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Argentina: Request for Stand-By Arrangement and Request for Extension of Repurchase Expectations—Staff Report; Assessment of the Risks to the Fund and the Fund's Liquidity Position and Report on Exceptional Access for Request of Stand-By Arrangement—Staff Supplements; Staff Statement; Press Release on the Executive Board Discussion; and Statement by the Executive Director for Argentina

In the context of the request for Stand-By Arrangement and request for extension of repurchase expectations, the following documents have been released and are included in this package:

- the request for Stand-By Arrangement and request for extension of repurchase expectations prepared by a staff team of the IMF, following discussions that ended on **September 10, 2003,** with the officials of Argentina on economic developments and policies. **Based on information available at the time of these discussions, the staff report was completed on September 15, 2003**. The views expressed in the staff report are those of the staff team and do not necessarily reflect the views of the Executive Board of the IMF.

- a staff supplement of **September 15, 2003** on assessment of the risks to the Fund and Fund's liquidity position.

- a staff supplement of **September 16, 2003** on exceptional access for request of Stand-By Arrangement.

- a staff statement of **September 20, 2003** updating information on recent developments.

- a Press Release summarizing the **views of the Executive Board as expressed during its September 20, 2003 discussion** of the staff report that completed the requests.

- a statement by the Executive Director for Argentina.

The documents listed below have been separately released.

Letter of Intent sent to the IMF by the authorities of Argentina
Memorandum of Economic and Financial Policies by the authorities of Argentina

The policy of publication of staff reports and other documents allows for the deletion of market-sensitive information.

To assist the IMF in evaluating the publication policy, reader comments are invited and may be sent by e-mail to publicationpolicy@imf.org.

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INTERNATIONAL MONETARY FUND

ARGENTINA

Request for Stand-By Arrangement and Request for Extension of Repurchase Expectations

Prepared by the Western Hemisphere Department
(In consultation with other departments)

Approved by John Dodsworth and G. Russell Kincaid

September 15, 2003

- **The authorities have requested a new three-year SBA** to succeed the transitional arrangement that expired on August 31, 2003.
- **Exceptional access is requested**: 424 percent of quota (almost SDR 9 billion), of which 279 percent of quota would become available during 2003–04. With this level of access, Fund exposure would stay broadly constant over the period of the arrangement, September 2003–September 2006 (Table 1). The phasing will help the authorities maintain a comfortable level of reserves while preserving resources to support the reform agenda in 2005–06 (Table 2).
- **Strategic objectives of the program**: begin restoring fiscal solvency within a fiscal framework that includes the provinces and makes room for adequate social and infrastructure spending; implement a credible sovereign debt restructuring; restructure banks; improve the framework for restructuring corporate debt, including that of the utility companies; and instill legal certainty to improve business confidence and growth.
- **These policies would be supported by institutional strengthening**: especially improved tax administration; reform of intergovernmental relations; greater central bank independence and effective bank supervision.
- **The policy agenda is sequenced to ensure adequate consultation and ownership.** The authorities' commitments are contained in the Letter of Intent and Memorandum of Economic and Financial Policies that was circulated on September 12, 2003 (http://www.imf.org); the key commitments are summarized in Box 1.
- **Close coordination with the World Bank and the IDB continues.** This is necessary to ensure an appropriate division of labor on policies and adequate financing plans.
- **The staff teams** that visited Buenos Aires during August 4–18 and September 2–10, 2003 comprised (on one or both missions) J. Dodsworth (Head, and senior resident representative), J. Thornton, A. Cebotari, L. Giorgianni, J. Nelmes (all WHD), A. Arvanitis (PDR), M. Petri (FAD), P. Breuer, C. Lim, and R. Thorne (all ICM), R. Weeks-Brown (LEG), and L. Sahasranam and L. Ali (both WHD, assistants); and were assisted by L. Cubeddu, the resident representative. An MFD mission, led by D. Hoelscher, overlapped with WHD missions. Mr. Zoccali, Alternate Executive Director, participated in the discussions during the August mission.

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I. Introduction

1. **The Argentine authorities have prepared an economic program aimed at reestablishing sustained growth and reducing widespread poverty.** Toward this end, the program seeks to address vulnerabilities arising from the massive debt overhang in the public and private sectors, an undercapitalized and unprofitable banking system, and a poor investment environment. The authorities have requested that this program be supported by a three-year Stand-By Arrangement (SBA) in an amount equivalent to almost SDR 9.0 billion (424 percent of quota), to succeed the transitional SBA that expired on August 31, 2003. In addition, they have requested that repurchase expectations arising during the first year of the arrangement (about SDR 1.9 billion) be extended to an obligations basis. Given scheduled repurchases, full utilization of the proposed arrangement would leave Fund exposure broadly unchanged by the end of the arrangement at SDR 10.9 billion, or 517 percent of quota—although exposure is phased to fall in the first year of the arrangement before recovering as structural reforms take hold.

2. **The critical condition for the success of the program is adequate political commitment to its implementation.** This staff paper begins by reviewing the achievements and lessons from the transitional arrangement, and the political context, as essential background to assessing the prospects for success of the proposed program. Section III of the paper explains the strategic goals of the medium-term framework for 2004–06, especially the outlook for key macroeconomic targets and core structural reforms that are focused in three main areas: structural fiscal reforms, the banking system, and institutional reforms to improve the investment climate. The details of the economic program for 2003–04, the first year of the arrangement, are contained in Section IV. Section V reviews program financing issues, including the key role that is being played by official sector financial support, and points to the risks to the program and, thereby, to the Fund. The staff appraisal, contained in Section VI, expresses staff support for the program, while assessing the manifold risks to it that will require rigorous implementation of planned measures and a generally improved political consensus in Argentina.

II. The Transitional Arrangement: Achievements and Lessons

3. **The transitional SBA that expired in August was approved after protracted negotiations in 2002 failed to result in an agreement on a sustainable medium-term program.** The transitional program aimed at: (i) maintaining macroeconomic stability through the May 2003 presidential elections; (ii) initiating some structural reforms; and (iii) giving time to the new government to develop a medium-term reform agenda. The program was narrowly focused on fiscal and monetary policies during the first half of 2003, and on initiating a banking strategy and fiscal reforms. To provide breathing room during the political transition, the program aimed at zero net payments to the IFIs, and allowed for the accumulation of arrears on defaulted public debt predicated on good-faith efforts in negotiations with creditors.

4. **The transitional program has helped maintain macroeconomic stability.** Close implementation of the agreed quantitative fiscal and monetary programs, together with an

abatement of political uncertainties, provided the basis for a rebound in confidence and output, and a strengthening of financial variables in 2003 (Figures 1–4).

- **Output and employment have been recovering and inflation has fallen.** Real GDP has been growing by 5–6 percent in 2003, driven by a gradual recovery in private consumption, a rebound in investment from a low base and, more recently, by strong growth of agricultural exports. Unemployment has declined to 15½ percent in May 2003 (from a peak of 21½ percent last year), but about 55 percent of the population still remains below the poverty line. The increase in consumer prices so far this year has been contained to 2½ percent, reflecting the still large output gap, the appreciation of the *peso*, and the continuing freeze on utility tariffs.

- **The *peso* has appreciated and interest rates have declined.** The *peso* has appreciated by about 15 percent against the U.S. dollar this year, mainly reflecting large trade surpluses (averaging about US$1½ billion a month), a stronger demand for local assets, and continued accumulation of arrears. The central bank has made net purchases of about US$3.8 billion in the foreign exchange market, bringing gross international reserves to about US$13.6 billion at end-August; during January–August, net payments to the IFIs totaled about US$1 billion. Interest rates on three- and six-month central bank paper (*lebacs*) have fallen to about 4 percent and 7¼ percent, respectively, compared with over 25 percent at the beginning of the year.

- **Tax revenue increased sharply and fiscal spending pressures were resisted.** The authorities remain well on course to meet the program objective of a consolidated primary surplus of 2½ percent of GDP in 2003. Indeed, the consolidated primary surplus has been overperforming relative to the bi-monthly targets. This overperformance has reflected stronger-than-expected income tax revenues and tight control over spending at both the federal and provincial levels, while arrears on VAT refunds to exporters have been reduced by over 20 percent.

- **A prudent monetary policy stance contributed to reducing inflation expectations.** As confidence and economic activity improved during the first half of 2003, and the *peso* appreciated, the monetary program was adjusted to accommodate faster growth in base money, which mainly reflected strengthened money demand and more rapid reserve accumulation. These conditions facilitated the liberalization of the bulk of exchange controls, the lifting of most restrictions on bank deposits in April–May,[1] and the beginning of the steady redemption of quasi-monies.[2] In the first eight months of 2003, private sector deposits grew by 15 percent and the banking system liquidity

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[1] In April 2003, depositors were offered a combination of cash, time deposits and government bonds in exchange for deposits "reprogrammed" in 2002; deposits not exchanged (about Arg$8 billion of the Arg$16 billion in reprogrammed deposits at end-March) will be released according to the reprogrammed schedule, or ongoing court injunctions (*amparos*).

[2] By early September 2003, around 60 percent of the original stock of quasi-monies (about Arg$7¾ billion) had been redeemed for pesos.

ratio rose sharply to over 25 percent, reflecting deposit growth, high legal reserve requirements, and lack of new bank lending (private credit is down by 9¾ percent in the year, but the decline appears to be bottoming out).

5. **However, progress on structural reforms was limited and there were policy reversals and setbacks.** This experience conveys clear lessons about the importance of political consensus for carrying forward structural reforms in Argentina. As indicated above, structural measures under the program were confined to initial steps on bank restructuring, preparation of fiscal reform legislation, and maintaining a measure of legal certainty. Even this streamlined structural reform agenda suffered important delays. There were also a number of setbacks including: (i) the introduction of excessive, albeit temporary, forbearance in bank regulations, which continues to delay the assessment of the true financial condition of banks as well as their restructuring; and (ii) the further erosion of creditors' rights through a temporary stay on mortgage foreclosures, and the exemption of Argentine-owned media companies from the cramdown provision in the insolvency law.

6. **The banking system is currently liquid but continues to generate significant losses, and credit has still to revive** (Annex I). Monthly losses were nearly Arg$600 million during the first half of 2003, after losses of Arg$1.5 billion a month in 2002. Bank losses mainly result from: (i) high nonperforming loans (which average about 50 percent of total loans); (ii) an interest rate mismatch between assets and liabilities; (iii) the asymmetric indexation of bank assets and liabilities; and (iv) the court ordered repayment of deposits (*amparos*), from which losses are estimated to total about US$2½ billion.[3] In August, congress approved amendments to the financial institutions law and the central bank charter that strengthen the bank resolution capabilities of the central bank, introduce limited protection for officials involved in bank resolution, and give greater scope for credit to government associated with payments to IFIs. Argentina's experience demonstrates again that an unrestructured banking system will find it difficult to revive lending.

7. **Preparations have recently advanced for the planned restructuring of public debt.**[4] Financial advisors were appointed in February 2003 to assist in designing the framework for the debt restructuring and in managing relations with private creditors. A series of meetings with private creditors was held in early June 2003, and selected creditors were subsequently invited to join consultative groups set up by the authorities to share information and better understand investors' needs and expectations. So far, four creditor consultative groups—representing institutional and retail creditors from the United States, Europe and Japan—have been formed. Nevertheless, some creditors have been frustrated by the limited progress in carrying these initial steps to a decisive stage and by continuing

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[3] The pace of *amparos* continues to decline, from an average of Arg$400 million a month in January–June to Arg$250 million a month in July–August.

[4] About US$100 billion of public debt is nonperforming (53 percent of total public debt), most of which is held by external creditors (Annex II).

uncertainties about the government's intentions regarding the restructuring—conveying the clear lesson about the importance of moving quickly to normalize relations with all creditors.

8. **There appears to have been little restructuring of private corporate debt.** About 65 percent of the roughly US$50 billion (40 percent of GDP) of private corporate debt is estimated to be nonperforming (a large portion of which is accounted for by the utility companies) with creditors mostly being nonresidents (Box 2). Most of the completed deals are reported to be refinancing or rollover operations, rather than the deep restructuring (e.g., debt reduction and debt-to-equity conversions) that is often needed in a post-crisis environment to ensure debt sustainability. The limited progress appears to reflect mainly uncertainties regarding future economic policies, and delays in renegotiating utility companies' concession agreements and approving interim tariff increases. The lesson from this experience, as well as from the experience of other crisis countries, is the importance of creating the necessary conditions for private debt restructuring in order for investment and growth to revive in a sustained way.

III. Proposed Medium-Term Framework

A. Political Context

9. **President Kirchner's government took office in late May, ending a prolonged period of political uncertainties about the presidential succession.** Many observers assess that President Kirchner's initial actions have given priority to consolidating his popular base with the people. Since the election, the President has enjoyed exceptionally high approval ratings in the opinion polls. The polls indicate particular support for recent actions supporting human rights and attacking corruption and vested interests. Congress has generally supported the President on these measures. Some of the President's early actions have included: (i) retiring high ranking military officers; (ii) bringing to justice military officers accused of crimes committed during the military regime of 1976–82; (iii) tackling corruption in the federal police and pensioner welfare system; and (iv) supporting the impeachment of Supreme Court Justices.

10. **The government's economic strategy has taken some time to emerge.** The President has spoken repeatedly about the importance he attaches to Argentina moving away from crisis-oriented economic measures, and to normalizing economic relations and policies. However, on sensitive issues such as utility tariffs, bank compensation, and external creditors, many in the administration appear to have adopted a relatively hard line.

11. **Provincial and gubernatorial elections, concentrated in the August–December period, have kept many political uncertainties alive.** Before the end of this year, some 17 provincial governors will be elected along with one-half of the lower house (130 seats) and one-third of the Senate (24 seats). President Kirchner is backing a range of candidates in an attempt to build a center-left political base of his own, and deepen his influence in congress. Thus, the outcome of these elections will be crucial for the orderly implementation

of the medium-term economic program because many initiatives, especially involving fiscal and other structural reforms, will require support from congress and provincial legislatures.

B. Strategic Goals

12. **The strategic goal of the program is to deepen and broaden structural reforms that are essential for restoring sustained growth and reducing poverty** (MEFP ¶3).[5] Medium-term growth depends upon strong policy implementation, particularly with respect to achieving sustainable public finances (including through restructuring public debt), advancing implementation of the bank strategy, and making decisive progress in private debt restructuring. These policies need to be supported by other essential structural reforms aimed at institutional strengthening, including of the tax system, intergovernmental relations, central bank independence, and legal predictability. However, a strong political consensus still needs to be developed in these areas. Accordingly, the program's strategy envisages a carefully sequenced agenda, allowing sufficient time for developing support and implementing it (¶4).

13. **The strategic objective for public debt is to reduce the debt-to-GDP ratio from its projected end-December 2003 level of about 150 percent of GDP to a sustainable level**—thereby building market confidence and allowing Argentina to regain market access. This requires: (i) a significant increase in the consolidated primary surplus; and (ii) reaching agreement with creditors on a debt restructuring that will need to involve significant debt service relief and the rollover of most maturing domestic debt during the program period. It is important that the authorities move as quickly as possible to complete a restructuring that is both acceptable to creditors and fits within a credible financing envelope, as the longer an agreement is postponed, the greater the threat of litigation against Argentina.

14. **Raising the consolidated primary surplus over the medium term is needed to**: (i) meet obligations due to multilateral and official creditors, and on currently performing debt ("phase 1" debt, plus bonds issued to compensate banks, depositors, and civil servants);[6] and (ii) underpin an early and credible restructuring of defaulted debt, including "phase 2" debt (Annex II). The authorities have yet to quantify the path for the primary surplus of the consolidated public sector beyond the target of 3 percent for 2004, although they have committed to raise the surplus to levels sufficient to meet the above objectives (¶8). However, even primary surpluses in the range of 4½–5 percent of GDP, and a debt restructuring involving a haircut on phase 2 debt deeper than that indicated by current prices of defaulted bonds, would leave the post-restructuring debt ratio at uncomfortably high levels for several years.

15. **Fiscal structural reforms are needed to achieve the required primary surpluses.** With public spending already compressed, and concentrated largely on wages and pensions

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[5] Hereafter, references to MEFP paragraphs will be denoted by the symbol ¶.

[6] The primary surplus to meet these obligations alone over the medium term would need to be about 3½ percent of GDP even on relatively optimistic assumptions regarding market access.

at the federal level, there is not much scope for large-scale spending cuts in the short term. Further fiscal consolidation to achieve the required primary surplus must, therefore, be sought mainly by implementing structural fiscal reforms aimed at boosting revenues, limiting expenditure growth and improving its efficiency, and anchoring adjustment at the level of the provinces. These fiscal reforms are anticipated to be developed during 2004 and implemented in 2005.

16. **Comprehensive reforms are needed to restore the soundness of the banking system and restart financial intermediation**. The priorities are to phase out regulatory forbearance, and rebuild banks' capital and profitability. The latter is likely to involve further consolidation of the banking system and reform of the public banks. The challenge will be to ensure that bank resolution proceeds in an orderly way, and that fiscal costs do not undermine the public debt objective. Critical measures are planned for the first year of the program.

17. **A more predictable legal environment and accelerated restructuring of troubled corporate debt are essential complements to the banking strategy.** The primary role of the government would be to improve the legal, regulatory, and institutional conditions needed to facilitate restructuring and normalize relations between creditors and debtors. Advancing the restructuring of utility company debt will be crucial to the success of the debt restructuring strategy. In addition, instilling greater legal predictability is key to a fundamental transformation of the investment climate. The specific measures to achieve these objectives are phased for implementation during the program period; it will be imperative to avoid developing inconsistent initiatives that would adversely affect market assessment of legal predictability.

18. **A wide range of institutional reforms is also envisaged.** The policy framework in other structural areas includes changes to the central bank charter to strengthen independence and move toward an inflation targeting framework, reform of the regulatory framework for the privatized utility companies (including provisions for tariff increases), further liberalization of exchange controls, improvements in tax administration and budget management, a start on pension reform, and efforts to remove constraints on exports. These reforms have been sequenced for implementation during 2004–06.

C. Macroeconomic Framework

19. **The proposed macroeconomic framework aims to lay the basis for sustained growth and low inflation, reduced poverty and unemployment, and restoring a viable debt position** (¶¶5–6 and Annex III). The framework assumes a steady improvement in confidence to reestablish market access for the public and private sectors, and to induce a reflow of flight capital.

- **Growth.** The authorities expect growth to remain robust through 2003–06, underpinned by a recovery in investment and a gradual return of private capital flows (Text Table A and Table 4). However, by 2006, real output will still be below the 1998 level.

Text Table A. Macroeconomic Framework, 2003-06

	2003	2004	2005	2006
Real GDP growth 1/	5.5	4.0	4.0	4.0
Inflation (e.o.p.) 1/	5.6	10.5	8.0	6.5
External trade balance				
(In billions of U.S. dollars)	15.5	14.2	13.8	13.2
(In percent of GDP)	12.4	9.7	8.6	7.5
Gross international reserves, baseline				
(In billions of U.S. dollars)	13.6	15.7	16.7	18.4

1/ Year-on-year percent change.

- **Inflation.** Core inflation would be maintained in single digits during the program period, although headline inflation is projected to rise temporarily in 2004 on account of utility tariff adjustments.

- **External.** The large trade surplus is projected to decline somewhat, as the output gap narrows and the real exchange rate appreciates (Table 5). The framework provides for additional reserve accumulation of about US$4½–5 billion from current levels, thereby increasing gross international reserves to about US$18½ billion by end-2006 (Table 6).

Achieving the macroeconomic objectives will depend upon maintaining disciplined monetary and fiscal policies, successful implementation of the banking strategy, improvements in the investment climate, and the good-faith efforts of Argentina to address the debt overhang.

IV. The Economic Program for 2003–04

A. Fiscal Policy

20. **The fiscal program is centered around raising the consolidated primary surplus from 2½ percent of GDP in 2003 to 3 percent of GDP in 2004** (Text Table B and Tables 7–9).[7] In 2003, the primary balance target is expected to be met through continued recovery of tax revenues and tight control of spending at the federal and provincial levels. In 2004, adjustment at the federal level would be achieved mainly through improvements in tax compliance as a result of the administrative reforms expected to be

Text Table B. Fiscal Program

	2002	2003	2004
(In percent of GDP)			
Federal revenues	18.2	20.3	20.3
Federal primary expenditures	17.2	18.2	17.9
Federal primary balance	0.9	2.1	2.4
Provincial primary balance	-0.1	0.4	0.6
Consolidated primary balance	0.9	2.5	3.0

[7] If augmented to include debt recognition operations, including issuance of bonds to compensate banks, depositors, and civil servants, the primary balance is projected to record a deficit of 3.8 percent of GDP in 2003, and a surplus of 1.9 percent in 2004.

approved by congress by end-November 2003 (Box 3 and ¶29), and reductions in primary spending equivalent to about ¼ percent of GDP (Table 8).

21. **Expenditure plans in 2004 will include new spending initiatives on public infrastructure and the core social safety net.** Public investment—mainly infrastructure and housing—is projected to increase by about 0.4 percent of GDP (to about 2 percent of GDP). In addition, the ongoing economic recovery has enabled the authorities to shift the focus of core social safety net spending away from employment support in favor of direct assistance programs for the elderly and children. The spending initiatives are to be absorbed mainly by limiting increases in the public wage and pension bill and in transfers for job support programs. The fiscal program also provides for the elimination, by March 2004, of arrears on VAT refunds that have accumulated to exporters (¶13).

22. **Contingency measures will be implemented to ensure achievement of the primary surplus targets.** In the event of a shortfall in fiscal revenues, or increased spending by provincial governments related to MDB disbursements, the authorities have agreed to take compensating measures. Such measures could include: (i) including excises into the base of the VAT; (ii) increasing excise duties; and (iii) eliminating cross-crediting of the fuel tax against the VAT and income taxes. These measures are envisaged for eventual incorporation in the planned tax reform (¶28).

23. **Provincial adjustment is being achieved through spending controls and limiting borrowing** (Table 9). Provincial adjustment in 2004 is to be underpinned by the continued operation of bilateral agreements, which are expected to be ratified by provincial legislatures by end-March 2004 (¶17). The staff places the highest importance on early approval and ratification of the bilateral agreements, which provide orderly financing in exchange for a commitment to increase fiscal savings. The bilateral agreements have proven effective, thus far, in anchoring fiscal adjustment by the provinces.

24. **The fiscal financing gap for 2004 is projected to be about US$12 billion, after payments on a contractual basis on nonperforming debt** (Table 10). The authorities are aiming for a public debt restructuring that would eliminate the financing gaps and achieve a sustainable debt profile over the medium term. An agreement with creditors would reduce the uncertainty stemming from the threat of litigation, though this has been limited thus far. A normalization of relations with creditors, together with a more sustainable debt level, would allow the authorities to rebuild market confidence and regain market access over time.

25. **The authorities are developing an offer to creditors for the restructuring of public debt.** The authorities have indicated that they would move toward a completion of the restructuring by mid-2004, following an initial announcement at the Annual Meetings.[8] Feedback from creditors on the design of the offer could play a helpful role in achieving a high participation rate while staying within the authorities' financial constraints. The

[8] The authorities have not informed the staff yet as to the details of the announcement that they intend to make.

authorities have stated that they will keep Fund staff informed of progress in reaching a restructuring agreement that is consistent with medium-term sustainability (¶20). This will allow the staff to evaluate whether the restructuring agreement has the prospect of closing future financing gaps and is consistent with reducing IFI exposure starting from 2007.

26. **Public sector debt is projected to rise by about US$15½ billion (12 percent of GDP) during July–December 2003 to US$186½ billion** (Table 11 and Table II.1 of Annex II). The main components of the increase are: (i) government support for the financial system, including bonds to be issued to compensate for the balance sheet impact of asymmetric indexation and to finalize compensation for *pesoization* (US$3.2 billion), and to compensate depositors (US$1.3 billion); (ii) the net effect of moving bonds held mainly by domestic pension funds from phase 1 to phase 2 debt (about US$6½ billion);[9] (iii) the redemption of quasi-monies (US$1.9 billion); and (iv) the continued accumulation of interest arrears on defaulted debt. The authorities have indicated that they will not compensate banks for *amparo* losses, but will identify measures by December 2003 that would strengthen the banking system (see Section IV.C. below); debt for this purpose is not included in the projection.[10]

Structural fiscal reforms

27. **Structural fiscal reforms are needed to raise the revenue-to-GDP ratio and put the public finances on a sustainable path**. The program provides for the strengthening of revenues through some tax policy measures that would serve to support the 2005 budget; as well as a reform of intergovernmental relations. Other measures are limited mainly to improving tax compliance. Tax administration measures (that are in line with previous technical assistance recommendations) are expected to be approved by congress by end-November 2003; and improvements in customs administration and social security collections (to be developed with staff assistance) will start being implemented by March 2004 (¶29).

28. **Staff argued that the tax system should be reformed to allow for a gradual increase in the revenue-to-GDP ratio while phasing out distortionary taxes**. The reforms should aim to: (i) broaden the VAT base; (ii) increase excise taxes; (iii) reduce the minimum income threshold of the personal income tax, and subject interest and dividend income to final withholding; and (iv) phase out the distortionary taxes on financial transactions and exports. The authorities took the view that political and social constraints prevented their

[9] In August 2003, the authorities issued an executive decree that moved some US$13 billion of bonds held mainly by domestic pension funds from phase 1 debt into phase 2 debt at the value of the bonds prior to the phase 1 exchange (US$19–20 billion including arrears); these pension funds had not accepted the *pesoization* of their guaranteed loans denominated in foreign currency.

[10] In 2004, the debt stock of the consolidated public sector will continue to rise as a result of: (i) debt recognition operations by the federal government and the provinces, mainly as a result of court injunctions (US$1.6 billion); and (ii) the effect of inflation on indexed debt (US$3.6 billion).

acting on the minimum threshold of the personal income tax, while the scope and timing for reducing the financial transactions and export taxes are constrained by limited alternative sources of revenue. However, they committed to considering next year a package of tax reforms that would form the basis for the 2005 budget, including a gradual easing of the financial transactions tax beginning in mid-2004 (¶28); the export tax would begin to be lowered very gradually from January 2005.

29. **The authorities committed to a timetable—but no details—for intergovernmental reform.** The main focus of the reform is expected to be on reforming tax-revenue sharing arrangements, and introducing borrowing limits for the provinces. These should be complemented by reforms aimed at strengthening provincial revenue-raising capabilities, a more equitable distribution of federal transfers among provinces, and the introduction of binding debt and deficit limits for each province. Formal agreement on a reform proposal is expected to be reached with provincial governors by end-March 2004, with congressional approval of legislation by the following August (¶31).[11]

30. **Fiscal adjustment would also be supported by improvements in public expenditure management.** The authorities have agreed to develop an action plan by mid-2004 that will establish a timetable for: (i) the incorporation of all extra-budgetary activities and contingent liabilities into the central government budget; and (ii) the adoption of common standards for budget coverage, classification and accounting at all levels of government to enable reporting on consolidated government activities in a timely manner (¶30).

31. **The authorities have also committed not to *increase* revenue earmarking.** This is a minimum objective, given that about 40 percent of federal tax revenue is earmarked (excluding transfers to provinces and social security revenues). The staff urged a reduction in revenue earmarking to give added flexibility to fiscal policy; however, the authorities stated that this would only be possible over time because of the need to build the necessary political support for a reduction.

32. **The authorities are developing a detailed plan for pension reform.** The relative roles of the private and public pillars in the future pension system are being debated within the government and a proposal will be presented in early 2004 (see ¶32). The World Bank has recommended the strengthening of both pension pillars, while avoiding additional fiscal pressures on the public pillar. For the public pillar it will be important to: (i) create a basic anti-poverty system for the poorest elderly in a fiscally sustainable way; (ii) reduce the 30-year minimum contribution requirement with actuarially reduced benefits; and (iii) close loopholes on self- and temporary employment. In addition, staff recommended changes in the funded pillar to: (i) gradually increase contribution rates to their previous level; (ii) review

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[11] The authorities explained that reaching agreement with governors on a proposal before end-March 2004 was complicated by the gubernatorial and congressional elections being held in August–December 2003.

the disability and survivor insurance to reduce costs; and (iii) increase the transparency and efficiency in the management of pension fund portfolios.

B. Monetary and External Policies

Monetary policy

33. **Monetary policy will continue to aim at entrenching low inflation expectations.** The authorities' monetary program maintains the growth of the augmented monetary base broadly in line with nominal GDP growth through end-2004 (Text Table C and Table 12). This represents a moderation of base money growth relative to 2003, which the staff regards as prudent given the significant remonetization that has already taken place. Base money growth would be driven mainly by international reserves accumulation. Operationally, the authorities will seek to control the monetary base through open market operations involving *lebacs*, while limiting sales of foreign exchange reserves for intervention—within the framework of a continued flexible exchange rate policy.

Text Table C. Monetary Framework, 2003-04
(In billions of pesos, unless indicated otherwise)

	2003			2004			
	Aug.	Oct.	Dec.	Mar.	Jun.	Sep.	Dec.
Net international reserves (NIR), baseline	-11.7	-11.6	-11.3	-11.2	-8.7	-8.1	-5.5
Net domestic assets (NDA), baseline	55.0	55.9	59.1	57.4	58.0	57.7	59.3
Monetary base 1/	43.3	44.3	47.8	46.3	49.3	49.6	53.8
Memorandum items:							
NIR, baseline (US$ billions)	-4.0	-4.0	-3.9	-3.9	-3.0	-2.8	-1.9
NIR, floor (US$ billions) 2/	...	-4.5	-4.4	-4.4	-3.5	-3.3	-2.4
NDA, ceiling 2/	...	57.4	60.5	58.9	59.5	59.2	60.8
Gross international reserves, baseline (US$ billions)	13.6	13.4	13.6	13.3	14.3	14.9	15.7

1/ Augmented to include federal and provincial quasi-monies; program indicative target.
2/ Program performance criterion.

34. **To enhance the credibility and effectiveness of monetary and exchange rate policies the authorities propose to move to an inflation targeting regime by end-2004.** The aim will be to establish a clear focus on price stability, allow the central bank greater policy/instrument independence, and also increase the accountability of the central bank. The staff supports this proposal and the authorities have established a working group to prepare recommendations (by end-March 2004), including possible amendments to strengthen the central bank charter to achieve these objectives (¶34). During the transition to inflation targeting, the program incorporates an indicative target band on inflation, which has been initially set at 7–11 percent for projected end-2004 inflation.

Balance of payments and financing policies

35. **In 2004, Argentina will face a sizable external financing gap of about US$6½ billion** (Table 6), notwithstanding a continued large current account surplus and the further accumulation of arrears to the private sector. This is based on the staff's assumption that net private capital outflows would continue in the short term, even if legal and institutional reforms succeed in improving the business climate. Part of the gap reflects an increase of over US$2 billion in gross reserves, which is consistent with programmed base money expansion. The financing gap is assumed to be fully met by new program financing by the IFIs and a rescheduling by Paris Club creditors. In 2004, net flows from Argentina to the Fund are estimated at US$340 million, principally on account of interest charges.

36. **Consolidating a supportive medium-term external outlook is also predicated on trade policies.** The authorities have committed to phase in measures removing disincentives to exports by: (i) eliminating the export receipt surrender requirement by July 2004 (¶25); (ii) increasing trade openness by phasing out special regimes in line with existing Mercosur commitments by January 1, 2006 (¶26); (iii) phasing out export taxes beginning January 1, 2005 (¶13); and (iv) eliminating arrears on VAT refunds by end-March 2004 (¶13). The authorities have also indicated their intention to foster export diversification by actively participating in multilateral and regional trade negotiations.

C. Bank Restructuring Policies

37. **The main planks of the bank restructuring strategy for 2003–04 are to**: (i) phase out temporary forbearance on private loan classification and provisioning by end-2003; (ii) complete the placement of bank compensation bonds and identify any additional measures needed to strengthen the banking system in light of losses from judicial injunctions (*amparos*); (iii) begin a system-wide diagnosis of bank viability, including measures to improve bank profitability; (iv) sequence the restructuring of public banks to ensure their adherence to commercial principles; and (v) further strengthen the institutional framework for bank supervision and resolution. These steps should pave the way toward restructuring financial institutions in an orderly and even-handed way, and securing the recapitalization/restructuring of viable banks—necessary conditions for reviving credit flows and improving financial intermediation in Argentina.

38. **The elimination of forbearance and clarification of the policy on bank compensation will set the stage for initiating bank restructuring in 2004.** The planned phase-out of regulatory forbearance on private loan classification and provisioning at end-December 2003 would ensure the timely recognition of losses, improve the transparency of bank balance sheets, and accelerate restructuring (¶41). The authorities have committed to compensating banks for asymmetric *pesoization* and indexation by December 2003, following the approval of legislation authorizing bond issuances to cover bank losses from asymmetric indexation (¶ 39). Congress rejected, however, the bill authorizing bank compensation for losses arising from *amparos*, and the authorities have, thus far, been

reluctant to take remedial measures.[12] The staff stressed the importance of developing an alternative strategy for addressing this issue, and the authorities have agreed to identify measures needed to assure the strength of the system by the time of the first review of the program (¶39).

39. **The strategy for strengthening the soundness of private banks relies on a full diagnosis and development of individual bank restructuring plans.** Based on the recently revised prudential regulations, banks will provide, by end-October, financial statements for September 2003 together with detailed business plans (including time-bound plans for full compliance with prudential regulations) and cash flow projections (¶42). On this basis, the central bank will assess the potential for banks to meet prudential requirements. This is a first step toward an overall assessment of likely capital needs for the banking system as prudential regulations are progressively tightened over the coming years. Given the fact that banks continue to be loss-making, the authorities have agreed to consider implementation of measures that would enhance bank profits, including: (i) the payment of market interest rates on any new financing to the government; (ii) the phased reduction in the financial transactions tax; and (iii) reductions in reserve requirements. The precise timetable for these measures will be determined as progress is made in bank diagnosis.

40. **As a first step toward assessing the future strategic role of the public banks, due diligence and strategic reviews of the two largest public banks have been initiated.** The authorities have issued bids to conduct this work for *Banco de la Nación* and *Banco de la Provincia de Buenos Aires*, which account for roughly one-third of banking system assets. The international firms are to be selected for both banks by mid-February 2004, with work to be completed by end-August 2004 (¶38). Based on these reviews, an action plan for the public banking sector will be developed by the authorities, with implementation expected to begin by end-2004. A third and smaller regional public bank, *Banco de la Ciudad de Buenos Aires*, accounting for less than 3 percent of bank assets, was reluctant to participate in the due diligence exercise and repaid in full central bank rediscounts. The central bank will continue to closely monitor this bank and ensure that it remains in compliance with prudential regulations.

41. **Strengthening the institutional framework for bank restructuring is another key plank of the banking strategy.** Progress has recently been made in this area with the passage of the revised financial institutions law and the establishment of a Financial Sector Restructuring Unit (FSRU), which is charged with the coordination and monitoring of bank reforms. The authorities have agreed to issue soon the FSRU's terms of reference, which will, inter alia, clarify its functions and ensure its mandate does not overlap with that of the central bank (¶37).

42. **The authorities also indicated that they are considering establishing a new regulatory agency, separate from the central bank, to conduct bank supervision.** The staff viewed with concern the possible disruptive impact on bank restructuring efforts of such

[12] Failure to effect compensation for *amparos* is estimated to reduce bank capital by roughly 30 percent.

a change. To safeguard against this possibility, the authorities agreed to establish a committee to begin preparatory work for ensuring a smooth transition to a new independent regulatory agency (¶36). The staff proposed that the mandate for any new agency should include the regulation of capital markets and pension funds to minimize possibilities for regulatory arbitrage. The authorities, however, were reluctant to unify supervision, preferring, instead, to improve coordination among the existing regulatory bodies. In September, congress rejected proposed amendments to the central bank charter that would have strengthened the bank's budgetary independence.[13] Staff viewed with concern this development and the issue will be taken up by the working group on enhancing central bank independence and accountability.

D. Corporate Debt Restructuring and Legal Framework

43. **The authorities recognize the importance of accelerating private debt restructuring in tandem with efforts to restore normalcy in the banking system.** They view the government's role, however, as limited by the necessarily private and voluntary nature of debt negotiations. Their strategy, thus, centers on maintaining a regulatory and legal framework, including for the insolvency system, that is conducive to speedy restructuring negotiations and a resumption of credit flows to viable firms.

44. **Policy commitments in the corporate restructuring area include:** (i) undertaking a detailed corporate sector survey that seeks to clarify the current financial condition of firms; (ii) developing by March 2004 voluntary workout principles, based on international best practice, to be used by debtors and creditors engaged in restructuring discussions; and (iii) reforms to strengthen the insolvency system, including through measures aimed at making the system more efficient in a number of respects (¶46–48). The authorities view these commitments as sufficient to ensure an orderly resolution of troubled corporate debt, and have agreed to review and, if necessary, adapt the strategy over time, in light of the experience with the initial restructuring cases.

45. **Restoring predictability of the legal system and ensuring contractual certainty are key objectives of the program.** The authorities are committed to avoiding any future infringements of creditor rights and to developing broader reforms to restore confidence in the rule of law. They plan to address the need to protect poor debtors through a strategy consistent with respect for creditor rights and focused on those affected by mortgage foreclosures. The strategy, initiated with the compilation of a registry of affected debtors during June–August, will be firmed by end-September 2003, within the envelope of available fiscal resources.[14] The development of this strategy should avoid the need for any further stays on mortgage foreclosures. In this context, a voluntary stay was announced by bankers' associations immediately following the September 2 expiration of the statutory stay. The

[13] Shifting approval of the central bank's administrative budget from the executive to the congress was a structural benchmark under the transitional SBA.

[14] The universe of debtors with a pending foreclosure is relatively small—roughly 13,200 debtors with mortgages totaling less than Arg$560 million.

authorities will also review the need to limit the scope of the earlier exemption of media companies from the cramdown provision and are committed to abstaining from granting exemptions to any other sectors (¶50). Broader reforms to restore legal certainty and ensure protection of property rights will be developed by a high-level commission by June 2004.

E. Utility Companies

46. **The authorities agreed to establish a more transparent and predictable framework for the renegotiation of public concessions, but did not commit to a timetable to implement specific measures.** In July, legislation was submitted to congress that: (i) gives to the executive the power to renegotiate the concessions on a fast track basis; (ii) permits the executive to grant interim tariff increases in advance of the final renegotiation; and (iii) extends the renegotiation period by an additional year, to end-2004. While the authorities will work with congress to ensure passage of this legislation before the end of the year, they were reluctant to commit to a timetable to carry out the renegotiation of public services and infrastructure concessions (¶45). The authorities argued that social and political considerations prevented them from announcing a specific timetable for the renegotiation program, or a date for introducing interim tariff increases. On this latter point, staff stressed that any tariff increase should be accompanied by a scheme to protect lower income households.

47. **The authorities are working to strengthen the regulatory framework under which concessionaires would be expected to develop credible business plans, allowing them to restructure their debts with external creditors.** In this regard, a new renegotiation commission was created in June 2003, co-chaired by the ministry of economy and production and the ministry of planning and public works, to develop a new general regulatory framework, and carry out the renegotiation of the 63 concessions (¶44).[15] The new framework, which is being developed in collaboration with the World Bank, establishes: (i) a transparent mechanism for adjusting future tariffs; and (ii) clear rules for monitoring and penalizing concessionaires that do not meet obligations under the contract. Staff stressed the need for a speedy conclusion of the renegotiation process and establishment of a new regulatory framework which would allow concessionaires to begin to cover investment costs, and resolve the legal claims levied against the government in the international arbitration tribunals (currently these claims amount to US$18 billion).

[15] Utility and public infrastructure concessions include: gas (11); electricity (11); water (1); telecommunication (2); inter-urban roads (15); urban access roads (4); railroads (11); ports (4); bus terminals (1); dredging (1); airports (1); and postal service (1).

V. Program Modalities

A. Program Financing

48. **Financing issues**: The gross external financing requirements for the period 2004–06 are estimated to average US$25 billion a year, including debt service obligations on unrestructured public and private debt. The authorities are seeking to meet these financing needs through: (i) a restructuring of public debt; (ii) new purchases under the requested Fund arrangement of almost SDR 9 billion (about US$12.5 billion); (iii) extension of repurchase expectations totaling the equivalent of about SDR 1.94 billion during the first year of the arrangement;[16] (iv) broadly maintaining exposure by the World Bank and the IDB, involving new disbursements by these institutions totaling about US$6 billion; and (v) a requested rescheduling of obligations to Paris Club and other bilateral creditors for all principal payments due during the program period, including payments arising during the deferral period, estimated at about US$3.2 billion. As explained above, the authorities are actively engaged in seeking a restructuring of sovereign obligations to private creditors and facilitating corporate debt restructuring so as to normalize the arrears situation as soon as possible. Paris Club creditors have already signaled their preparedness to provide general financing assurances for the program;[17] and the authorities will continue to collaborate closely with the World Bank and the IDB.

B. Exceptional Access Criteria

49. **The case for exceptional access based on the consideration of the four substantive exceptional access criteria is as follows:** [18]

- **Exceptional balance of payments pressures in the capital account.** The exceptionally high access proposed under the new program (424 percent of quota) reflects the large financing needs that Argentina faces over the next three years. The external financing gaps projected over the program period mainly reflect the need to restructure public and private debt and to rebuild reserves. The balance of payments projections are based on the assumption that it will take time to normalize relations with the international community and establish confidence.

[16] This includes a repurchase expectation amounting to the equivalent of SDR 198 million that arises on September 19, 2003. This extension of this repurchase expectation is being proposed for Board approval in a separate paper because it arises prior to the likely date of Board consideration of this paper.

[17] In a meeting on September 11, the Paris Club agreed to provide general financing assurances that would cover a rescheduling of arrears and principal falling due during the period of the arrangement, although the specifics would be addressed at the time of the negotiations.

[18] See the Acting Chairman's Summing Up of: "Review of Access Policy Under the Credit Tranches and the Extended Fund Facility, and Access Policy in Capital Account Crises—Modifications to the Supplemental Reserve Facility and Follow-Up Issues Related to Exceptional Access Policy," BUFF/03/28, March 5, 2003. In the Board meeting on access policy, Directors recognized that some of the substantive criteria for exceptional access will generally not be met in cases where a debt restructuring is needed.

- **Debt sustainability analysis.** Reflecting the need for debt restructuring, Argentina does not meet the debt sustainability and external financing criteria for exceptional access. Under the program, the authorities have committed to engage in good-faith negotiations with their private creditors on the formulation of a debt restructuring proposal.

- **Expectation of re-entry to capital markets.** Argentina's re-entry to international capital markets in the period of the proposed arrangement is unlikely. As such, a significant primary surplus and continued support from multilateral institutions will be required for some time to close projected external and fiscal financing gaps.

- **Strong program design and implementation prospects.** The program has yet to be fully elaborated and key differences of view with the authorities may put at risk program implementation prospects. The fact that important fiscal, banking, and other structural reforms will only be elaborated later in the program is a key program weakness, especially given the program's front-loaded phasing.

C. Phasing

50. **Purchases under the program are phased to avoid linkage of disbursements with repurchases, as well as to associate key purchase dates with structural conditionality.** Both considerations are crucial for the credibility of the program and for establishing an incentive structure under the program that would encourage the authorities to carry forward the critical structural reform agenda. At the same time, the proposed phasing is consistent with the reserve objectives of the program. Thus, during the first year of the arrangement, Fund exposure would decline by about US$800 million (Text Table D). This is largely recouped in September 2004, the start of the second year of the program, although net purchases would still remain slightly negative at that point. The fourth program review in September 2004 would be completed only if an acceptable 2005 budget is submitted to congress, with agreed tax reform and approval of the intergovernmental legislation. Net payments to the Fund (including charges) over the period of the arrangement are estimated at about US$1.8 billion.

Text Table D. Phasing Under the SBA, 2003-06
(In billions of U.S. dollars)

	Repurchases 1/	Purchases	Net purchases	Net payments 2/
Total arrangement	12.5	12.5	0.0	-1.8
Arrangement years:				
Sept 2003-Aug 2004	7.3	6.5	-0.8	-1.3
Sept 2004-Aug 2005	2.9	3.2	0.3	-0.3
Sept 2005-Sept 15, 2006	2.3	2.8	0.5	-0.2

1/ Assumes that all repurchase expectations are converted to an obligations basis.
2/ Includes interest and charges (- implies payments to the Fund).

D. Capacity to Repay the Fund

51. **The Fund will remain highly exposed to Argentina for some time.**[19] If all resources available under the program are purchased as scheduled, outstanding Fund credit will remain at 517 percent of quota (about 8½ percent of GDP) at the end of the arrangement in September 2006 (Table 13). The Fund will account for about 15 percent of Argentina's external public debt. Payments to the Fund will be around 17 percent of exports of goods and services in 2004 and about 8 percent on average in 2005–06. This level of payments should be manageable provided the program is fully implemented and purchases from the Fund are made on time. Purchases under the program, however, will impose a heavy repayment burden for Argentina in 2007–08, when payments to the Fund are projected to increase to around 12½ percent of exports of goods and services and about 13 percent of federal government revenue. Reestablishing market access by that time will depend upon the success of the restructuring in reducing Argentina's debt ratio. Given the uncertainties that surround the prospects for market reentry, risks will remain high regarding the authorities' capacity to make scheduled repayments to the Fund at the conclusion of the proposed arrangement. Thus, the medium-term outlook assumes that, contingent on the normal applicable requirements for Fund support, including a satisfactory policy stance, Fund financial support to Argentina would likely continue for some time after the end of the proposed new arrangement, albeit on a generally declining scale (Annex II).

52. **Argentina's decision to briefly accumulate arrears to the Fund on September 9, 2003 also adds to these risks.** The decision to accumulate arrears was taken notwithstanding Argentina's relatively comfortable gross reserve position at that time. Argentina has now cleared these arrears, but the incident will have added to the risks to the capacity to repay the Fund.

53. **With the proposed arrangement for Argentina, a prolonged user of Fund resources, the Fund will be assuming somewhat larger risks than in other cases.**[20] Although appropriate country comparisons are difficult given the diversity of individual country circumstances, illustrative comparisons with the recent Fund-supported programs of Brazil (2002), Turkey (2002), Uruguay (2002), Ecuador (2000), and Russia (1998) indicate that, on average, in the year of approval of the arrangement and in the three subsequent years: (i) Fund credit outstanding in these countries remained at about 525 percent of quota, but a significantly smaller share of GDP (averaging about 5.5 percent of GDP); and (ii) repurchases absorbed a significantly smaller share of export receipts (about 5 percent on average), and about 10 percent of gross international reserves.

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[19] A fuller description of the risks to the Fund and the Fund's liquidity position are contained in a separate paper that is being prepared for Directors in accordance with the new exceptional access policy.

[20] See Table 14, which compares proposed access levels against a broader set of metrics, as required under the new exceptional access procedures.

E. Risks to the Program

54. **The main risk to the program is that key elements of fiscal and banking reforms that are crucial to sustainability will only be formulated at a later stage.** The authorities view this sequencing of actions under the program as necessary to develop a strong domestic consensus for the reforms and to facilitate their implementation. However, this approach carries many risks:

- The electoral cycle of ongoing congressional and gubernatorial elections, and the administration's need to consolidate its influence, constrains the room for maneuver presently, and creates uncertainties about the eventual political consensus for key parts of the program.

- In particular, there is the clear risk that the absence of up-front strong commitments masks fundamental differences of view with the staff on key policy areas which will only become apparent later.

- In the fiscal area, the lack of specific commitment on the medium-term fiscal effort involves large uncertainties and risks undermining the credibility of the debt restructuring strategy.

- A major risk—and source of market concern—is the authorities' strategy for restructuring their debt with private creditors. Good-faith efforts in pursuing the restructuring will be essential on the part of the authorities, and an early and sustainable restructuring is crucial to the ultimate success of the program.

- As a result, the program's reviews will be especially important. In the immediate future, the first program review (December 2003) will provide an early indicator of political commitment. At that time, the 2004 budget will be nearing congressional approval, and the authorities will need to identify measures to strengthen the banking system in light of *amparo*-associated losses.

- In subsequent reviews during 2004, the authorities will need to specify in detail their plans for intergovernmental relations reforms, tax reforms, and public bank reforms, among others. Importantly, the government will need to specify the primary surplus for 2005 based on specific debt restructuring assumptions.

F. Program Monitoring

55. **Given the high access and considerable risks, the program will be subject to close monitoring.** As indicated above, the burden on the program and financing assurance reviews will be high—much greater than under the transitional arrangement—especially as program policies will need to be strengthened over time. The first review will be bi-monthly followed by quarterly reviews, including financing assurance reviews, that will allow for a revision of the policy stance if necessary.

56. **Structural conditionality**: Structural performance criteria and benchmarks in the proposed program concentrate on the critical areas of fiscal reform, bank restructuring and improving the investment climate. Over the past nine months, Argentina has initiated reforms in these areas, but a large agenda remains. In the public sector, reforms concentrate on putting revenue collections on a firmer footing. Measures to strengthen tax compliance and tax administration are included in the first year of the program and further measures on tax policy reform and reform of intergovernmental relations will be specified at the time of the fourth review. Reforms in the financial system aim at addressing the difficulties that emerged from the 2001–02 crisis and improving the soundness of the banking system; they include the removal of temporary forbearance on private loan classification and provisioning, finalization of compensation to banks associated with asymmetric *pesoization* and indexation, and beginning the strategic review of public banks. To improve the investment climate and remove obstacles to sustained growth, the proposed program envisages strengthening creditors' rights and improving the regulatory framework for utility companies.

57. **Quantitative performance criteria are included on:** (i) the cumulative primary balance of the federal government; (ii) the stock of federal government debt; (iii) the stock of central bank NIR; and (iv) the stock of central bank NDA (augmented by quasi-monies). Indicative targets have been set for: (i) the cumulative overall cash balance of the federal government; (ii) the stock of domestic arrears of the federal government; (iii) the cumulative primary balance of the provincial governments; (iv) the stock of debt of the consolidated public sector; and (v) the monetary base (augmented by quasi-monies). An indicative target band on 2004 projected inflation has also been set.

58. **Continuous performance criteria are proposed as follows:** (i) on the non-accumulation of arrears to bilateral and multilateral creditors; (ii) on the prohibition of new tax amnesties; and (iii) the adoption of no statute or other legal instrument that provides a means for any involuntary suspension or other restraint of creditors' rights.

59. **The safeguard procedures implemented by the BCRA under the transitional program were in line with staff recommendations.** This will help provide the accounting and control of Fund resources. Close monitoring should also help further protect Fund resources.

VI. Staff Appraisal

60. **The crisis of 2001–02 has left Argentina, a prolonged user of Fund resources, with formidable economic problems and deep social divisions.** Given the extent of poverty and unemployment, the policymaking environment will remain difficult for some years. It will, thus, be crucial for the government to forge a strong social consensus in support of the adjustment and reform measures envisaged under the program.

61. **Good progress has been made in stabilizing the economic and social situation since the crisis.** However, the recovery is still narrowly based and exposed to many vulnerabilities. Macroeconomic policies under the transitional program succeeded in bringing back a measure of confidence that—along with a still depreciated real exchange rate—underpins the recent advances in growth and employment. From the viewpoint of medium-

term prospects, however, the implementation of structural policies under the transitional program was disappointingly slow, and there were several setbacks in developing the more favorable investment climate that is needed to broaden the base of the recovery and ensure its durability.

62. **To sustain growth and significantly reduce poverty, consistent implementation of a comprehensive reform and adjustment program is required.** Unless decisive progress is made in clearing the legacy of the crisis—including the large debt overhang, the breakdown of bank intermediation, tax distortions, and an uncertain investment climate—growth may quickly fade. The authorities' economic program appropriately gives priority to the issues of fiscal sustainability and normalization of relations with creditors, while moving ahead with a banking strategy, a new regulatory framework for utilities, and a wide range of supporting institutional reforms.

63. **The program's sequencing is designed to give sufficient time for both technical preparation of reforms and establishing broad ownership.** To be effective, the authorities will need to work closely with Fund and World Bank staff in elaborating the reform strategy during the course of program reviews. Staff would stress that in moving forward with reforms there is no further margin for delays in the schedule.

64. **Fiscal adjustment, which is at the core of the program, will be needed over a prolonged period to bring the public finances to a sustainable path.** While staff recognizes that fiscal targets for the medium term are difficult to specify in advance of a debt restructuring agreement, it is regrettable that the authorities felt unable to define more clearly the envelope of resources available from 2005 onward. In the staff view, a consolidated primary surplus well beyond the 3 percent of GDP planned for 2004 will be required to service debt, including obligations arising from the debt restructuring, in future years. It is essential that the authorities consider how such primary surpluses can be achieved. The risk that the primary surpluses will be insufficient to cover future restructured debt payments could reduce the chances of a successful debt restructuring.

65. **To protect social expenditures and allow higher public investment, fiscal consolidation will need to be based on a comprehensive tax reform.** It is not feasible to achieve the required higher medium-term primary surpluses entirely through rationalization of current expenditures, which are already highly compressed. Revenue measures will be needed and staff fully supports the authorities' initiative to improve the currently deficient tax administration. This, however, will need to be supported—at least from 2005 onward—with a broadening of direct and indirect tax bases and a reduction of tax exemptions. Within this framework, the distortive financial transactions tax and export tax should be phased out as quickly as possible.

66. **Provincial governments also need to contribute to greater fiscal effort, and this will require a reform of intergovernmental relations.** Following the upcoming provincial elections, a concerted effort will be needed to formulate appropriate proposals and secure an agreement with governors of provinces by early 2004. The envisaged reforms of the co-

participation law and the new fiscal responsibility law are politically sensitive areas, but critically important for the sustainability of medium-term public finances.

67. **The authorities should proceed as quickly as possible to conclude a sovereign debt restructuring consistent with medium-term sustainability.** Staff welcomes the authorities' indication that they wish to complete a restructuring by mid-2004 and notes also their commitment to keep staff informed of progress toward such an agreement. On this basis, and in light of the steps the authorities have taken thus far to begin to engage creditors in a collaborative process, as summarized above, staff is satisfied that the authorities have met the good-faith criteria established under the Fund's policy for lending into arrears, and urges the authorities to remain consistent with these criteria in the period leading up to the final exchange offer.

68. **There should be no further delay in the implementation of the banking strategy.** Particular attention should be paid to identifying offsetting measures to ensure banking system solvency, following the decision of the congress not to compensate for losses from *amparos*. The authorities should also make up for lost time in diagnosing the financial condition of the banking system and developing a comprehensive strategy for the private banks. While the staff welcomes the issuance of the bids for the due diligence of the two large public banks, much remains to be done in this area and the authorities are encouraged to move quickly to define the strategic role of the public banks and identify appropriate restructuring plans.

69. **Strengthening central bank autonomy is essential for the successful implementation of inflation targeting and restructuring of the financial system.** The establishment of a task force to make proposals on central bank autonomy should be used to generate a consensus within Argentina on the appropriate role of the central bank. The implications of separating bank supervision from the central bank should be studied carefully. There is a danger that such a move could disrupt the bank restructuring process at a crucial time in its implementation. If the decision is made to go ahead with a separate supervisory agency, the new institution should be given full independence and be mandated to oversee all aspects of financial sector supervision.

70. **The government will need to accord greater priority to establishing a conducive investment climate.** Winning back the trust of domestic and foreign investors will rest chiefly on the expectation that the rule of law will be upheld, contracts respected, and the rights of creditors and debtors alike protected. Improving the investment climate will also require a coordinated effort by the executive, congress, and the judicial system to avoid taking decisions that respond to vested interests.

71. **The problems of the utility companies should be addressed expeditiously within a transparent and time-bound framework.** Establishing an even-handed regulatory environment for the privatized utility companies is key to ensuring continued private investment in infrastructure capacity—which is needed for long-term efficiency gains and growth. In this context, the authorities are encouraged to work expeditiously with the utility

companies to renegotiate concessions and put in place a predictable mechanism for adjusting tariffs, which is needed to clarify the financial position of the companies and facilitate the restructuring of their high indebtedness. At same time, measures should be considered, in consultation with the World Bank, to avoid tariff adjustments imposing undue hardships on the poor.

72. **Full cooperation with the multilateral development banks will be important to secure necessary program financing**. Argentina will face large external financing needs in the years to come, notwithstanding a continued large current account surplus and further accumulation of arrears to the private sector. In the absence of access to international capital markets, Argentina will have to rely on financing from multilateral development institutions to support spending on infrastructure and the social safety net, if it is to avoid excessive dependence on central bank credit. The government is, thus, encouraged to work closely with the MDBs to ensure timely implementation of financing plans and associated policies. This will be needed to give assurances that, during the period of the proposed arrangement, Argentina will be able to meet prospective external financing needs.

73. **Staff supports the proposed program and recommends approval of the SBA and extension of the requested repurchase expectations, but recognizes that there are significant implementation and other risks.** Rigorous implementation of planned measures will be required for the program to achieve its objectives. So far as the implementation of structural policies is concerned, the authorities will need to improve performance relative to the transitional program. Significant risks also arise from the fact that key fiscal and banking reforms, crucial for sustainability, will only be fully elaborated and implemented at a later stage in the program. The discussions revealed differences of view between the authorities and staff—for instance, on medium-term primary surpluses and bank compensation policy—that will need to be addressed and appropriate policies adopted as the program progresses. While this will be challenging, the staff welcomes the authorities' demonstrated ownership of the program during the negotiations, as well as President Kirchner's own personal involvement in the process. Staff regrets that Argentina fell temporarily into arrears with the Fund and the authorities are strongly urged to remain current on their obligations in the future. Staff also recommends that the authorities continue with their practice of publishing staff papers so as to promote wider understanding of the program.

Box 1. Structural Performance Criteria and Structural Benchmarks: September 2003–March 2004

I. Performance Criteria

Continuous performance criteria

- Non-accumulation of arrears to bilateral and multilateral creditors (TMU, Section III).
- No new tax amnesties (MEFP ¶29).
- No statute or other legal instrument will be adopted that provides a means for any involuntary suspension or other restraint of creditors' rights (MEFP ¶50).

End-November 2003

- Congressional approval of tax administration reform legislation (MEFP ¶29).

End-December 2003

- Congressional approval of 2004 federal budget that is consistent with a primary surplus target of 2.4 percent of GDP in 2004 for the federal government (MEFP ¶12).
- All competitiveness plans to be eliminated (MEFP ¶12).
- Finalize the compensation to banks for losses associated with asymmetric *pesoization* and indexation (MEFP ¶39).
- Terminating temporary forbearance on private loan classification and provisioning (MEFP ¶41).
- Congressional approval of legislation on the framework for utility concessions (MEFP ¶45).

End-March 2004

- The federal government and a critical mass of provincial governors to reach agreement on the principles for intergovernmental reform and fiscal responsibility legislation (MEFP ¶31).
- Federal-provincial bilateral agreements shall become effective through their ratification by the provincial legislatures representing at least 100 percent of 2002 consolidated provincial deficit (MEFP ¶17).

II. Structural Benchmarks

Continuous

- Provide Fund staff with monthly information on provincial government financing with a delay of less than 55 days (TMU, Section III).

End-October 2003

- Government to announce the scope of public debt to be restructured, the treatment of initial claims and past due interest, and the general terms of the new debt instruments to be issued in the exchange (MEFP ¶19).

End-December 2003

- Report of working group on Insolvency Law reform (MEFP ¶48).

End-February 2004

- Complete selection of accounting and consulting firms to begin the strategic review of the two largest public banks (MEFP ¶38).

End-March 2004

- Working group charged with the design of reforms of the central bank charter to publish report containing its key findings and recommendations (MEFP ¶34).
- Launch of second tax administration reform focusing on improving customs administration and social security collections (MEFP ¶29).
- Elimination of arrears on VAT refunds to exporters (MEFP ¶13).

Box 2. Private Corporate Debt

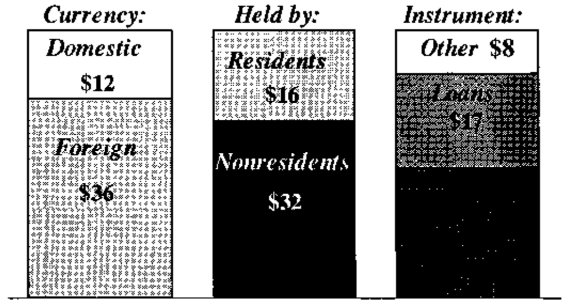
Around 65 percent of the roughly $50 bn. in private corporate debt is estimated to be nonperforming.

Table. Private Corporate Debt Estimates
(As of end-March 2003)

	Billions US$	Percent of 2003 GDP
Total	**47.8**	**37.9**
Bonds and securities	19.0	15.0
Commercial Banks	25.0	19.8
Official creditors & MDBs	3.1	2.5
Suppliers and others	0.8	0.6
Memorandum items		
External debt	31.6	25.1
Short-term	13.8	11.1
Medium- to long-term	17.8	14.3
Estimated troubled debt	28-33	22-26

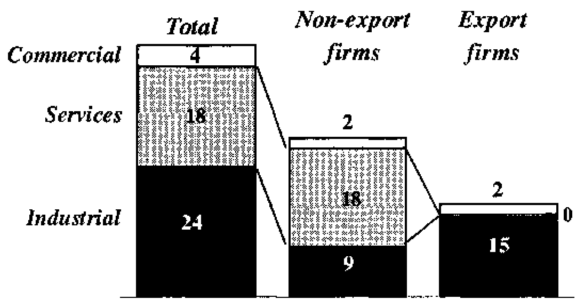
Roughly 75 percent of corporate debt is in fx, ⅔ is held by nonresidents, and about ½ is bonded debt

Private Corporate Debt
(March 2003, $48 billion or 37 percent GDP)

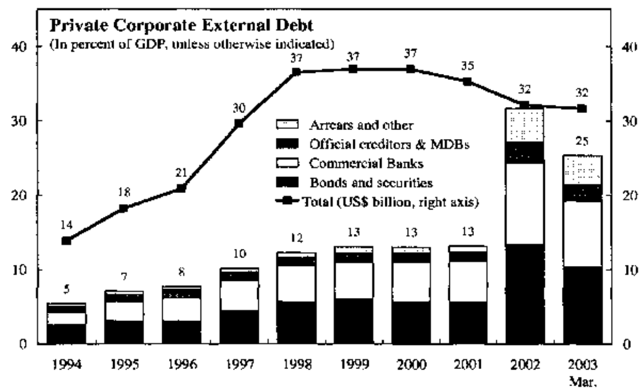


About ⅔ of private corporate indebtedness is owed by non-exporting firms.

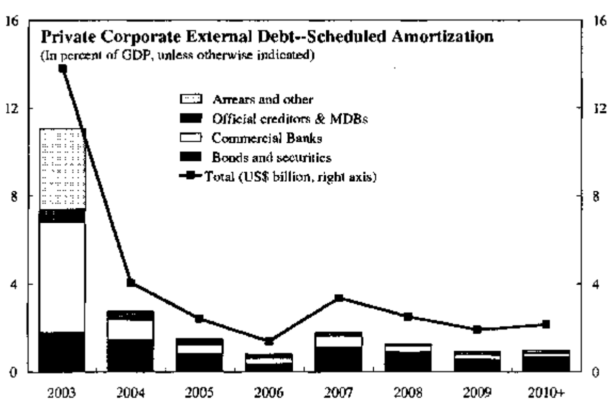
Structure of Private Corporate Debt
In billions of US dollars (based on 350 highly indebted firms)



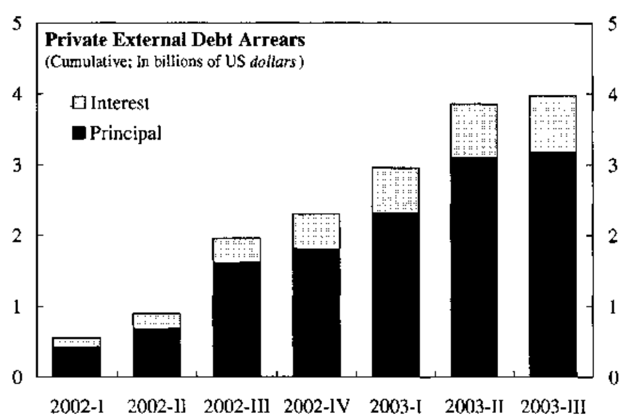
Despite some recent de-leveraging, the external corporate debt-GDP ratio has doubled from 2001.



While most external debt is of short-term maturity (especially bank loans), a large share is accounted for by arrears ...



...which continue to rise at a rate of 60 percent of debt falling due.



Box 3. Tax Administration Reforms

The authorities announced an important tax administration reform package on June 17, 2003, aimed at combating tax evasion and improving voluntary tax compliance. The measures—which are being implemented through a combination of legislation, executive decrees, and resolutions by the tax authority (AFIP)—aim at:

- **Increasing penalties for tax evasion, including prison sentences ranging from three to ten years.** In the case of false invoices, both the issuer and the user will be held responsible for the forgone tax revenue; fines for undeclared workers will be increased by assuming that the undeclared work resulted in under-declared income tax and VAT, which will be applied presumptively.

- **Making operational a new system of tax tribunals.** Three courts now handle new tax disputes, to which AFIP is expected to bring about 60 large cases by end-year.

- **Closing loopholes in the income tax by evaluating transfer pricing for exports involving related parties at market prices.** Special controls for tax havens and back-to-back credits will be implemented. The information gathered from satellite observation of agricultural land will be used for assessing underreporting of agricultural sales.

- **Strengthening compliance with the VAT.** The registration requirements for the VAT will be revamped with new registrants having to issue special invoices and withhold 100 percent of the VAT liability. 1000 new tax inspectors will be hired to check whether stores are issuing invoices, and the inspectors will have the power to impose fines or close the store.

- **Strengthening the tax regime for small taxpayers by increasing the presumptive rates.**

- **Improving the targeting of tax audits by creating a system for ranking the revenue risk of each taxpayer.**

- **Creating a unified registration system and database for businesses in conjunction with the Ministry of Justice and the provinces.** Access to the database will be controlled through the federal tax identification number, and the database will contain online information on the directors of each business to control the creation of fraudulent businesses.

- **Improving information sharing between the federal and provincial governments through the wider adoption of the federal tax identification number by the provinces.**

Table 1. Argentina: Net Debt Service to the IFIs, 2003-06
(In billions of U.S. dollars)

	2003			2004	2005	2006			Sep. 2003-
	Jan.-Aug.	Sep.-Dec.	Year			Jan.-Aug. 1/	Sep.-Dec.	Year	Aug. 2006 2/
IMF 3/									
A. Debt service	3.0	3.4	6.4	5.7	3.6	1.7	1.0	2.6	14.3
Principal 4/	2.5	3.2	5.7	5.2	3.0	1.1	0.8	1.9	12.5
Interest	0.5	0.2	0.7	0.5	0.6	0.5	0.2	0.7	1.8
B. Disbursements	3.0	2.9	5.9	5.3	2.8	1.5	0.0	1.5	12.5
C. Net debt service (A-B)	0.0	0.5	0.5	0.3	0.7	0.2	1.0	1.2	1.8
D. Credit outstanding	15.2	14.8	14.8	15.0	14.8	15.2	14.4	14.4	
World Bank									
A. Debt service	2.2	1.1	3.3	1.1	1.3	1.0	0.5	1.5	4.5
Principal	1.2	1.0	2.2	0.8	0.9	0.7	0.4	1.1	3.4
Interest	0.3	0.1	0.4	0.3	0.4	0.3	0.2	0.5	1.1
Arrears clearance	0.8	0.0	0.8	0.0	0.0	0.0	0.0	0.0	0.0
B. Disbursements 5/	1.5	1.0	2.5	0.8	0.9	0.7	0.4	1.1	3.4
C. Net debt service (A-B)	0.8	0.1	0.9	0.3	0.4	0.3	0.2	0.5	1.1
D. Credit outstanding	7.9	7.9	7.9	7.9	7.9	7.9	7.9	7.9	
IDB									
A. Debt service	2.0	1.0	2.9	0.9	1.1	1.2	0.6	1.8	4.1
Principal	0.8	0.8	1.6	0.4	0.6	0.9	0.4	1.3	2.7
Interest	0.4	0.2	0.6	0.5	0.5	0.3	0.2	0.5	1.5
Arrears clearance	0.7	0.0	0.7	0.0	0.0	0.0	0.0	0.0	0.0
B. Disbursements 5/	1.7	0.8	2.5	0.4	0.6	0.9	0.4	1.3	2.7
C. Net debt service (A-B)	0.3	0.2	0.4	0.5	0.5	0.3	0.2	0.5	1.5
D. Credit outstanding	8.6	8.6	8.6	8.6	8.6	8.6	8.6	8.6	

Sources: IMF, World Bank, and IDB.

1/ For the Fund, January-September.
2/ Figures for the Fund are for the period of the arrangement (September 2003-06).
3/ Assumes an exchange rate of US$1.3875 per SDR.
4/ Repurchases are on an obligations basis.
5/ Preliminary projections.

Table 2. Argentina: Proposed Schedule of Purchases Under the SBA, 2003-06

Date	Purchases In millions of SDRs	Purchases In percent of Quota	Purchases In millions of U.S. dollars 1/	Conditions 2/
Scheduled purchases	8,981.0	424.2	12,461	
2003				
September, 2003	1,830.0	86.4	2,539	Board approval of SBA
December 15, 2003	241.0	11.4	334	First review; end-October 2003 performance criteria
2004				
March 15, 2004	2,100.0	99.2	2,914	Second review; end-December 2003 performance criteria
June 15, 2004	500.0	23.6	694	Third review; end-March 2004 performance criteria
September 15, 2004	740.0	35.0	1,027	Fourth review; end-June 2004 performance criteria
December 15, 2004	490.0	23.1	680	Fifth review; end-September 2004 performance criteria
2005				
March 15, 2005	532.5	25.2	739	Sixth review; end-December 2004 performance criteria
June 15, 2005	532.5	25.2	739	Seventh review; end-March 2005 performance criteria
September 15, 2005	532.5	25.2	739	Eighth review; end-June 2005 performance criteria
December 15, 2005	432.5	20.4	600	Ninth review; end-September 2005 performance criteria
2006				
March 15, 2006	366.7	17.3	509	Tenth review; end-December 2005 performance criteria
June 15, 2006	366.7	17.3	509	Eleventh review; end-March 2006 performance criteria
September 15, 2006	316.6	15.0	439	End-June 2006 performance criteria
Memorandum items:				
2003	2,071.0	97.8	2,873	
2004	3,830.0	180.9	5,314	
2005	2,030.0	95.9	2,817	
2006	1,050.0	49.6	1,457	
Quota	2,117.1	100.0	2,937	

1/ Assumes an exchange rate of US$1.3875 per SDR.

2/ All purchases are subject to adherence to the continuous performance criteria. In addition, and for the period that sovereign arrears to private external creditors persist, purchases will be subject to financing assurances reviews.

Table 3. Argentina: Quantitative Performance Criteria and Indicative Targets, 2003-04 1/

(In millions of Argentine *pesos*, unless otherwise noted)

	Actual	Performance Criteria			Indicative Targets		
	End-Jun.	2003		End-Mar.	2004		
	2003	End-Oct.	End-Dec.	2004	End-Jun.	End-Sep.	End-Dec.
Fiscal targets							
1 Cumulative primary balance of the federal government (floor)	4,930	6,940	7,790	1,100	5,550	7,780	10,000
2 Cumulative overall cash balance of the federal government (indicative target)	1,423	600	350	-670	2,130	2,560	3,150
3 Federal government debt stock (ceiling, in billions of *pesos*)	438	520	530	540	550	560	570
4 Stock of federal government arrears (indicative target)	5,971	4,590	5,000	4,170	5,070	3,970	4,660
5 Cumulative primary balance of the provincial governments (indicative target)	1,556	...	1,480	180	1,290	2,230	2,480
6 Consolidated public sector debt stock (indicative target, in billions of *pesos*)	494	542	552	563	574	584	594
Monetary targets							
7 Stock of net international reserves of the central bank (in millions of U.S. dollars) (floor) 2/	-4,049	-4,500	-4,400	-4,350	-3,500	-3,300	-2,400
8 Stock of augmented monetary base (indicative target) 2/ 3/	43,272	44,305	47,770	46,260	49,320	49,625	53,805
9 Stock of augmented net domestic assets of the central bank (ceiling) 2/ 3/	55,014	57,355	60,530	58,875	59,470	59,195	60,765
10 Consultation mechanism on projected end-2004 inflation (indicative target) 4/							
Upper limit	...	...	11.0	11.0	11.0	11.0	...
Lower limit	...	...	7.0	7.0	7.0	7.0	...

1/ Continuous and structural performance criteria also apply. The performance criteria will be calculated as defined in the Technical Memorandum of Understanding.
2/ Actual figures for end-August 2003.
3/ Includes quasi-monies in circulation.
4/ As described in the Technical Memorandum of Understanding.

Table 4. Argentina: Selected Economic and Financial Indicators, 1999-2006

					Proposed Program			
	1999	2000	2001	2002	2003	2004	2005	2006
(Annual percentage changes; unless otherwise indicated)								
National income and prices								
GDP at constant prices	-3.4	-0.8	-4.4	-10.9	5.5	4.0	4.0	4.0
Consumer prices (average)	-1.2	-0.9	-1.1	25.9	14.4	9.4	8.6	7.1
Consumer prices (end-of-period)	-1.8	-0.7	-1.5	41.0	5.6	10.5	8.0	6.5
Social indicators 1/								
Population below poverty line (in percent)	27.1	29.7	35.4	53.0	54.7	...	...	...
Population below extreme poverty line (in percent)	7.6	7.5	12.2	24.8	26.3	...	...	...
Unemployment rate	13.8	14.7	18.3	17.8	15.6	...	...	...
External sector								
Exports, f.o.b. (U.S. dollars)	-11.8	13.0	0.8	-3.1	11.7	3.3	6.9	6.6
Imports, c.i.f. (U.S. dollars)	-18.8	-1.0	-19.5	-55.8	48.7	16.9	16.0	14.9
Export volume	-0.7	2.7	4.6	-0.3	5.2	6.9	7.6	6.0
Import volume	-13.9	-0.9	-17.3	-54.5	44.5	15.4	15.1	13.8
Terms of trade (deterioration -)	-1.7	9.6	-0.6	-1.8	4.8	-4.6	-1.4	-0.4
Real effective exchange rate								
Average (depreciation -)	11.1	-0.7	5.9	-55.7	14.2	9.3	4.6	5.0
Money and credit								
Net domestic assets of the financial system	9.2	11.3	2.3	57.8	2.2	3.9	...	...
Credit to the private sector	-2.3	-3.8	-17.6	-14.5	-16.2	3.4	32.0	24.2
Augmented broad money 2/	3.2	3.2	-16.5	24.6	26.3	17.6	15.9	14.5
Augmented broad money/GDP (in percent)	29.5	31.0	28.6	26.4	30.1	30.6	33.5	35.3
Interest rate (30-day deposit rate, in percent) 3/	10.2	11.3	15.7	39.1	4.3	...	...	...
(In percent of GDP)								
Public sector savings (accrual basis)	-2.2	-2.1	-5.2	-16.5	-4.2	-2.3	...	...
Consolidated public sector primary balance	-0.8	0.4	-1.3	0.9	2.5	3.0	...	...
of which : Federal government	0.4	1.0	0.2	0.9	2.1	2.4	...	...
Consolidated public sector overall balance	-4.2	-3.6	-5.9	-1.5	0.1	0.9	...	...
Revenues	24.3	24.6	23.7	22.9	25.3	25.3	...	...
Expenditures 4/	28.5	28.2	29.6	24.4	25.2	24.4	...	...
Gross domestic investment	18.0	16.2	14.2	12.0	16.6	18.8	...	...
Gross national savings	13.8	13.1	12.5	21.4	22.8	23.8	...	...
Current account balance 5/	-4.2	-3.1	-1.7	9.5	6.2	5.0	5.0	4.1
Public sector total debt (end-of-year) 6/	47.4	50.8	62.4	150.7	149.4	...	...	...
Public sector external debt (end-of-year) 6/	29.9	29.9	32.9	88.0	87.3	...	...	...
(In percent of exports of goods and nonfactor services; unless otherwise indicated)								
Outstanding use of Fund resources								
(in percent of quota at end-of-period) 7/	154.1	183.2	525.3	498.2	504.8	510.2	505.4	490.4
Gross international reserves, baseline 8/	27.3	26.9	14.9	10.5	13.6	15.7	16.7	18.4
In months of imports of goods and services	10.0	9.8	6.5	9.7	9.2	9.2	8.5	8.3
Nominal GDP (in billions of Arg$)	283.5	284.2	268.7	312.6	367.6	416.9	461.0	501.5
(In billions of U.S. dollars)	283.5	284.2	268.7	101.5	124.9	146.6	160.8	175.9

Sources: Ministry of Economy; Central Bank of the Republic of Argentina; and Fund staff estimates.

1/ 2003 data are at end-May, other data are end-October.
2/ Includes quasi-monies in circulation.
3/ 2003 data are as of end-August.
4/ Excludes interest due on nonperforming debt.
5/ Includes payments on unrestructured public and private debt.
6/ Figures are staff estimates based on authorities' data.
7/ 2006 end-period number reflects the assumption that no successor arrangement is in place after September 2006.
8/ In billions of U.S. dollars. Historical figures include foreign currency securities repoed by the BCRA to banks.

Table 5. Argentina: Summary Balance of Payments, 1999-2006

	1999	2000	2001	2002	Projections 2003	2004	2005	2006
	(In billions of U.S. dollars)							
Current account 1/	**-11.9**	**-8.8**	**-4.5**	**9.6**	**7.7**	**7.3**	**8.0**	**7.2**
Trade balance	-2.2	1.1	6.2	16.7	15.5	14.2	13.8	13.2
Exports f.o.b.	23.3	26.3	26.5	25.7	28.7	29.7	31.7	33.8
Imports c.i.f.	-25.5	-25.3	-20.3	-9.0	-13.2	-15.4	-17.9	-20.6
Services and transfers	-9.7	-9.9	-10.7	-7.1	-7.8	-6.9	-5.8	-6.1
Of which: net interest payments 1/	-5.9	-5.9	-7.4	-7.1	-7.0	-5.0	-3.5	-3.2
Capital and Financial Account	**14.0**	**7.8**	**-16.5**	**-25.9**	**-18.5**	**-18.6**	**-14.8**	**-9.0**
Net public sector capital	10.6	8.1	-2.1	-6.0	-7.9	-9.0	-6.2	-3.9
Direct investment	7.2	8.4	3.4	1.7	0.4	0.5	0.8	1.0
Other net private sector capital 2/	-3.9	-8.7	-17.8	-21.6	-11.0	-10.1	-9.3	-6.1
Overall balance	**2.1**	**-1.0**	**-20.9**	**-16.3**	**-10.8**	**-11.3**	**-6.8**	**-1.9**
Financing	**-2.1**	**1.0**	**20.9**	**16.3**	**10.8**	**11.3**	**6.8**	**1.9**
Net international reserves (increase -) 3/	-2.1	1.0	20.9	4.8	-2.8	-1.9	-1.1	-2.2
Change in gross reserves	-1.1	0.4	12.0	4.4	-3.0	-2.1	-1.0	-1.7
Change in reserve liabilities (IMF)	1.0	-0.6	-8.9	-0.4	-0.2	-0.2	0.1	0.4
Purchases	0.0	2.1	10.6	0.0	5.9	5.3	2.8	1.5
Repurchases	1.0	1.5	1.6	-0.4	5.7	5.2	3.0	1.9
Exceptional financing	0.0	0.0	0.0	11.5	13.6	13.2	7.9	4.0
Arrears (before debt restructuring)	0.0	0.0	0.0	11.5	12.5	12.1	7.2	3.6
Rescheduling (official bilateral)	...	...	...	...	1.0	1.1	0.7	0.4
	(In percent of GDP, unless otherwise specified)							
Current account	**-4.2**	**-3.1**	**-1.7**	**9.5**	**6.2**	**5.0**	**5.0**	**4.1**
Trade account	-0.8	0.4	2.3	16.5	12.4	9.7	8.6	7.5
Exports, f.o.b.	8.2	9.3	9.9	25.3	23.0	20.2	19.7	19.2
Imports c.i.f.	-9.0	-8.9	-7.6	-8.9	-10.6	-10.5	-11.1	-11.7
External debt service ratio 4/	**100.3**	**105.2**	**108.4**	**98.4**	...	...	...	...
Of which: public sector debt	49.4	54.8	65.0	46.8	...	...	...	...
Memorandum items:								
Current account excluding interest payments on nonperforming debt, in percent of GDP	-4.2	-3.1	-1.7	13.7	9.4	7.4	6.8	5.8
Exports volumes, percent change	-0.7	2.7	4.6	-0.3	5.2	6.9	7.6	6.0
Imports volumes, percent change	-13.9	-0.9	-17.3	-54.5	44.5	15.4	15.1	13.8
Net international reserves 3/ 5/	8.7	8.3	0.4	-3.6	-0.7	0.5	1.0	1.9
LIBOR (six months U.S. dollar deposits)	5.5	6.6	3.7	1.9	1.3	2.0	4.5	5.5

Sources: Ministry of Economy and Fund staff estimates.

1/ Includes interest due on nonperforming debt but excludes interest on arrears.

2/ Includes errors and omissions.

3/ Gross reserves before 2002 include foreign currency securities repoed by the BCRA to banks. Fund repurchases are on an obligations basis. SDR amounts are converted to US dollars at a rate of 1.3875 per SDR.

4/ As percentage of exports of goods and nonfactor services.

5/ In months of imports of goods and nonfactor services.

Table 6. Argentina: External Financing Requirements and Sources, 2001-06
(In billions of U.S. dollars)

			Projections			
	2001	2002	2003	2004	2005	2006
Gross financing requirements	**58.8**	**31.7**	**31.3**	**29.8**	**24.7**	**21.5**
Current account deficit 1/	4.5	-9.6	-7.7	-7.3	-8.0	-7.2
Capital outflows	54.4	41.2	39.0	37.1	32.7	28.6
Public sector amortization	21.2	7.7	18.3	15.3	10.7	8.3
IMF	1.2	0.8	5.7	5.2	3.0	1.9
Multilateral loans	0.9	2.6	5.3	1.2	1.5	2.4
Official bilateral creditors	0.5	0.5	0.7	1.1	0.7	0.8
Bonds and notes	7.2	3.1	6.4	7.8	5.5	3.1
Other	11.5	0.7	0.2	0.1	0.1	0.1
Private sector amortization	17.0	20.0	14.5	14.4	13.9	14.3
Other private sector flows, net (+outflows) 2/	16.1	13.6	6.2	7.4	8.1	6.0
Available financing	**58.8**	**31.7**	**19.9**	**23.4**	**20.7**	**18.5**
Capital inflows	46.8	27.2	22.9	25.5	21.7	20.2
Foreign direct investment	3.4	1.7	0.4	0.5	0.8	1.0
Disbursements to public sector 3/	28.1	0.8	0.4	1.2	1.1	1.2
Private sector borrowing	15.3	13.2	9.5	11.6	12.6	14.4
Exceptional financing	0.0	11.5	12.5	12.1	7.2	3.6
Public sector arrears accumulation	0.0	7.8	7.6	8.9	5.8	3.6
Private sector arrears accumulation	0.0	3.7	5.0	3.2	1.4	0.1
Gross reserves accumulation (- increase)	12.0	4.4	-3.0	-2.1	-1.0	-1.7
Financing gap	**0.0**	**0.0**	**11.5**	**6.4**	**3.9**	**3.0**
Program financing	...	...	10.4	5.3	3.3	2.6
IMF	...	...	5.9	5.3	2.8	1.5
World Bank and IDB 4/	...	...	4.6	0.0	0.4	1.2
Rescheduling official bilateral	...	...	1.0	1.1	0.7	0.4

Source: Fund staff estimates based on BCRA data.

1/ Includes interest on nonperforming debt.

2/ Includes errors and omissions.

3/ Includes project loans by MDBs in 2004-06.

4/ Excludes project loans.

Table 7. Argentina: Consolidated Public Sector Operations, 1999-2004 1/

	1999	2000	2001	2002	2003 Jan.-Jul.	2003 Prog.	Prog. 2004
	(In billions of Argentine *pesos*)						
Revenues	**69.0**	**70.0**	**63.6**	**71.5**	**54.3**	**92.9**	**105.4**
Tax revenues	49.7	51.5	47.2	52.4	41.9	71.9	81.7
Social security contributions	10.9	10.7	9.6	9.7	6.8	11.5	13.0
Other revenues	8.4	7.7	6.8	9.4	5.6	9.6	10.7
Primary expenditures	**71.1**	**68.7**	**67.2**	**68.8**	**46.9**	**83.6**	**92.8**
Wages	26.6	26.6	26.4	26.2	16.7	29.3	32.2
Goods and services	6.8	6.0	6.3	6.3	4.7	8.3	8.7
Transfers to the private sector	27.2	26.8	25.7	28.6	19.4	33.9	35.7
Of which: federal pensions	17.4	17.4	16.6	16.5	10.8	18.8	20.6
Capital spending	5.6	4.3	3.9	2.8	2.3	5.3	7.9
Other	4.9	5.0	4.9	5.0	3.8	6.8	8.3
Primary balance	**-2.1**	**1.3**	**-3.6**	**2.7**	**7.3**	**9.3**	**12.5**
Interest cash	9.7	11.5	12.4	7.5	4.0	8.9	8.8
Overall balance	**-11.8**	**-10.3**	**-16.0**	**-4.8**	**3.4**	**0.4**	**3.7**
Arrears and interest capitalization 2/	...	...	1.8	49.4	11.7	21.3	21.2
Debt recognition 3/	1.9	1.6	1.6	0.5	2.4	6.1	4.5
Bank compensation 4/	0.0	0.0	0.0	48.2	0.0	17.2	0.0
Augmented overall balance	**-13.6**	**-11.8**	**-19.3**	**-103.0**	**-10.8**	**-44.1**	**-22.0**
	(In percent of GDP)						
Revenues	**24.3**	**24.6**	**23.7**	**22.9**	**14.8**	**25.3**	**25.3**
Tax revenues	17.5	18.1	17.6	16.8	11.4	19.6	19.6
Social security contributions	3.8	3.8	3.6	3.1	1.9	3.1	3.1
Other revenues	3.0	2.7	2.5	3.0	1.5	2.6	2.6
Primary expenditures	**25.1**	**24.2**	**25.0**	**22.0**	**12.8**	**22.7**	**22.3**
Wages	9.4	9.4	9.8	8.4	4.5	8.0	7.7
Goods and services	2.4	2.1	2.3	2.0	1.3	2.2	2.1
Transfers to the private sector	9.6	9.4	9.6	9.2	5.3	9.2	8.6
Of which: federal pensions	6.1	6.1	6.2	5.3	2.9	5.1	4.9
Capital spending	2.0	1.5	1.5	0.9	0.6	1.5	1.9
Other	1.7	1.8	1.8	1.6	1.0	1.8	2.0
Primary balance	**-0.8**	**0.4**	**-1.3**	**0.9**	**2.0**	**2.5**	**3.0**
Interest cash	3.4	4.1	4.6	2.4	1.1	2.4	2.1
Overall balance	**-4.2**	**-3.6**	**-5.9**	**-1.5**	**0.9**	**0.1**	**0.9**
Arrears and interest capitalization 2/	...	...	0.7	15.8	3.2	5.8	5.1
Debt recognition 3/	0.7	0.6	0.6	0.1	0.7	1.6	1.1
Bank compensation 4/	0.0	0.0	0.0	15.4	0.0	4.7	0.0
Augmented overall balance	**-4.8**	**-4.2**	**-7.2**	**-32.9**	**-2.9**	**-12.0**	**-5.3**
Memorandum item:							
Real primary spending (percent change) 5/	3.3	-2.5	-1.1	-18.6	3.6	6.2	1.5

Source: Ministry of Economy; and Fund staff estimates.
1/ Revenues and primary spending before 2003 include payments with bonds.
2/ Includes interest (arrears) on non-performing debt.
3/ Reflects the settlement of obligations in bonds, often as a result of judicial rulings.
4/ Compensation to banks for asymmetric *pesoization* and asymmetric indexation of balance sheets.
5/ Real spending is calculated as nominal spending deflated by the consumer price index.

Table 8. Argentina: Federal Government Operations, 1999-2004 1/

	1999	2000	2001	2002	2003 Jan.-Jul.	2003 Prog.	Prog. 2004
	(In billions of Argentine *pesos*)						
Revenues	**55.0**	**55.5**	**50.6**	**56.8**	**43.6**	**74.6**	**84.8**
Tax revenues	38.6	40.7	37.4	41.8	33.9	58.4	66.4
Social security contributions	10.9	10.7	9.6	9.7	6.8	11.5	13.0
Non-tax revenues	5.5	4.1	3.6	5.3	2.8	4.8	5.4
Primary expenditures	**54.0**	**52.7**	**50.0**	**53.8**	**38.1**	**66.8**	**74.7**
Primary expenditures (excluding provinces)	36.1	34.7	33.1	36.3	25.5	45.0	50.0
Wages	8.5	8.1	7.7	8.0	5.9	10.1	11.1
Goods and services	2.6	2.3	2.2	2.5	1.7	3.0	3.4
Pensions	17.4	17.4	16.6	16.5	10.8	18.8	20.6
Transfers to private sector	6.4	6.2	5.8	8.7	6.4	11.2	11.0
Capital	1.0	0.7	0.6	0.5	0.6	1.4	2.6
Other	0.1	0.1	0.1	0.1	0.2	0.5	1.3
Transfers to provinces	17.8	18.0	17.0	17.5	12.5	21.7	24.7
Primary cash balance	**1.1**	**2.7**	**0.6**	**3.0**	**5.5**	**7.9**	**10.1**
Interest cash	8.2	9.7	10.2	6.8	3.8	7.4	6.9
Overall cash balance	**-7.2**	**-6.9**	**-9.6**	**-3.8**	**1.7**	**0.4**	**3.2**
Interest capitalization	...	...	0.4	32.6	3.7	7.5	10.3
Accumulation of arrears 2/	...	...	1.4	16.0	7.4	12.7	10.2
Debt recognition 3/	1.9	1.6	1.6	0.5	2.3	5.7	2.9
Bank compensation 4/	0.0	0.0	0.0	48.2	0.0	17.2	0.0
Augmented overall balance	**-9.0**	**-8.5**	**-13.0**	**-101.1**	**-11.7**	**-42.7**	**-20.2**
	(In percent of GDP)						
Revenues	**19.4**	**19.5**	**18.8**	**18.2**	**11.9**	**20.3**	**20.3**
Tax revenues	13.6	14.3	13.9	13.4	9.2	15.9	15.9
Social security contributions	3.8	3.8	3.6	3.1	1.9	3.1	3.1
Non-tax revenues	1.9	1.4	1.3	1.7	0.8	1.3	1.3
Primary expenditures	**19.0**	**18.6**	**18.6**	**17.2**	**10.4**	**18.2**	**17.9**
Primary expenditures (excluding provinces)	12.7	12.2	12.3	11.6	6.9	12.2	12.0
Wages	3.0	2.8	2.9	2.6	1.6	2.8	2.7
Goods and services	0.9	0.8	0.8	0.8	0.5	0.8	0.8
Pensions	6.1	6.1	6.2	5.3	2.9	5.1	4.9
Private sector transfers	2.3	2.2	2.2	2.8	1.7	3.0	2.6
Capital	0.3	0.2	0.2	0.1	0.2	0.4	0.6
Other	0.0	0.0	0.0	0.0	0.1	0.1	0.3
Transfers to provinces	6.3	6.3	6.3	5.6	3.4	5.9	5.9
Primary cash balance	**0.4**	**1.0**	**0.2**	**0.9**	**1.5**	**2.1**	**2.4**
Interest cash	2.9	3.4	3.8	2.2	1.0	2.0	1.6
Overall cash balance	**-2.5**	**-2.4**	**-3.6**	**-1.2**	**0.5**	**0.1**	**0.8**
Interest capitalization	...	...	0.1	10.4	1.0	2.0	2.5
Accumulation of arrears 2/	...	...	0.5	5.1	2.0	3.5	2.5
Debt recognition 3/	0.7	0.6	0.6	0.1	0.6	1.5	0.7
Bank compensation 4/	0.0	0.0	0.0	15.4	0.0	4.7	0.0
Augmented overall balance	**-3.2**	**-3.0**	**-4.8**	**-32.4**	**-3.2**	**-11.6**	**-4.8**

Source: Ministry of Economy; and Fund staff estimates.

1/ Revenues and primary spending before 2003 include payments with bonds.
2/ Includes interest (arrears) on non-performing debt.
3/ Reflects the settlement of obligations in bonds, often as a result of judicial rulings.
4/ Compensation to banks for asymmetric *pesoization* and asymmetric indexation of balance sheets.

Table 9. Argentina: Provincial Government Operations, 1999-2004

	1999	2000	2001	2002	2003 Jan.-Jun.	2003 Prog.	Prog. 2004
	(In billions of Argentine *pesos*)						
Revenue	**31.8**	**32.5**	**29.9**	**32.2**	**19.9**	**40.1**	**45.3**
Tax	11.0	10.9	9.8	10.6	6.9	13.5	15.3
Nontax	2.9	3.6	3.2	4.1	2.4	4.8	5.2
Transfers from federal government	17.8	18.0	17.0	17.5	10.7	21.7	24.7
Primary spending (commitment)	**35.0**	**34.0**	**34.1**	**32.5**	**18.3**	**38.6**	**42.8**
Personnel	18.0	18.6	18.8	18.2	9.4	19.2	21.1
Goods and services	4.2	3.7	4.1	3.8	2.6	5.2	5.3
Private sector transfers	3.4	3.2	3.2	3.4	1.9	3.8	4.1
Transfers to municipalities	4.8	4.9	4.8	4.8	3.0	6.3	6.9
Capital	4.7	3.6	3.3	2.3	1.4	3.9	5.3
Primary balance (commitment)	**-3.2**	**-1.5**	**-4.2**	**-0.3**	**1.6**	**1.5**	**2.5**
Net arrears reduction (-, accumulation)	...	...	...	1.0	0.8	1.0	0.2
Primary balance (cash)	-3.2	-1.5	-4.2	-1.3	0.8	0.5	2.2
Interest (cash)	1.4	1.9	2.4	1.5	0.6	2.0	2.1
Overall cash balance	**-4.6**	**-3.3**	**-6.6**	**-2.8**	**0.2**	**-1.5**	**0.2**
Debt recognition expenditures 1/	...	...	...	...	0.0	0.4	1.6
Interest capitalization 2/	0.0	0.0	...	8.3	0.6	1.8	2.4
Interest arrears	0.0	0.0	0.0	0.8	0.6	1.0	0.7
Augmented balance	**-4.6**	**-3.3**	**-6.6**	**-11.9**	**-1.0**	**-4.7**	**-4.5**
	(In percent of GDP)						
Revenue	**11.2**	**11.4**	**11.1**	**10.3**	**11.2**	**10.9**	**10.9**
Tax	3.9	3.8	3.6	3.4	3.9	3.7	3.7
Nontax	1.0	1.3	1.2	1.3	1.3	1.3	1.3
Transfers from federal government	6.3	6.3	6.3	5.6	6.0	5.9	5.9
Primary spending (commitment)	**12.4**	**12.0**	**12.7**	**10.4**	**10.3**	**10.5**	**10.3**
Personnel	6.4	6.5	7.0	5.8	5.3	5.2	5.1
Goods and services	1.5	1.3	1.5	1.2	1.4	1.4	1.3
Private sector transfers	1.2	1.1	1.2	1.1	1.1	1.0	1.0
Transfers to municipalities	1.7	1.7	1.8	1.5	1.7	1.7	1.7
Capital	1.6	1.3	1.2	0.7	0.8	1.1	1.3
Primary balance (commitment)	**-1.1**	**-0.5**	**-1.6**	**-0.1**	**0.9**	**0.4**	**0.6**
Net arrears reduction (-, accumulation)	...	...	...	0.3	0.4	0.3	0.1
Primary balance (cash)	-1.1	-0.5	-1.6	-0.4	0.4	0.1	0.5
Interest (cash)	0.5	0.7	0.9	0.5	0.3	0.6	0.5
Overall cash balance	**-1.6**	**-1.2**	**-2.5**	**-0.9**	**0.1**	**-0.4**	**0.0**
Debt recognition expenditures 1/	...	...	...	...	0.0	0.1	0.4
Interest capitalization 2/	0.0	0.0	...	2.7	0.3	0.5	0.6
Interest arrears	0.0	0.0	0.0	0.3	0.3	0.3	0.2
Augmented balance	**-1.6**	**-1.2**	**-2.5**	**-3.8**	**-0.5**	**-1.3**	**-1.1**
Memorandum items:							
Provincial financing (net)	1.6	1.3	2.6	0.7	-0.3	0.4	0.0
Amortization	...	-0.9	-0.8	-0.6	-0.8	-2.1	-0.6
Gross financing	...	2.2	3.4	1.3	0.6	2.5	0.6

Sources: Ministry of Economy; and Fund staff estimates.

1/ Reflects the settlement of obligations in bonds, often resulting from judicial rulings.

2/ Staff estimates.

Table 10. Argentina: Projected Fiscal Financing Gap, 2004 1/

(In billions of U.S. dollars)

A. Total financing needs:	**23.7**
Financing needs of federal government	**23.8**
Debt service to IFIs	7.6
BCRA (IMF debt service) 2/	5.7
World Bank	1.1
IDB	0.9
Bilateral debt service	1.4
Phase two debt service	12.6
Other private debt service 3/	1.9
Debt service to BCRA on quasi-money bonds	0.3
Net financing needs of provinces 4/	**-0.1**
B. Financing sources:	**11.9**
Primary balance of federal government	3.5
Program financing	6.6
BCRA (IMF disbursements)	5.3
World Bank	0.8
IDB	0.4
Rollover of bilateral debt	1.1
Rollover of domestic private debt 5/	0.5
Rollover by BCRA of quasi-money bonds	0.3
C. Financing gap (A-B) 6/	**11.7**
Memorandum item:	
Financing gap excluding phase 2 debt service	-0.9

Source: Fund staff estimates based on Ministry of Economy and Production data.

1/ Assumes that all debt service will be paid according to contractual obligations.

2/ Includes IMF repurchases on an obligations basis.

3/ Includes interest and amortization of phase 1 debt, bank compensation bonds, bonds issued in the deposit-bond exchange, tax payments with defaulted bonds, bonds issued in connection with court orders, and other debt-creating expenditures recorded below the line.

4/ Defined as debt service (net of intergovernmental debt service) minus primary cash balance.

5/ Assumes 100 percent rollover of phase 1 debt and bank compensation bonds.

6/ To be financed by debt restructuring and other sources.

Table 11. Argentina: Debt of the Consolidated Public Sector, 1993-2003 1/

(In billions of U.S. dollars at end period)

	1993	1994	1995	1996	1997	1998	1999	2000	2001	2002	2003 Jun. (Est.)	2003 Dec. (Proj.)
I. Total public debt (II + III)	75.3	88.1	97.0	107.0	110.2	122.2	134.5	144.5	167.8	152.9	171.2	186.6
II. Federal government (a+b)	69.6	80.7	87.1	97.1	101.1	112.4	121.9	128.0	144.5	137.3	152.6	179.5
(a) Medium- and long-term debt (i+ii)	69.6	80.7	87.1	97.1	101.1	109.1	117.7	122.9	137.7	136.2	150.7	177.3
(i) Treasury bills and bonds	47.5	56.4	58.3	68.8	74.1	78.2	85.8	93.1	55.1	75.6	84.2	114.9
(ii) Loans	22.1	24.3	28.8	28.3	27.0	30.9	31.9	29.8	82.7	60.6	66.5	62.4
Multilaterals	11.0	11.8	15.4	16.4	16.8	19.1	20.3	21.8	32.4	31.1	31.2	31.4
IMF	3.7	4.3	6.1	6.3	5.9	5.4	4.5	5.1	14.0	14.3	15.0	14.8
World Bank	3.6	3.8	4.5	5.3	5.8	7.4	8.6	9.1	9.7	8.5	8.1	7.9
Inter-American Development Bank	3.7	3.7	4.8	4.8	5.0	6.3	7.2	7.6	8.7	8.4	8.0	8.6
Official creditors	9.7	11.0	11.6	10.2	8.1	7.5	5.9	4.6	4.5	4.9	5.1	5.2
Paris Club	7.4	8.0	8.0	6.7	5.1	4.5	3.2	2.4	1.9	2.2	2.3	...
Other bilaterals	2.2	3.0	3.6	3.4	3.0	2.9	2.7	2.2	2.6	2.7	2.8	...
Guaranteed loans (Phase 1 debt)	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	42.3	22.8	28.2	23.8
Banks and others	1.5	1.6	1.8	1.7	2.2	4.3	5.7	3.5	3.6	1.8	2.0	2.0
(b) Short-term debt	0.0	0.0	0.0	0.0	0.0	3.3	4.2	5.1	6.7	1.1	1.8	2.2
III. Provincial governments 2/	5.7	7.4	9.9	9.9	9.1	9.9	12.6	16.5	23.3	15.6	18.6	7.1
Memorandum items:												
Arrears (US$ millions)	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	12.0	18.4	...
Principal	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	7.7	11.5	...
Interest	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	4.3	6.9	...
Total public debt (in percent of GDP) 3/	31.8	34.2	37.6	39.3	37.6	40.9	47.4	50.8	62.4	150.7	141.0	149.4
Federal government	29.4	31.3	33.8	35.7	34.5	37.6	43.0	45.0	53.8	135.4	125.7	143.7
Provincial governments	2.4	2.9	3.8	3.6	3.1	3.3	4.4	5.8	8.7	15.4	15.3	5.7
Percent of federal government debt in foreign currency	60.2	61.5	62.2	61.6	89.8	92.0	93.3	95.6	96.8	75.8	72.2	...

Source: Ministry of Economy and Production.

1/ Debt outstanding on a placement basis.

2/ Excluding intragovernmental obligations.

3/ The calculation uses US$ GDP of the preceding 12 months.

Table 12. Argentina: Summary Operations of the Financial System, 1999-2004 1/

	1999	2000	2001	2002	2003 Aug.	2003 Dec.	2004 Mar.	2004 Jun.	2004 Sep.	2004 Dec.
	(In billions of pesos, end of period)									
	I. Central Bank									
Net international reserves 2/	13.2	3.2	-7.1	-20.9	-11.7	-11.3	-11.2	-8.7	-8.1	-5.5
Net domestic assets	3.3	11.9	19.0	50.1	51.8	58.5	57.4	58.0	57.7	59.3
Credit to the public sector (net)	5.3	5.3	12.3	54.1	53.5	56.1	56.7	56.7	56.7	56.7
Credit to the financial sector (net)	1.3	1.0	-0.9	22.4	15.3	15.2	15.2	15.2	15.2	15.1
Central bank bonds (*Lebacs*)	...	...	...	-3.2	-8.3	-4.6	-6.2	-5.6	-5.9	-5.2
Official capital and other items (net)	-3.3	5.6	7.5	-23.3	-8.7	-8.3	-8.3	-8.3	-8.3	-7.3
Monetary base	16.5	15.1	11.9	29.2	40.1	47.2	46.3	49.3	49.6	53.8
Currency issued	16.5	15.1	11.0	18.8	24.9	30.6	29.6	31.6	31.6	34.4
Bank deposits at the central bank	...	...	0.9	10.3	15.1	16.5	16.6	17.7	18.0	19.4
	II. Banks and Nonbank Financial Institutions									
Net foreign assets	-2.1	2.4	-6.2	-27.4	-15.9	-9.2	-9.2	-5.7	-6.0	0.4
Net domestic assets	72.0	71.3	66.4	92.9	92.1	94.0	95.0	97.9	99.4	101.1
Credit to the public sector (net)	18.8	19.7	24.1	85.1	78.1	78.7	79.4	80.2	81.0	81.9
Credit to the private sector	70.6	67.9	56.0	47.8	40.1	40.1	39.4	40.7	41.5	41.5
Claims on the central bank (net)	3.8	3.5	4.7	-12.6	-4.6	-6.9	-5.1	-4.6	-4.1	-3.3
Capital and reserves	-16.9	-17.3	-16.5	-26.0	-22.6	-21.4	-20.8	-20.2	-19.7	-19.4
Other	-4.3	-2.5	-1.9	-1.5	1.1	3.4	2.1	1.8	0.7	0.5
Private sector deposits	69.9	73.7	60.2	65.5	76.2	84.7	85.8	92.1	93.4	101.5
Local currency	26.7	26.0	15.9	63.3	72.9	81.0	82.0	88.1	89.2	97.0
Foreign currency	43.2	47.7	44.2	2.2	3.4	3.7	3.8	4.1	4.1	4.5
	III. Consolidated Financial System									
Net foreign assets 2/	11.1	5.5	-13.3	-48.3	-27.6	-20.5	-20.4	-14.4	-14.1	-5.2
Net domestic assets	72.5	80.7	82.5	130.3	126.0	133.2	133.1	135.4	136.4	138.3
Credit to the public sector (net)	24.1	25.0	36.4	139.3	131.6	134.8	136.1	136.9	137.7	138.6
Credit to the private sector	70.6	67.9	56.0	47.8	40.1	40.1	39.4	40.7	41.5	41.5
Net capital, reserves, and other assets	-22.2	-12.2	-9.9	-56.8	-45.6	-41.7	-42.4	-42.1	-42.8	-41.7
Liabilities to the private sector (broad mone	83.6	86.3	69.3	81.9	98.4	112.6	112.7	121.0	122.3	133.2
Currency in circulation	13.7	12.6	9.1	16.4	22.2	27.9	26.9	28.9	28.9	31.7
Local currency deposits	26.7	26.0	15.9	63.3	72.9	81.0	82.0	88.1	89.2	97.0
Foreign currency deposits	43.2	47.7	44.2	2.2	3.4	3.7	3.8	4.1	4.1	4.5
Memorandum items:										
M1 3/	20.1	18.7	20.8	35.6	37.7	42.2	40.3	43.4	43.8	48.2
M3 4/	83.6	86.3	72.0	89.7	101.6	113.3	112.7	121.0	122.3	133.2
	(Annual percent change)									
Augmented monetary base 5/	0.8	-8.8	-3.0	152.2	50.6	29.6	20.9	14.6	12.6	12.6
M1 3/	-1.8	-6.8	10.7	71.4	24.9	18.7	15.3	19.4	13.9	14.1
M3 4/	3.2	3.2	-16.5	24.6	22.0	26.3	21.4	26.1	16.0	17.6
Credit to the private sector	-2.3	-3.8	-17.6	-14.5	-22.6	-16.2	-12.0	-4.7	1.3	3.4

Sources: Central Bank of the Republic of Argentina; and Fund staff estimates.

1/ Projections based on data up to July 2003. Foreign currency items in projections are valued at the program exchange rate of Arg$2.90 per U.S. dollar.

2/ Historical figures exclude foreign currency securities repoed by the BCRA to banks. BCRA liabilities have been revised from previous presentations to include all official foreign currency liabilities with original maturity of less than one year.

3/ Currency in circulation plus demand deposits plus quasi-monies in circulation.

4/ M1 as defined in footnote 3, plus foreign- and domestic-currency time and savings deposits.

5/ Monetary base plus quasi-monies in circulation.

Table 13. Argentina: Indicators of Capacity to Repay the Fund, 2003-10

(In billions of SDRs unless otherwise indicated)

	2003					2006						
	Jan.-Aug.	Sep.-Dec.	Year	2004	2005	Jan.-Sep.15	Sep.16-Dec.	Year	2007	2008	2009	2010
Net purchases	0.4	-0.3	0.1	0.1	-0.1	0.2	-0.6	-0.3	-3.1	-3.7	-2.2	-1.1
Purchases 1/	2.2	2.1	4.2	3.8	2.0	1.1	0.0	1.1	0.0	0.0	0.0	0.0
Repurchases 2/	1.8	2.3	4.1	3.7	2.1	0.8	0.6	1.4	3.1	3.7	2.2	1.1
Charges	0.4	0.1	0.5	0.4	0.4	0.3	0.1	0.4	0.3	0.2	0.1	0.0
Payments to the Fund (charges and principal)												
In billions of SDRs	2.2	2.4	4.6	4.1	2.5	1.1	0.6	1.7	3.4	3.8	2.3	1.1
In billions of U.S. dollars 3/	3.0	3.4	6.4	5.7	3.5	1.5	0.9	2.4	4.8	5.3	3.1	1.6
In percent of exports of goods and NFS	9.4	10.5	19.8	17.1	9.7	4.0	2.4	6.3	12.0	12.8	7.2	3.5
In percent of GDP	2.4	2.7	5.1	3.9	2.2	0.9	0.5	1.4	2.5	2.7	1.5	0.7
In percent of quota	101.9	115.3	217.2	193.3	117.8	51.0	30.6	81.6	162.0	180.7	106.7	0.1
In percent of gross international reserves	22.2	24.9	46.9	36.2	20.7	8.5	4.9	13.0	26.6	30.2	18.0	9.2
Fund credit outstanding (end period)												
In billions of SDRs	10.9	10.7	10.7	10.8	10.7	10.9	10.4	10.4	7.3	3.6	1.4	0.3
In billions of U.S. dollars 3/	15.3	14.8	14.8	15.0	14.8	15.2	14.4	14.4	10.1	5.0	1.9	0.4
In percent of exports of goods and NFS	47.7	46.1	46.1	45.1	41.8	40.1	38.1	38.1	25.4	12.0	4.5	0.8
In percent of GDP	12.3	11.9	11.9	10.2	9.2	8.6	8.2	8.2	5.4	2.5	0.9	0.2
In percent of quota	516.8	504.8	504.8	510.2	505.4	516.7	490.4	490.4	342.7	169.5	65.9	12.0
In percent of gross international reserves	112.7	109.0	109.0	95.4	88.9	86.2	78.1	78.1	56.3	28.3	11.1	2.0

1/ Assumes that all puchases are made under the three-year SBA.
2/ Excludes repurchase expectations converted to an obligations basis
3/ Projections assume an exchange rate of US$1.3875 per SDR.

Table 14. Argentina: Proposed Access, 2003

	Proposed Arrangement	High-Access Cases 1/ Proposed Arrangement (Percentile)	20th Percentile (Ratio)	80th Percentile (Ratio)	Average	Normal Access Cases Proposed Arrangement (Percentile)	20th Percentile (Ratio)	80th Percentile (Ratio)	Average
Access									
In millions of SDRs	8,981	55	3,048	14,635	9,232	100	33	401	379
Average annual access	141	23	124	434	265	100	21	51	40
Total access in percent of: 2/									
Actual quota	424	36	302	790	634	100	32	75	63
Calculated 11th review quota	258	64	101	414	247	100	13	42	32
Gross domestic product	10	89	3	7	6	100	1	3	2
Gross international reserves	92	76	27	121	80	91	5	47	46
Exports of goods and nonfactor services	39	77	11	43	30	100	2	7	6
Imports of goods and nonfactor services	71	86	14	49	35	100	2	7	5
Total external debt stock	9	52	5	15	11	88	2	7	5
M2	20	79	4	18	18	89	1	13	120

Proposed phasing (in percent of quota) 3/	Year 1	Year 2	Year 3
SBA/EFF	221	108	95

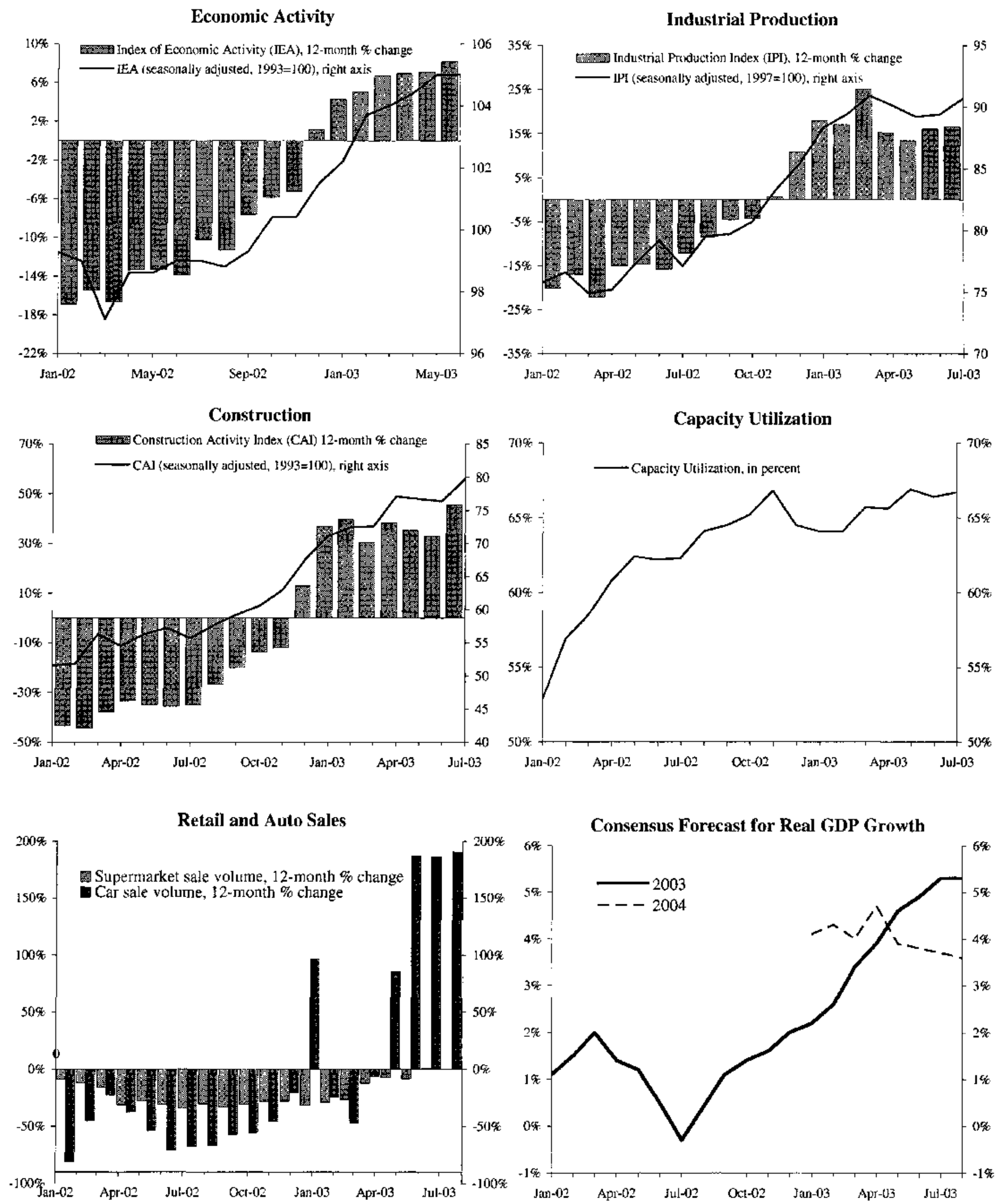
Source: Executive Board documents, MONA database, and Fund staff estimates.

1/ High access cases include all available data at approval and on augmentation for the 22 requests to the Board since 1994 which involved the use of the exceptional circumstances claus Exceptional access augmentations are counted as separate observations. For the purpose of measuring access as a ratio of different metrics, access includes augmentations and previou drawn amounts.

2/ The data used to calculate all ratios is the projection, at the time of program approval, for the year in which the program is approved.

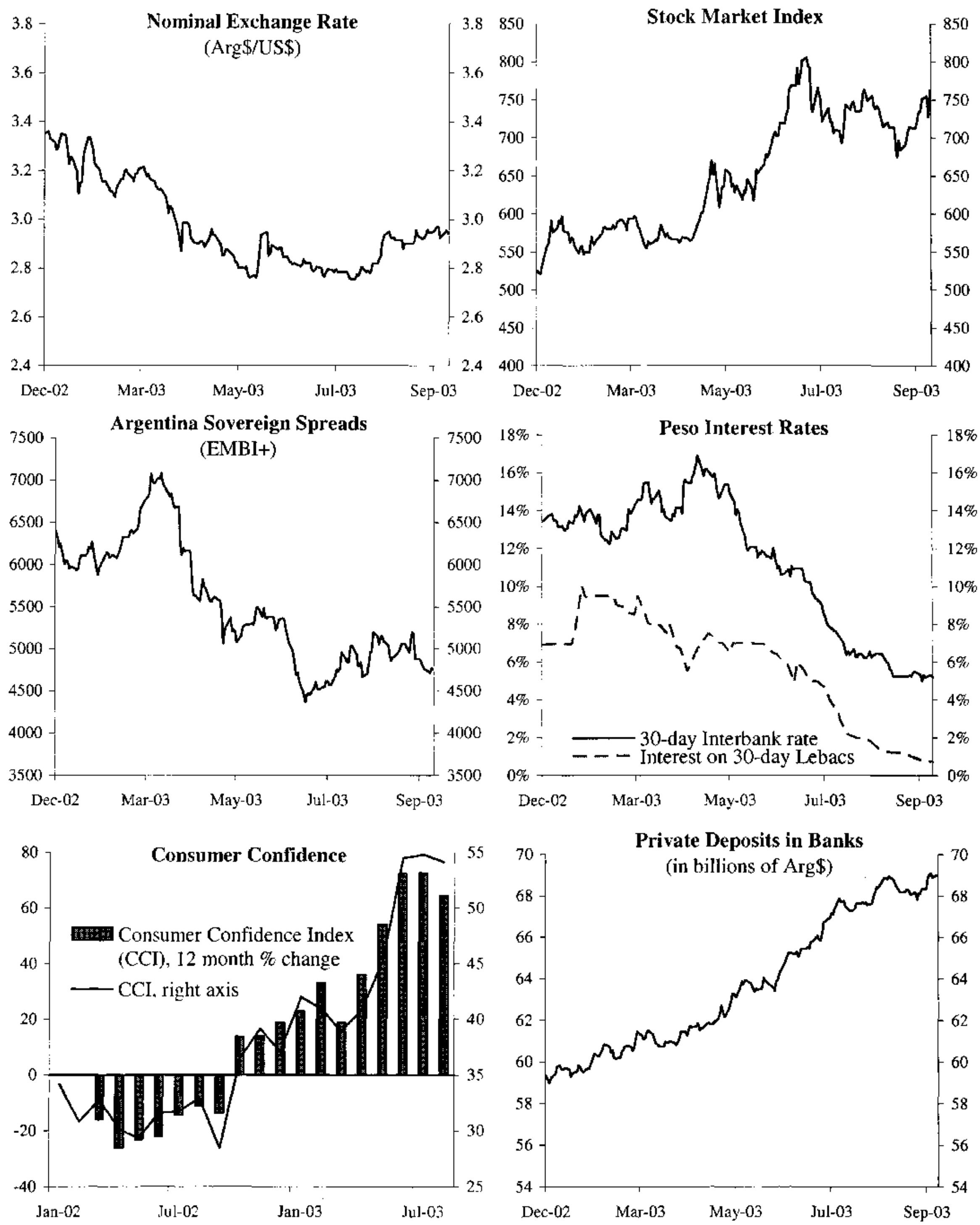
3/ Phasing is based on program years.

Figure 1. Argentina: Indicators of Real Activity



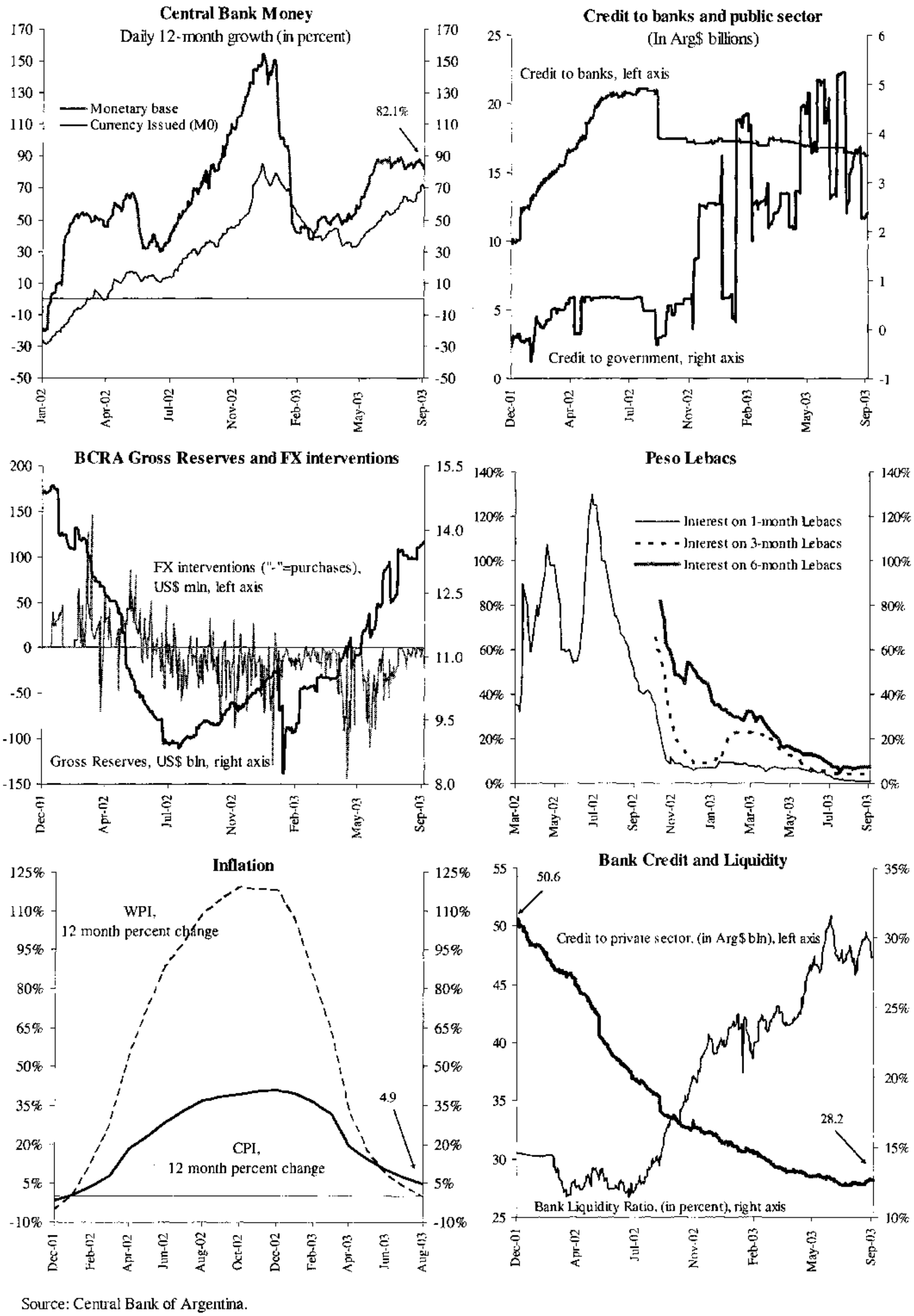
Sources: Ministry of Economy of Argentina; and INDEC.

Figure 2. Argentina: Confidence Indicators



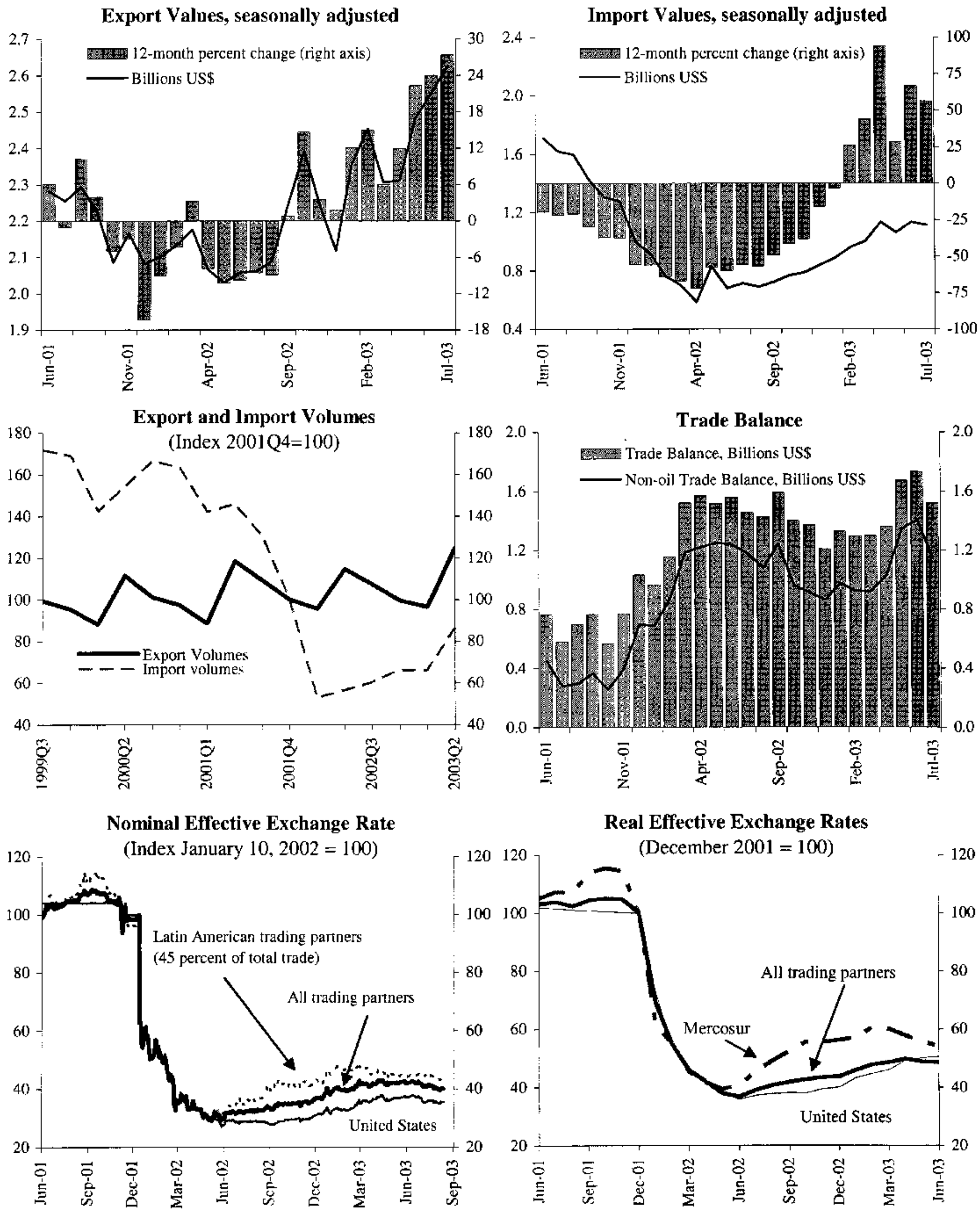
Source: Central Bank of Argentina, Ministry of Economy, and INDEC.

Figure 3. Argentina: Recent Monetary Developments



Source: Central Bank of Argentina.

Figure 4. Argentina: External Sector Developments



Sources: Argentina Ministry of Finance; and staff estimates.

BANKING SYSTEM: RECENT DEVELOPMENTS AND PROSPECTS

I. LEGAL, REGULATORY, AND INSTITUTIONAL DEVELOPMENTS

1. **Most restrictions on bank deposits were lifted in the first half of 2003.** Limits on the withdrawal of sight and saving deposits (the *corralito*) were lifted in December 2002 and, in April 2003, most remaining reprogrammed time deposits (the *corralón*) were freed. As a result, by end-August 2003, only around 9 percent of total deposits were subject to withdrawal restrictions.[1]

2. **Prudential rules were revised during the first half of 2003.** The central bank issued regulations that: (i) established a limit on banks' open foreign exchange positions equal to 30 percent of capital; (ii) introduced triggers for access to emergency liquidity assistance, while retaining broad discretionary powers for the BCRA board; (iii) phased in the market valuation of government bonds and loans and introduced limits on exposure to the public sector; (iv) eased private loan classification and provisioning rules through end-2003; (v) phased in over five years the recognition of losses from *amparos*;[2] and (vi) lowered the capital adequacy ratio from 11.5 to 8 percent, and phased in over five years the requirements for interest rate risk and exposure to the public sector.

3. **Legal amendments to the Financial Institutions Law (FIL) and central bank charter were approved by congress in September 2003.** The amendments to the FIL strengthened the central bank's tools for bank resolution, including through: (i) facilitating asset transfer from failed banks to financial trusts; (ii) establishing asset valuation rules; (iii) accelerating procedures for the appointment of receivers for failed banks; (iv) imposing limits to the ability of the judiciary to reverse central bank decisions on asset transfers; and (v) introducing limited protection against civil suits for public officials. The central bank charter was also modified to clarify the central bank's authority to provide emergency liquidity support to banks.

4. **The institutional framework for bank restructuring was modified.** The authorities established a joint ministry of economy-BCRA financial system restructuring unit. The unit is to oversee the rehabilitation of banks that have needed extensive liquidity assistance.

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[1] In April 2003, depositors were offered a combination of cash, time deposits, and government bonds in exchange for deposits "reprogrammed" in 2002; depositors that did not participate in the exchange will have their deposits released according to the reprogramming schedule.

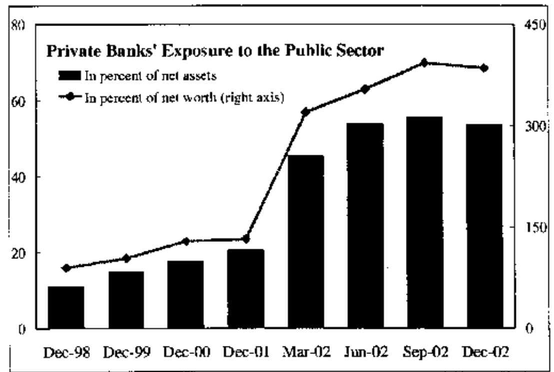
[2] In the event that banks are not compensated for losses associated with *amparos*, losses should be recognized upfront, resulting in many banks to become insolvent.

II. Financial Conditions of the Banking System

Changes in the financial position of banks in 2002

5. **During 2002, a number of policy actions and economic developments combined to result in a significant change in the structure of private bank balance sheets.**

- On the asset side, banks' exposure to the government more than doubled (to about half of assets), while credit to the private sector contracted sharply. The increase in government exposure was, by and large, linked to the issuance of compensation bonds for asymmetric *pesoization* of bank balance sheets.[3]



- The restrictions on, and reprogramming of, bank deposits eroded confidence in the banking system and, together with the sharp contraction in economic activity, resulted in a further disintermediation of domestic financial savings—accelerating a trend that had started prior to the crisis. Deposits fell sharply, necessitating higher reliance on liquidity support from the central bank.[4] Liquidity was, however, gradually rebuilt, in preparation for the liberalization of deposits, which began at the end of the year.

- Other factors that contributed to alter the structure of bank balance sheets were: (i) the sharp devaluation of the *peso* and the incomplete pass-through to domestic prices and wages; (ii) the asymmetric *pesoization* and the asymmetric indexation of bank assets and liabilities; (iii) the presence of external liabilities that could not be *pesoized*; and (iv) the sharp deterioration in asset quality. While, on aggregate, private banks' *long* net foreign exchange position remained broadly unchanged during the year, there were a number of banks that, by end-2002, carried a short foreign exchange position.

- By end-2002, public and domestic private banks had increased market share at the expense of foreign banks.

Share of bank assets (in percent)	2001	2002
Public banks	32	38
Domestic private banks	20	24
Foreign banks	48	38

[3] As of end-2002, about 35 percent of private banks' exposure to the government was accounted for by compensation bonds, and another 19 percent by guaranteed loans linked to the phase 1 debt swap.

[4] The simultaneous reduction in private sector credit and private deposits was also facilitated by the option offered to bank clients to cancel credits with restricted deposits.

Banks' financial conditions: June 2003

6. **In 2003 the banking system has shown some signs of recovery from the recent crisis.** Based on current prudential regulations, the banking system appears to be solvent and highly liquid. Based on bank financial statements for end-June 2003 (Table I.1):

- The net worth of the banking system is equivalent to 12.8 percent of unweighted assets;
- Private sector deposits have been returning to the banking system, growing by 9 percent in the first half of 2003;
- Liquidity ratios are high at 25 percent compared to 11 percent a year earlier.[5]

7. **However, the banking system remains highly vulnerable**:

- The data may not reflect the underlying financial condition of the banks because of forbearance on private loan classification and provisioning, the phase-in of market valuation of government exposure, and the delayed recognition of *amparo*-related losses;
- Financial losses are high, with the annualized return on assets for the first six months of 2003 estimated at negative 3.7 percent;
- These losses reflect: (i) provisioning for a high level of nonperforming loans; (ii) a large interest mismatch between assets and liabilities;[6] (iii) asymmetric indexation of bank assets; (iv) the progressive amortization of losses from *amparos*; (v) high and unremunerated reserve requirements; (vi) the taxation of checking account transactions, which contributes to low intermediation; (vii) high operating costs; and (viii) high foreign exchange losses due to *peso* appreciation as, on average, the system is long in dollars;
- Cash flows are low because a significant portion of bank income is accrued in the form of indexation;

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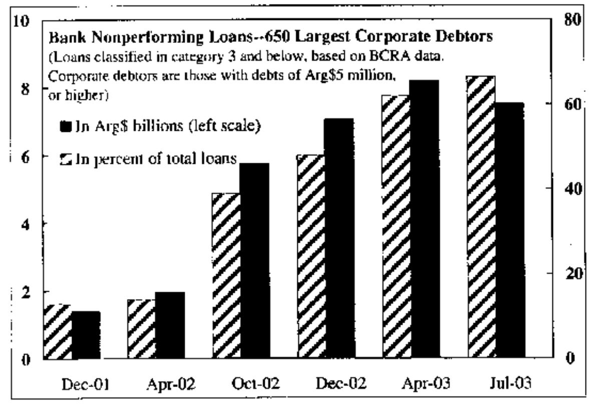
[5] Defined as the ratio of cash and reserves at the central bank to total deposits.

[6] The increased reliance on government bonds, which pay a coupon of between 2 and 4 percent and capitalize the inflation adjustment, and the progressive liberalization of deposits paying market rates have resulted in a mismatch between interest received and interest paid. This mismatch is more accentuated when measured on a cash basis, that is, net of the effect of inflation indexation. The size of the interest rate mismatch is sensitive to inflation and exchange rate developments. Given that banks are "long" on inflation indexation, and that dollar liabilities carry a much higher yield than dollar assets (comprising mostly dollar-denominated compensation bonds), *ceteris paribus*, the mismatch worsens if the *peso* depreciates, but improves if inflation is higher.

- Private sector credit has contracted sharply, reflecting lack of demand from creditworthy borrowers, high perceived credit risk by banks, and banks' reluctance to reduce liquidity due to uncertainties;



- Nonperforming loans are estimated at almost 50 percent of bank credit to the private sector (both on- and off-balance sheet), with the ratio estimated to be higher for the largest corporate borrowers;

- Exposure to the government is expected to remain high for some time, and currently amounts to 3½ times reported bank capital.

Banks' medium-term prospects

8. **The banking system also faces structural constraints that will affect the sector's medium-term prospects**. These could make the restructuring of the financial system a protracted process requiring strong policy implementation for a considerable period of time.

- *Bank intermediation.* Sustained economic growth will require improved financial intermediation. Private sector credit growth following deep banking crises is frequently slow to recover reflecting lack of investment opportunities or banks' efforts to recover and protect capital. Successful reintermediation will require sustainable macroeconomic adjustment, as well as efforts to return banks to soundness and profitability, including through careful management of costs and loan restructuring.

- *Exposure to the government.* The banking system is highly exposed to the public sector. As a percent of capital, total exposure increased from 160 percent at end-2000 to about 350 percent in June 2003. The expected slow recovery of private credit will make it difficult for the banking system to diversify assets. Moreover, a restructuring of sovereign debt held by banks could cause widespread insolvency.

- *Banking sector consolidation.* The banking system underwent considerable consolidation throughout the 1990s, with the total number of banks falling by half during the decade. Further consolidation, through mergers and acquisitions, may become necessary if private sector credit demand does not recover, or if operating costs cannot be lowered.

- *Role of the public banks.* The public banks are perceived by the public to have unlimited access to emergency liquidity and to be safe from closure. Efforts must be made to ensure that such banks do not impede competition within the banking system.

Table I.1: Summary Financial Statements of the Banking System, 2001–June 2003
(In billions of *pesos*; unless otherwise indicated)

	2001 1/	2002	June 2003 2/
Balance sheet			
Assets	124.0	187.4	181.9
Cash	9.9	15.9	20.6
Public sector bonds and loans	28.0	92.4	87.9
Federal and provincial	28.0	90.4	83.9
BCRA	0.0	2.0	4.0
Gross loans (excluding public sector)	50.2	39.6	35.6
Nonfinancial private sector, net	47.6	26.7	23.7
Loan loss provisions	-2.3	-10.6	-9.1
Other assets	38.3	50.1	48.0
Total liabilities	107.7	161.2	159.6
Deposits	66.4	74.8	82.7
Public sector	2.8	7.9	10.1
Private sector	63.6	66.6	72.3
BCRA liquidity assistance	4.5	20.3	20.5
External credit lines	8.1	25.7	21.3
Other financing	23.9	29.6	26.5
Other liabilities	4.8	10.7	8.5
Capital	16.3	26.3	23.5
Income statement			
Total profit/loss	-0.2	-18.2	-3.4
Financial income	15.4	48.3	7.0
Financial expenses	-8.8	-34.3	-7.9
Provisioning charges	-3.3	-10.1	-1.1
Administrative expenses	-7.3	-9.8	-3.6
Other income/expenses	3.7	-0.4	2.3
Taxes	-0.3	-0.5	-0.2
Inflation profit/loss 3/	0.0	-11.7	0.0
Financial soundness indicators (in percent)			
Capital to assets	13.2	14.0	12.8
Provisions to gross loans	18.1	32.5	31.2
Government exposure to assets (excluding BCRA)	22.6	48.3	45.8
Government exposure to capital (excluding BCRA)	171.5	344.4	357.6
Liquid funds to total deposits	14.9	21.2	24.9
ROA 4/	-0.2	-3.4	-3.7
ROE 4/	-1.5	-24.6	-28.9

Source: Banco Central de la República Argentina.

1/ Due to asymmetric *pesoization* in February 2002, data for 2001 are not comparable with those for 2002—03.
2/ Income statements for 2003 are cumulative for the first half.
3/ Inflation accounting was introduced in 2002 and affects 2002 results; it was subsequently removed.
4/ Does not consider inflation accounting. Returns for 2003 are annualized based on the first half. Assets are end-year.

DEBT SUSTAINABILITY AND THE SOVEREIGN DEBT RESTRUCTURING

1. This Annex discusses Argentina's public debt sustainability, and provides information on the projected availability of resources to meet debt service due to official and private creditors.

I. BACKGROUND

2. **In November 2001, Argentina embarked on a two-phase approach to debt restructuring to deal with a debt service burden that was no longer sustainable:**

- **The first phase ("phase 1") was aimed mainly at domestic creditors.** The exchange involved an offer to exchange all U.S. dollar and Argentine *peso* bonds for new domestic guaranteed loans. It was completed in December 2001 with about US$42 billion of federal government bonds exchanged, and was later extended to include Arg$23 billion of provincial debt. Debt restructured in phase 1 has continued to be serviced.

- **The second phase ("phase 2") was to be aimed mainly at foreign creditors.** However, on December 23, 2001, the authorities declared a moratorium on the service of bonds held by private creditors and of debt to most official bilateral creditors. As a result, the phase 2 restructuring was never initiated.

3. **Phase 2 debt is projected to reach US$89 billion by end-2003** (Table II.1). Most of this debt is held by external creditors—both institutional and retail—from Europe, Japan, and the United States. In August 2003, the authorities issued an executive decree that moved some US$13 billion of bonds held mainly by domestic pension funds from phase 1 into phase 2 (these bonds had an original value, after including arrears, of US$19–20 billion prior to the phase 1 exchange); the pension funds had not accepted the *pesoization* of their guaranteed loans denominated in foreign currency.

4. **The authorities intend to announce the broad terms of a restructuring offer to creditors at the 2003 Annual Meetings.** In particular, they have said that they will clarify the scope of debt to be restructured, the treatment of initial claims, including past due interest, and the general terms of the new restructured instruments.

II. DEBT FINANCING AND SUSTAINABILITY ANALYSIS

5. **The baseline scenario makes the following assumptions** (with details shown in Table II.2):

- A constant primary surplus of 3 percent of GDP from 2004–10.

- The program macroeconomic framework.

- Exposure to the IFIs is kept constant during the program period, and is then reduced by US$1.5 billion each year from 2007 onwards, of which US$1 billion relates to the

Fund and US$0.5 billion to the World Bank and IDB. A rollover of principal to Paris Club and other creditors throughout the projection period is also assumed.

- New domestic financing at market rates is assumed to be sufficient to roll over 100 percent of phase 1 loans, bank compensation bonds, and other provincial debt throughout the projection period.

- The BCRA is assumed to roll over 100 percent of maturing quasi-money bonds. Bonds issued for deposit conversion and to compensate civil servants for unpaid wages (averaging about US$1 billion a year) are assumed to be amortized on the scheduled dates.

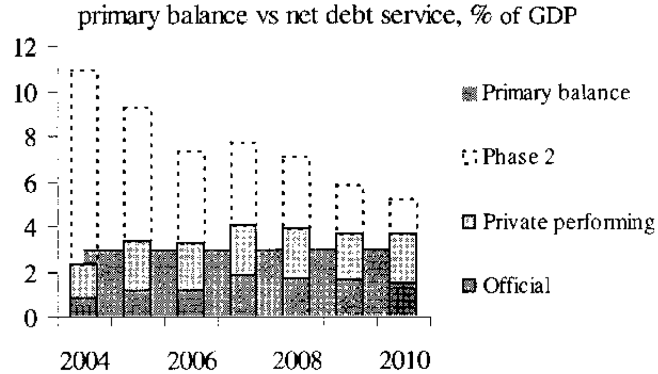
- No additional market access beyond these rollovers is assumed.

6. **On these assumptions, the baseline scenario gives the following results:**

- There would be large financing gaps during 2004–06, averaging 6 percent of GDP a year (assuming phase 2 creditors are paid on a contractual basis); these large gaps would persist in the outer years, averaging 3.5 percent of GDP a year (Table II.3). Excluding phase 2 debt service would reduce the financing gaps to zero on average during the program period and to 0.9 percent of GDP on average in the outer years.

Baseline Scenario

primary balance vs net debt service, % of GDP



- Net debt service to the official sector and on performing private debt would consume 3.3 percent of GDP on average over 2005–06, the final two years of the program period. IFIs and other official debt would account for one-third of this amount.

- The financing need for servicing the official sector and the performing private debt would rise to 4 percent of GDP in the outer years, reflecting declining IFI exposure from 2007 onwards.

- Thus, a primary surplus of 3 percent of GDP would not be sufficient to cover payments due on official debt and private performing debt after 2004; it would also leave no room for payments to phase 2 creditors (Text Figure).

- The assumed rollover of domestic debt cannot be taken as assured.

- Other ways to close the financing gaps (beyond increasing the primary surplus) include broadening the restructuring beyond phase 2 debt, and using international reserves.

III. Sensitivity Analysis

7. **The baseline scenario is sensitive to key assumptions** (Table II.4):

- A change in the primary surplus naturally has a one-for-one effect on the size of the financing gap.
- A 1 percentage point reduction in the growth rate during 2004–10, to 3 percent over the program period, and below 3 percent thereafter, would raise the financing gap by 0.1 percentage points of GDP on average a year during the program period and around 0.2 percent of GDP on average during 2007–10.
- A 10 percent step depreciation in the exchange rate in 2004 compared with the baseline would increase the financing gap by about 0.2 percent of GDP on average a year.
- A 3 percentage point higher interest rate applying to new market borrowing during 2004–10 would increase the financing gap by about 0.3 percentage point of GDP throughout the period.
- An assumption of 50 percent rollover by phase 1 and bank creditors, rather than 100 percent, would raise financing gaps by around 1 percent of GDP a year, while an assumption of 50 percent rollover by depositors, rather than zero, would reduce the financing gap by only 0.1 percent of GDP per year.
- Financing gaps could also be reduced by the resumption of new domestic and international market access before 2010.
- In summary, the above results show that the size of financing gaps is sensitive to various assumptions but, in the absence of changes in the primary surplus, it is difficult to envisage a scenario that allows performing debt and restructured phase 2 debt to be serviced on a sustained basis.

Table II.1. Projected Consolidated Public Debt: 2001-03

(In US$ billions, end period)

	2001	2002	2003 June Est.	2003 Dec Proj.
Total debt (I+II)	**167.8**	**152.9**	**171.2**	**186.6**
In percent of GDP 2/	*62.4*	*150.7*	*141.0*	*149.4*
I. Federal government	**144.5**	**137.3**	**152.6**	**179.5**
A. Official debt	36.8	36.0	36.3	36.6
1. Multilaterals	32.4	31.1	31.2	31.4
IMF	14.0	14.3	15.0	14.8
World Bank	9.7	8.5	8.1	7.9
IADB	8.7	8.4	8.0	8.6
2. Bilateral	4.5	4.9	5.1	5.2
B. Private creditors	42.3	98.4	111.7	136.1
1. Performing debt	42.3	37.0	43.2	46.6
a. Banks (Bodens), compensation for:	0.0	8.9	8.8	12.9
Asymmetric pesoization	0.0	0.0	6.4	8.3
Foreign exchange exposure (Cobertura bonds)	0.0	2.4	2.4	3.2
Asymmetric indexation	0.0	0.0	0.0	1.3
b. Depositors (Bodens)	0.0	5.3	5.7	7.2
Exchange of deposits for bonds	0.0	...	5.7	5.9
Compensation associated with deposit liberalization	0.0	...	0.0	1.3
c. Civil servants (compensation for 2001 13 percent wage cut)	0.0	0.0	0.6	1.2
d. Phase 1 debt 1/	42.3	22.8	28.2	25.4
2. Nonperforming (Phase 2) debt	...	61.4	68.5	89.4
C. BCRA (Quasi-monies bonds)	0.0	0.0	0.7	2.6
D. Other	65.4	2.9	3.8	4.2
Treasury bills, bonds and other short-term instruments	61.8	0.0	0.0	0.3
Central bank short-term financing	0.0	1.1	1.8	1.9
Banks and other	3.6	1.8	2.0	2.0
II. Provincial governments (net of intergovernmental debt)	**23.3**	**15.6**	**18.6**	**7.1**
Memorandum items:				
Nonperforming debt 3/	...	92.8	84.9	100.2
Performing debt	167.8	60.1	86.2	86.4
Multilaterals 4/	32.4	14.3	31.2	31.4
Private creditors, BCRA, and other	135.4	38.1	45.7	51.5

Sources: Argentine authorities; and staff projections.

1/ Includes provincial debt assumed by the federal government.

2/ The calculation uses US$ GDP of the preceding 12 months.

3/ This includes the sum of nonperforming Phase 2 debt, bilateral, bank and other debt, and assumes half of provincial debt is nonperforming.

4/ Reflects arrears to multilateral development banks at end 2002.

Table II.2. Baseline Assumptions

(In percent, unless stated otherwise)

	2004	2005	2006	2007	2008	2009	2010
A. Macro assumptions							
Real GDP growth	4.0	4.0	4.0	3.7	3.5	3.4	3.3
CPI inflation (average)	9.4	8.6	7.1	5.6	4.4	3.4	2.9
Nominal exchange rate (Arg$ per US$) average	2.84	2.87	2.85	2.89	2.91	2.94	3.00
B. Policy assumptions							
Primary balance (in percent of GDP)	3.0	3.0	3.0	3.0	3.0	3.0	3.0
Official rollover (in percent of principal)							
IMF	103	95	100	77	80	67	59
WB/IDB	100	100	100	80	76	74	76
Bilateral	100	100	100	100	100	100	100
Private sector rollover (in percent of principal)	72	76	85	87	87	92	91
Phase 1 debt	...	100	100	100	100	100	100
Bank compensation bonds	100	100	100	100	100	100	100
Deposit bonds	0	0	0	0	0	0	0
Compensation for civil servants	0	0	0	0	0	0	0
Quasi-money bonds and other provincial debt	100	100	100	100	100	100	100
Amortizations on new borrowing	...	100	100	100	100	100	100

Table II.3. Argentina: Medium-Term Consolidated Government Financing Projections Before Further Debt Restructuring, 2004-10

	2004	2005	2006	2007	2008	2009	2010
(In billions of US$, unless stated otherwise)							
A. Financing Needs	**24.8**	**24.1**	**24.1**	**27.8**	**28.2**	**28.7**	**26.5**
Total cash interest	6.7	7.1	8.0	7.8	7.5	7.2	7.3
Official	1.5	1.8	2.0	2.1	2.0	1.9	1.8
IMF	0.5	0.6	0.7	0.8	0.7	0.6	0.6
World Bank and IDB	0.7	0.9	1.0	1.0	1.0	0.9	0.9
Bilateral 1/	0.3	0.3	0.3	0.3	0.3	0.3	0.3
Debt held by private creditors	5.2	5.3	5.9	5.7	5.5	5.3	5.5
Performing debt	1.6	2.2	2.8	3.2	3.4	3.7	4.1
Non-performing (Phase 2) 2/	3.6	3.1	3.1	2.6	2.1	1.6	1.4
Quasi-money bonds	0.1	0.1	0.1	0.0	0.0	0.0	0.0
Amortizations	18.1	17.0	16.1	20.0	20.7	21.5	19.3
Official	7.5	5.2	5.0	7.9	8.5	5.8	5.5
IMF	5.2	3.0	1.9	4.3	5.1	3.1	2.4
World Bank and IDB	1.2	1.5	2.4	2.4	2.1	1.9	2.0
Bilateral	1.1	0.7	0.8	1.1	1.4	0.9	1.1
Debt held by private creditors	10.3	11.4	10.5	11.6	11.7	15.1	13.2
Performing debt	1.4	4.9	6.6	7.3	7.5	12.1	11.2
Nonperforming (Phase 2) 2/	9.0	6.5	4.0	4.3	4.2	3.0	2.0
Quasi-money bonds	0.3	0.4	0.5	0.5	0.5	0.5	0.5
B. Financing sources	**13.1**	**13.9**	**16.4**	**18.9**	**20.0**	**22.6**	**21.6**
New borrowing	8.7	9.1	11.1	13.3	14.1	16.4	15.1
Official	7.6	5.0	5.0	6.4	7.0	4.3	4.0
IMF	5.3	2.8	1.9	3.3	4.1	2.1	1.4
World Bank and IDB	1.2	1.5	2.4	1.9	1.6	1.4	1.5
Bilateral	1.1	0.7	0.8	1.1	1.4	0.9	1.1
Private 3/	0.8	3.6	5.6	6.4	6.5	11.5	10.6
Rollover of quasi-money bonds by BCRA	0.3	0.4	0.5	0.5	0.5	0.5	0.5
Primary balance (authorities' baseline scenario)	4.4	4.8	5.3	5.6	6.0	6.3	6.5
in percent of GDP	*3.0*	*3.0*	*3.0*	*3.0*	*3.0*	*3.0*	*3.0*
C. Financing gap (=A-B) 4/	**11.7**	**10.2**	**7.7**	**8.9**	**8.2**	**6.1**	**4.9**
in percent of GDP	*8.0*	*6.4*	*4.4*	*4.8*	*4.1*	*2.9*	*2.3*
D. Consolidated government debt 4/	**193**	**195**	**197**	**196**	**194**	**188**	**182**
in percent of GDP	*132*	*122*	*112*	*105*	*98*	*90*	*84*
Memo items:							
Primary surplus required to service official debt	1.3	1.9	2.0	3.6	3.5	3.4	3.3
in percent of GDP	*0.9*	*1.2*	*1.1*	*1.9*	*1.7*	*1.6*	*1.5*
Primary surplus required to service official and performing private debt	3.5	5.4	5.8	7.7	7.9	7.7	8.0
in percent of GDP	*2.4*	*3.3*	*3.3*	*4.1*	*3.9*	*3.7*	*3.7*
Financing gap before Phase 2 debt service	-0.9	0.5	0.5	2.1	1.9	1.4	1.5
in percent of GDP	*-0.6*	*0.3*	*0.3*	*1.1*	*0.9*	*0.7*	*0.7*
Total cash interest (in percent of GDP)	*4.6*	*4.4*	*4.5*	*4.2*	*3.8*	*3.5*	*3.4*
Of which: excluding Phase 2 interest payments	*2.1*	*2.5*	*2.8*	*2.8*	*2.7*	*2.7*	*2.7*
Interest capitalization (in percent of GDP)	*2.5*	*1.9*	*1.5*	*1.1*	*0.8*	*0.6*	*0.5*

Source: Fund staff estimates.

1/ Assumes a rescheduling in which amortization is fully rolled over.

2/ Excludes cash interest and amortization payment needs arising from principal and interest arrears.

3/ New borrowing results from the assumed full rollover at market interest rates of Phase 1 loans, quasi-money bonds and other provincial debt.

4/ Assumes financing gaps will be eliminated by debt restructuring or other means and therefore will not add to debt levels or create interest costs.

Table II.4. Argentina: Sensitivity of Financing Gaps

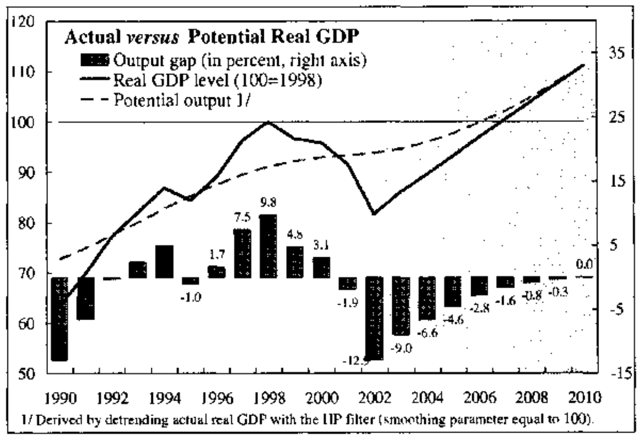
	2004	2005	2006	2007	2008	2009	2010
Financing gaps excluding phase 2 debt 1/ (In percent of GDP, unless otherwise indicated)							
Baseline scenario	**-0.6**	**0.3**	**0.3**	**1.1**	**0.9**	**0.7**	**0.7**
Sensitivity to primary surplus							
primary surplus higher by 1 percent a year	-1.6	-0.7	-0.7	0.1	-0.1	-0.3	-0.3
primary surplus lower by 1 percent a year	0.4	1.3	1.3	2.1	1.9	1.7	1.7
Sensitivity to GDP growth							
GDP growth higher by 1 percent a year	-0.7	0.2	0.2	0.9	0.7	0.4	0.4
GDP growth lower by 1 percent a year	-0.6	0.4	0.4	1.3	1.2	0.9	1.0
Sensitivity to nominal exchange rate							
Nominal exchange rate 10 percent more appreciated from 2004 onwards	-0.7	0.1	0.1	0.9	0.7	0.5	0.5
Nominal exchange rate 10 percent more depreciated from 2004 onwards	-0.5	0.6	0.5	1.4	1.2	0.9	1.0
Sensitivity to Libor rate							
Interest rates 3 percent higher	-0.3	0.6	0.5	1.4	1.2	0.9	1.0
Interest rates 1 percent lower	-0.7	0.2	0.2	1.0	0.9	0.6	0.6
Sensitivity to rollover rates							
Depositors roll over at 50 percent rather than 0 percent	-0.7	0.1	0.2	1.0	0.9	0.6	0.7
Banks and phase 1 rollover at 50 percent rather than 100 percent	-0.4	1.4	1.6	2.3	1.9	2.6	2.0
Memorandum item:							
Phase 2 contractual debt service	*8.6*	*6.0*	*4.0*	*3.6*	*3.2*	*2.2*	*1.6*

Source: Fund staff estimates

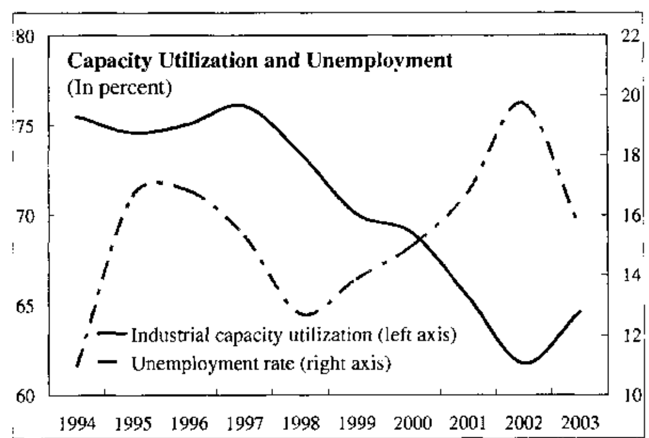
1/ On a contractual basis. Excludes cash interest and amortization payment needs arising from principal and interest arrears.

MEDIUM-TERM MACROECONOMIC FRAMEWORK

1. **The program's macroeconomic framework incorporates ambitious growth targets** (Figure 1). The economy is projected to expand by 5½ percent in 2003 and by about 4 percent a year in 2004–06, well above Argentina's long-term growth performance of 2 percent during 1968–2001. These above average growth rates are not, however, unprecedented for Argentina, and mainly reflect the economy's cyclical recovery from the sharp output contraction (18 percent) experienced during 1999–2002. Even under such a favorable outlook, however, output would still be over at least 3 percent below its pre-crisis peak by the end of the program in 2006.



2. **The near-term growth outlook is favorable**: (i) the economy has been expanding for four consecutive quarters and consumer confidence has been recovering strongly; (ii) the sizeable real depreciation of the *peso* and a subdued wage response have improved the competitiveness of exports and labor-intensive industries (such as machinery and textiles), and also encouraged significant import substitution; (iii) availability of credit is also not expected to restrain growth initially, as some firms have been able to use retained earnings and have diverted funds from debt service; and (iv) excess industrial capacity and high unemployment indicate that there should be few capacity or resource constraints to growth in the short run, although there are already indications of capacity constraints in some sectors (such as textile and machinery) that have been leading the recovery. However, in the absence of new investment, the limited installed capacity in the traded good sector could be a potential bottleneck to growth in the medium term.



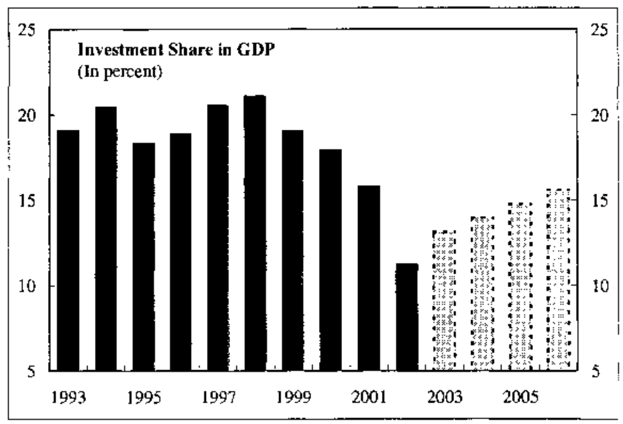
Text Table A: Contributions to Real GDP Growth

	Avg. 1991-01	Program 2003	Program Avg. 2004-06
	(In percent)		
Real GDP growth	3.5	5.5	4.0
Consumption	4.1	5.0	3.7
Investment	6.8	22.8	10.2
Exports of GNFS	8.1	6.3	6.3
Imports of GNFS	21.6	32.7	15.0
Contributions to GDP growth	3.5	5.5	4.0
Consumption	3.2	4.1	3.0
Investment	1.0	2.6	1.4
Net exports	-0.6	-1.2	-0.4

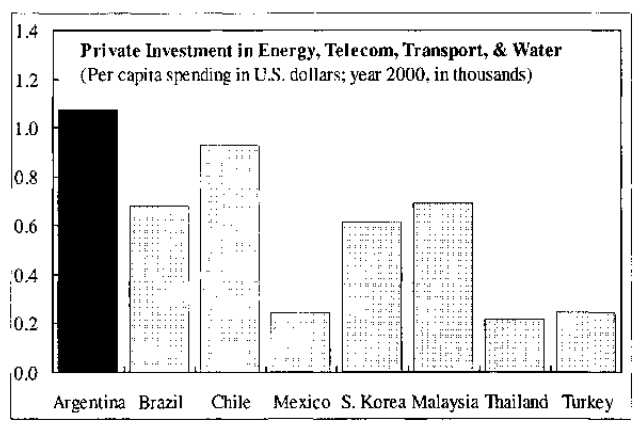
3. **In 2003, growth has been underpinned by a gradual recovery in consumption and pent-up investment demand**. After contracting by nearly 50 percent during 1999–2002, private investment is estimated to grow by 23 percent, driven mainly by restocking and

capacity building in import-substitution sectors (Text Table A). The upturn in consumption is estimated to be less marked (5 percent), reflecting a gradual recovery in real incomes. Even so, the contribution to growth of consumption is expected to be strong, owing to its large share in GDP (around 80 percent). The recent revival in exports (volumes are up 6 percent in the year to July) has made the recovery more broad based. However, the concurrent sharp increase in imports, mainly for capital and intermediate goods (over 45 percent in the year to July) will result in a negative contribution to growth from the external sector in 2003.

4. **Above-trend growth is projected also in 2004–06, on account of sustained capital accumulation in sectors that have benefited from the real depreciation of the *peso*.** Although Argentina's initial endowments for growth (such as infrastructure and education) are broadly favorable, its installed productive capacity is skewed towards services (about 70 percent of GDP) and exports in commodities and agricultural products (70 percent of total exports). Unlocking Argentina's growth potential will, therefore, require significant new investment to expand productive capacity in the traded goods sector and labor-intensive industries. During 2004–06, investment is projected to grow at over 10 percent a year in real terms, and the share of investment in GDP to rise, though by 2006 it would still be below pre-crisis levels. A greater outward orientation of the economy will also be needed for Argentina to fully realize the growth dividend from the sharp real exchange rate depreciation. The expansion of new capacity is expected to translate into higher export volume growth (in the order of 6–8 percent) during 2004–06.



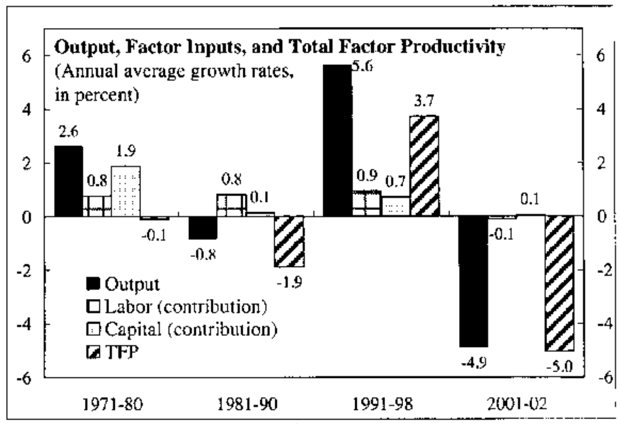
5. **A number of bottlenecks will need to be eliminated to sustain investment flows during the program.** Progress is needed on clearing the legacy of the crisis, including: (i) the restoration of financial intermediation and normalization of bank-client relations; (ii) higher national savings to compensate for the likely lack of access to international capital markets in the near term; (iii) the normalization of relations with external creditors; (iv) the introduction of a revised regulatory framework for utility companies;[1] and (v) a fundamental improvement in the business climate. Fiscal policy would also



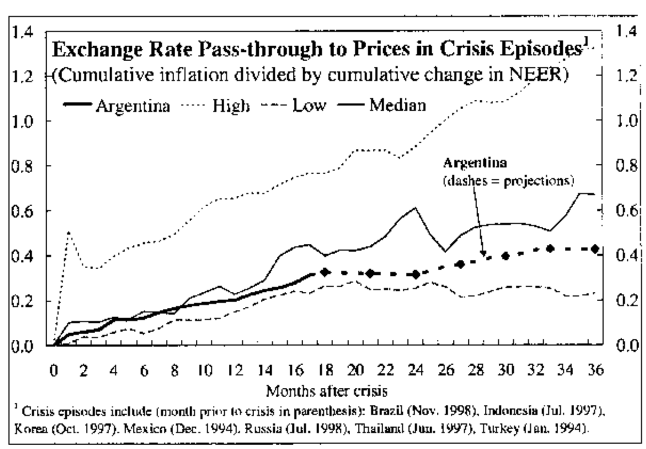
[1] The utility companies accounted for the majority of new private investment in the 1990s, but their investment programs have been halted pending resolution of the freeze on their tariffs.

facilitate higher domestic investment—indirectly by helping sustain the recent increase in national savings, and directly through an increase in public spending for infrastructure. However, the direct impact of public investment on overall growth would remain modest as public investment is relatively low in relation to GDP after the heavy privatization program of the 1990s.[2]

6. **In the post-program period, output growth is expected to decelerate towards its long-run potential of about 3 percent.** This will require reversing the sharp decline in total factor productivity observed during the crisis. Preliminary estimates suggest that total factor productivity growth of 1–1½ percent per year would be needed to support the envisaged output growth.[3] Even though this pace is much lower than that experienced in the nineties (5 percent), it is still well above the average of close to zero in the past 30 years. Cross-country empirical evidence suggests that reversing the recent sharp decline in productivity could be facilitated by greater macroeconomic and political stability, a further opening of the economy, higher spending on R&D and information technology, maintaining the private orientation in infrastructure investment, and institutional reform.



7. **The program targets underlying inflation in the single digit range and envisages a gradual appreciation of the real exchange rate.** The precise inflation path will depend on the extent of the recovery in real wages (which have fallen by about 20 percent from pre-crisis levels), the size of the prospective increases in utility tariffs, and the evolution of the exchange rate.[4] On current trends, average inflation in 2003 is projected to stay below 5 percent. And, while headline inflation is

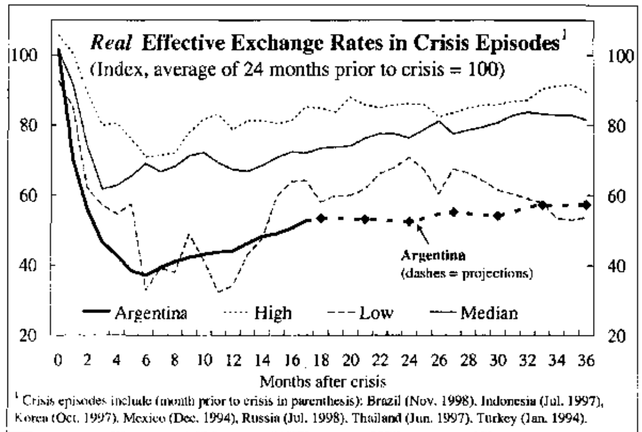


[2] Statistically, the contribution of infrastructure investment to growth is not large: every 1 percent increase in the stock of infrastructure is estimated to raise GDP by 0.23 percent.

[3] This assumes (i) net capital accumulation of around 1¾ percent a year (or, equivalently, gross investment growing at about 8 percent a year), which is slightly above the 1½ percent average observed in the nineties; (ii) labor input growth of about 1¾ percent, broadly in line with the average of the nineties; and (iii) a 0.52 labor factor share.

[4] Illustratively, a 10 percent increase in average tariffs could result in a 2 percent upfront rise in the price level. Including second round effects, the price increase could exceed 4 percent.

likely to rise in subsequent years—on account of adjustments in utility tariffs and some wage increase—underlying inflation is expected to remain moderate, in the 4–7 percent range, throughout the program period. With the nominal exchange rate assumed to remain broadly constant, the exchange rate pass-through to prices is estimated at around 45 percent by end-2004—somewhat below the pass-through observed in other recent crisis episodes. The incomplete pass-through reflects the persistence of large output gaps, the economy's low degree of openness, and the *pesoization* of most of the balance sheet of the corporate sector. During the program period, the real exchange rate is expected to appreciate, as domestic inflation remains temporarily above foreign inflation. Even so, by end-2006, the real effective exchange rate would still be over 35 percent more depreciated than in 2001.



Real **Effective Exchange Rates in Crisis Episodes**[1]
(Index, average of 24 months prior to crisis = 100)

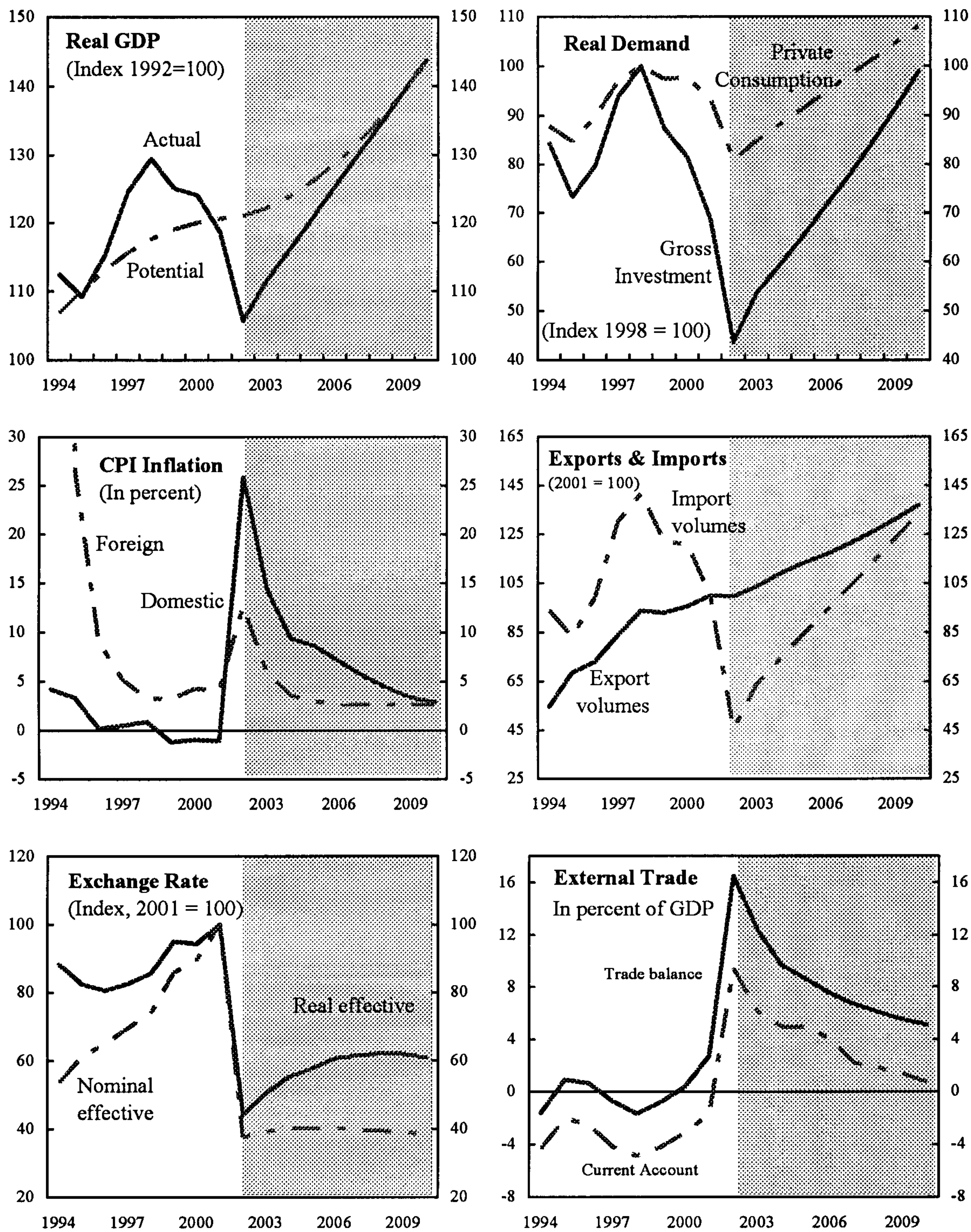
[1] Crisis episodes include (month prior to crisis in parenthesis): Brazil (Nov. 1998), Indonesia (Jul. 1997), Korea (Oct. 1997), Mexico (Dec. 1994), Russia (Jul. 1998), Thailand (Jun. 1997), Turkey (Jan. 1994).

8. **The trade surplus is projected to decline from 12½ percent of GDP in 2003 to 7½ percent by 2006**, as the output gap narrows and the real exchange rate appreciates. Export volumes are projected to grow by over 5 percent in 2003, accelerating to 6–7½ percent in 2004–06, as private investment recovers, industrial capacity is expanded, and access to credit by exporters improves. After falling by almost 70 percent during 1998–2002, import volumes are expected to rebound in line with the sharp recovery in investment and Argentina's high dependence on capital good imports—imports are projected to grow by over 44 percent in 2003, and about 14–15 percent in 2004–06.[5]

9. **Projections of private capital flows turn on the status of relations with external creditors, fiscal solvency, the pace of reforms, and business confidence**. Argentina is assumed to regain gradual access to credit markets after the completion of the sovereign debt restructuring. In the meantime, it is expected that firms that make progress in private external debt restructuring would be able to unlock new external financing flows. As such, new borrowing by the private sector is assumed to increase gradually over the medium term. Foreign direct investment is projected to gradually increase to about 1 percent of GDP per year—as confidence in doing business in Argentina is restored—but would remain significantly below its historical average of about 2¾ percent of GDP (1994–2000). During the life of the arrangement, therefore, debt-creating and other capital inflows will primarily originate from repatriation of flight capital and deposits of residents abroad (which are estimated at over $110 billion). International reserve accumulation during 2004–06 is projected at over US$4¾ billion, bringing gross reserves to about US$18½ billion by the end of the arrangement period (roughly equivalent to 8½ months of imports of goods and nonfactor services).

[5] Nearly 45 percent of Argentina's installed capital in machinery and transport is imported.

Figure III.1. Argentina: Medium-term Macroeconomic Framework



Source: Staff estimates.

FUND RELATIONS
(As of July 31, 2003)

I. Membership Status: Joined September 20, 1956, Article VIII

A. Financial Relations

II. General Resources Account:	**In millions of SDRs**	**In percent of Quota**
Quota	2,117.10	100.00
Fund holdings of currency	12,724.72	601.04
Reserve position in Fund	0.02	0.00

III. SDR Department:	**In millions of SDRs**	**Percent of Allocation**
Net cumulative allocation	318.37	100.00
Holdings	747.98	234.94

IV. Outstanding Purchases and Loans:	**In millions of SDRs**	**In percent of Quota**
Extended Fund arrangements	597.76	28.23
Stand-By Arrangements	10,116.79	477.86

V. Latest Financial Arrangements

			SDR Millions	
Type	**Approval Date**	**Expiration Date**	**Amount Approved**	**Amount Drawn**
Stand-By	01/24/03	08/31/03	2,174.50	1,948.30
Stand-By	03/10/00	01/23/03	16,936.80	9,756.31
Of which: SRF	01/12/01	01/11/02	6,086.66	5,874.95
EFF	02/04/98	03/10/00	2,080.00	0.00

VI. Projected Obligations to the Fund: (Under the Repurchase Expectation Assumptions) (SDR millions; based on existing use of resources and present holdings of SDRs):

	Forthcoming				
	2003	**2004**	**2005**	**2006**	**2007**
Principal	3,008.23	4,971.15	1,280.63	995.50	459.04
Charges/interest	192.01	132.33	47.84	22.69	4.26
Total	3,200.24	5,103.48	1,328.47	1,018.18	463.30

VII. Safeguards Assessments: Under the Fund's safeguards assessment policy, the Central Bank of Argentina (BCRA) is subject to an assessment with respect to the proposed Stand-By Arrangement. A safeguards assessment of the BCRA was completed on September 05, 2002. The assessment concluded that: (i) substantial risks might exist in the system of internal controls; (ii) a more robust financial reporting framework should be developed; and (iii) the central bank's operational independence from government interference needs strengthening. Staff recommendations included: (i) publication of the 2001 financial statement; (ii) strengthening controls over the reporting of program data; (iii) issuance of a resolution requiring the preparation of financial statements in accordance with International Accounting Standards (IAS); and (iv) signing of memoranda of understanding between the central bank and the government, determining the conditions under which realized central bank profits are transferred to the government. Recommendations (i)-(ii)-(iv) have been implemented. In the proposed program (see paragraph 53 of the Memorandum of Economic and Financial Policies), the authorities commit to preparing the financial statements of the central bank in accordance with IAS for the year ending on December 31, 2003, and issuing the audited financial statements within four months of year-end. Staff will continue monitoring the implementation of the recommended measures.

B. Nonfinancial Relations

VIII. Exchange Rate: On March 27, 1991, a law was passed guaranteeing the full convertibility of the austral under a currency board arrangement and pegging the austral at ₳10,000 per U.S. dollar. On January 1, 1992 the *peso* was substituted for the austral at a rate of 1 peso per 10,000 australes. On January 7, 2002, the currency board arrangement was abandoned in favor of a dual exchange rate regime with an official rate of Arg$1.4 per U.S. dollar for most trade, trade finance, and public sector transactions; remaining transactions were at a market floating rate. On February 11, 2002, the dual exchange rate regime was abolished and substituted by a floating regime with no pre-announced rate of the exchange rate.

All Article VIII restrictions have been removed other than: (i) the restriction arising from the freezing of deposits pursuant to the *corralón* (which has been approved by the Board until the earlier of March 2004 or the conclusion of the next Article IV consultation with Argentina); and (ii) a restriction arising from limitations on the ability of financial institutions to make moderate loan amortization payments.

IX. Last Article IV Consultation: The 2002 Article IV consultation was concluded by the Executive Board on January 8, 2003 (EBS/02/214).

X. Fourth Amendment: Argentina has accepted the Fourth Amendment to the Articles of Agreement.

XI. Technical Assistance, 2002–03

Missions	Purpose	Time of Delivery
FAD	Tax Administration	January 2002
LEG	Insolvency Law and Other Legal Issues	March 2002
MAE	Bank Restructuring	March 2002
LEG	Insolvency Law and Other Legal Issues	April 2002
MAE	Bank Restructuring	April 2002
MAE	Bank Restructuring	May 2002
MAE	Bank Restructuring	June 2002
MAE	Bank Restructuring	July 2002
MAE	Bank Restructuring	August 2002
MAE	Bank Restructuring	September 2002
FAD	Public Expenditure Management	September 2002
LEG	Insolvency Law and Other Legal Issues	November 2002
FAD	Customs Administration	November 2002
MAE	Development of Banking Model	November 2002
FAD	Tax Policy	February 2003
MAE	Bank Restructuring	March 2003
FAD	Intergovernmental Relations	April 2003
MAE	Bank Restructuring	May 2003
MAE	Bank Restructuring	July 2003
MAE	Bank Restructuring	August 2003

XII. Resident Representative: Mr. John Dodsworth has been the senior resident representative in Buenos Aires since July 2003. Mr. Luis Cubeddu has been the resident representative since September 2002.

RELATIONS WITH THE WORLD BANK GROUP[1]

1. Bank lending to Argentina as of August 31, 2003 totaled US$18.3 billion (net of cancellations). Thirty two loans totaling US$3.9 billion remain under execution, with about US$1.6 billion undisbursed. Out of these, 29 are for investment operations, totaling US$3.2 billion in commitments, of which US$1.4 remain undisbursed. The remaining three are adjustment operations totaling US$703 million in commitments, of which US$246.7 million remain undisbursed.

2. The last Country Assistance Strategy (CAS) Report was discussed at the Board on June 27, 2000 and was subsequently updated via a CAS Progress Report dated October 1, 2001. The strategic guidelines outlined in those documents have been to a significant extent overcome by the dramatic events at the end of 2001 and their drastic impact on economic, political, and social conditions. The Bank has since then adjusted its proposed strategy to respond to the needs emerging from the acute increase in poverty and indigence levels and to support the transition towards the normalization of the economic and social conditions. The Bank's response to the crisis situation has included three major steps thus far.

3. In 2002, US$270 million were re-allocated from existing projects to emergency social programs in the areas of nutrition, health, and education. Second, in January 2003 the Board approved the Heads of Household loan for US$600 million, which constitutes the main program of the Duhalde administration to assist the unemployed, benefiting about 2 million households. Third, in May 2003, the Board approved a US$500 million Economic and Social Transition Loan that has supported the redemption of the quasi-monies issued by the provinces and ensured continued execution of programs dealing with the provision of essential social services.

4. Despite efforts to improve performance of the Bank's investment portfolio through restructuring and resolving some operational issues emerging from the crisis, implementation progress and the pace of disbursements has been slow. Better progress has been made in the case of the adjustment portfolio, where an amount of US$622 million remained undisbursed in early CY2003 corresponding to a Structural Adjustment Loan and three Provincial Reform Loans to the provinces of Santa Fe, Cordoba, and Catamarca. After a process of renegotiation of these operations in order to adjust them to post crisis conditions, a total of $US375 million have been disbursed in recent months. The remaining balance (US$246.7) is expected to be disbursed by end CY03. Finally, a proposed Health Adjustment Loan is planned for Board presentation shortly.

5. A new Country Assistance Strategy is expected to be presented to the Board by the end of this calendar year.

[1] Prepared by the staff of the World Bank on 9/8/03.

Financial Relations with the World Bank

(In millions of U.S. dollars)

	Commitments (Net of Cancellations)	Disburse-ments	Undisbursed Amount
I. IBRD Operations (as of August 31, 2003)			
Fully disbursed loans	**14,414.6**	**14,414.6**	**0.0**
Loans in process of disbursement	**3,853.5**	**2,242.2**	**1,611.3**
A. Investment operations			
Agriculture and Rural Development	246.5	88.9	157.6
Power	30.0	2.2	27.8
Municipal/Provincial Development	430.9	379.6	51.3
Water Sector	30.0	4.5	25.5
Social sector	1,170.3	649.2	521.1
Finance, infrastructure, and natural resources	1,192.0	646.9	545.1
Public administration	50.80	14.6	36.2
B. Adjustment operations	703. 0	456.30	246.70
Total loans	**18,268.1**	**16,656.8**	**1,611.3**

II. IFC Operations (as of July 31, 2003)

	Loans	Equity	Quasi	Partici-pation
Held	700.2	194.6	173.4	862.8
Disbursed	693.5	134.7	173.4	862.8
Pending commitment	72.0	0.4	3.5	500.0

III. IBRD Loan Transactions (as of August 31, 2003)

	Actuals (Calendar Year)					
	1998	1999	2000	2001	2002	2003
Disbursements	2,030.6	1,572.9	1,018.8	1,328.8	424.5	1,260.6
Debt service payments	350.2	445.0	538.1	675.5	1,869.8	1,886.1
Net transfers	1,680.4	1,127.9	480.7	653.2	-1,445.3	-625.5

Source: World Bank.

RELATIONS WITH THE INTER-AMERICAN DEVELOPMENT BANK[1]

Portfolio

1. The Bank adjusted its activities in Argentina in 2002 and 2003 to better respond to a new economic, social and political context. In particular:

   - Tightened supervision of its portfolio to take into account harsher fiscal constraints;
   - Focused its activities on helping the country protect social expenditure through the reformulation of its social portfolio. To this end, in March 2002, board authorization was given to redirect US$694.2 million from low-performing operations of lesser priority to support the Argentine government's Social Emergency Plan for social protection and containment programs, with special emphasis on food, medicines, and education programs. Results to date have been positive both in terms of physical and disbursement targets;
   - Supported the development of the productive sectors through the execution of direct loans to the provinces, in particular by providing support to export-oriented small- and medium-sized enterprises (SMEs). Work is also underway to reformulate the Bank's productive sector portfolio in order to redirect resources from active projects that are less likely to meet their original objectives towards initiatives that help revitalize economic activity and improve the competitiveness of the productive sectors. This revitalization package would total US$400 million.

2. Early in 2003 the second tranches of two sector loans were reformulated in order to better respond to new needs: the Financial Sector Program in the amount of US$243 million, and the Sector Program to Support the Federal Pact for Growth and Fiscal Discipline in the amount of US$246.7 million. Each of these second tranches was split into two, the first half of each having already been disbursed and the second half of each, for a total of US$218 million, is expected to be disbursed in the fourth quarter of 2003.

3. As of August 30, 2003 disbursements for the year totaled US$1.9 billion with US$900 million remaining to be disbursed during before year-end.

[1] Prepared by IDB staff, September 2003.

Lending Program and Country Strategy

4. Under the umbrella of the Transition Program agreed upon between Argentina and the IMF, on February 5, 2003 the Bank approved an emergency loan for US$1.5 billion to protect social expenditure. This loan has been fully disbursed. The Bank is currently exploring the possibility of approving a second emergency loan in the amount of US$500 million, within the framework of the new agreement between the IMF and Argentina.

5. Additionally, two direct loans to the provinces of Salta and Río Negro were approved in 2003, for a total of US$86 million, with the objective of revitalizing economic growth by supporting productive sectors with greater comparative advantages. Several technical cooperation operations are also in preparation that aim to improve the competitiveness of small- and medium-sized enterprises and to strengthen the financial sector.

6. The Bank has carried out missions to begin discussing its future lending program with the new authorities as well as the priorities to be agreed upon in its country strategy for the period 2004–07. Work on this strategy has been initiated through a series of internal workshops in the Bank and through the elaboration of sector-specific studies. Discussions and a series of workshops are planned with the government, private sector and civil society and are expected to take place throughout the fourth quarter with the aim of approving this strategy early in 2004.

STATISTICAL ISSUES

1. The statistical information on basic indicators for surveillance is published in a timely manner and is reliable. Argentina has subscribed to and is in full observance of the Special Data Dissemination Standard (SDDS) and, on the basis of the metadata provided by the authorities and reviewed by IMF staff, it meets the SDDS specifications for the coverage, periodicity, and timeliness of the data, and for the dissemination of advance release calendars. Also Argentina has begun to disseminate a partial version of the template on reserves and international liquidity both on its national web site and to provide the data for a database maintained by the Fund.

National Accounts

2. In June 1999, the Ministry of Economy published and updated series of annual and quarterly national accounts estimates for the period 1993–1997 (at current prices and at 1993 constant prices), using a new 1993 benchmark and base year. These series have been carried forward to the most recent periods, although data reported for previous years have not been revised yet and they are still published at constant prices of 1986. The new series have resulted in a significant downward revision of current prices GDP estimates by 8–9 percent.

Prices

3. Consumer prices and producer prices are collected by the National Institute of Statistics (INDEC) and the indices are published monthly in a timely fashion. In December 2000, INDEC released a new CPI index (base 1999) for the Gran Buenos Aires, which replaces the index (base 1988) available since June 1989. The new index introduces an expanded basket (40 percent more items than the old index) and revised weights according to the household expenditure survey for 1996–97.

Other Real Sector Data

4. The National Institute of Statistics has recently published detailed accounts on industrial activity, remuneration and hours worked. Employment surveys are conducted three times a year (May, August and October) and data are published in May and October.

Government Finance Statistics

5. Information on revenue and expenditure of the Central Government, decentralized agencies, public enterprises and social security system is available on a cash basis with a lag of 1½ –2 months, but data on the provincial public finances are available only on commitments basis and with considerable delays and in summary form. Annual time series for the consolidated central government and for state governments that are consistent with the 1986 GFS standards are available through 1999 on the website of the Ministry of Economy.

Monetary Statistics

6. Monthly data on the central bank, deposit money banks, and the banking survey are published in the Central Bank of the Republic of Argentina's (BCRA) Statistical Bulletin, accessed through the Internet. Data for the central bank are available with a six-week lag, but longer delays may occur, particularly with respect to the audited end-year central bank balance sheet. Complete balance sheet data for deposit money banks are unavailable since December 2001. Data published in *IFS* are based, with few adjustments, on the BCRA Statistical Bulletin.

Public Debt

7. Prior to 1994, data on public sector debt were incomplete and not available on a timely basis. The statistical information has improved both as regards coverage and currentness, and the data are now available on a quarterly basis, but frequent revisions are made to the stock of outstanding debt reflecting the regularization of previously undocumented obligations. Detailed information on public debt is available on Argentina's national SDDS website. A comprehensive report on provincial government debt in 1996 and 1997 was published by the federal government in July 1998.

Balance of Payments

8. In April 1999, the Ministry of Economy published a revised set of balance of payments statistics including annual data for 1992–1993 and annual and quarterly data thereafter. The new set incorporates improved data on holdings of foreign financial assets and of direct external debt of the Argentine nonbank private sector. The Ministry of Economy also publishes annual international investment position data for 1991 onwards. Quarterly balance of payments data are published with a two to three-month lag. Monthly trade data are published with a six-week lag. Annual international investment position data are published within six months of the reference period. Balance of payments, trade, and international investment position data are available in the Internet.

9. The National Directorate of International Accounts (DNCI) of the Ministry of Economy has made significant progress in strengthening Argentina's balance of payments statistics. The DNCI's implementation of a number of guidelines set forth in the fifth edition of the *Balance of Payments Manual (BPM5)*, in particular, has enhanced the coverage of the services components of the current account and both inflows and outflows in the financial account. The authorities have also implemented the recommendations of the 1997 and 1998 balance of payments missions, which resulted in improved estimates on capital flows related to the Argentine nonfinancial private sector's portfolio investment.

INTERNATIONAL MONETARY FUND

Argentina—Assessment of the Risks to the Fund and the Fund's Liquidity Position

Prepared by the Finance and Policy Development and Review Departments

In consultation with other Departments

Approved by Eduard Brau and G. Russell Kincaid

September 15, 2003

1. As set out in the policy on exceptional access, this note assesses the risks to the Fund arising from the exposure and the effect on the Fund's liquidity position from the proposed three-year stand-by arrangement (SBA) with Argentina.[1] Specifically, it examines the impact of the proposed access of almost SDR 9 billion (424 percent of quota) on near-term Fund liquidity. It first discusses the proposed access level against the backdrop of Argentina's large and prolonged use of Fund credit.

Background

2. **Argentina has had a long and extensive financial relationship with the IMF.** On September 1, 2003, Argentina's outstanding use of Fund credit equaled SDR 10.9 billion, or 517 percent of quota. Outstanding Fund credit has exceeded 100 percent of quota since 1983, and with the proposed SBA, it will remain above this level through August 2009. Argentina has been among the five largest users of Fund credit in all but two of the last twenty years. Its use has been high compared with other high access cases and with other prolonged users (Figure 1). In most other cases where members faced capital account crises and access was exceptional, Fund credit peaked for a few years and was brought down quickly (see Figure 1). Among members identified as prolonged users of Fund resources, Argentina has been the largest user of Fund resources for 12 of the last 17 years. Its debt to the Fund represents about 8 percent of Argentina's consolidated public sector debt.

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[1] See "The Acting Chair's Summing Up of the Review of Access Policy under the Credit Tranches and the Extended Fund Facility", and "Access Policy in Capital Account Crises—Modifications to the Supplemental Reserve Facility and Follow-Up Issues Related to Exceptional Access Policy".

3. **The concentration in the Fund's lending to a few members has increased in recent years, and Argentina's share in total Fund credit has risen (Figure 2).** The top five borrowers' share of total Fund credit outstanding has risen from about 50 percent in 1990 to about 86 percent at end-July 2003 (see Figure 2).

4. **On September 9, 2003, Argentina failed to meet a SDR 2.09 billion repurchase obligation to the Fund and went into arrears.** At that date, Argentina's gross international reserves stood at about SDR 9.9 billion. Argentina cleared its overdue obligations on September 11, 2003.

Near-term impact on Fund finances

5. **The proposed access of almost SDR 9 billion would reduce the Fund's liquidity by the same amount, as measured by the forward commitment capacity** (FCC).[2] This result together with the impact of past arrangements would encumber the FCC by a total of SDR 14.7 billion (Table 1).[3] The Fund's current one year FCC, at SDR 64 billion, could accommodate the proposed commitment.

6. **Based on the proposed SBA and the repurchase schedules under past arrangements, the Fund's exposure to Argentina would remain at an exceptionally high level until early 2008.** Argentina is currently the Fund's third largest debtor and accounts for 16 percent of the Fund's credit outstanding as of September 1, 2003 (see Table 1). Fund credit outstanding would remain at about SDR 11 billion through late-2006 and above the cumulative limit for exceptional access of 300 percent of quota through early 2008.

7. **Indicators of Fund exposure underscore the high level of risk to the Fund's balance sheet and Fund income from Argentina's use of Fund resources**:

- **Under the proposed arrangement, total credit to Argentina would continue at about twice the current level of the Fund's precautionary balances for the next three years.** In the event of non payment of principal, the Fund's precautionary balances, i.e., reserves and balances that have been set aside in the first Special Contingency Account (SCA-1), would not be sufficient to cover the arrears that could arise.

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[2]The FCC, introduced in December 2002, is the principal measure of Fund liquidity. The one-year FCC indicates the amount of quota-based, nonconcessional resources available for new lending over the next 12 months. See also "The Fund's Liquidity Position—Review and Outlook".

[3] The total impact on the FCC is defined as the sum of outstanding credit and undrawn commitments less repurchases one-year forward.

- **Interest payments on credit to Argentina, including under the proposed SBA, would reach nearly three times the Fund's residual burden-sharing capacity.**[4] In the event of nonpayment of charges, the loss of income would exceed the current free capacity under burden sharing. Absent a modification of the burden-sharing mechanism, the income shortfall would have to be compensated through an increase in the rate of charge or through reductions in precautionary balances. The latter were judged in November 2002 already to be insufficient.[5] To spread the burden, the burden-sharing mechanism could be modified. Modifications could include: a lowering of the floor on remuneration to the 80 percent limit stipulated in the Articles of Agreement (Article V, Section 9 (a));[6] an activation of the burden-sharing mechanism immediately after a nonpayment (i.e., without the normal six months deferral);[7] and exclusion of surcharges from coverage under burden sharing.

8. **Argentina's substantial exposure going forward involves high risks to the Fund and that exposure is most likely to remain high for quite some time.** Given the large repayments to the Fund from 2007 onward, Argentina is expected to seek future Fund financial support, probably at a reduced level.

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[4]The Fund has a "burden-sharing" mechanism to offset income losses from the non-payment of interest. This mechanism works through an increase in the rate of charge and a decrease in the rate of remuneration. Residual burden-sharing capacity represents "free capacity" and hence is the appropriate metric against which to evaluate projected charges. Current free capacity under the Fund's burden-sharing mechanism, is about SDR 160 million. It is arrived at by adjusting the total current capacity of the Fund's burden-sharing mechanism (SDR 290 million) for the amount being used to offset deferred charges and to accumulate balances in the Special Contingent Account. The capacity of the Fund's burden-sharing mechanism is limited by the floor to the rate of remuneration, currently 85 percent of the SDR interest rate, while the Articles of Agreement set an overall floor at 80 percent of the SDR interest rate. For more information on the burden-sharing mechanism, see "Review of the Fund's Income Position, the Rate of Charge, Precautionary Balances and Burden Sharing for FY 2003 and FY 2004" and "Financing the Fund's Operations—Review of Issues". See also "Access Policy in Capital Account Crises—Modifications to the Supplemental Reserve Facility and Follow-Up Issues Related to Exceptional Access Policy".

[5]In the November 2002 discussion on the Fund's policy on precautionary balances, the Board supported a doubling of the target for precautionary balances over five years, and the maintenance of the present system of accumulating these balances. See "Concluding Remarks by the Acting Chair, The Fund's Policy on Precautionary Financial Balances".

[6]As described in Box 4 of the paper on "Access Policy in Capital Account Crises" for the current rules on rate of remuneration.

[7] Unpaid charges continue to accrue as income for six months after the emergence of arrears. After six months, overdue charges are deferred and burden sharing is activated for current charges as well as the existing overdues. Given the size of Argentina's interest payments, the loss of income from the accumulated unpaid charges cannot be fully recovered the first time the burden-sharing is activated.

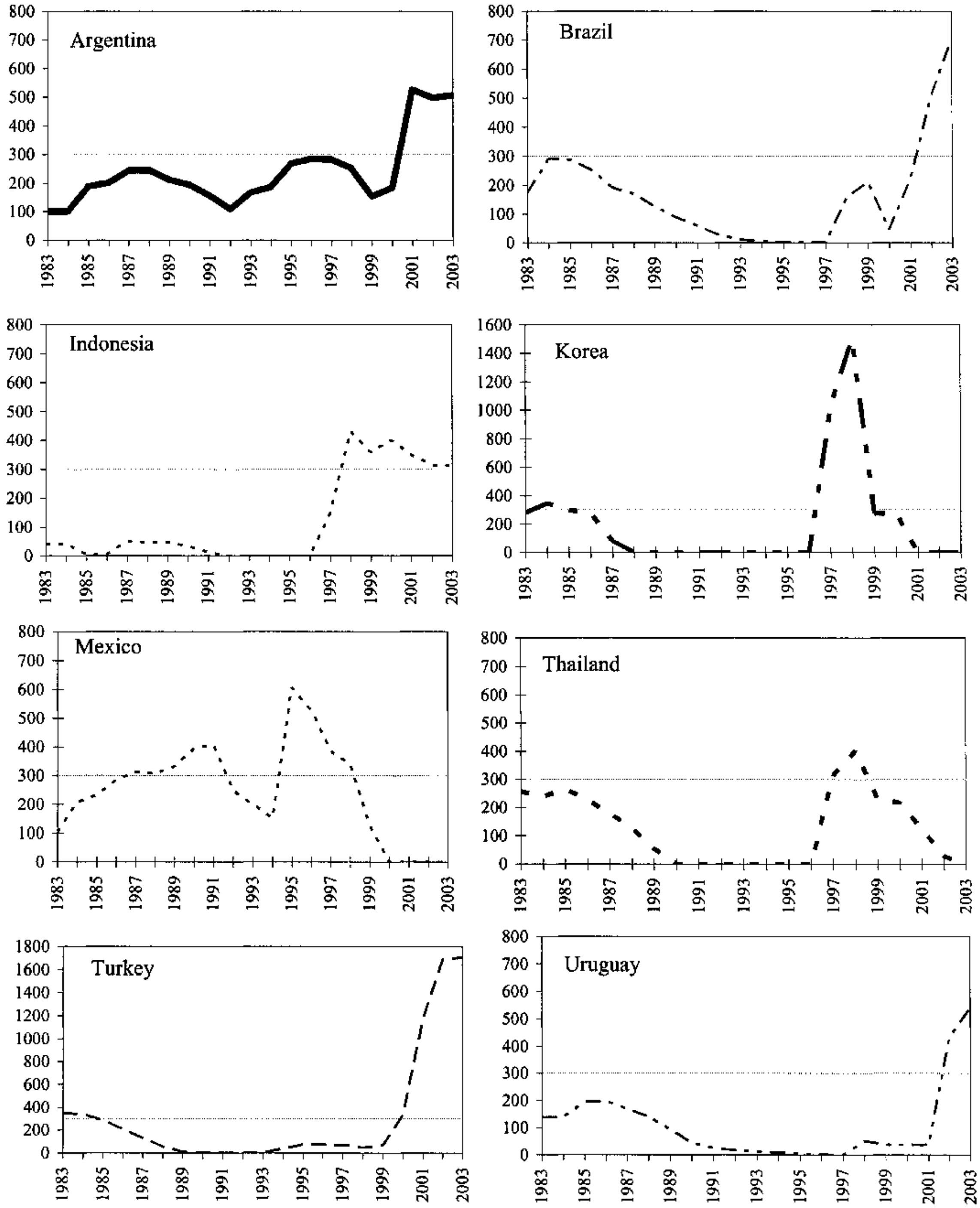
Assessment

9. **While the Fund's overall liquidity position would remain adequate, with the proposed access of almost SDR 9 billion the Fund would remain highly exposed to Argentina both in terms of the stock of outstanding credit and the projected flow of charges for an extended period of time.** Moreover, in the event of nonpayment of principal, the Fund's precautionary balances would not be sufficient to cover the total amount of arrears that could arise. Nonpayment of charges and the resulting loss of income could require a modification in the Fund's burden-sharing policy.

10. **Argentina's substantial exposure to the Fund entails important risks.** These risks relate less to Argentina's capacity to generate the resources necessary to make the relatively limited payments due during the program period to the Fund and multilateral development banks. Over the three-year program period, Argentina is not expected to make net payments of principal to the Fund and multilateral creditors, and its large and growing international reserves together with existing baseline policies should be sufficient for Argentina to make payments related to charges and interest. Instead, the risks are affected principally by the willingness and capacity of the government to implement policies tied to subsequent program reviews that will support the increase in the primary surplus and other policy reforms necessary to create conditions for lasting growth, repair the damage to Argentina's financial system and to lay the foundation for a debt restructuring with private creditors that ensures sustainability and restores market access. Its ability to achieve these conditions is essential for its capacity to repay Fund credit over time. The proposed program creates additional potential risks to the Fund, because of the limited definition of policies and the adjustment path contained in this medium-term program, and the implications that this may be perceived to have for future Fund-supported programs. The circumstances that led to the adoption of this program framework in this specific context are highly exceptional. The decisions the Fund makes in the context of the forthcoming reviews of this program will be very important in minimizing the risk that this program would lead to pressures to erode the strength of future Fund-supported programs.

Figure 1. Fund Credit Outstanding in Exceptional Access Cases, 1983 - July 2003

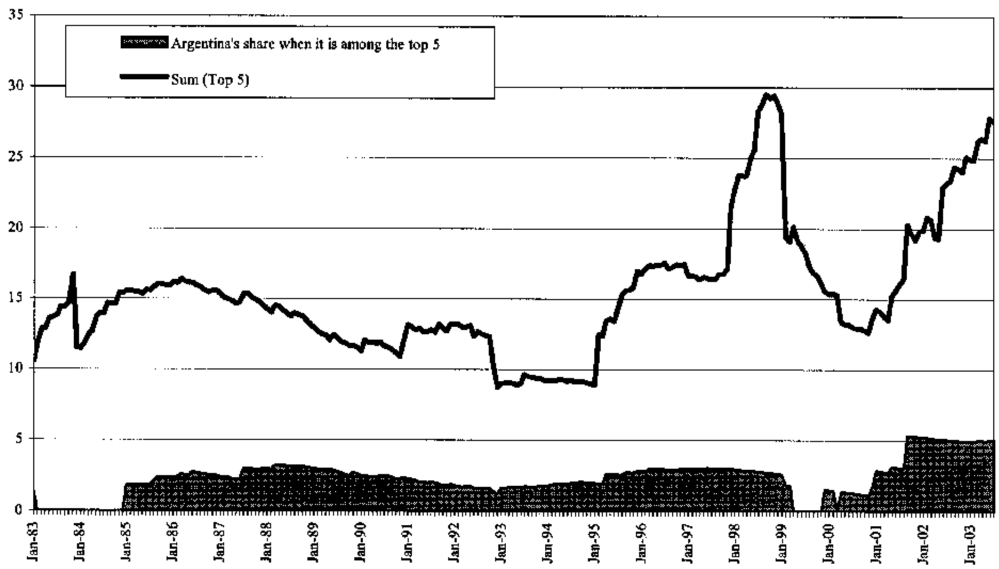
(percent of quota)



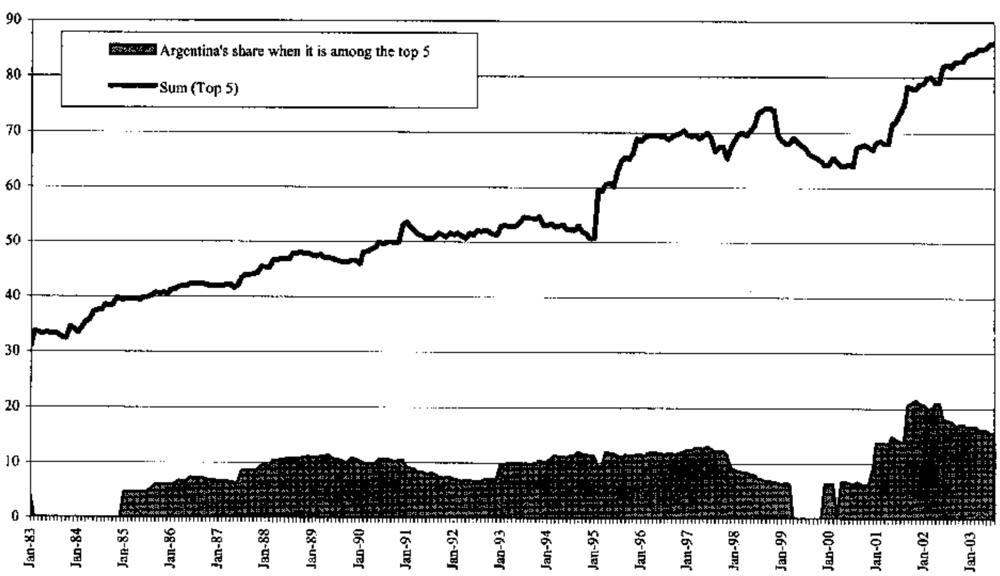
Source: *International Financial Statistics*.

Figure 2. GRA Fund Credit Outstanding for Top Five Users
(January 1983 - July 2003)

In Percent of Total Quotas



In Percent of Total Fund Credit Outstanding



Source: *International Financial Statistics* and Finance Department.

Table 1. Argentina: Impact on Fund Finances
(In billions of SDRs, and end of period, unless otherwise indicated)

	2002	9/1/03 1/	2003	Sep. 2006
Exposure				
Fund credit outstanding to Argentina 2/	10.5	10.9	10.7	10.9
Under past arrangements	10.5	10.9	8.6	1.9
Under proposed new commitment	n.a.	n.a.	2.1	9.0
Fund credit outstanding to Argentina (percent of total outstanding credit) 2/	16.6	16.0	...	...
Fund credit outstanding to 5 largest debtors (percent of total outstanding credit)	84.0	86.2	...	...
Liquidity				
One-year Forward Commitment Capacity (FCC)	54.7	63.6	...	...
Argentina's impact on FCC 2/ 3/	-11.3	-14.7	-13.9	...
Under past arrangements, adjusted 4/	-11.3	-5.7	-4.9	...
Under proposed new commitment	n.a.	-9.0	-9.0	...
Prudential Measures				
Fund credit outstanding to Argentina as a percent of current precautionary balances 2/ 5/	204	201	197	200
Based on past arrangements	204	201	159	35
Based on proposed new commitment	n.a.	n.a.	38	165
Argentina's annual charges as a percent of Fund's residual burden-sharing capacity 2/ 6/	n.a.	n.a.	299	...
Based on past arrangements	n.a.	n.a.	285	...
Based on proposed new commitment	n.a.	n.a.	14	...
Memorandum items:				
Argentina's debt to IMF as a percent of its total public external debt 7/	15.9	...	13.2	...
Argentina's debt to IMF as a percent of its total public debt	9.3	...	7.9	...
Argentina's debt to multilaterals as a percent of its total public debt	20.3	...	16.8	...
Fund's precautionary balances 8/	5.2	5.4	5.4	...
Fund's residual burden-sharing capacity 6/	0.2	0.2	...	...
Undrawn commitments to Argentina 2/	7.0	9.0	6.9	0.0
Based on past arrangements	7.0	0.0	0.0	0.0
Based on proposed new commitment	n.a.	9.0	6.9	0.0
Annual charges 2/ 9/	0.5	n.a.	0.5	0.4
Based on past arrangements	0.5	n.a.	0.5	0.1
Based on proposed new commitment	n.a.	n.a.	0.02	0.3

Source: Staff estimates.

1/ Assumes Argentina's new SBA for SDR 8.981 billion will be approved in September 2003.
2/ Including proposed new commitment to Argentina and assuming that purchases take place as scheduled and repurchases are made on obligations basis.
3/ Forward Commitment Capacity is a measure of the resources available for new financial commitments in the coming year, equal to uncommitted usable resources plus repurchases one-year forward minus the prudential balance. A single country's impact on the FCC is defined as the sum of outstanding Fund credit and undrawn commitments minus repurchases one-year forward.
4/ Credit outstanding less repurchases one-year forward.
5/ Excluding the portion of reserves earmarked for employee benefits per the implementation of IAS 19.
6/ Burden-sharing capacity is calculated based on the floor for remuneration at 85 percent of the SDR interest rate (see Decision No. 12989 (03/36), adopted 4/21/03). Residual burden-sharing capacity is equal to the total burden-sharing capacity minus the portion being currently utilized to offset deferred charges and to build SCA-1 balances.
7/ Staff estimate based on authorities' figures, and assuming 25 percent of provincial debt is external debt.
8/ Figures reflect the implementation of IAS 19. See *Review of the Fund's Income Position, the Rate of Charge, Precautionary Balances and Burden Sharing for FY2003 and FY 2004* (EBS/03/43, 4/7/03).
9/ Flows during the period. Annual flows for 2003 appear under December 2003. Charges for 2006 are for the first nine months.

INTERNATIONAL MONETARY FUND

ARGENTINA

Report on Exceptional Access For Request of Stand-By Arrangement

Prepared by the Western Hemisphere and
Policy Development and Review Departments

(In consultation with the Finance, International Capital Markets and Legal Departments)

Approved by John Dodsworth and G. Russell Kincaid

September 16, 2003

I. Introduction

1. **As set out in the new framework for exceptional access cases, this separate report evaluates the case for exceptional access under the proposed stand-by arrangement with Argentina, based on consideration of the four substantive exceptional access criteria in capital account crises.**[1] The four substantive criteria are: exceptional balance of payments pressures in the capital account; a rigorous and systematic debt analysis that indicates there is a high probability that debt will remain sustainable; good prospects of regaining access to private capital markets within the time Fund resources would be outstanding; and a reasonably strong prospect of program success. The Board recognized that where debt restructuring is needed, difficult and well-informed assessments would be required to deal with the financial challenges and needs that are fundamentally different from those of countries with a sustainable debt burden. In particular, the substantive criteria for exceptional access in capital account crisis would generally not be met.

2. **Directors generally agreed that access in debt restructuring cases would normally be expected to be within the access limits, although there could be rare circumstances warranting exceptional access.** One such circumstance would arise where the country is not in a position to make significant net repurchases to the Fund and there are large scheduled repurchase obligations.[2] The staff proposed some general guidelines to help

[1] See "The Acting Chairman's Summing Up of Review of Access Policy Under the Credit Tranches and the Extended Fund Facility", and "Access Policy in Capital Account Crises—Modifications to the Supplemental Reserve Facility and Follow-Up Issues Related to Exceptional Access Policy." Where time permits, this separate report is to be provided in advance of the circulation of program documents, which was not the case for Argentina. In all cases, this report would be included in the program documents and hence the need for this separate report.

[2] See page 20 of "Access Policy in Capital Account Crises—Modifications to the Supplemental Reserve Facility and Follow-Up Issues Related to Exceptional Access Policy."

inform access policy in a restructuring context: (i) as in all Fund-supported programs, its design needs to ensure that Fund access does not substitute for adequate adjustment effort over the medium term; (ii) Fund financing should not be made available to continue payments on a restructured stock of debt that would be unsustainable, or unaffordable without exceptional financing from the IMF; and (iii) Fund financing should not unduly increase the rigidity of the member's debt stock by leaving, for example, the member country with an excessively large debt to the international financial institutions.

3. **Access under the proposed arrangement with Argentina would clearly be exceptional.** Argentina's outstanding use of Fund resources at end-August was over 500 percent of quota, which is above the cumulative access limit (300 percent of quota) in the credit tranches and under the EFF. Consequently, any proposed access—even one SDR—would trigger the exceptional access procedures. In addition, and reflecting the balance of payments needs arising from large repurchases falling due to the Fund over the arrangement period, the proposed access of 424 percent of quota over the three-year arrangement exceeds the annual access limit of 100 percent of quota.

4. **Against this background, this paper considers each of the four exceptional access criteria in turn in Argentina's case.**

II. Criterion 1: Balance of Payments Need

5. **The exceptionally high access proposed under the new arrangement (424 percent of quota) reflects the large financing needs that Argentina faces over the next three years.** The external financing gaps projected over the program period mainly reflect the need to restructure public and private debt and to rebuild reserves. The balance of payments projections are based on the assumption that it will take time to normalize relations with the international community and establish confidence.

6. **The gross external financing requirements for the period 2004–06 are estimated to average US$25 billion a year, including debt service obligations on a contractual basis on unrestructured public and private debt.** The authorities are seeking to meet these financing needs through: (i) a restructuring of public debt; (ii) new purchases under the requested Fund arrangement of almost SDR 9 billion (about US$12.5 billion); (iii) extension of repurchase expectations totaling the equivalent of about SDR 1.94 billion during the first year of the arrangement;[3] (iv) broadly maintaining exposure by the World Bank and the IDB, involving new disbursements by these institutions totaling about US$6 billion; and (v) a requested rescheduling of obligations to Paris Club and other bilateral creditors for all principal payments due during the program period, including payments arising during the deferral period, estimated at about US$3.2 billion. The authorities are actively engaged in seeking a restructuring of sovereign obligations to private creditors and facilitating corporate debt restructuring so as to normalize the arrears situation as soon as possible. Paris Club

[3] This includes a repurchase expectation amounting to the equivalent of SDR 198 million that arises on September 19, 2003. The extension of this repurchase expectation has been proposed for Board approval in a separate paper because it arises prior to the likely date of Board consideration of the request for the proposed SBA.

creditors have already signaled their preparedness to provide general financing assurances for the program;[4] and the authorities will continue to collaborate closely with the World Bank and the IDB.

III. Criterion 2: Debt Sustainability Analysis

7. **Reflecting the fact that Argentina has defaulted on a portion of its sovereign debt and the need therefore for a debt restructuring, Argentina does not meet the debt sustainability criterion for exceptional access.** The baseline debt sustainability analysis shows continued financing gaps from 2005 onwards (Annex). The analysis shows that with a constant primary surplus of 3 percent of GDP during 2004–10, even with generous rollover assumptions and a complete write down of Argentina's Phase 2 debt, financing gaps would arise in the outer years.

8. **The authorities are aiming for a public debt restructuring that would, in conjunction with revised fiscal commitments associated with the restructuring, eliminate financing gaps going forward and achieve a sustainable debt profile over the medium term.** The authorities are developing an offer to private creditors for the restructuring of public debt. They have indicated the desire to move toward completion of a debt restructuring by mid-2004, following an initial announcement at the IMF-World Bank Annual Meetings. Under the proposed program, the authorities have committed to engage in good-faith negotiations with their private creditors on the formulation of a debt-restructuring proposal and to keep staff informed of progress in reaching a restructuring agreement. This will allow staff to evaluate whether the restructuring offer has the prospect of closing future financing gaps and is consistent with reducing IFI exposure starting from 2007.

IV. Criterion 3: Capital Market Re-entry

9. **Argentina's re-entry to international capital markets during the period of the proposed Fund arrangement is unlikely**. New domestic financing at market rates is assumed to be sufficient to roll over 100 percent of phase 1 loans, bank compensation bonds, and other provincial debt. The central bank is assumed to roll over 100 percent of maturing quasi-money bonds. Bonds issued for deposit conversion and to compensate civil servants for unpaid wages (averaging US$1 billion per year during 2004-06) are assumed to be amortized on their scheduled dates. No additional market access beyond these rollovers is assumed for the period 2003-10. A successful restructuring, as well as a significant increase in the fiscal primary surplus and a strengthening of other policy reforms are necessary to restore market access, create the conditions for lasting growth, and repair the damage to Argentina's financial system and restore market access. Argentina's ability to achieve these conditions is essential for its capacity to repay Fund credit over time.

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[4] In a meeting on September 11, the Paris Club agreed to provide general financing assurances that would cover a rescheduling of arrears and principal falling due during the period of the arrangement, although the specifics would be addressed at the time of the negotiations.

V. Criterion 4: Strong Program Design and Implementation Prospects

10. **The strategic objectives of the authorities' program (http://www.imf.org) are:** to begin restoring fiscal solvency within a fiscal framework that includes the provinces and makes room for adequate social and infrastructure spending; to implement a credible sovereign debt restructuring; to restructure banks; to improve the framework for restructuring corporate debt, including that of the utility companies; and to instill legal certainty to improve business confidence and growth. The program includes quantitative and structural performance criteria and benchmarks in the critical areas of macroeconomic policy, fiscal reform, bank restructuring, and the improvement of the investment environment.

11. **The program has yet to be fully elaborated and key differences of view with the authorities may put at risk its implementation prospects.** The fact that important fiscal, banking, and other structural reforms will only be elaborated later in the program is a key program weakness, especially given the front-loaded phasing of purchases under the proposed SBA.

12. **With the proposed arrangement for Argentina—a prolonged user of Fund resources—the Fund will assume somewhat larger risks than in other recent cases of exceptional access (Table 1).** Although appropriate country comparisons are difficult given the diversity of individual country circumstances, illustrative comparisons with the recent Fund-supported programs of Brazil (2002), Turkey (2002), Uruguay (2002), Ecuador (2000), and Russia (1998) indicate that, on average, in the year of approval of the arrangement and in the three subsequent years: (i) Fund credit outstanding in these countries remained at about 525 percent of quota, but a significantly smaller share of GDP (averaging about 5.5 percent of GDP); and (ii) repurchases absorbed a significantly smaller share of export receipts (about 5 percent on average), and about 10 percent of gross international reserves.

13. **The key risks to the program are set out in the main staff report (http://www.imf.org).** Significant risks arise from the fact that key fiscal and banking reforms that are crucial to sustainability will only be fully elaborated and formulated at a later stage. In the fiscal area, the lack of specific commitment on the medium-term fiscal effort involves large uncertainties and risks undermining the credibility of the debt restructuring strategy. The electoral cycle of ongoing congressional and gubernatorial elections and the administration's need to consolidate its influence constrain the room for maneuver presently, and create uncertainties about the eventual political consensus for key parts of the program. The authorities view the sequencing of actions under their program as necessary to develop a strong domestic consensus for reforms and to facilitate their implementation. There is however, a clear risk that the absence of up-front strong commitments masks fundamental differences of view with the staff on key policy areas, which will only become apparent later. Another major risk—and source of market concern—is the authorities' strategy for restructuring their debt with private creditors. Good-faith efforts in pursuing the restructuring, including demonstrated willingness to make additional fiscal efforts to assure the restructured debt can be serviced, will be essential on the part of the authorities, and an early and sustainable restructuring is crucial to the ultimate success of the program. Notwithstanding the above, the authorities have demonstrated considerable ownership of this Fund-supported

program during its negotiations with a high degree of personal involvement by President Kirchner.

Table 1. Argentina: Proposed Access, 2003

	Proposed Arrangement	High-Access Cases 1/ Proposed Arrangement (Percentile)	20th Percentile (Ratio)	80th Percentile (Ratio)	Average (Ratio)	Normal Access Cases Proposed Arrangement (Percentile)	20th Percentile (Ratio)	80th Percentile (Ratio)	Average (Ratio)
Access									
In millions of SDRs	8,981	55	3,048	14,635	9,232	100	33	401	379
Average annual access	141	23	124	434	265	100	21	51	40
Total access in percent of: 2/									
Actual quota	424	36	302	790	634	100	32	75	63
Calculated 11th review quota	258	64	101	414	247	100	13	42	32
Gross domestic product	10	89	3	7	6	100	1	3	2
Gross international reserves	92	76	27	121	80	91	5	47	46
Exports of goods and nonfactor services	39	77	11	43	30	100	2	7	6
Imports of goods and nonfactor services	71	86	14	49	35	100	2	7	5
Total external debt stock	9	52	5	15	11	88	2	7	5
M2	20	79	4	18	18	89	1	13	120
Proposed phasing (in percent of quota) 3/		Year 1	Year 2	Year 3					
SBA/EFF		221	108	95					

Source: Executive Board documents, MONA database, and Fund staff estimates.

1/ High access cases include all available data at approval and on augmentation for the 22 requests to the Board since 1994 which involved the use of the exceptional circumstances clause or SRF resources. Exceptional access augmentations are counted as separate observations. For the purpose of measuring access as a ratio of different metrics, access includes augmentations and previously approved and drawn amounts.

2/ The data used to calculate all ratios is the projection, at the time of program approval, for the year in which the program is approved.

3/ Phasing is based on program years.

Debt Sustainability and the Sovereign Debt Restructuring

1. This Annex discusses Argentina's public debt sustainability, and provides updated information on the projected availability of resources to meet debt service due to official and private creditors.

A. Background

2. **In November 2001, Argentina embarked on a two-phase approach to debt restructuring to deal with a debt service burden that was no longer sustainable:**

- **The first phase ("phase 1") was aimed mainly at domestic creditors.** The exchange involved an offer to exchange all U.S. dollar and Argentine *peso* bonds for new domestic guaranteed loans. It was completed in December 2001 with about US$42 billion of federal government bonds exchanged, and was later extended to include Arg$23 billion of provincial debt. Debt restructured in phase 1 has continued to be serviced.

- **The second phase ("phase 2") was to be aimed mainly at foreign creditors.** However, on December 23, 2001, the authorities declared a moratorium on the service of bonds held by private creditors and of debt to most official bilateral creditors. As a result, the phase 2 restructuring was never initiated.

3. **Phase 2 debt is projected to reach US$89 billion by end-2003 (Table 1).** Most of this debt is held by external creditors—both institutional and retail—from Europe, Japan, and the United States. In August 2003, the authorities issued an executive decree that moved some US$13 billion of bonds held mainly by domestic pension funds from phase 1 into phase 2 (these bonds had an original value, after including arrears, of US$19–20 billion prior to the phase 1 exchange); the pension funds had not accepted the *pesoization* of their guaranteed loans denominated in foreign currency.

4. **The authorities intend to announce the broad terms of a restructuring offer to creditors at the 2003 Annual Meetings.** In particular, they have said that they will clarify the scope of debt to be restructured, the treatment of initial claims, including past due interest, and the general terms of the new restructured instruments.

B. Debt financing and sustainability analysis

5. **The staff's baseline scenario makes the following assumptions** (with details shown in Table 2):

- A constant primary surplus of 3 percent of GDP from 2004–10.

- The program macroeconomic framework as illustrated in the authorities' Memorandum of Economic and Financial Policies (http://www.imf.org).

- Exposure to the IFIs is kept constant during the program period, and is then reduced by US$1.5 billion each year from 2007 onwards, of which US$1 billion relates to the

Fund and US$0.5 billion to the World Bank and IDB. A rollover of principal to the Paris Club and other creditors throughout the projection period is also assumed.

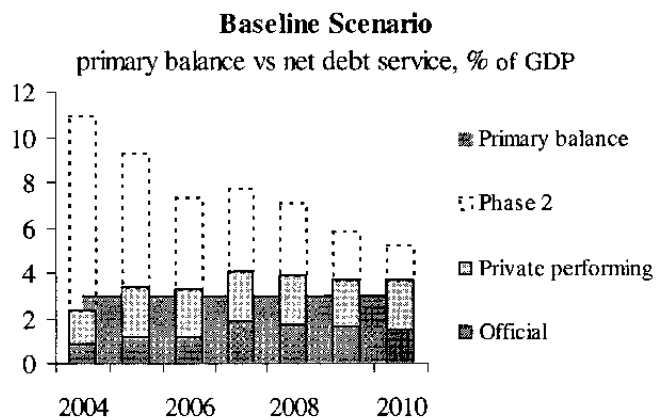
- New domestic financing at market rates is assumed to be sufficient to roll over 100 percent of phase 1 loans, bank compensation bonds, and other provincial debt throughout the projection period.

- The BCRA is assumed to roll over 100 percent of maturing quasi-money bonds. Bonds issued for deposit conversion and to compensate civil servants for unpaid wages (averaging about US$1 billion a year during 2004-06) are assumed to be amortized on the scheduled dates.

- No additional market access beyond these rollovers is assumed.

6. **On these assumptions, the baseline scenario gives the following results:**

- There would be large financing gaps during 2004–06, averaging 6 percent of GDP a year (assuming phase 2 creditors are paid on a contractual basis); these large gaps would persist in the outer years, averaging 3.5 percent of GDP a year (Table 3). Excluding phase 2 debt service would reduce the financing gaps to zero on average during the program period and to 0.9 percent of GDP on average in the outer years.



- Net debt service to the official sector and on performing private debt would consume 3.3 percent of GDP on average over 2005–06, the final two years of the program period. IFIs and other official debt would account for one-third of this amount.

- The financing need for servicing the official sector and the performing private debt would rise to 4 percent of GDP in the outer years, reflecting declining IFI exposure from 2007 onwards.

- Thus, a primary surplus of 3 percent of GDP would not be sufficient to cover payments due on official debt and private performing debt after 2004; it would also leave no room for payments to phase 2 creditors (Text Figure).

- The assumed rollover of domestic debt cannot be taken as assured.

- Other ways to close the financing gaps (beyond increasing the primary surplus) include broadening the restructuring beyond phase 2 debt, and using international reserves.

C. Sensitivity analysis

7. **The baseline scenario is sensitive to key assumptions** (Table 4):

- A change in the primary surplus naturally has a one-for-one effect on the size of the financing gap.

- A 1 percentage point reduction in the growth rate during 2004–10, to 3 percent over the program period, and below 3 percent thereafter, would raise the financing gap by 0.1 percentage points of GDP on average a year during the program period and around 0.2 percent of GDP on average during 2007–10.

- A 10 percent step depreciation in the exchange rate in 2004 compared with the baseline would increase the financing gap by about 0.2 percent of GDP on average a year.

- A 3 percentage point higher interest rate applying to new market borrowing during 2004–10 would increase the financing gap by about 0.3 percentage points of GDP throughout the period.

- An assumption of 50 percent rollover by phase 1 and bank creditors, rather than 100 percent, would raise financing gaps by around 1 percent of GDP a year, while an assumption of 50 percent rollover by depositors, rather than zero, would reduce the financing gap by only 0.1 percent of GDP per year.

- Financing gaps could also be reduced by the resumption of new domestic and international market access before 2010.

- In summary, the above results show that the size of financing gaps is sensitive to various assumptions but, in the absence of changes in the primary surplus, it is difficult to envisage a scenario that allows performing debt and restructured phase 2 debt to be serviced on a sustained basis.

Table 1. Projected Consolidated Public Debt: 2001-03

(In US$ billions, end period)

	2001	2002	2003 June Est.	2003 Dec Proj.
Total debt (I+II)	**167.8**	**152.9**	**171.2**	**186.6**
In percent of GDP 2/	*62.4*	*150.7*	*141.0*	*149.4*
I. Federal government	**144.5**	**137.3**	**152.6**	**179.5**
A. Official debt	36.8	36.0	36.3	36.6
1. Multilaterals	32.4	31.1	31.2	31.4
IMF	14.0	14.3	15.0	14.8
World Bank	9.7	8.5	8.1	7.9
IADB	8.7	8.4	8.0	8.6
2. Bilateral	4.5	4.9	5.1	5.2
B. Private creditors	42.3	98.4	111.7	136.1
1. Performing debt	42.3	37.0	43.2	46.6
a. Banks (Bodens), compensation for:	0.0	8.9	8.8	12.9
Asymmetric pesoization	0.0	0.0	6.4	8.3
Foreign exchange exposure (Cobertura bonds)	0.0	2.4	2.4	3.2
Asymmetric indexation	0.0	0.0	0.0	1.3
b. Depositors (Bodens)	0.0	5.3	5.7	7.2
Exchange of deposits for bonds	0.0	...	5.7	5.9
Compensation associated with deposit liberalization	0.0	...	0.0	1.3
c. Civil servants (compensation for 2001 13 percent wage cut)	0.0	0.0	0.6	1.2
d. Phase 1 debt 1/	42.3	22.8	28.2	25.4
2. Nonperforming (Phase 2) debt	...	61.4	68.5	89.4
C. BCRA (Quasi-monies bonds)	0.0	0.0	0.7	2.6
D. Other	65.4	2.9	3.8	4.2
Treasury bills, bonds and other short-term instruments	61.8	0.0	0.0	0.3
Central bank short-term financing	0.0	1.1	1.8	1.9
Banks and other	3.6	1.8	2.0	2.0
II. Provincial governments (net of intergovernmental debt)	**23.3**	**15.6**	**18.6**	**7.1**
Memorandum items:				
Nonperforming debt 3/	...	92.8	84.9	100.2
Performing debt	167.8	60.1	86.2	86.4
Multilaterals 4/	32.4	14.3	31.2	31.4
Private creditors, BCRA, and other	135.4	38.1	45.7	51.5

Sources: Fund staff estimates based on historical data provided by the Argentine authorities.

1/ Includes provincial debt assumed by the federal government.

2/ The calculation uses US$ GDP of the preceding 12 months.

3/ This includes the sum of nonperforming Phase 2 debt, bilateral, bank and other debt, and assumes half of provincial debt is nonperforming.

4/ Reflects arrears to multilateral development banks at end 2002.

Table 2. Baseline Assumptions

	2004	2005	2006	2007	2008	2009	2010
	(in percent, unless stated otherwise)						
A. Macro assumptions							
Real GDP growth	4.0	4.0	4.0	3.7	3.5	3.4	3.3
CPI inflation (average)	9.4	8.6	7.1	5.6	4.4	3.4	2.9
Nominal exchange rate (Arg$ per US$) average	2.84	2.87	2.85	2.89	2.91	2.94	3.00
B. Policy assumptions							
Primary balance (in percent of GDP)	3.0	3.0	3.0	3.0	3.0	3.0	3.0
Official rollover (in percent of principal)							
IMF	103	95	100	77	80	67	59
WB/IDB	100	100	100	80	76	74	76
Bilateral	100	100	100	100	100	100	100
Private sector rollover (in percent of principal)	72	76	85	87	87	92	91
Phase 1 debt	...	100	100	100	100	100	100
Bank compensation bonds	100	100	100	100	100	100	100
Deposit bonds	0	0	0	0	0	0	0
Compensation for civil servants	0	0	0	0	0	0	0
Quasi-money bonds and other provincial debt	100	100	100	100	100	100	100
Amortizations on new borrowing	...	100	100	100	100	100	100

Source: Fund staff estimates based on historical data provided by the Argentine authorities.

Table 3. Argentina: Medium-Term Consolidated Government Financing Projections
Before Further Debt Restructuring, 2004-10

	2004	2005	2006	2007	2008	2009	2010
	(In billions of US$, unless stated otherwise)						
A. Financing Needs	**24.8**	**24.1**	**24.1**	**27.8**	**28.2**	**28.7**	**26.5**
Total cash interest	6.7	7.1	8.0	7.8	7.5	7.2	7.3
Official	1.5	1.8	2.0	2.1	2.0	1.9	1.8
IMF	0.5	0.6	0.7	0.8	0.7	0.6	0.6
World Bank and IDB	0.7	0.9	1.0	1.0	1.0	0.9	0.9
Bilateral 1/	0.3	0.3	0.3	0.3	0.3	0.3	0.3
Debt held by private creditors	5.2	5.3	5.9	5.7	5.5	5.3	5.5
Performing debt	1.6	2.2	2.8	3.2	3.4	3.7	4.1
Non-performing (Phase 2) 2/	3.6	3.1	3.1	2.6	2.1	1.6	1.4
Quasi-money bonds	0.1	0.1	0.1	0.0	0.0	0.0	0.0
Amortizations	18.1	17.0	16.1	20.0	20.7	21.5	19.3
Official	7.5	5.2	5.0	7.9	8.5	5.8	5.5
IMF	5.2	3.0	1.9	4.3	5.1	3.1	2.4
World Bank and IDB	1.2	1.5	2.4	2.4	2.1	1.9	2.0
Bilateral	1.1	0.7	0.8	1.1	1.4	0.9	1.1
Debt held by private creditors	10.3	11.4	10.5	11.6	11.7	15.1	13.2
Performing debt	1.4	4.9	6.6	7.3	7.5	12.1	11.2
Nonperforming (Phase 2) 2/	9.0	6.5	4.0	4.3	4.2	3.0	2.0
Quasi-money bonds	0.3	0.4	0.5	0.5	0.5	0.5	0.5
B. Financing sources	**13.1**	**13.9**	**16.4**	**18.9**	**20.0**	**22.6**	**21.6**
New borrowing	8.7	9.1	11.1	13.3	14.1	16.4	15.1
Official	7.6	5.0	5.0	6.4	7.0	4.3	4.0
IMF	5.3	2.8	1.9	3.3	4.1	2.1	1.4
World Bank and IDB	1.2	1.5	2.4	1.9	1.6	1.4	1.5
Bilateral	1.1	0.7	0.8	1.1	1.4	0.9	1.1
Private 3/	0.8	3.6	5.6	6.4	6.5	11.5	10.6
Rollover of quasi-money bonds by BCRA	0.3	0.4	0.5	0.5	0.5	0.5	0.5
Primary balance (authorities' baseline scenario)	4.4	4.8	5.3	5.6	6.0	6.3	6.5
in percent of GDP	*3.0*	*3.0*	*3.0*	*3.0*	*3.0*	*3.0*	*3.0*
C. Financing gap (=A-B) 4/	**11.7**	**10.2**	**7.7**	**8.9**	**8.2**	**6.1**	**4.9**
in percent of GDP	*8.0*	*6.4*	*4.4*	*4.8*	*4.1*	*2.9*	*2.3*
D. Consolidated government debt 4/	**193**	**195**	**197**	**196**	**194**	**188**	**182**
in percent of GDP	*132*	*122*	*112*	*105*	*98*	*90*	*84*
Memo items:							
Primary surplus required to service official debt	1.3	1.9	2.0	3.6	3.5	3.4	3.3
in percent of GDP	*0.9*	*1.2*	*1.1*	*1.9*	*1.7*	*1.6*	*1.5*
Primary surplus required to service official and performing private debt	3.5	5.4	5.8	7.7	7.9	7.7	8.0
in percent of GDP	*2.4*	*3.3*	*3.3*	*4.1*	*3.9*	*3.7*	*3.7*
Financing gap before Phase 2 debt service	-0.9	0.5	0.5	2.1	1.9	1.4	1.5
in percent of GDP	*-0.6*	*0.3*	*0.3*	*1.1*	*0.9*	*0.7*	*0.7*
Total cash interest (in percent of GDP)	*4.6*	*4.4*	*4.5*	*4.2*	*3.8*	*3.5*	*3.4*
Of which: excluding Phase 2 interest payments	*2.1*	*2.5*	*2.8*	*2.8*	*2.7*	*2.7*	*2.7*
Interest capitalization (in percent of GDP)	*2.5*	*1.9*	*1.5*	*1.1*	*0.8*	*0.6*	*0.5*

Source: Fund staff estimates.

1/ Assumes a rescheduling in which amortization is fully rolled over.
2/ Excludes cash interest and amortization payment needs arising from principal and interest arrears.
3/ New borrowing results from the assumed full rollover at market interest rates of Phase 1 loans, quasi-money bonds and other provincial debt.
4/ Assumes financing gaps will be eliminated by debt restructuring or other means and therefore will not add to debt levels or create interest costs.

Table 4. Argentina: Sensitivity of Financing Gaps

	2004	2005	2006	2007	2008	2009	2010
	Financing gaps excluding Phase 2 debt 1/ (in percent of GDP, unless stated otherwise)						
Baseline scenario	**-0.6**	**0.3**	**0.3**	**1.1**	**0.9**	**0.7**	**0.7**
Sensitivity to primary surplus							
Primary surplus higher by 1 percent a year	-1.6	-0.7	-0.7	0.1	-0.1	-0.3	-0.3
Primary surplus lower by 1 percent a year	0.4	1.3	1.3	2.1	1.9	1.7	1.7
Sensitivity to GDP growth							
GDP growth higher by 1 percent a year	-0.7	0.2	0.2	0.9	0.7	0.4	0.4
GDP growth lower by 1 percent a year	-0.6	0.4	0.4	1.3	1.2	0.9	1.0
Sensitivity to nominal exchange rate							
Nominal exchange rate 10 percent more appreciated from 2004 onwards	-0.7	0.1	0.1	0.9	0.7	0.5	0.5
Nominal exchange rate 10 percent more depreciated from 2004 onwards	-0.5	0.6	0.5	1.4	1.2	0.9	1.0
Sensitivity to Libor rate							
Interest rates 3 percentage points higher	-0.3	0.6	0.5	1.4	1.2	0.9	1.0
Interest rates 1 percentage point lower	-0.7	0.2	0.2	1.0	0.9	0.6	0.6
Sensitivity to rollover rates							
Depositors roll over at 50 percent rather than 0 percent	-0.7	0.1	0.2	1.0	0.9	0.6	0.7
Banks and Phase 1 roll over at 50 percent rather than 100 percent	-0.4	1.4	1.6	2.3	1.9	2.6	2.0
Memo item:							
Phase 2 contractual debt service	8.6	6.0	4.0	3.6	3.2	2.2	1.6

Source: Fund staff estimates

1/ On a contractual basis. Excludes cash interest and amortization payment needs arising from principal and interest arrears.

Statement by the IMF Staff Representative
September 20, 2003

The following information has become available following publication of the staff report. It does not affect the thrust of the staff appraisal.

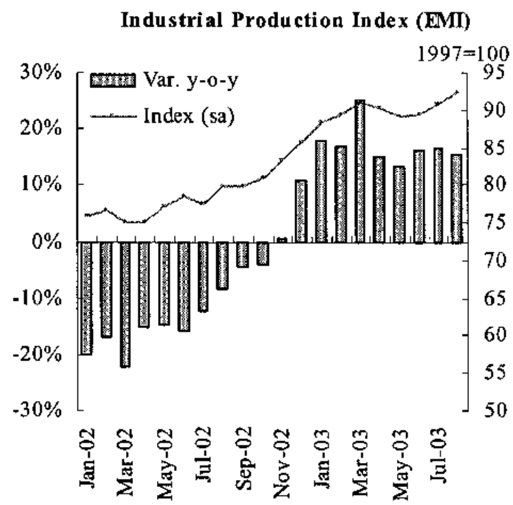
1. **Political Developments**

Candidates supported by President Kirchner prevailed in key provinces in last Sunday's gubernatorial and congressional elections. This augurs well for further expanding the President's power base, though more elections are to be held before end-November, involving 9 governors, 53 deputies, and 18 senators.

2. **Economic Developments**

Economic indicators point to a continuing recovery. In August, industrial production increased for the third consecutive month led by automobile production and continued growth in the import substitution sectors.

In August, federal tax collections continued to be strong and the primary surplus was about Arg$ 200 million above projections. This bodes well for achievement of the 2003 consolidated primary surplus target of 2.5 percent of GDP.



3. **The 2004 Budget**

On September 17, the government submitted to Congress the 2004 federal budget. On the basis of preliminary data available to staff, the proposed budget appears to be in line with the program's macroeconomic framework and consolidated primary surplus target of 3 percent of GDP. As in previous years, meeting fiscal targets will require under-execution of budget expenditures (by roughly 0.4 percent of GDP).

4. **Sovereign Debt Restructuring**

On September 12, a New York court ruled in favor of a large holder of defaulted Argentine bonds. However, the judge granted a 45-day stay of execution to allow the Argentine government time for appeal. On Monday, the authorities plan to announce details of their restructuring plan.

Press Release No. 03/160
CORRECTED: October 15, 2003
FOR IMMEDIATE RELEASE
September 20, 2003

International Monetary Fund
Washington, D.C. 20431 USA

IMF Approves US$12.55 Billion Three-Year Stand-By Credit for Argentina

The Executive Board of the International Monetary Fund (IMF) today approved a three-year, SDR 8.98 billion (about US$12.55 billion) Stand-By Credit Arrangement for Argentina to succeed the arrangement that expired on August 31, 2003 (see Press Release No. 03/09). In addition, the Executive Board approved the authorities' request for an extension of repayment expectations to an obligations schedule in an aggregate amount equivalent to SDR 1.74 billion (about US$2.43 billion).

Following the 24-member Executive Board's discussion of Argentina, which took place in Dubai, United Arab Emirates, ahead of the 2003 joint World Bank-IMF Annual Meetings, Anne Krueger, First Deputy Managing Director and Chair of the Board, said:

"The IMF Executive Board has approved the Argentine authorities' requests in the context of a medium-term economic program that seeks to restore sustained growth and improve poverty and equity indicators in Argentina.

"Over the past year and, since January, in the context of the transitional arrangement with the Fund, Argentina made a welcome start in restoring a measure of economic stability, with growth and confidence recovering, unemployment declining, and inflation being held under firm control. Notwithstanding this progress, many key challenges still face Argentina, and these are addressed in the new medium-term program.

"Argentina's new medium-term economic program has three fundamental elements. First, a medium-term fiscal framework to meet growth, employment, and social equity objectives, while providing a sound basis for normalizing relations with all creditors and ensuring debt sustainability. Second, a strategy to assure the strength of the banking system and facilitate the increase in bank lending that is essential to support the recovery. Third, institutional reforms to facilitate corporate debt restructuring, address issues of the utility companies, and fundamentally improve the investment climate. These actions are carefully sequenced within the program to promote greater ownership.

"The fiscal framework is at the core of the program. It targets a consolidated primary surplus of 3 percent of GDP in 2004, based on firm control over expenditures at the federal and provincial levels, and improvements in tax administration. The authorities have committed to primary surpluses in subsequent years that ensure a sustainable fiscal position over the medium term. Toward this end, the authorities have recognized the importance of undertaking further tax reform, while also securing early consensus on reforming intergovernmental relations. These actions are to be carried to a decisive stage in 2004.

"Regarding the financial program, the medium-term program seeks to entrench broad price stability, while implementing a comprehensive banking restructuring strategy. Toward this end, the monetary program is designed to anchor inflation expectations in the single digit range, helped by further institutional reforms. Thus, the authorities intend to study proposals for enhancing the central bank's independence, and to move to an inflation-targeting framework by end-2004. The banking strategy contains commitments to bring the regulatory and supervisory framework to international standards, to fostering the restructuring and recapitalization of public and private banks, and to implement compensating measures to offset the impact of official sector actions on banks' balance sheets.

"The authorities have committed to move ahead on several important fronts in the new program. The reform strategy includes commitments to put in place conditions that would foster corporate debt restructuring, which is also a key condition for renewed financial intermediation, develop a new regulatory framework for the utility companies, and take other actions that are crucial for legal predictability in Argentina.

"The Fund recognizes that a number of risks are associated with the proposed program, including those arising from the fact that key elements of fiscal and banking reforms that are crucial to sustainability will only be formulated at a later stage. Decisive policy actions by the Argentine authorities, along with strong policy ownership, will be crucial to minimize these risks.

"Finally, the authorities have continued to work toward restructuring sovereign debt. The Fund looks forward to continued progress being made in normalizing relations with creditors. Early conclusion of a sustainable restructuring agreement, which would pave the way for Argentina to return to capital markets, is fundamental to the success of the program," Ms. Krueger stated.

ANNEX

Program summary:

The Argentine authorities have prepared a three-year economic program aimed at establishing sustained growth, reducing widespread poverty and addressing a number of vulnerabilities—including from a massive debt overhang in the public and private sectors, an undercapitalized banking system stressed by crisis, and a weakened investment environment.

Growth and inflation: GDP growth is targeted to reach 5.5 percent in 2003 and stay at around 4 percent in 2004-06. **Core inflation** is expected to be maintained in single digits.

Fiscal policy will aim to raise the consolidated primary surplus from 2½ percent of GDP in 2003 to 3 percent in 2004. Beyond 2004, the authorities have committed to primary surpluses at levels sufficient to cover net payments on performing debt and obligations that may result under a debt restructuring agreement.

Structural fiscal reforms are envisaged to underpin the programmed fiscal consolidation and facilitate the phasing out of tax distortions. The reforms are sequenced to give time to build consensus. The authorities have committed to submit tax reform and intergovernmental reform legislation to Congress during 2004, with a view to their being introduced in the context of the 2005 budget.

Monetary policy will continue to aim at entrenching low inflation expectations, with base money growth driven mainly by the accumulation of international reserves. The authorities are considering moving to an inflation targeting regime by end-2004, and implementing supportive reforms aimed at increasing the autonomy of the central bank.

Banking reforms: The program aims at strengthening the soundness of the overall system and putting public banks on a sound financial footing. By end-2003, the authorities plan to eliminate temporary forbearance on the classification and provisioning of private loans and compensate banks for asymmetric pesoization and asymmetric indexation. As regards losses experienced by banks because of the legal injunctions (*amparos*), the authorities have committed to assess their impact and to identify measures to strengthen the system by end of 2003.

Debt restructuring: The authorities have also committed to advance negotiations with external creditors that is consistent with medium-term sustainability. They aim to conclude negotiations by mid-2004.

Utility companies, the authorities aim to obtain congressional approval by end-2003 of new legislation that delegates powers to the executive branch to renegotiate public concessions and effect interim tariff increases.

Predictable legal framework: the authorities will commit review the effectiveness of the insolvency system with a view to putting in place a legal and regulatory framework conducive to progress in private corporate debt restructuring.

Argentina joined the IMF on September 20,1956. Its quota is SDR 2.117 billion (about US$2.959 billion). Its outstanding use of IMF credit currently totals SDR 8.85 billion (about US$12.37 billion).

Statement by A. Guillermo Zoccali on Behalf of his Argentine Authorities
September 20, 2003

Overview

1. At the outset, I wish to acknowledge and express on behalf of my authorities sincere appreciation to the Managing Director, the management team and staff for their tireless efforts leading to the proposed recommendation of approval of a new three-year Stand by Arrangement with Argentina, to succeed the recently expired transitional program. They are also deeply grateful to Executive Directors and to their authorities for their willingness to remain engaged and supportive. The combination of a prolonged recession leading to the eruption of the crisis at end-2001 and the unprecedented economic and social dislocation that followed it severely tested Argentine people and institutions. It also served to reaffirm their desire for improved governance, a democratic process of renewal, and for keeping the country fully integrated to the international community of nations.

2. The twenty six Board meetings, both formal and informal, that were required since the crisis began, before consideration could be given to this medium-term program, are an indication of the difficulties for arriving at a common view on the set of conditions deemed necessary for sustainability in the presence of a very perverse dynamic.

3. In early 2002 Argentina exhibited a collapsing level of economic activity associated with the disorderly exit from the currency board arrangement, combined with a lack of access to official and private credit, a default on public bonded debt, widespread resort to quasi-money issuance by the provinces, frozen bank deposits and an inadequate social safety net. These constraints confronted the transitional administration, exacerbated governance concerns and complicated the initial dialogue with the Fund. In addition, the IFIs, including the Fund, received sizable net payments during this very difficult period. The magnitude of the imbalances and the perceived lack of financing may have contributed to the disorderliness of the adjustment path. The level of net Fund assistance granted in the capital account cases listed in Figure 1 of the staff paper on the assessment of the risks to the Fund and to its liquidity position (EBS/03/130, Supplement 2), serves also to give credence to the importance of some concrete, early element of exogenous support in capital account crisis countries not only to mitigate the costs of initially stabilizing the economy but, as importantly, to help catalyze more rapidly the broader conditions for private debt restructuring and for investment and growth to revive in a sustained fashion.

The Stepping Stone for Recovery

4. The transitional SBA with the Fund provided not only breathing room during the political transition to the May 2003 presidential elections, but as noted in the main staff report, helped to maintain macro-economic stability and the recovery in output and employment that began in the second half of 2002. In fact, the macro-economic targets of the program were met with wide margins. While technical factors such as the higher level of

inflation after the abandonment of the currency peg and the low level of capacity utilization and high unemployment may have contributed to limited pass-through and larger tax revenue, the critical factor behind the success of the transitional program has been the enhanced business and consumer confidence stemming from the prudent management of fiscal, monetary and social policies by my authorities since May 2002. This included holding primary expenditure and real wages in check, while enhancing social outlays and their effectiveness. GDP growth, which had eluded Argentina for over four years, has now been observed during the last five consecutive quarters.

5. In 2003, all the components of aggregate demand showed considerable strength. Most noticeable has been the rebound in investment, particularly in sectors that benefited from the import substitution process unleashed by the substantial real depreciation of the peso. Consumption spending was also helped by the improved liquidity that ensued from the many voluntary schemes implemented to terminate the generalized bank deposit freeze. Similarly, the relatively rapid moderation of price adjustments, the reinstatement of the temporary 13 percent cut of July 2001 in public sector wages, and the rise in employment contributed to the improved consumer sentiment. More recently, increases in minimum wages and in pensions, both of which were seriously eroded in real terms, served to sustain consumption growth without altering the path of fiscal consolidation. Although, real wages have increased in 2003, it is important to note the renewed productivity growth and that the draft budget for 2004 maintains the public sector wage bill, at about 2.7 percent of GDP, as another indication my authorities' commitment to fiscal restraint.

6. The significant external trade surplus has also contributed to the ongoing expansion. It is noteworthy that this is taking place in an environment of reinvigorated import growth. This underlying strength of the export drive is expected to continue in response to the more favorable international prices and, the lagged effect of the depreciation. Moreover, the context of full normalization of VAT refunds to exporters envisaged by next March, the improving liquidity conditions in the domestic financial system, and the gradual elimination of distortive export taxes, all suggest a substantial scope for further export growth, which my authorities consider as an essential component for restoring external viability.

7. The trend of fiscal consolidation initiated in 2002 was clearly policy-induced. The improvement in tax revenue reflects not only the continued growth momentum in the economy, but also the progress made in strengthening tax collection and fostering tax compliance. Export taxes introduced at the height of the crisis provided a timely revenue boost for the implementation of a broad-based social safety net to assist the most vulnerable segments of the population. In this regard, my authorities prioritized social outlays. They also embarked on increasing the efficiency and targeting of the heads *of households* program that provides critical income support to unemployed heads of households, while ensuring that the right incentives are in place for seeking gainful employment. Primary expenditure during the first half of this year was in real terms 28 percent lower than in the same period of 2001 and shows the commitment of my authorities to fiscal discipline. They are also fully aware of the distortive character of the export taxes and are planning their phased elimination beginning in January 1, 2005, in the context of a revenue-enhancing reform of the tax system and a second

round of administrative reforms to strengthen tax administration, in particular customs and social security collection.

8. On the monetary front, inflation has been much lower than projected at the outset of the transitional program, notwithstanding a significant expansion of base money in the first half of 2003. This confirms the rebound in money demand, which remains strong, and the importance of monitoring developments given the significant scope for further money demand growth. In any event, consumer price inflation has been on a downward trend from the beginning of the year with negative readings in recent months. Cumulative consumer price inflation for the first 8 months of 2003 was only 2.5 percent, while wholesale prices registered a negative 1 percent. The return of confidence in the peso, despite the virtual elimination of administrative and exchange controls introduced at the height of the crisis, accompanied the process of disinflation and may be ascribed to consistent implementation of prudent macroeconomic policies by the authorities. In this context, market interest rates fell sharply, particularly for Central Bank paper (Lebacs), the stock of which continues to grow providing the central bank with an effective instrument for indirect monetary control. The rate for 30 and 180-day central bank paper declined from 9.5 and 33.5 percent p.a., respectively, at end-January when the transitional arrangement was approved to 1 and 7.1 percent p.a., respectively, at end-August when the arrangement expired. Thus, the basis is being laid for moving towards adoption of a credible inflation-targeting regime, to be formally introduced by end-2004. While efforts are continuing to further enhance the independence and accountability of the central bank to the congress and the public, the credibility of the new regime ultimately will rest on the track-record of the monetary authority to reign in inflation.

9. The much improved financial market conditions and the meaningful progress noted in Paragraph 39 of my authorities' MEP to deal with the effects of asymmetric pesification and indexation attest also to the pragmatism guiding my authorities in the area of prudential strengthening and the strategy to build up the soundness of the banking system. The staff finds in annex 1 of the main document that the banking system appears solvent and highly liquid based on current prudential regulations, but remains highly vulnerable, in particular due to high financial losses and non-performing assets. This points to the importance of the staff's initial assessment regarding the nature of the problem and its dynamics. My authorities consider that the assertion that private sector credit growth following deep banking crises is frequently slow to recover, does not adequately characterize the Argentine situation, where there was no initial private sector credit overhang and the current level is at a historical low. They also note that financial losses have been declining sharply. The negative annualized returns on bank assets alluded to in paragraph 7 of the same annex have been fallen steadily from 12 percent in the first semester of 2002, to 6 percent in the second half of the year, to 3.7 in the first semester of 2003 and in current financial market conditions, my authorities consider a break-even likely as early as this semester. Moreover, the substantial reduction in real interest rates and the stability in the nominal exchange rate, despite the continued liberalization of foreign exchange market access, are contributing to reducing the size of the mismatch problem. Similarly, non-performing loans have fallen on average to 37 percent of bank credit. The higher ratio given in the staff report actually corresponds to the largest corporate borrowers, which reflect in particular pending debt restructurings of

privatized utility and concessions. In addition, the increasing opportunity cost for banks from very high liquidity positions, some Arg.$ 3.5 billion in excess of prudential requirements, is acting as an incentive for private sector credit to grow again. The stock of private sector credit contracted from 23 percent of GDP in 1998 to the historical low of only 8 percent last July. This level contrasts with the 40 percent average in Latin American economies. It also points to the substantial scope for further growth of private sector credit in Argentina and to the return of the banking system to profitability, in the context of the greater predictability offered by the new medium-term program. In sum, my authorities remain intent on strengthening the soundness of the banking system, both in the private and public banks, on prudently phasing out forbearance and in creating the conditions to for managing the balance-sheet mismatch risk and reinvigorating credit intermediation to the private sector to maintain the growth momentum.

The Medium-term Program for Growth and Fiscal and Debt Sustainability

10. The new three-year economic program for which Fund support is being requested, represents a fully-owned and finely-sequenced macro and structural policy framework for steadily achieving fiscal and external sustainability. It attempts to safeguard essential social and basic infrastructure spending to mitigate poverty conditions affecting over 50 percent of the population. It would also allow Argentina to establish a consolidated primary surplus of 3 percent of GDP, in contrast with an average adjusted deficit of some 2 percent of GDP in the period 92/01 and, in subsequent years, to conduct policy to ensure an extension of the trend of primary surplus initiated in 2002, and strengthened in 2003 and 2004, so as to produce levels sufficient to cover net payments on performing public debt and obligations that may result under a debt-restructuring agreement. Normalizing relations with external creditors and giving sustainability to the public debt represents a critical goal of the government, in the recognition that this is essential for reestablishing judicious access to private capital flows to support growth. My authorities have also sought to work in the broader reforms of intergovernmental finances that have been pending in Argentina since 1996, anchoring in the interim fiscal discipline at the provincial level in the continuation of annual bilateral agreements that have been yielding concrete results. They are also fully intent on restoring confidence in the rule of law that was unavoidably disrupted in the aftermath of the crisis. They are also keenly aware of the overwhelming demand for transparency and good governance in the country to make Argentina predictable and accountable. In this regard, the administration of President Kirchner has prioritized the revamping of the judicial system to make it more effective, among others through the introduction of a consultative process for the appointment of new members to the Supreme Court and for the selection of judges in general.

11. Concrete actions have also been taken early on in the new administration to combat corruption, as for example the recent intervention in PAMI the provider of health coverage and other services for retired persons. Even more significant is the government's drive to decisively tackle tax evasion, which is high and became more prevalent with the advent of the crisis. For the first time, special tax courts have become operational and 60 large cases will be heard by these tribunals before the end of the year. These measures to foster tax compliance are expected to be strengthened with rapid approval by Congress of an anti-

evasion package with harsh penalties for tax abuses i.e. operations with tax havens, informal employment practices and creation of phantom businesses. Moreover, it is worth highlighting that my authorities have not resorted to any kind of tax amnesty, and have included this as a continuous structural performance criterion during the life of the program.

12. The bold policy measures taken by the Administration of President Kirchner thus far, and the comprehensive nature of the conditionality established for the period September 2003/March 2004, include continuous and structural performance criteria and benchmarks. A partial listing verifies the substantive nature of the commitments which, inter alia, contain legislative approval of the 2004 budget, the tax administration reform package and the framework legislation for the renegotiation of privatized utility and infrastructure concessions; the ratification of bilateral fiscal agreements with the provinces; the termination of temporary forbearance for the valuation of private sector loans; formal agreement on the objectives of intergovernmental reform and fiscal responsibility legislation; and elimination of VAT arrears to exporters and a tax reform that includes the phased reduction in the financial transactions tax; these provide a clear indication of the earnestness of the effort of adjustment and reform to underpin the objective of achieving sustainability. As a result of a straightforward approach, President Kirchner now enjoys an approval rating of around 80 percent. His public endorsement of the Memorandum of Economic and Financial Policies (MEP) and the three-year arrangement with the IMF, covering three-quarters of his term office, reinforces the likelihood that the policy undertakings the Board is considering, can be successfully implemented.

13. The assertion in the staff document that the main risk to the program lies in key elements of fiscal and banking reforms left for formulation at a later stage, is tantamount to discounting altogether the value of the policy-induced trend increase in the primary surplus, noted in Paragraph 8 of my authorities' MEP, and of the substantive listing of conditions of macro-relevance program to ensure permanence and consistency into the medium-term. The sequencing also points to a well thought-out and challenging road map for garnering the broad-based support that is required to advance implementation of structural reforms, which have eluded Argentina for many years. The program is also based on a realistic macro-economic framework and estimate of potential growth in the medium-term, derived from the new set of relative prices and structural orientation of the economy aimed at achieving fiscal and debt sustainability, as well as the extent of spare capacity and pent up demand. Additionally, the built-in incentive structure to perform is far from lax given the intensity of the envisaged monitoring and reviews, the number and combination of pc's and benchmarks and the fact that the phasing is far from being a just a roll-over of maturities that fall due to the Fund. In fact, Fund exposure during the first year of the arrangement would also decline by about US$ 800 million (or some 30 percent of quota), and the gross exceptional assistance envisaged never exceeds the initial level of credit outstanding. This incentive structure points to the authorities' motivation of using the program as a platform for moving away from crisis-oriented measures, and for securing the normalization of economic relations with creditors in an environment of sustained growth.

14. To achieve debt sustainability and restructure the sovereign debt, my authorities are fully aware that Argentina will have to sustain the fiscal consolidation effort underway at both the federal and provincial levels. It goes without saying that sustainability is not only a matter of the given percentage of primary surplus being targeted but, as importantly, of the macro-economic conditions, i.e. the level of real interest and exchange rates, and the strength of economic activity. The assumptions on this front are in my authorities view conservative. Maintaining the momentum of growth, however, is deemed critical for the credibility of this effort. The Argentine economy has already experienced the effects of several failed attempts of ambitious fiscal tightening that only weakened growth and, in the end, delayed the desired fiscal consolidation; with the undesirable by product of a sovereign debt default. By safeguarding the growth objective, my authorities aim at ensuring that this new round of fiscal consolidation is consistent with the requirements for debt sustainability. In setting the level of primary surplus for 2003, my authorities also clearly indicated their commitment to ensure a level of primary surplus in subsequent years that is consistent with the sustainability objective, i.e. to cover the payments on the now performing debt and those that may arise from a debt restructuring agreement with private creditors. This strong and specific statement of the intention of my authorities in this area, seems to be downplayed in the third bullet of paragraph 54 of the main staff document on the risks to the program. The sustainability exercise prepared by staff is circumscribed to the period 2004/10, and is not necessarily in step with the term structure that may accompany the sovereign debt restructuring agreement. Moreover, the fact that the exercise does not contemplate any access to private financing during the period can be considered unduly pessimistic. In fact, one of the objectives of the medium-term program is to reestablish access to judicious levels of voluntary market financing, consistent with the experience of other countries that have successfully restructured their debt, and initiated a process of strong growth that reinforces the sustainability objective.

15. My authorities' strategy for restructuring their debt with private creditors is characterized by staff as a major risk to the program and source of market concern, justified only by the indirect connection made to the need for good-faith efforts in pursuing the restructuring. At the same time, there is recognition of my authorities' efforts to engage creditors in a constructive dialogue, including through the establishment of consultative working groups and widespread dissemination of information that will soon be reinforced by targeted websites in compliance with the criterion for exceptional access. In this regard, my authorities have consistently affirmed from the outset of the negotiations on a medium-term program with the Fund and other IFI's, in 2002, that once a medium-term macroeconomic program could be agreed and supported by the international financial community, they would immediately proceed with negotiations leading to the resolution of the restructuring of the sovereign debt in arrears. As indicated in the MEP describing their program, my authorities have made arrangements to present to private creditors next Monday here in Dubai the basic features of a restructuring offer on which they have been intensely working during with the assistance of international legal and financial advisors. In sum, my authorities consider that they are taking all necessary steps to move forward with complicated the restructuring of Argentina's sovereign debt and trust that this good faith will receive the continued support of the international financial community.

Conclusion

16. In keeping with my Argentine authorities' commitment to full transparency and the importance attached to their policy undertakings and relations with Fund, they have consented to the Fund's publication of the LOI, MEP and TMU, together with the associated staff documents prepared for the Board's consideration of their request for Stand-by Arrangement and Extension of Repurchase Expectations and a statement of their views. Posting is expected shortly in conformity with the Fund's general policy on transparency.

17. Lastly, the crisis in Argentina has produced an unprecedented deterioration in the standard of living of its people, which my authorities are determined to revert. Credibility will not be attained overnight. Macro-economic stability and recovery is an important first step, and the process of institutional and structural reform has been set in train. The support of the Fund and of the international community for Argentina's medium-term policy framework is now needed to give time for these actions to advance and bear fruit. As important, is the considered judgment providing confidence in the policy orientation to create the conditions for predictability and growth opportunities that will help to resolve the pending restructuring of the sovereign debt.