 2021's record and reaching 0.13% of GDP in two months of 2022.

TO BE ALERT

The FOMC dot-plot median projection for the Fed Funds rate was at

1.75-2%.

for December 2022, which entails six more hikes this year.

WHAT'S COMING NEXT?

- The March 16th FOMC's dot-plot showed a startlingly hawkish shift in projections for the Fed Funds rate, with governors betting on seven 25-basis point hikes in 2022 towards a 1.75-2% range. Chairman Powell has weighted the possibility of a 50-basis point hike, which last occurred in the year 2000. The next FOMC is scheduled for May 4th.
- The Treasury faces ARS 1.6 trillion maturities in peso-nominated debt between April and May, including the TV22 dollar-linked bond and several CER-adjusted letters. Indexed debt made up around 80% of the total in the last auctions.
- Minister Guzman is keeping a tight eye on natural gas prices: Argentina will need to import around 25% of total demand this winter, and with a BTU going for USD 30, the dollar needs could rise to USD 4.9 billion across 2022.
- Monthly inflation surprised at 4.7% in February. With another gas hike, school starting and unstable food prices, March's record will likely beat 5%. This rhythm also puts pressure on the BCRA's crawling peg, which is currently at an 43.3% annualized for the official dollar. We believe the windfall from soybeans at USD 625 per ton and the IMF deal will allow the FX rate to close 2022 around ARS 160.3 per dollar, 56% devaluation against 56% inflation.

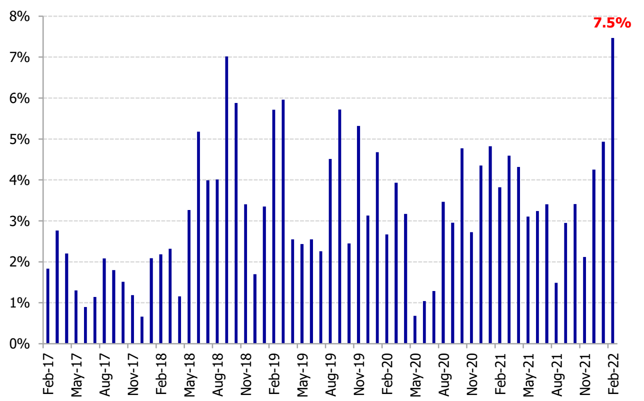
SUMMARY OF MAIN INDICATORS

	Last	Previous		Last	Previous
Economic activity			**Financial data**		
Economic activity (MoM s.a.)	0.9%	1.3%	Inflation (monthly)	4.7%	3.9%
Consumer confidence (MoM)	-1.8%	6.3%	FX spread (21day avg.)	84.7%	103.6%
Industrial activity (MoM s.a.)	-5.5%	1.2%	Country risk (bps 21day avg.)	1,834	1,779
International accounts			**External data**		
Current Account (USD BN)	0.37	3.44	Soybean price (per ton, 21day avg.)	617.3	573.8
CB Reserves (USD BN 21day avg.)	37.15	37.71	Brazilian activity (MoM s.a.)	0.3%	0.5%
Primary balance (ARS BN)	-76.28	-18.76	Financial Conditions Index	20.0	31.7

Source: Econviews base on multiple sources - Based on working days only

GRAPH OF THE MONTH:

Inflation in food and beverages soared in February
Monthly variations



Source: Econviews based on INDEC

RECENT ECONOMIC DEVELOPMENTS

FEB	FEB	MAR	MAR	MAR	MAR	MAR
24th	27th	1st	14th	18th	19th	25th
Econviews Monthly #212: A mild IMF deal that serves a purpose + special analysis on the fintech industry	**Russian banks disconnected from SWIFT**, range of sanctions applied against country, S&P 500 falls 5%.	President Fernández opens 2022 legislative period, says **utility hikes will be in line with wage raises.**	With global oil prices above 120 per barrel, **YPF hikes gas 11.5%**, the year's second after February's 9% increase.	**Senate gives final approval to IMF deal**, vote split 56-13 as Cristina Kirchner's wing opposes the agreement.	Fernández announces **"War against inflation"** to begin, with price controls and Funds for agro goods.	**Econviews Monthly #213**

POLITICS

Alberto Fernández managed to push the IMF deal through both chambers of Congress, but at the cost of nearly breaking the ruling coalition. 28 Deputies and 13 Senators closer to VP Cristina Kirchner voted against the agreement, forcing the Government to lean on the opposition to reach a majority. While the dissident faction led by Cristina and her son Máximo Kirchner has not publicly split with the President, their control over key state agencies such as the Secretary of Energy or the Social Security Administration casts doubt on the ability of achieving IMF targets. The final bill set guidelines for a 2.5% of GDP primary deficit this year, with a significant reduction in energy subsidies and a 1% ceiling for BCRA financing.

PANDEMIC

Argentina recorded its first Covid case on March 3rd, 2020. Two years later, with 90% of population having received at least one shot and 41% already boosted, the final restrictions such as in-school masking or virtual university classes are fading away. After the January Omicron spike, daily cases are back down to 5,000 on average, with deaths below 50 per day, marking the end of the third wave of infections, smaller than the previous two but still significant. With temperatures falling as the autumn season sets in, a slight uptick in cases in the last weeks and warnings about new variants, authorities are advancing with a 4th booster shot for health workers and seniors, but economic and social activity has all but normalized.

ECONOMIC ACTIVITY

The final numbers show GDP grew 10.3% in 2021, a stronger than expected recovery from the pandemic and leaving a 4.1% statistical carryover for 2022. However, January's figures show a weak start for both Industry, which fell 5.5% monthly s.a., and Construction, which slumped 3.9%. Automotive production was hit even worse, sinking 31% against December. Covid-related staff shortages played a significant part and will not affect February's records: for example, the auto industry bounced back 15%. Other setbacks such as import restrictions will still weigh on the recovery. Combined with the fallout from the IMF deal and Ukraine, we expect activity to contract 0.2% in Q1, but maintain our 3.5% growth forecast for the full year.

INFLATION

February's monthly mark was surprisingly high at 4.7%, the worst record since March 2021. This prompted President Fernández to declare a "war on inflation", which watered down to a handful of price controls and funds for agro goods. Food and beverages shot up 7.5%, with strong seasonal effects, followed by transport (4.9%) and home equipment (4.4%). March's figure will likely top 5%, as the Ukraine War's impact on commodity prices, YPF's second gas hike of 2022 (11.5%), and education costs due to the beginning of the school year will all push CPI upwards. April's record could see some oxygen as fruit and vegetable prices moderate. In year-on-year terms inflation hit 52.3%. For now, we hold our 56% forecast for 2022.

MONETARY SECTOR

The BCRA's third hike of the year took the Leliq policy rate up 200 basis points to 44.5%. Interest-bearing liabilities will be the main factor of expansion for the Monetary Base this year, which we estimate at 54.8%. The IMF's monetary program set a 1% limit for Central Bank deficit monetization and a USD 5.8 billion target for reserve accumulation. Dollar inflows will increase during the harvest months of March-June: already, the BCRA bought back USD 439 million in reserves in 23 days of March. This seasonality, plus the rate hikes, are keeping the parallel FX rates in check. The BCS sits at ARS 200.1, an 80.9% spread. Nonetheless, the BCRA will probably need to step up the official FX rate's devaluation from its current 43%

FISCAL ACCOUNTS

Argentina's primary deficit slipped to ARS 76.2 billion in February, four times February 2021's mark. Energy subsidies practically amounted to the month's deficit, at ARS 76.1 billion, with 94% year-on-year growth. The bump in natural gas prices will increase the fiscal cost despite the adjustment in utility rates, which will average 50-60%. This is currently the weakest link in the IMF program. Pensions increased 60.5% to ARS 335 billion. Overall expenditures grew 70% to ARS 922 billion, above revenues which were up 61.5%, at ARS 846 billion. Export taxes made up a tenth of total income and will benefit from the commodity price boom. Our base scenario is that primary deficit will be 2.7% of GDP this year, 0.2% above IMF's target.

I. An IMF program that nobody likes but everybody needs

A Program in search of support

The IMF program was finally approved by Congress, though at a heavy cost for the government because Cristina and the Campora opposed it. Fernández had to rely on the opposition for the approval in Congress, and had a setback regarding the law because the opposition was only willing to vote for the new IMF financing without any mention to the content of the program. This was seen as a defeat for Minister Guzman who was seeking broad support for the program, which he did not get from the opposition, nor from Cristina.

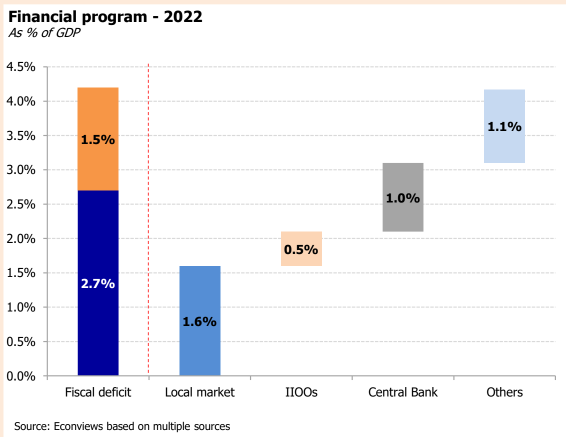
This situation raises key questions regarding what will happen with the government coalition, and about the ability of President Fernandez to maintain governance the rest of his mandate. Everything indicates that Cristina will distance herself from Fernández, though it remains unclear whether she will break with him or if they will manage to work out a new agreement, an initiative that is favored by many Peronist governors and mayors in order to improve their chances to win in the 2023 general elections.

The disagreements within the government and the new more difficult economic environment, which requires austerity and tough policy measures, **indicate that there is a fertile ground for the opposition to win next year's presidential election**. True, many things can happen until then but if the political scenario moves in this direction, markets could well begin to slowly improve during this period and help to stabilize the financial situation.

The IMF program does not remove economic uncertainty

The IMF agreement falls short of the comprehensive program that markets were expecting and that the US Treasury and Fund senior management have been talking all along. One can see the glass half empty, and argue that this is a very weak program, that there will still be large fiscal and external imbalances, that there is little hope that the foreign exchange restrictions will be removed or softened or that inflation will drop. Besides, there are there are no structural reforms whatsoever that generate hopes of a turnaround in economic growth, which at best can be mediocre. And all these arguments are largely true.

However, one can also see the glass half full, especially if the alternative was no agreement and a chaotic scenario. **The program limits the amount of Central Bank financing to the Treasury to 1% of GDP**. It stops short of setting a limit on the growth of money supply, but at least there are some restrictions on monetary policy. It also asks for positive real interest rates which has forced the Central Bank to increase the policy rate by six and a half percentage points since the beginning of the year. Rates are not yet positive in real terms given that inflation has been accelerating, but at least they have gone up.



There are also targets on fiscal policy, with a primary deficit of 2.5% of GDP this year, 1.9% for 2023 reaching balanced accounts by 2025. Again, not very ambitious, but at least in the right direction. Besides, given the increases in energy prices brought about by the war in Ukraine, the target now looks ambitious.

Finally, there is a target for the accumulation of international reserves of at least 5.8 billion dollars for the whole year, which at first glance looks modest, given that the IMF is lending 4.4 billion dollars in new money. However, the target won't be easy to meet for two reasons. First, the Central Bank lost rough 2.6 billion dollars in the first two months of the year, which means that it needs to accumulate roughly 4 billion dollars until the end of the year. Second, this target is difficult to reach while the spread between the official and the parallel exchange rates remains 70% or higher, as we expect. The increase in energy prices could complicate the external accounts, though they seem to be compensated by the rise in metals and agricultural commodities that Argentina exports.

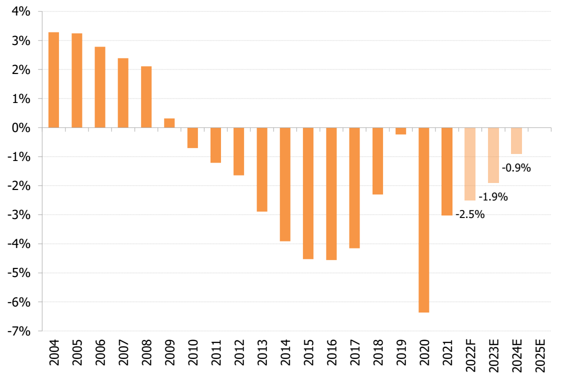
Who is happy with this agreement? Probably nobody. The government is relieved because it avoided a default, but is worried about the prospects of less freedom in policy making, about the impact it had on the coalition, about the debates generated, about the hike in utility rates, and about the possible discussions during the IMF quarterly revisions, which are likely to be tense. The opposition does not like the program either, namely because it does not address in a decisive way the large macro imbalances and many critical economic issues such as inflation, the FX spread, the *cepo* or the energy problems. **It postpones the difficult economic policy decisions for the next administration.**

Less is known about what the IMF thinks, though one can infer some disagreement as the policy measures in the program are extremely light compared to any other programs worldwide. It is uncommon for the IMF to accept controls on the Current Account of the balance of payments, to tolerate a large spread between the official and parallel exchange rates, or not to include meaningful structural reforms. **This is a weak program whichever way one looks at it, and far away from the comprehensive program that the Fund was looking for.**

While this is a "light" program, recent events suggest that it will end up being a demanding one for the government, and that it will not be easy to meet the targets. The war in Ukraine had a big impact on commodity prices, and for Argentina it meant a blessing and a course. The good news that the price of soybeans and of other commodity exports reached high levels and that export revenues will go up. The bad news is that energy imports, especially of LNG, will cost much more as they are likely to increase from 1.1 billion dollars last year to around 5 billion dollars this year. The effect is likely to be small one way or the other on the trade balance, but the impact will be large on the fiscal side. The trade off will be between higher utility rates or larger subsidies, which in either case implies problems for the government.

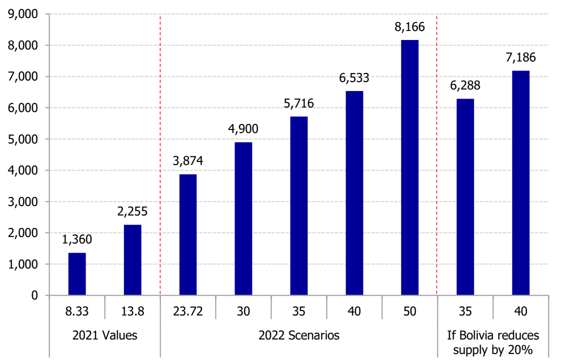
Inflation is the second area of concern, as it reached 4.7% in February, a month when inflation is traditionally low, and it looks that it will be at least 5% in March. These figures indicate that inflation will be well over the 43% annual rate that was used in the IMF program, and that it will also widely exceed the upper bound which was 48%. It now looks that the consensus average, which stands at 55%, is very conservative and that inflation could easily be 60% or even higher.

Primary deficit: IMF agreement goals
As % of GDP



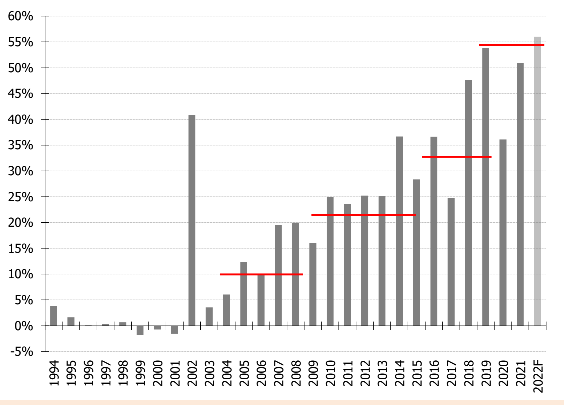
Source: Econviews based on MECON and IMF

Scenarios of USD demand for LNG imports
In million USD (vertical axis) - In USD/MMBTU (horizontal axis)



Source: Econviews based on own estimates

Inflation
Annual variations - End of period



The fiscal deficit is a third challenge. The program aims a primary deficit of 2.5% of GDP compared with 3.1% of GDP last year. The fiscal target looked ambitious but reachable when the agreement was announced in February, but it looks difficult to achieve now after the increase in world of LNG and the strong resistance that there is within the government coalition to raise utility rates. The opposition is opposed to any increase in taxes. The obvious question is whether the government will be willing or able to reduce transfers to the provinces or other expenses, which at the moment looks the only way to address the larger imbalance.

The logic behind the "light" agreement was to design a program that was at least realistic and with targets that could be met, on the idea that this was better than no program at all. Unfortunately, it now looks that even the light program will not be met and that the quarterly reviews will become a replay of the daunting negotiations of the program.

II. Debt Sustainability: it's the liquidity, stupid

Finally, Argentina signed a deal with the IMF, but the agreement has not dispelled the concerns about a new debt restructuring around 2025, when the payments of principal to private bondholders reach 6.9 billion dollars. If Argentina's country risk at time remains in the 1,000 points the country will still would not have access to the international markets and hence would not be able to refinance part of the debt. In that case a restructuring would be all but inevitable.

However, if in 2023 a new government comes in and it puts together a credible macroeconomic program with the support of the IMF and other multilateral organizations it is possible, and even likely, that Argentina can get through without any restructuring.

As we will show in this report**, Argentina does not have a traditional solvency problem, which is typically assess based on the capacity to pay using ratios such as debt to GDP.** Under reasonable assumptions, the debt to GDP ratio can drop to less than 40% of GDP by 2030, a figure that in most circumstances would allow a normal payment of the debt. Though one needs to keep in mind that this is Argentina, where normal circumstances are the exception rather than the rule.

The main problem, besides adopting a strong fiscal path, is to reestablish credibility, especially after the frustrated experience of the Macri administration. **The paradox is that with credibility the debt is sustainable, but without it a restructuring is unavoidable.** In economics this is known as a dual equilibrium, but there is no easy formula to determine how to move from the bad equilibrium to the good one.

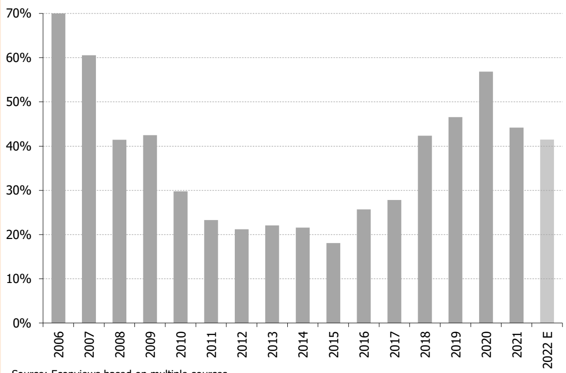
On the positive side, even if Argentina eventually needs to restructure the debt because the financial conditions remain adverse, it can probably do it without haircuts and even offering much better financial conditions to the bondholders.

It seems clear that, in the near future, Argentina will not have access to the international financial markets. For most of the new financing, even to pay for external debt, the government will have to raise funds in the domestic market in pesos. **This seems the right strategy because it would allow Argentina to avoid the dependence on the external markets and hence reduce vulnerability.**

Our estimates indicate that by 2030 most of the new debt will be in pesos even with access to international markets, though the debt stock in dollars would remain higher. Given our history of high inflation and the uncertainty about the evolution of interest rates, **it seems reasonable that the capital markets should develop using indexed bonds**. This was the way countries like Brazil, Chile and Colombia among others did it.

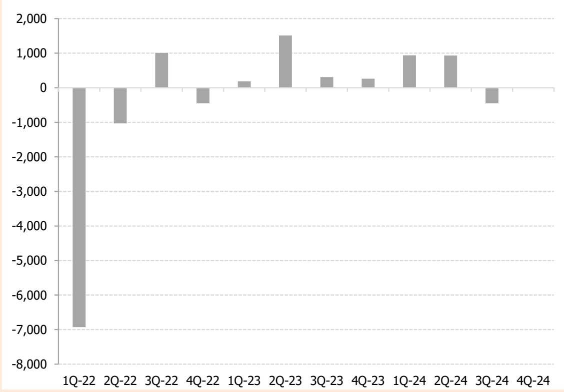
It is thus surprising that the IMF raises questions about the benefits of indexed instruments, especially because the alternatives look much worse. Using bonds at fixed rates is non-viable, while relying on floating rate instruments run the risk of limiting the ability of the Central Bank to use tight money to fight inflation.

Net Public Debt
As % of GDP - Net debt excludes intra-public sector debt; includes warrants



Source: Econviews based on multiple sources

Maturities after the agreement: disbursements are higher in 2022
Original maturities net of disbursements, USD million at 1 SDR = 1.39 USD



One final point is that the government has been in the comfort zone issuing peso denominated debt, because those bonds have found very good reception. However, on must keep in mind that there is a *cepo* in place, there is a large stock of pesos, firms have more pesos than they want (because they cannot pay dividends or some imports) and hence **those pesos have few options where to go**. If the *cepo* were removed from one day to other, there could be a stampede and interest rates could skyrocket. The implication is that the *cepo* may stay longer than the new administration would like. The length of the transition will be dictated by the financial conditions, especially the reduction in the FX spread.

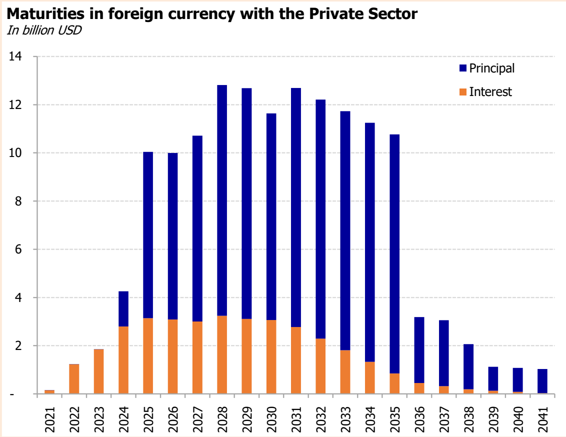
I. Assessing the debt sustainability

To assess the sustainability of the debt, there are two things to consider: **whether Argentina is solvent, and whether Argentina has enough liquidity to face its debt maturities.**

In this section we propose a Debt Sustainability Analysis (DSA) to assess the evolution of the Net Debt relative to GDP until 2030. We define Net Debt as the Gross Debt minus all debt held by agencies of the government; that is, discounting loans between different branches of the Public Sector such as those that arose from the nationalization of AFJPs or transfers from the Central Bank, or eventually using pockets of liquidity in some State agencies.

In 2019, net debt reached 46.6% of GDP. With the collapse in GDP due to the pandemic and the quarantine in 2020, this ratio shot up to 56.9% (53.3% excluding warrants), but in 2021 it fell to 44.2% despite higher indebtedness. This was due to three factors: the USD 5.1 billion in payments to the IMF during 2021, economic recovery, and appreciation of the real exchange rate.

For 2022, we project that the ratio will fall to 41.5%, even though the IMF will be returning the amount paid during the past year: exchange appreciation weighs more. These figures are not at all "high" for countries that generate confidence and can rollover their maturities. And yet, the market is betting that Argentina will default its creditors in the next 4 years with a high probability. **Credibility is the issue.** In 2025, maturities with the market amount to 10 billion dollars between interest and capital in bonds. With the IMF and multilaterals practically all used up, Argentina must regain access to the markets. For that, it will be necessary to shift towards a more pro-market rhetoric, to have the deficit under control and to have recomposed BCRA reserves, which will ultimately reduce Argentina's risk premium.



The evolution of the debt is strongly dependent on a number of assumptions. First, the evolution of global inflation, particularly in the USA, and interest rates will affect the ratio of debt to GDP measured in USD in two ways: a stronger peso (real appreciation) caused by a weaker dollar will reduce the burden of the debt, while higher international rates will increase the burden of interests and thus the debt ratio too.

On a local level, economic growth and the fiscal path will be determinant for the evolution of the debt, but the exchange rate evolution will affect the ratio too. **In the simplest terms, for a given real interest rate, the rate of economic growth must be larger for the debt ratio to fall in time**. If they are equal, then only a primary surplus can decrease the net debt to GDP ratio.

With this in mind, we have created three scenarios with different projections for the relevant variables.

Macroeconomic Asumptions

Variation avg. y/y, % of GDP and in basis points

IMF	GDP	Inflation	FX	CPI USA	Primary Balance	EMBI
2022	3.5%	51.7%	34.1%	7.7%	-2.5%	1,800
2023	3.0%	45.9%	49.0%	6.2%	-1.9%	1,500
2024	3.0%	36.8%	35.0%	5.4%	-0.9%	1,000
2025	3.0%	31.5%	28.0%	3.0%	0.0%	700
2026	3.0%	25.0%	21.0%	3.0%	0.5%	600
2027	3.0%	20.0%	16.0%	3.0%	0.5%	500
2028	3.0%	15.0%	11.0%	3.0%	0.5%	400
2029	3.0%	15.0%	12.0%	3.0%	0.5%	400
2030	3.0%	12.5%	9.0%	3.0%	0.5%	400

Negative	GDP	Inflation	FX	CPI USA	Primary Balance	EMBI
2022	2.0%	61.7%	54.1%	7.7%	-2.7%	1,800
2023	1.5%	55.9%	59.0%	6.2%	-2.0%	1,700
2024	1.5%	46.8%	45.0%	5.4%	-2.0%	1,300
2025	1.5%	41.5%	38.0%	3.0%	-1.0%	1,000
2026	1.5%	35.0%	31.0%	3.0%	-1.0%	900
2027	1.5%	30.0%	26.0%	3.0%	-1.0%	800
2028	1.5%	25.0%	25.0%	3.0%	-1.0%	800
2029	1.5%	25.0%	25.0%	3.0%	-1.0%	800
2030	1.5%	22.5%	19.0%	3.0%	-1.0%	800

Positive	GDP	Inflation	FX	CPI USA	Primary Balance	EMBI
2022	4.0%	41.7%	24.1%	7.7%	-2.5%	1,700
2023	3.5%	35.9%	30.0%	6.2%	-1.0%	1,400
2024	3.5%	26.8%	25.0%	5.4%	0.0%	700
2025	3.5%	21.5%	20.0%	3.0%	0.5%	500
2026	3.5%	15.0%	13.0%	3.0%	1.0%	450
2027	3.5%	10.0%	6.5%	3.0%	1.0%	400
2028	3.5%	5.0%	2.0%	3.0%	1.0%	300
2029	3.5%	5.0%	2.0%	3.0%	1.0%	300
2030	3.5%	5.0%	2.0%	3.0%	1.0%	300

Source: Econviews

Under the former assumptions, the net debt to GDP ratio follows the path that is shown below. On the IMF scenario, the net debt stabilizes in 2024 at a higher level than the current one (but presents important challenges). On the negative scenario, it becomes explosive. On a positive scenario, the debt becomes sustainable and falls as share of GDP over time. Let's take a closer look.

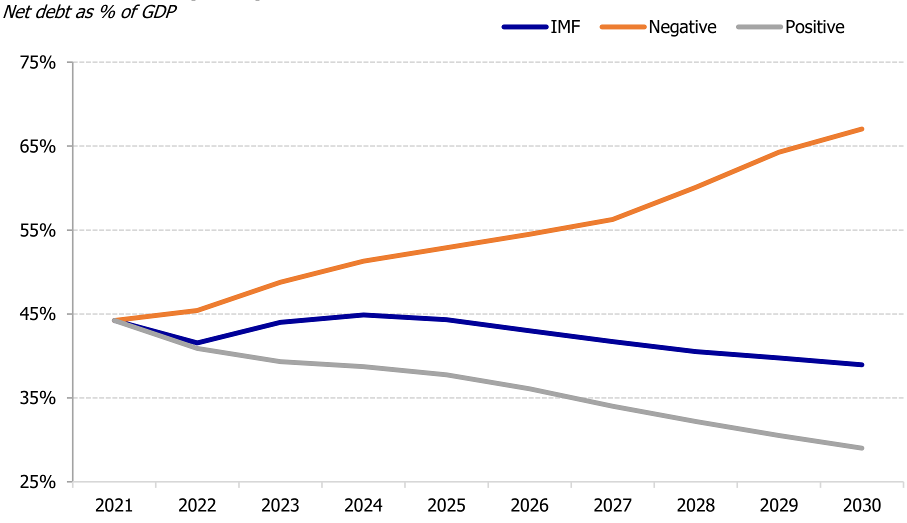
Net debt path

As % of GDP

	IMF	Negative	Positive
2021	44.2%	44.2%	44.2%
2022	41.5%	45.4%	40.9%
2023	44.0%	48.8%	39.3%
2024	44.9%	51.3%	38.7%
2025	44.3%	52.9%	37.7%
2026	43.0%	54.5%	36.1%
2027	41.7%	56.3%	34.0%
2028	40.5%	60.1%	32.2%
2029	39.8%	64.3%	30.5%
2030	38.9%	67.0%	29.0%

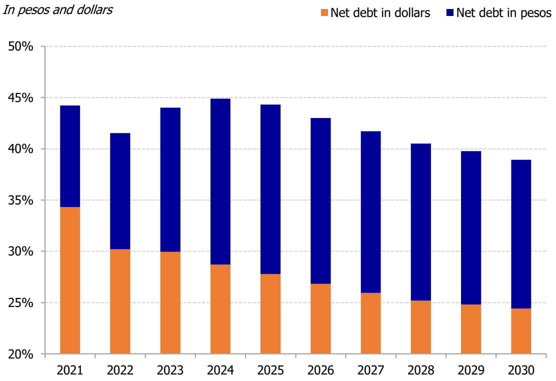
Source: Econviews

Debt sustainability analysis
Net debt as % of GDP



Source: Econviews

Net debt to GDP
In pesos and dollars



Source: Econviews

Scenario N° 1

Let's start with the first scenario, which proposes the fiscal path of the agreement with the IMF until 2025 and a primary surplus of 0.5% of GDP since 2026. An important feature of this scenario is that it assumes a GDP growth of 3.5% in 2022 and of 3% onwards, which is clearly optimistic.

We assume that the total debt is financed locally until 2024 and international capital markets are open to Argentina since 2025, allowing for a rollover of the heavy maturities in dollars that start on that year.

Debt in dollars will rise in 2022 due to new financing from the IMF and other international organizations but will nevertheless fall as % of GDP **due to appreciation of the exchange rate vs the average of 2021.** A 34% average variation of the FX rate in 2022 is consistent with a 56% variation measured from Dec-21 to Dec-22. Under this scenario, debt in dollars would continue to fall and then stabilize measured against GDP once access to international markets is regained. By then, **there would be no primary deficit.**

In 2023, important challenges arise. The growing burden of the inflation-adjusted debt is coupled with higher real interest rates: **if capital controls (*cepo*) are to be lifted, the real interest rate must rise on CER bonds, probably to around 4%. Lower interest rates would not allow for a rollover of maturities and investors would dollarize their debt holdings.**

This is an important issue, because with international markets closed, all existing and new debt must be financed locally. Under these circumstances, financial needs rise by 2.2% of GDP in 2023, after excluding assistance from the Central Bank of 0.6% of GDP in accordance with the agreement with the IMF.

In this scenario, **net debt in pesos rises from the current estimate of 10% of GDP to 16.5% in 2025** and would stabilize below that level in the following years provided a primary surplus is reached from 2026 onwards.

Net debt path: Scenario 1

As % of GDP

	Net debt in pesos	Net debt in dollars	Net debt
2021	9.9%	34.3%	44.2%
2022	11.3%	30.2%	41.5%
2023	14.1%	30.0%	44.0%
2024	16.2%	28.7%	44.9%
2025	16.5%	27.8%	44.3%
2026	16.2%	26.8%	43.0%
2027	15.8%	25.9%	41.7%
2028	15.3%	25.2%	40.5%
2029	15.0%	24.8%	39.8%
2030	14.5%	24.4%	38.9%

As for net debt in dollars, **the ratio to GDP would drop by 10 percentage points from a current estimate of 34.3% by 2030.**

Under these assumption Argentina would not face a solvency problem, as the debt to GDP ratio would reach 45% in 2025 and drop and progressively drop to 38.9% in 2030, but there might still be challenges to service the debt due high principal payments. In any case, a complete lift of the *cepo* in 2023 is not in cards, and it could remain through 2024. Under these circumstances, it becomes clear that Argentina needs to speed up its reduction of the primary deficit.

<u>Scenario N° 2</u>

Under scenario 2, GDP grows at a slower pace, there is a persistent deficit and inflation remains high, and as a result a higher exchange rate is needed. Under this scenario, Argentina cannot get back to international capital markets due to extremely high interest rates.

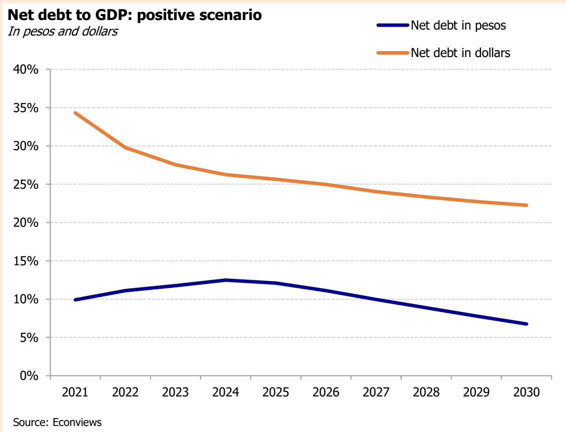
The debt to GDP ratio becomes explosive and it keeps growing in time. A higher real exchange rate is needed and the size of net debt in dollars does not substantially shrink over time. Higher inflation leads to higher interest rates domestically. Financing such debt locally would not be possible given the size of the market, **and a new restructuring would be needed.**

The main takeaway of this theoretic exercise is that Argentina cannot continue with primary deficits in the coming years.

Net debt path: Scenario 2

As % of GDP

	Net debt in pesos	Net debt in dollars	Net debt
2021	9.9%	34.3%	44.2%
2022	12.5%	33.0%	45.4%
2023	15.7%	33.1%	48.8%
2024	19.0%	32.2%	51.3%
2025	21.1%	31.7%	52.9%
2026	23.3%	31.2%	54.5%
2027	25.5%	30.8%	56.3%
2028	28.5%	31.6%	60.1%
2029	31.6%	32.7%	64.3%
2030	33.9%	33.1%	67.0%



<u>Scenario N° 3</u>

Under scenario 3, the primary deficit is reduced faster than the on the first scenario and there is primary surplus since 2025 of 0.5% of GDP and of 1% onwards. This optimistic scenario also assumes higher growth, lower inflation and a relative appreciation of the exchange rate compared to scenario 1. Country risk falls faster, and financing abroad becomes cheaper.

While there are still challenges in terms of financing of the local debt before the access to international markets, the burden of the debt is lower and the **extra financing needed for 2023 halves compared to scenario 1.**

The mix of lower deficit, lower interest rates coupled with higher GDP growth and a lower real exchange rate allows the net debt to fall to nearly 29% of GDP in 2030.

Debt in dollars would progressively fall as % of GPD owing to high growth, a lower real exchange rate and reduced country risk. Most importantly, despite a growing financing in the local market in pesos, **the continued primary surplus would also lead to a drop of net debt in pesos to nearly 7% of GDP.**

This theoretical exercise indicates that Argentina does not face a solvency problem, provided the fiscal deficit is reduced in coming years. But it raises serious concerns regarding the liquidity needs under no

Net debt path: Scenario 3

As % of GDP

	Net debt in pesos	Net debt in dollars	Net debt
2021	9.9%	34.3%	44.2%
2022	11.1%	29.8%	40.9%
2023	11.8%	27.5%	39.3%
2024	12.5%	26.2%	38.7%
2025	12.1%	25.6%	37.7%
2026	11.1%	25.0%	36.1%
2027	10.0%	24.0%	34.0%
2028	8.9%	23.3%	32.2%
2029	7.8%	22.7%	30.5%
2030	6.8%	22.3%	29.0%

access to international capital markets. Furthermore, it shows that growth is essential for the sustainability of the debt.**

A combination of primary surplus, decent economic growth and lower inflation are the key ingredients to the sustainability of the debt in the long term. Achieving them is no easy task though, and in the short run can be unfeasible: a stabilization plan that reduces inflation and the fiscal deficit would probably mean a contraction of activity in the short run. There are no easy choices, **but Argentina needs an economic plan to tackle its multiple macroeconomic imbalances.**

II. Liquidity is the main issue

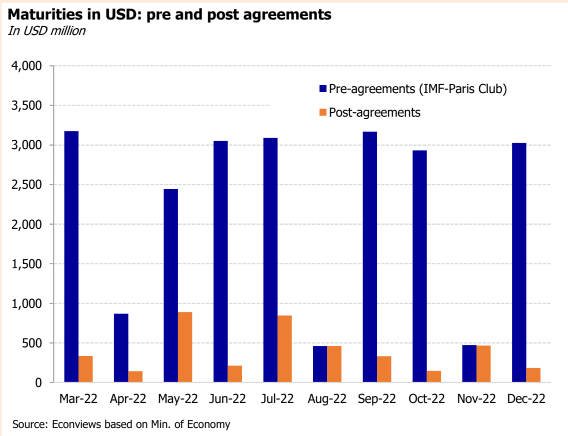
Dollar-denominated debt

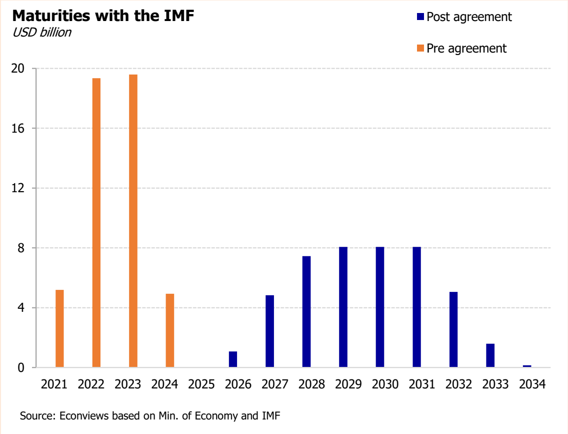
The 2022 landscape changed completely after the IMF agreement. In addition to capital maturities with the IMF, this year maturities with the Paris club also had to be faced. The agreement with the IMF was a necessary condition for the corresponding restructuring with this organization. **The government announced that the USD 2 billion maturity will be postponed for two and a half years**, but conditions will continue to be negotiated until next June.

Between interest on public securities, plus the maturities of capital and interest on loans from international organizations, from March to the end of the year, **Argentina had to face payments of USD 22.7 billion dollars - a figure higher than the trade surplus estimated for this year.** But the agreement with the Fund and the Paris Club will allow the country to avoid large capital maturities with these two organizations, and after March maturities add up to only USD 4 billion, including interest payments to bondholders and capital and interest to other multilateral organizations (IDB, BIRF, etc.)

Under the new agreement, and provided quarterly goals are met (though there might be waivers), the IMF will make quarterly disbursements until 2024 to cover the pre-agreement maturities, and each disbursement will be repaid in a period of 10 years with a 4.5-year grace period, with payments until 2032. That is, each disbursement will be repaid -after 4.5 years- in a period of 5.5 years. Assuming that payments are made uniformly over this period, the maturity profile is stretched through a longer period and is not as concentrated. But could be challenging regardless. **From 2028 to 2031, Argentina faces maturities with the IMF of around 8 billion per annum.**

But the challenge begins before, in 2025. Having restructured almost 68 billion dollars with private bondholders in 2020, the maturity profile for the rest of the Fernández administration cleared up. In 2024 the first principal maturities begin, which together with interest maturities add up to some USD 4.3 billion. **But in 2025 total maturities with the creditors of restructured bonds add up to about USD 10 billion**, and until 2035 even larger maturities will have to be faced each year. The market is already assigning 2025 a high probability of default. **And in 2028 the situation becomes much more complicated: extremely high maturities with private bondholders and the IMF combine to exceed 20 billion dollars.**

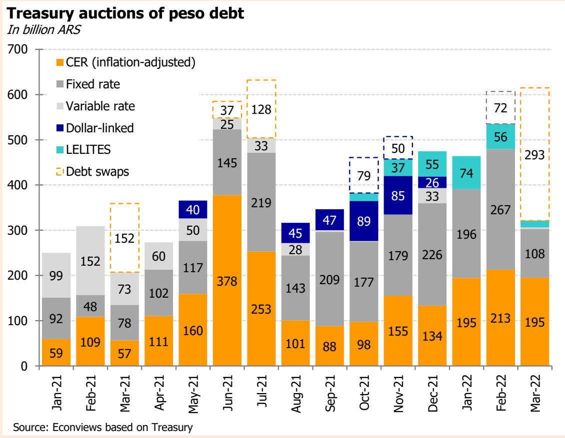




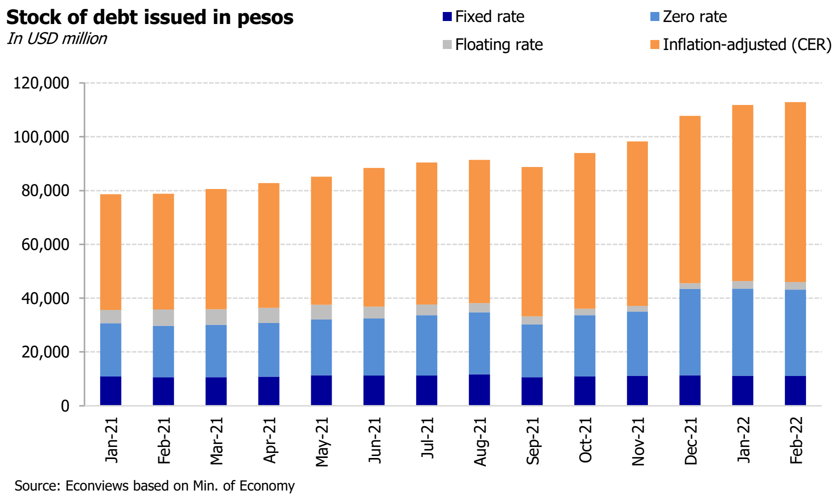
Under these circumstances, it becomes clear that regaining access to international markets in 2025 will be key to avoiding a new restructuring. Without generating credibility, the battle will be lost before it starts.

Peso-denominated debt

Aside from the bonds issued during the debt restructuring of 2020, the Fernandez administration has not issued fresh dollar debt**. In order to make peso-nominated debt more attractive, it has relied on CER (inflation-adjusted) and dollar-linked instruments**. **CER securities made up 50% of 2020's new debt and 38% of last year's.** Dollar-linked bonds made their debut in October 2020 to contain a run against the Peso and represent 7% of debt issued since 2019.

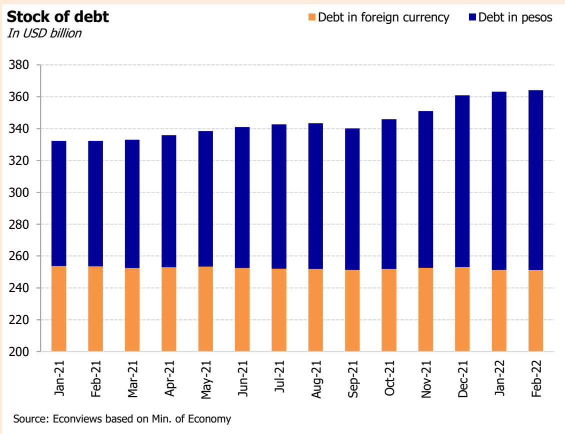


The recent evolution of inflation-adjusted debt has been remarkable. While in December 2019 it represented 34% of the total stock of debt issued in pesos, a year later it amounted to 53% and as of last February, the stock of CER bonds makes up more than 59% of the peso-denominated debt stock.



Indexed peso debt is growing: why that is not bad news

Some concerns have been raised regarding the growing size of indexed debt, as it cannot be diluted with inflation. **But the growth of this stock is hedged with the growth of fiscal revenues derived from inflation**. And thus, we believe that issuing indexed debt can help develop the local capital market. As we have shown in the DSA section of this report, **putting fiscal accounts in order and achieving decent growth would reduce the burden of peso-debt even if all of it becomes indexed.**



As almost no new debt has been issued in dollars, the stock of peso-denominated debt has been constantly growing and as the Treasury will reduce its assistance from the Central Bank, this trend will continue in the future. In January 2021, the stock of peso-debt represented less than 24% of total gross debt under normal payment situation, slightly above than a year before. But as of last month, **debt issued in peso now represents 31% of total Gross Debt. We estimate that peso debt will represent nearly 28% of total Net Debt in 2022.**

And as we have shown, even after access to international capital markets is regained, debt peso is likely to continue growing in size and proportion: we estimate that by 2030 nearly 40% of the net debt will be denominated in pesos.

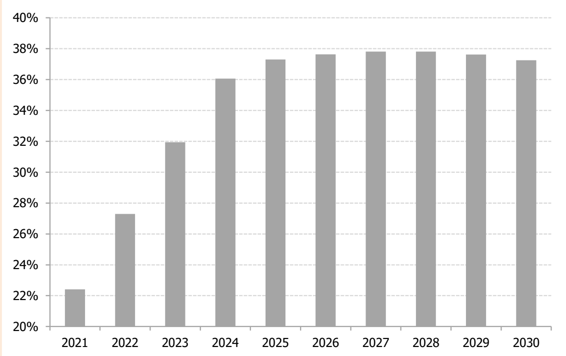
Across 2021, the Treasury raised ARS 4.4 trillion, 1.7 trillion in CER instruments and 1.74 trillion in Discount bills and other fixed rate bonds.

Most peso debt is short-term, with an average duration of 187 days upon issuance in 2021. For Treasury discount bills, this figure slipped from 161 to 139 days over the last year, while APR climbed 10 points to 47.4% in the latest auctions. However, in a recent swap for CER bonds, investment funds showed interest in inflation-adjusted debt with maturities in 2026/28, clearing over ARS 293 billion which were set to expire on March 18th. A few days later, the Treasury brought in ARS 266 billion in CER titles with an average 300-day duration.

Inflation adjusted instruments have helped to extend maturities. As liquidity needs pile up, it is important that the government issues new debt with longer duration. In Q1-2022, the Government has issued ARS 1.3 trillion, 45% in CER instruments, 43% in fixed rate bills and the rest through Lelites and one new variable rate bill. **April and May's auctions will be demanding, as ARS 1.7 trillion mature over those two months**, including ARS 206 billion from a CER letter and ARS 218 billion from a dollar-linked bond which may be swapped. The maturity calendar for the rest of the year is neater, with ARS 2.5 trillion expiring in the second half of 2022. 40% of that, or 1 trillion, only in September, mainly from the T2X2 CER bond.

What is the future of the new debt in pesos? Inflation-adjusted instruments with a longer duration will likely grow in size as well as dollar-linked bonds that allow investors to hedge against inflation and a devaluation. But short-term discount bills have beaten indexed instruments in the last few months as their yields are positive in real terms. Real interest rates and short durations can mean liquidity challenges, and a better strategy for future debt issuing would be indexed debt plus a higher rate but with a longer duration.

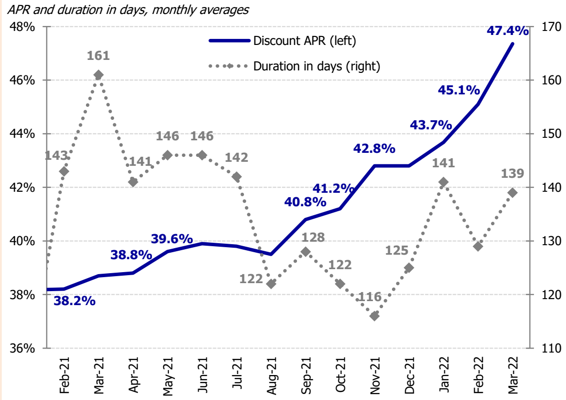
Net peso debt as % of total net debt



Source: Econviews

Discount bills

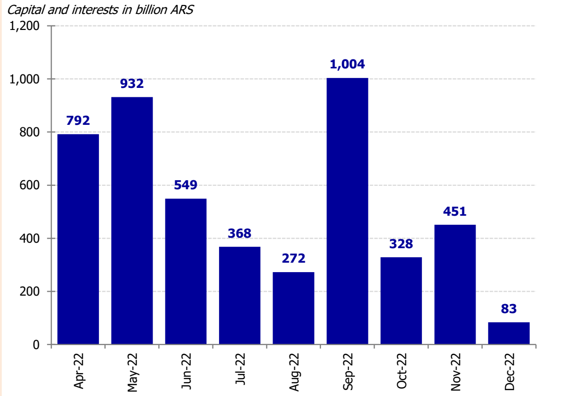
APR and duration in days, monthly averages



Source: Econviews based on Treasury

Maturities in ARS

Capital and interests in billion ARS



Source: Econviews based on OPC

Base Scenario

	2019	2020	2021 F	2022 F	2023 F
Inflation (eop)	53.8%	36.1%	50.9%	56.0%	41.0%
Inflation (aop)	53.5%	42.0%	48.4%	53.5%	46.9%
Exchange rate ARS/USD (eop)	59.90	84.15	102.75	160.31	221.34
Real exchange rate ARS/USD (eop, Dec-01=100)	150.8	158.3	137.1	146.6	151.5
Paralell exchange rate ARS/USD (eop)	74.6	140.3	203.1	272.5	343.1
Spread with official exchange rate (eop)	24.6%	66.8%	97.7%	70.0%	55.0%
Gross reserves (USD billion, eop)	44.8	39.4	39.5	45.5	48.5
Policy rate (eop)	55.0%	38.0%	38.0%	44.5%	38.0%
GDP (YoY)	-2.0%	-9.9%	10.3%	3.5%	3.0%
Formal wages in real terms (aop, YoY)	-5.6%	-2.0%	0.4%	-2.5%	0.0%
Primary surplus (% GDP)	-0.4%	-6.5%	-3.0%	-2.7%	-2.0%
EMBI Argentina (spread in bps, eop)	1744	1368	1703	1100	900
Public net debt (% GDP)	43.6%	53.3%	44.2%	41.5%	44.0%
Current account (% GDP)	-0.8%	0.9%	0.7%	0.6%	0.5%

Source: EconViews

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