MONTHLY REPORT

ECONVIEWS
ECONOMÍA Y FINANZAS

February 2023
Issue #224

THE MONTH AT A GLANCE

RECENT DEVELOPMENTS

- US inflation accelerated to 0.5% monthly in January leaving the year-on-year variation at 6.4%. Together with an unexpectedly strong jobs reports (+517,000 nonfarm payrolls) and 2.3% monthly growth in retail sales, the economy is far from cooling down. The Federal Reserve hiked its policy rate 25 bps to 4.50-4.75% on February 1st, and the S&P 500 has fallen 3.5% since.
- Argentina's GDP grew 5.2% in 2022. A 1.0% monthly fall in December leaves a -1.4% statistical carryover for 2023.
- Argentine monthly inflation leapt from 5.1% in December to 6% in January and reached a new high of 98.8% year-on-year. For now, the Central Bank has kept its Leliq policy rate at 75%.
- The Argentine debt rally cut short in mid-January, with dollar bonds falling 3.1% since then. Country risk went from a low of 1,815 bps to 2,070 bps. Yields on 2023 CER-indexed bonds have been highly unstable. Stocks also lost wind and the Merval index slumped 3.2% over the last month.
- Despite squabbles between Government and opposition on a possible local debt restructuring in 2024, the Treasury obtained ARS 401.7 bn in the last auction, with maturities for ARS 294.4. As a result all money raised in the next auction will be practically all net financing.

FIGURE OF THE MONTH

Argentine dollar bonds slumped

3.1%

since the Government announced its USD 1 billion debt buyback on January 18th.

TO BE ALERT

After losing USD 192 million in January, the Central Bank sold another

913mn

in the first15 working days of February.

WHAT'S COMING NEXT?

- Markets are starting to buy into the Fed's hawkish speak, with futures now pricing three more 25 bps hikes to a 5.25-5.50% terminal rate in June, with cuts to 5-5.25% by December. Only a month ago, the consensus was that the Fed would stop at 5%.
- Monthly inflation is likely to come around 5.8% in February and the year-on-year variation will surpass 100% for the first time since the 90s. We think it will remain at this level until December, as the comparison base from 2022 for upcoming months is 6% on average.
- Despite increased rainfall in the second half of January, the drought situation is still critical. The Buenos Aires trade board forecast a 23% fall in output, leading to USD 10 billion in export losses and 0.4% of GDP less in direct revenues for the Treasury. In a stress scenario with lighter rains, the losses could amount to USD 14 billion.
- To address the shortage of dollars, the Central Bank sped up the official FX rate's depreciation from 5.2 to 5.8% monthly, or from 85 to 100% annualizing the last 5 days. We believe it will implement a new round of the "soybean dollar" to seduce exporters.
- A lack of dollars may also lead the BCRA to up import controls. This will hurt manufacturing, which already slumped 1.2% in December, as food products make up 24% of INDEC's index, and also spillover to transport.

SUMMARY OF MAIN INDICATORS

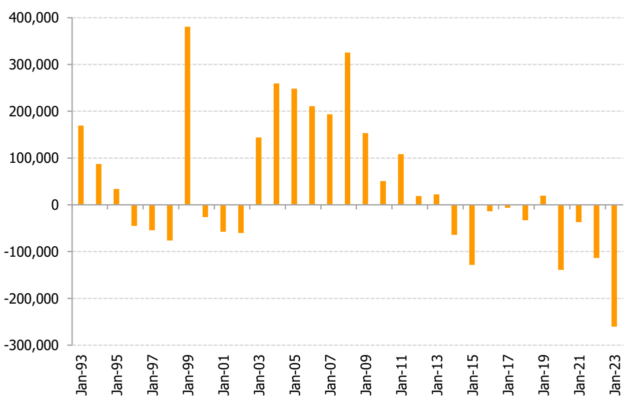
	Last	Previous		Last	Previous
Economic activity			**Financial data**		
Economic activity (MoM s.a.)	-1.0%	-0.7%	Inflation (monthly)	6.0%	5.1%
Consumer confidence (MoM)	-6.1%	7.3%	FX spread (21day avg.)	94.2%	92.2%
Industrial activity (MoM s.a.)	-1.2%	0.4%	Country risk (bps 21day avg.)	1,927	2,061
International accounts			**External data**		
Current Account (USD BN)	-3.03	-0.83	Soybean price (per ton, 21day avg.)	560.8	552.0
CB Reserves (USD BN 21day avg.)	41.32	43.40	Brazilian activity (MoM s.a.)	0.3%	-0.8%
Primary balance (ARS BN)	-203.94	-502.13	Financial Conditions Index	16.5	-2.4

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

GRAPH OF THE MONTH:

January's primary deficit was record

*ARS billions at Jan-23 prices, net of all property rents**



*All property rents are excluded due to historical measurement differences. Even when including them, Jan-23's deficit remains the highest in at least three decades.
Source: Econviews based on Min. of Economy and INDEC

RECENT ECONOMIC DEVELOPMENTS

JAN	JAN	FEB	FEB	FEB	FEB	FEB
26th	31st	1st	6th	14th	16th	23rd
Econviews Monthly #223: similarities and differences between 2015 and 2023 and a sectorial view of the year.	Without favorable effect from soybean dollar, **Central Bank ends January with net sales of USD 192 million**.	**IMF accuses USD 1 billion debt buyback of jeopardizing FX reserves** but will not address issue in its EFF review.	Government announces **10% discounts on selected meat cuts**, after wholesale price increases 30% in February.	**January's CPI print comes in at 6% monthly**, putting a reality check on Minister Massa's presidential dreams.	At ruling coalition meeting, **Pres. Fernández does not rule out re-election bid** despite poor public image.	Econviews Monthly #224

POLITICS

Bitter infighting between President Fernández and Interior Minister De Pedro, a possible candidate in the 2023 presidential, led the ruling coalition to establish a "political roundtable" to organize the campaign. For now, VP Cristina Kirchner sticks to her narrative that she is banned by the Supreme Court and will not run. Minister Massa's chances also look slimmer after January's hot CPI print. Fernández wants to go for re-election but he is very unpopular. Former VP Scioli is another possible name. Tensions are also rising on the opposition side as the August primaries draw nearer. Mayor of BA Larreta and former Security Minister Bullrich are sure to run, with former President Macri's role in the elections still a mystery.

IMF

Argentina is on track to miss the targets set for the first quarter of 2023. The stock of net reserves, under the IMF methodology, should reach USD 7.83 billion by the end of March, but now stands at barely USD 2.55 bn. The difference of 5.27 bn will be partly offset by the IMF net disbursements in March (some 1.89 bn), so there are now left 26 rounds to gather USD 3.86 bn, an almost impossible task even with another soybean-dollar scheme. The fiscal target also looks challenging, as the first month of the year -with seasonality in favor- amounted to more than half of the primary target of 441.5 billion pesos. A waiver and/or a request to adjust the goals now seem very likely.

ECONOMIC ACTIVITY

Activity slumped for a fourth straight month in December (-1.0%) and posted the first fall in the year-on-year comparison (-1.2%) since February 2021. Additionally, the series were revised downwards throughout 2022 and the year closed with an average growth of 5.2%, barely 0.1 p.p. above the statistical carryover left by 2021. Now the statistical carryover is negative (-1.4%) and the coming months are bound to take the hit from the drought, which will not only affect agricultural production, but also transport and linked industries. As consumption decelerates due to falling real incomes and the lack of dollars will limit industrial output, we have revised our GDP growth forecast for 2023 down to -1.0%.

INFLATION

Inflation in January accelerated to 6.03% after averaging 5% in the two previous months, while core inflation increased slightly to 5.35%. The acceleration was driven in part by some postponed and other scheduled adjustments in regulated prices, particularly in utility rates and telecommunications. Food inflation also went up to 6.8% from 4.7% in December, despite the relaunch of the "Fair Prices" program. The acceleration was driven in part by strong increases in seasonal fruits and vegetables, but it was rather widespread. As a result of high inertia, new increases in regulated items and the impact of the rise in wholesale beef prices, February's inflation is likely to have a floor of 5.8% m/m and surpass 100% y/y.

MONETARY SECTOR

Up to February 22nd, the Central Bank has accumulated sales of reserves of USD 1.11 billion, the worst start for a year since at least the beginning of the century, as the advancement of proceeds due to the soybean dollar scheme in December and the impact of the drought strongly reduced the supply of foreign currency. In response, the BCRA accelerated the crawling peg to over 100% annualized, or 6% monthly and we expect it to remain in line with inflation in coming months as there is no room to use the FX rate as an anchor for inflation. In the last auction, the effective rate of the short-term discount bill reached 118%, as the maturities in pesos become more challenging as we approach the elections.

FISCAL ACCOUNTS

Fiscal accounts posted the highest primary deficit at today's prices for the month of January since the start of the fiscal statistics in 1993, adjusting for the current methodology. Primary expenditures rose 6.2% YoY in real terms, driven by economic subsidies (17.5% YoY real) that had been stepped on in December to meet the fiscal target, and capital expenditures that rose 26.5% in real terms. Total revenues shrank 3.2% YoY in real terms, affected by a sharp drop in export duties (-29% YoY real) due to the advancement of proceeds in December, while revenues from the import tax fell 17.6%, resulting from restrictions to import and lower activity levels. We expect the primary deficit to reach 2.5% of GDP this year.

I. Politics and economics: the two-way highway

Is it the economy? Is it politics? The chicken or the egg? This is the question today in Argentina, where there is a debate regarding which is the biggest obstacle to turn around an economy that has been stagnating for more than a decade. Obviously, a switch towards better economic policies is necessary, but the key question is whether the main obstacle is reaching a good diagnosis of the situation, designing a comprehensive program or if the issue is that implementation requires a political leadership and vision until now elusive.

So far, it seems that in the Argentine economy there is an excess of diagnosis, and by and large there is agreement on what to do. There are still differences regarding the sequencing of policies (such as if structural reforms or stabilization policies should come first), about the speed (the old debate between shock or gradualism) and about the depth of the policy measures (i.e., how much to advance on labor market reforms, or on the pension system or on fiscal adjustment). But differences are within reasonable bounds.

The debate is shifting towards whether the next government will have the ability to implement the necessary policies. A devaluation or sharp increases in utility rates will certainly be unpopular and could generate resistance, protests and even some street violence as occurred during the 2001 crisis. The adjustment of the fiscal deficit will require reducing or eliminating many privileges and there are lobbies prepared to resist these changes. In sum, the problem is not only a debate over shock or gradualism, or on sequencing. An important piece of the coming puzzle is how to get political support for policies that in the past were difficult to implement, and how to assure their sustainability and avoid a reversal at a later state, as it happened several times in the past.

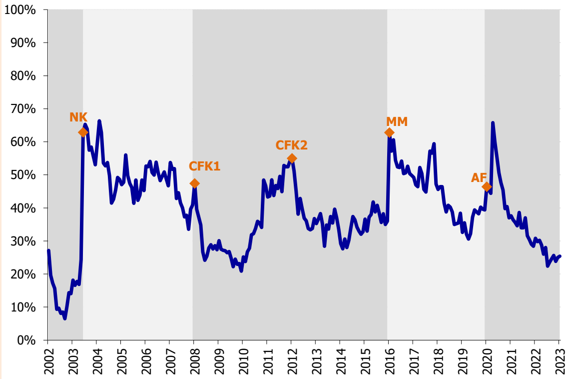
On both sides of the political spectrum there are hawks and doves. The discussion around the implementation of policies is whether a winner in the general election can implement them using the clout that comes naturally from winning an election, or if instead he or she should work with some members of the opposition in Congress in order to reach broader support for the program. This is perhaps the main difference between Patricia Bullrich and Horacio Rodriguez Larreta, the main opposition figures, and between the Kirchnerist/Cámpora wing and the more moderate candidates in the Peronist party.

It is difficult to know in advance which approach will work better to implement and maintain an economic program, though it is clear that leadership will be critical, the broader the support the better, and that the honeymoon period will be short.

Recent economic developments

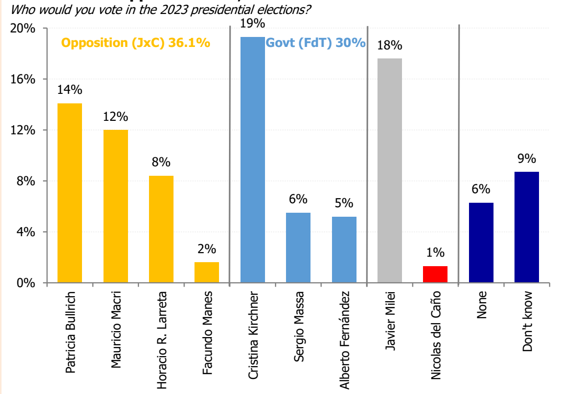
Reserves, inflation, the exchange rate and domestic debt are already setting the economic climate for the election year and could determine Sergio Massa's decision to run for president or not.

Confidence in the Government is at very low levels
In %- Econviews based on UTDT



Source: Econviews based on UTDT

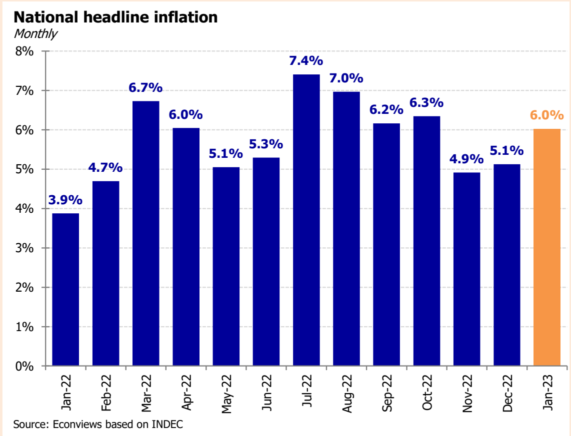
Polls show an opposition lead, but no clear favorite
Who would you vote in the 2023 presidential elections?



Source: Econviews based on Tres Punto Zero

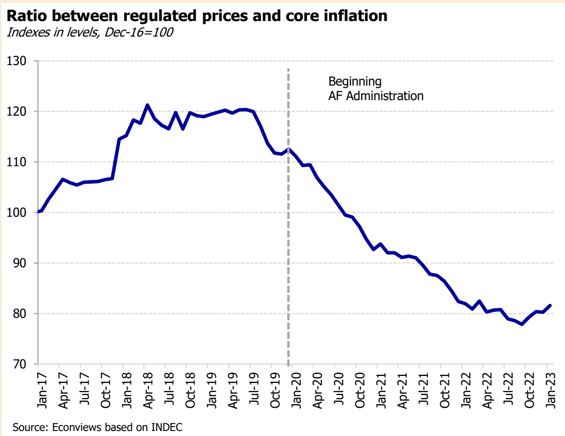
January's CPI print ended up at 6%, an unexpected setback for the government which was aiming for a three percent monthly rate as the elections get closer. The number came as a surprise, especially after the lower figures in November (4.9%) and December (5,4%), which had generated some hope in the administration. However, it seems that the battle against inflation is entering a new round in which the government has few tools to fight it, especially in an election year when the pressures will be quite strong to increase public expenditures and avoid a further weakening in economic activity.

So far, the government has managed a marginal improvement in the fiscal deficit, kept interest rates in line with inflation (one would not call them tight money) and used a variety of price agreements (now called "precios justos") to try to deal with inertia. **But the improvement in fundamentals is not large enough to bring down inflation and tame expectations**, while the imbalances in relative prices that the government is trying to correct (in part in its effort to comply with the IMF program) fuels inflation.



One of the difficulties is that the Central Bank needs to maintain the pace of depreciation in order to avoid an appreciation of the real exchange. But this means that it loses one of the main nominal anchors to control inflation. In addition, the need to reduce the fiscal deficit requires reductions in energy subsidies and hence increases in utility rates and other regulated prices that exceed the target of the price agreements in precios justos, that is currently 3.2%.

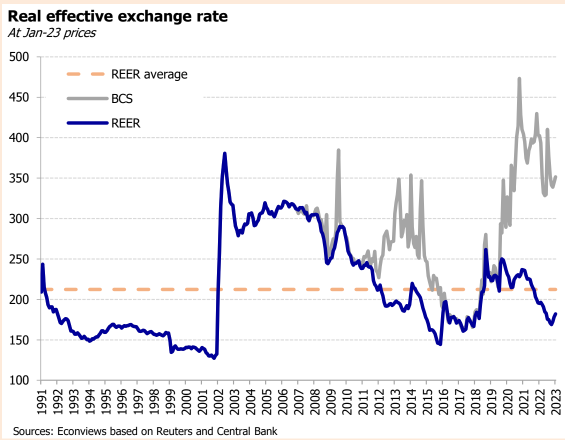
A precondition to reducing inflation is having brought relative prices close to equilibrium. Macri's effort to bring down inflation in 2016 in part failed because the adoption of tight money entered in conflict with the need to depreciate the currency and adjust utility rates. This time won't be different. In the meantime, inflation is likely to hover between 5.5 and 6.5 percent.



The second issue is the evolution of the parallel exchange rates, which typically act as a thermometer for programs' credibility. Currently it is marking high temperatures due to worries about the spread between the official and parallel exchange rates, which remains in the 100% range, an indication that there are concerns about inflation and the external balance.

The level of the parallel exchange rate looks high relative to historical figures. Is not far from the level it reached during the 2001 macro-crisis, while the current crisis does not seem to be as deep as that one, as we do not anticipate a banking or a debt crisis, at least of the magnitude of the one experienced in 2001.

On the other hand, it is clear that the official exchange rate is overvalued. While the Central Bank has accelerated the rate of depreciation to avoid further losses of reserves, it seems clear that at some point in the future there will be a step devaluation.



In this environment net reserves are under pressure. The current stock stands at around 2.2 billion dollars, completely inadequate for the normal functioning of the economy, but there is little chance that the situation is going to improve during the year under current policies. This means that FX restrictions will remain in place and are likely to be tightened while the

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situation persists, especially if, as a result of the drought, exports fall somewhere between 8 and 10 billion dollars this year.

A key question is what the government will do if reserves drop even further. It is an open secret that a new preferential exchange rate for soybean exporters is in the making, probably in April or May to induce producers to sell their crop. If that is not enough the most likely option is the creation of a second commercial exchange rate, perhaps similar to the soybean exchange rate, that can be used to provide incentives to exporters and dissuade importers. It would be a partial devaluation, that can perhaps maintain the illusion that it never happened, because there would still be an official exchange rate.

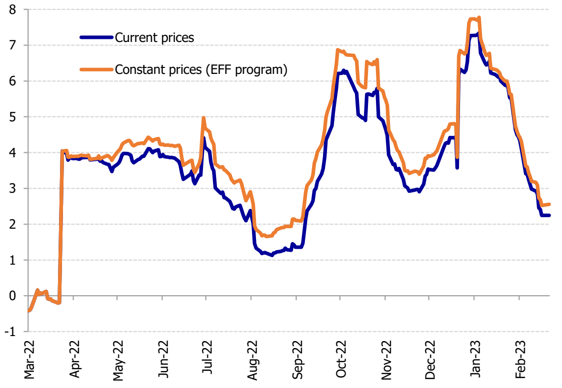
From a more fundamental point of view, these options indicate that the government can navigate through turbulent waters and somehow reach the end of the year with almost no reserves, but alive.

The final macroeconomic risk comes from the domestic debt. The outstanding debt is not particularly large, but markets are concerned about this administration's ability to roll it over. So far, the government has not been successful in extending the maturities beyond July, a month before the primaries take place. Given that most of the debt is held within the public sector, and that a large part of the balance is held by banks and insurance companies, there is a good chance that in the end the government can extend its maturities through regulation or political pressure. A new restructuring would be fatal for the development of the domestic capital markets and would end up in a new credit crunch as the chain of payments would suffer. Most likely, the Central Bank will prefer to print money and have a little more inflation than risk facing a crisis of the payment system.

In summary, in the most likely scenario the economy will muddle through till the elections, with inflation remaining at current levels, reserves would remain low but suffice, the Central Bank will continue to depreciate the currency in line with inflation, and the peso debt will be rolled over at shorter terms and higher interest rates. **The imbalances will not be corrected, the FX controls will remain in place and the burden of the adjustment will fall on the next administration.**

Net international reserves

In billion USD - IMF methodology



Source: Econviews based on BCRA, IMF and own estimates

II. ESG investment, a new dawn for Argentina

In the last few years, the world of investment has changed. It had to adapt to a global society that claims responsibility and not just profit maximizing when allocating capital. Or in other words, maximizing value can only take place when taking into account not just corporate risks but risks relevant to the broader society. In this philosophy firms are now accountable and more and more investors are uncomfortable in being lenders or shareholders of firms that are not transparent, do not consider social effects or do not care about climate change. The category of ESG investments seek to give a seal of approval to firms that are socially responsible, environmentally conscious and deal with the potential conflict of interests. Investments in the "ESG" category have been growing exponentially in the last decade**.**

Argentina is a laggard in this trend as is the rest of Latin America. However, there are some initiatives both from the regulator and from the market with the launching new funds exclusively allocated to sustainable investing. If the country eventually stabilizes and the local capital market grows, there will be an important role for ESG. Companies will have to align their strategies and their human capital either from the issuers' side or from the investing companies. In this note, we take stock of the global and local trends toward ESG investment.

Everyone goes ESG

Investors have been incorporating this concept into their investment decisions, making ESG increasingly important from the perspective of securing capital, both debt and equity. **ESG stands for 'Environmental, Social and Governance'** and it represents a set of standards that includes environmental, social and cooperative governance factors that could be added to the traditional financial criteria used for analyzing the risks and opportunities of an organization. In many ways these 3 categories can be considered risk factors and as such investors should price in risks when allocating capital. However, this is not always true and ESG investment ensures that these risks are being taken care. Furthermore, companies with good ESG grades receive more capital and this in principle goes along with market efficiency, as lower risk (social, environmental, etc.) receives more capital.

Each item implies different concepts. The environmental pillar stands for the CO2 and other gas emissions, resources used by the company, land and water use currently and in perspective, and sustainability, among others. It is a particularly complex pillar to report.

The social dimension is mainly related to employee management and other labor practices, including safety standards, it is related to the quality of products and services offered by a company or the relation with the customers and the community. The governance pillar is identified with corporate behavior and structure, including shareholders' rights, board diversity, and other characteristics.

Enviromental	Social	Governance
-GHS emissions	-Working conditions	-Codes and values
-Water and land use, Resource efficiency	-Health and safety	-Structure and board diversity, equity and inclusion
-Biodiversity	-Customers and community satisfaction	-Executive pay
-Recycling	-Diversity in staff	-Transparency and reports
-Climate Risk		

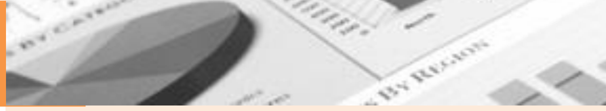
Although some authors believe that already in 1960 markets were talking about ESG, that was far too early. In 1990 some pooled funds started to consider it, but it was not until this century that it became a relevant factor. The first time the term ESG was officially used was in 2004, in a report known as “Who cares, Wins”. That paper was an initiative led by the United Nations and the International Finance Corporation, which asked major financial institutions to collaborate in planning a way of integrating environmental, social and governance concerns to the capital market.

Part of the reason for the exponential growth that the ESG registered recently is the fact that during the last few years new challenges related to sustainability (whether it be as a result of climate change, data security or demographic problems) **have appeared**, opening the path for new risks to be taken into consideration. According to a report presented in 2020 by CDP, an international non-profit organization that works with environmental data and projects, climate-related weather events are expected to cost businesses USD 1.3 trillion in a period of five years until 2026. And risks are not just limited to environmental issues.

New risks bring also new opportunities. Another factor that is developing ESG is a new generation of investors, which is looking forward to integrating ESG concepts alongside their traditional financial factors. One of the main boosts for the development of ESG was in 2015 when United Nations adopted the Sustainable Development Goals, which in a way represents this new generation of investors that gives special importance to sustainable growth. **Investors had shown the wish to invest in areas that adjusted more to their values and the reputational item plays its part.** Nowadays, it is difficult not to find any big company that does not have Corporate Social Responsibility (CSR) practices which in financial terms would be represented through the ESG. Such is the case that 90% of the firms that make up the S&P 500 index have some form of reporting on their ESG activities.

ESG ratings for bonds began around 2010, with several ESG data providers developing services to conduct ESG ratings for bond issuances. Some investors and asset managers developed their own tools to systematically integrate ESG data into debt analysis. **According to MCSI, another factor that has encouraged ESG expansion is the development of technological tools that help in the evaluation of ESG data.** This is related to new databases but also to the incorporation of artificial intelligence or related software that adds to the efficiency and analysis. Nonetheless, and even if in the last years an idea of open sourcing prevailed, **the availability of data and its quality keeps on being a limitation for the ESG world, especially as there is a lack of agreement when it comes to the variables that are included in ESG.**

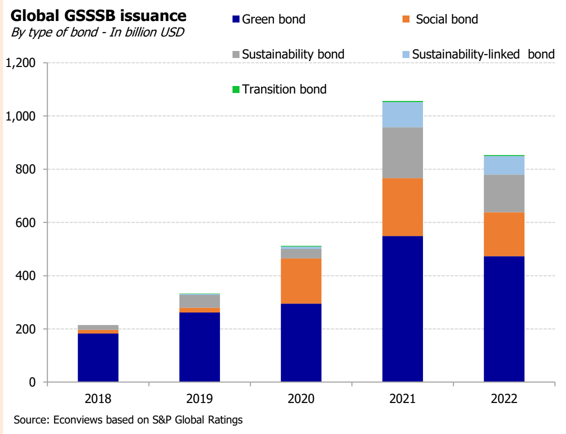
ESG concepts also brought a change in the relationship between shareholders and stakeholders. In this sense, a company manager should not just consider as a goal maximizing the investors’ revenue but also the relationship that the company has with stakeholders (being consumers, community, or other groups of interest) gains a new weight as they can pressure the company in certain ways.



Sustainable bonds and the market

S&P Global expressed that the issuance of green, social, sustainable, and sustainability-linked bonds (GSSSB) decreased from a maximum of USD 1.05 trillion in 2021 to USD 853.5 billion in 2022. This reduction comes as a result of a year in which many countries adopted a contractive monetary policy and global uncertainty due to the effects of the war in Ukraine and its global macroeconomic effects, which affected the financial markets.

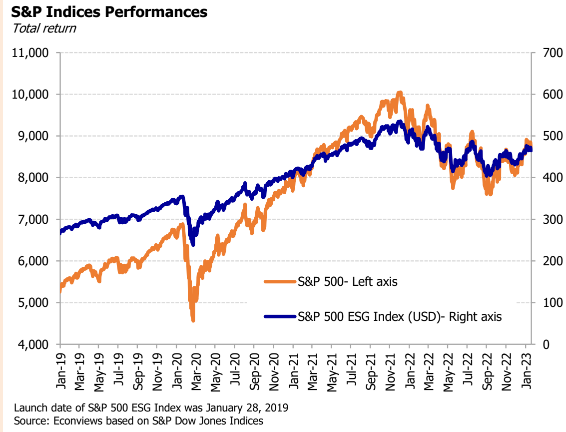
When it comes to equity, according to Morningstar, sustainable investing returns were similar to those of the traditional market. In line with this, the broad Morningstar US Sustainability Index fell 18.9% in 2022, outperforming the 19.5% decline of the Morningstar US Large-Mid Cap Index, while the S&P 500 fell 19.4%. ESG indices have proved more stable than the stock market as a whole in the last 3 years.



Source: Econviews based on S&P Global Ratings

GSSSB bonds in the global bond market have grown robustly, going from just 4% in 2018 to 12% in 2021. In 2022, even if the numbers for the ESG world were worse than the previous year, the share in the global bond market grew to 13% and is expected to continue on that path in the coming years.

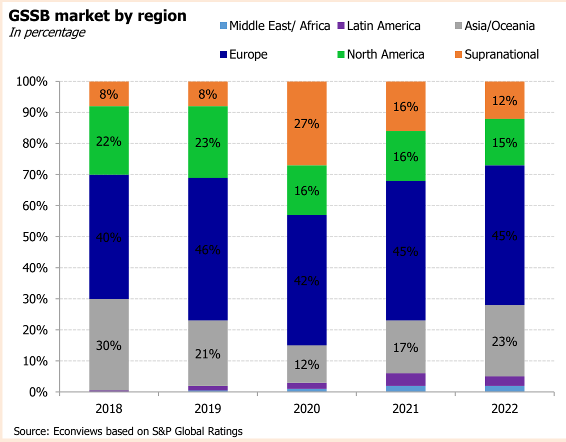
Green bonds represented 55.4% of the total GSSSB issuance in 2022, followed by Social bonds (19.3%). When it comes to the different sectors, in 2022, most sectors contracted. Nonfinancial corporate and sovereign issuance led the decline, down 28% compared to 2021, while financial services increased 14% year-on-year.



Launch date of S&P 500 ESG Index was January 28, 2019
Source: Econviews based on S&P Dow Jones Indices

In terms of ESG markets, the European one seems the most developed. In 2022, the European market represented 45% of the GSSSB global market. The podium is completed by Asia/Oceania, representing 15% of the global share of this market, and North America (15%). In 2022, the Asia-Pacific region proved to be resilient to macroeconomic uncertainties by growing 10% in terms of issuance when compared to 2021, while the Global GSSSB issuance contracted 19%.

Europe is one of the greatest supports of ESG investments, it is the earliest promoter of ESG standards and accounts for about 83% (in the last quarter of 2022) of all global ESG fund assets. Due to this, it stands as the most developed and diverse ESG market. While the United, which began working on this topic in 2011 and has more opposition than in other parts of the world, appears in second place with 11% of global ESG fund assets in the last quarter of 2022. In Asia, China and Japan play an important role in the ESG markets.



Source: Econviews based on S&P Global Ratings

2022 was not a particularly good year for ESG in the United States. According to Morningstar, sustainable funds ended in the black, netting more than USD 3 billion for the year, flows into U.S. sustainable funds peaked two years ago in the first quarter of 2021 and have fallen steadily since. **Much of this performance is related to the broad financial market**, **but the conversation around sustainable investing was increasingly plagued by concerns about greenwashing and an anti-ESG sentiment**, which is not helping.

New trends tend to generate controversy and ESG is not an exception. **The lack of uniformity and application of sustainability metrics casts doubt**

over ESG and is one of the reasons why debates and unsureness around the topic pop out. In May, TESLA, one of Elon Musk's companies, was booted from the S&P 500 ESG index over concerns about working conditions in its factories and the company's carbon impact. This measure taken by S&P Global generated controversy and debate regarding the parameters and definitions of the terms that apply to using ESG. The doubts came from the idea of how a company as big and popular as TESLA does not qualify as a top ESG company, and who could really define that. If countries keep on working on the development of their taxonomy, this problem could begin to be clarified.

As part of this doubts, getting the ESG label can mean different things at different points in time. For Standard & Poor's, in 2016 there was an excluded sector that was tobacco for guaranteed loan operations. In 2019 coal mines, controversial weapons, and palm oil were added. In 2020 opioids, adult entertainment (pornography), and usury were added. In 2021 soybean oil, the gaming industry, pesticides, and private prisons were added and in the coming years for sure it will face other changes. Global ESG rating firms include MSCI, Sustainalytics ESG, Bloomberg ESG, S&P, CDP Climate, ISS Ranking and Ratings, Moodys and FTSE Russell are some of the best-known providers in the global marketplace, and some of these firms are present in Argentina. MSCI and Bloomberg have more than 10,000 rated issuers. But recently criticism arose over how these companies were rating.

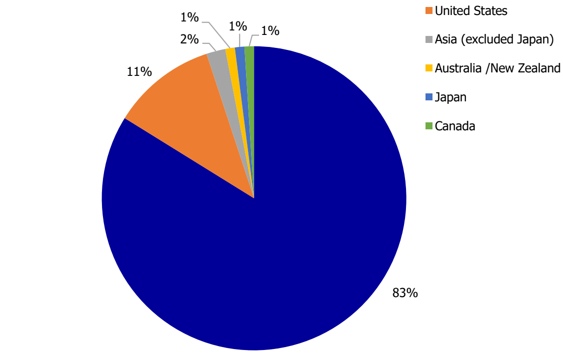
From the political side, some Republicans in the United States, who have previously presented their doubts about Climate Change, also exposed critics towards ESG investments, arguing that it prioritizes liberal goals over investor returns, harming US companies deemed insufficiently progressive and in turn hindering the wider economy.

According to MSCI´s research, 90% of the ESG regulations come from government agencies so the institutional view on ESG could be a great ally in its development or a great barrier and in this context, the EU and US government intensified their support towards them. **Despite the critics, ESG investments seem to be here to stay**. In this sense, last year, in the U.S. the government implemented changes in the retirement standards allowing a nexus between ESG and retirement plans.

But after all this analysis is good to ask ourselves whether investing in ESG is worth it. The BlackRock Institute says that companies with high **ESG ratings have better profitability, lower cost of capital, and lower "tail risk",** which is defined as low-probability, high-impact risk. According to research done on 748 company rating changes between 2016 and 2021, **there is evidence that rating upgrades on ESG-certified firms lead to a statistically significant asset price rise of 0.5% per month, while rating downgrades push risk-adjusted returns down by 1.2%.** In addition to this, a study among European firms found that **companies with good ESG practices have lower costs of debt than their peers without ESG practices.**

But not all that glitters is gold. As we are aware, ESG faces difficulties and one of these is related to a term known as greenwashing meaning a sort of "fake green" for referring to those strategies of companies that appear to apply green practices, but in reality, are not green as they look.

Global sustainable funds assets
Main players- Data as of December 2022



Source: Econviews based on Morningstar

Latin America follows from behind

Latin America seems way behind when compared to bigger players such are North America, Europe or Asia. Nevertheless, as has happened globally, the pandemic has changed the focus of many organizations who begun to give much more awareness to social matters. **As it happens in many parts of the world, the most important aspect of the ESG is usually associated with environmental matters but no one can deny that in recent years the 'S' has become more relevant.**

Since 2015 different countries in the region have started working with the ideas of ESG. Mexico was one of the first to adopt measures on the subject by launching a Consultative Committee on Green Finance (CCGF) and the Climate Bonds Initiative (CBI). In 2015, the Santiago Exchange created the Dow Jones Sustainability Chile Index (DJSI Chile). Chile recognizes climate change as a financial risk, which is an innovative approach to the way in which this aspect might be analyzed in the future when the consequences of climate change might affect economic performance. **Ever since approaches in different countries of the region can be identified.** Brazil also has been working with ESG and in 2020, its Central Bank launches its agenda of sustainability while BNDES included green loan concessions in its portfolio.

Since 2019, the Latin American ESG market has more than doubled. In 2019 there were only 14 issues with a value of 6,500 million dollars, in 2020 that number had been of 22 bonds for 22,000 million. In 2021, Latin American companies issued 36 bonds for a total of 32,000 million dollars under ESG criteria and for 2022, everything suggests that the number was higher than in 2021.

The ESG market in the region is way behind other regions but is growing steadily. As the latest news, in April 2022, Colombia became the first LATAM country to publish a green taxonomy. **These advancements are completely necessary.** According to CDP, climate change can cause economic losses of 17 trillion dollars in South America between 2021 and 2070. This includes, for example, 18 million fewer jobs in different sectors, such as agriculture, industrial production, retail trade and tourism, among others.

What about ESG investment in Argentina?

Sustainable finances are not developed in Argentina. In 2019, Argentine banks signed a Sustainable Finance Protocol with the goal to build a strategy for sustainable finance in the banking industry. But it was not until 2020 when the Technical Committee/ Roundtable on Sustainable Finance was created, led by the Ministry of Economy and with the support of the Inter-American Development Bank (IADB), that concrete measures on the subject began to become evident.

Argentina is part of the International Platform on Sustainable Finance (IPSF) led by the European Union which gathers 19 members that together represent 55% of global greenhouse gas emissions, 55% of the world GDP, and 51% of the world population. **International cooperation has been and will continue to be a key for Argentina to progress in the ESG**

environment. In line with this, the Finance Ministry further advanced a USD 1.2 million fund with the support of the Inter-American Development Bank (IADB) and the government of Germany to strengthen green fiscal policies.

Other institutions and Banks are working on different projects that focus on the development of sustainable finances in the country but one that must be distinguished is the work done by the National Securities Commission (CNV). **This Commission promoted resolution 896 in 2021 with 3 guides for socially responsible investments: one on ESG in particular, another for the issuance of green bonds and the third for external evaluators of green and sustainable issues.** In addition, the regulations include the Solidarity Financial Funds, sub-sovereign Green Bonds such as those issued by the provinces of La Rioja and Jujuy in 2017.

In 2021, the CNV authorized the first ESG Open-ended Mutual Funds (OMF). As months went by, the amount of ESG funds increased rapidly, they went from 2 in sep-21 to 7 in dec-2022, reaching a net worth of ARS 1,247 million for 2022. This represents only 0.04% of the total net worth of the mutual fund industry. According to the Argentina Association of Mutual Funds in 2022, ESG Funds accumulated net subscriptions of ARS 993 million. These numbers show that, although ESG investment has yet a long way to go in Argentina the progress evidenced in a little more than twelve months, gives hope for major development in the coming years.

BYMA, the owner of the stock market in Buenos Aires, has had a sustainability index since 2018. It was prepared with the support of the Inter-American Development Bank and it is built by 15 companies. The rules for exclusion from the index are that companies get a score of 0 in any of the 4 pillars or that have more than 5% of their sales associated with weapons, tobacco, gambling or alcohol. To prepare the index, the three ESG pillars weigh 26.67% and the millennium objectives 20%. The index is reviewed once a year.

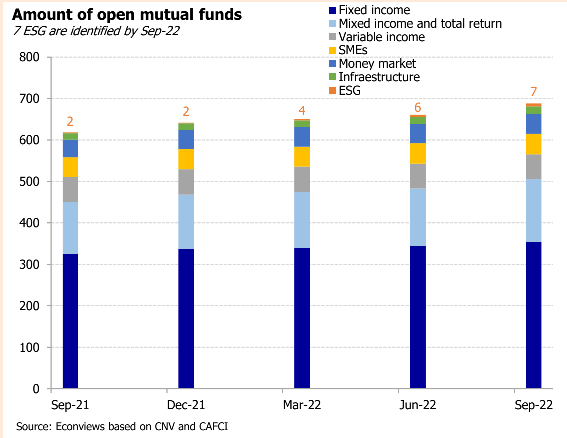
Argentina does not yet has a taxonomy defined for ESG matters, so the development of a specific taxonomy based on the characteristics and resources of the country could be key for consolidating ESG investments.

What to expect in the coming years

For what is sure, ESG is a critical must-do for all companies, regardless of size or industry, especially in the long run even if in the last year ESG investment experienced some criticism, especially in the United States. **Its further development in the coming years is inevitable and markets are aligned with this idea of considering sustainable investment as a priority.**

For 2023, **S&P Global estimates that the share of green, social, sustainable, and sustainability-linked bonds (GSSSB) in the overall market should represent 14%-16%. While global GSSSB issuance is expected to grow to USD 900 billion/1 trillion**, nearing the record of USD 1.06 trillion in 2021.

According to a poll conducted by IBD/TIPP, 77% of Americans believe that it is important to invest in companies that align with their personal values, for which researchers **predict ESG investing will more than double in the**

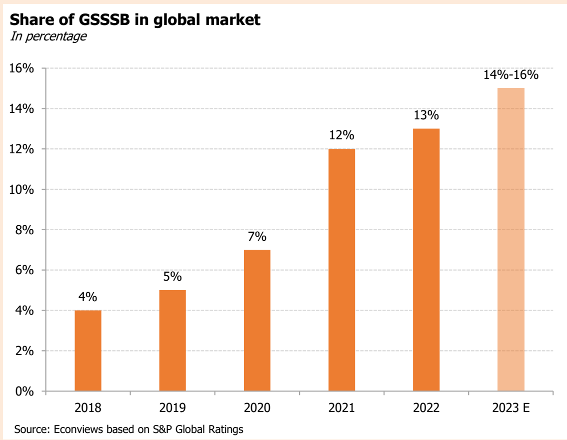


Open mutual funds in 2022

In million ARS

Type of fund	2022	% of the total
Money market	1,926,907	58.84%
Fixed income	904,643	27.62%
Mixed income	182,351	5.57%
SMEs	75,883	2.32%
Infraestructure	71,389	2.18%
Variable income	76,179	2.33%
Total return	36,258	1.11%
ESG	1,247	0.04%
Total	3,274,859	-

Source: Econviews based on CAFCI



next three years, as more investors align their portfolios with their principles. **ESG assets will account for 15% of U.S. and U.K. investments by 2025, according to a Dow Jones survey of investing professionals.**

In line with this, a study done by Bloomberg and Mubadala estimates that **in 2025, ESG assets could hit USD 50 trillion, representing more than a third of the projected USD 140.5 trillion in total global assets under management.** Though in the shareholder´s perception environmental aspects appeared as the most important one, social aspects are on the rise. When it comes to analyzing investment areas Renewables and Clean Energy are most favored (even if it is the one with the lowest expected return for 2023), followed by Waste reduction and processing.

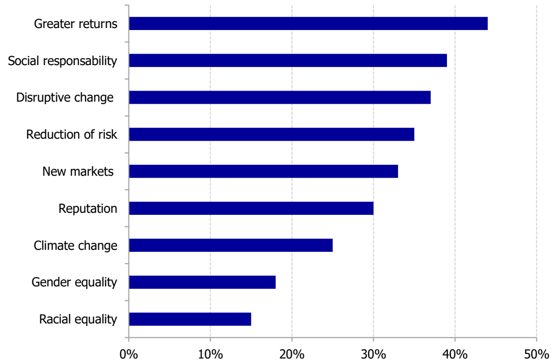
If we think longer term, according to a study done by MSCI, in the next two or three decades, only in the United States, the "millennials" are expected to direct between USD 15 trillion and USD 20 trillion into ESG investments, which would be roughly doubling the size of the U.S. equity market. The truth is that while greater returns might be a key motivation, the lack of defined standards is a limitation for the sector.

In the coming years, ESG will more and more drive investment decisions and it will come more relevant as a decision-making factor so those who ignored this new criterion, including countries, take the risk of being left aside.

As it is known, Latin America and of course Argentina, witness the ESG development from behind, though the development of this type of investment in the last years is evident. The region is facing a great opportunity given the international appetite to finance better social and environmental practices. In environmental terms, it is relatively well positioned but there are some things that Latin America could do relatively quickly and easily on the "S" side. One of them has to do with gender diversity.

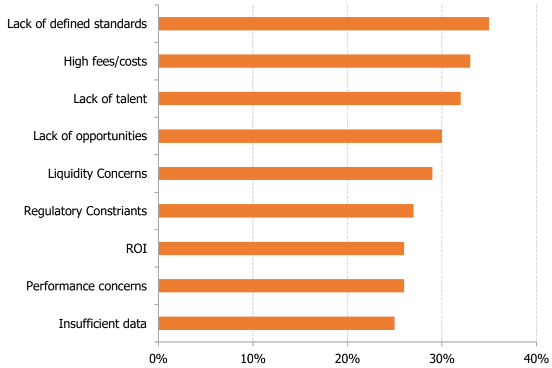
For Argentina in particular there is an opportunity that may appear in the next two years. In essence, Argentina has been disconnected from the international capital markets, though it is clear that at some point it will once again be an issuer of debt and shares in line with its relative weight in the economy. Today mutual funds in shares are a very small part of the menu in the capital market. In a scenario of greater stability, it is to be expected that there will be more dynamism for these products. **These changes that are likely of happening in the following years, open a possibility for ESG investments to flourish.**

Motivation for considering ESG in investment decision



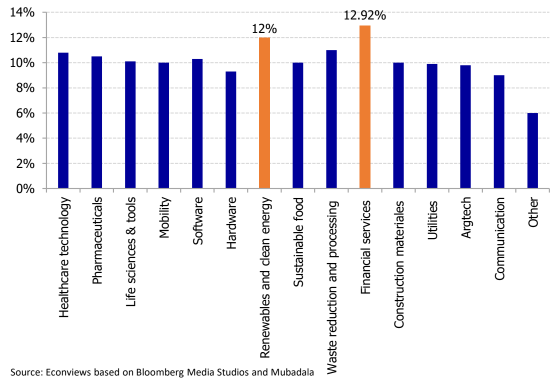
Source: Econviews based on Bloomberg Media Study and Mubadala

Barriers to considering ESG in investment decisions



Source: Econviews based on Bloomberg Medias Studio and Mubadala

Expected investment growth in 5 years
In percentage



Source: Econviews based on Bloomberg Media Studios and Mubadala

Base Scenario

	2019	2020	2021	2022 E	2023 E
Inflation (eop)	53.8%	36.1%	50.9%	94.8%	105.0%
Exchange rate ARS/USD (eop)	59.9	84.1	102.8	177.1	460.6
Exchange rate ARS/USD (eop, YoY)	58.4%	40.5%	22.1%	72.4%	160.0%
Real exchange rate ARS/USD (eop, Dec-01=100)	151.5	158.3	137.1	129.2	171.6
Paralell exchange rate ARS/USD (eop)	74.6	140.3	203.1	340.8	667.8
Spread with official exchange rate (eop)	24.6%	66.8%	97.7%	92.4%	45.0%
Gross reserves (USD billion, eop)	44.8	39.4	39.7	44.9	40.5
Net international reserves (USD billion, eop)	12.6	3.8	2.3	6.6	5.1
Policy rate (eop)	55.0%	38.0%	38.0%	75.0%	80.0%
GDP (YoY)	-2.0%	-9.9%	10.4%	5.2%	-1.0%
Formal wages in real terms (aop, YoY)	-6.0%	-1.9%	0.4%	-0.2%	-0.5%
Primary result (% GDP)*	-0.2%	-6.4%	-3.3%	-2.7%	-2.5%
Fiscal result (% GDP)*	-3.6%	-8.4%	-4.8%	-4.1%	-4.3%
EMBI Argentina (spread in bps, eop)	1,744	1,350	1,703	2,196	1,500
Public net debt (% GDP)	43.6%	52.7%	42.1%	34.8%	37.3%
Current account (% GDP)	-0.8%	0.8%	1.4%	-1.2%	-0.8%

Source: EconViews

*Excludes rents from primary debt issuance in 2022; PIPs below the line in 2019

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