Central Bank of Argentina

Report on BANKS

JANUARY 2004

Year I – No. 5

CONTENTS

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SUMMARY

* January was the fourth month in succession in which interest income was positive, standing at 0.4% of netted assets (NA). This improvement in part reflected the downward trend in interest paid on deposits.

* The total book profit recorded by private banks was -$300 million, equivalent to –0.3% of NA and –2.1% of net worth. In annualized terms, this has implied a ROA of –3.2% and a ROE of –25.3%. However, this low level of profitability was affected by non-recurring factors related to adjustments to the value of public sector assets as part of the progress required by the Central Bank towards valuation of such securities at market prices. Excluding these effects, annualized ROA would have totaled –0.5%.

* The activity level (measured in relation to NA) remained stable in the case of private banks. Deposit growth (3% in real terms) contributed a flow of funds of almost $2 billion, applied mainly to the building up of liquid assets ($1.1 billion). Funds continued to be allocated to private sector lending ($60 million), continuing with the trend that began in October 2003.

* Higher volumes of sight deposits led deposit growth in the last two months, more than offsetting the drop in time deposits. In the case of the latter, there was an increase in deposits for longer terms as a result of rising confidence in the banking sector.

* Loans to the private sector recorded a drop in non-performance, led by the consumer and housing portfolios, in a context noted for the growth in such lending.

* In the first month in which minimum capital regulations have taken effect, the financial system recorded a capital compliance to risk-weighted assets ratio of 14%, well in excess of the requirements of prudential regulations and international standards.

* Profitability in February is expected to improve compared to January, as a result of the lower negative adjustments related to the valuation of public sector assets and the better interest margins from the rise in short-term lending and the decline in interest paid on deposits.

Note: This report contains information from January 2004 balance sheets available at 03/03/04. Although information is provided for public banks on some variables, the description centers mainly on the private bank aggregate (including breakdowns by uniform sub-groups). Figures provided (particularly in the case of profitability) are preliminary, and may be subject to change.

Chart 1

Exchange rates

- 2003 -

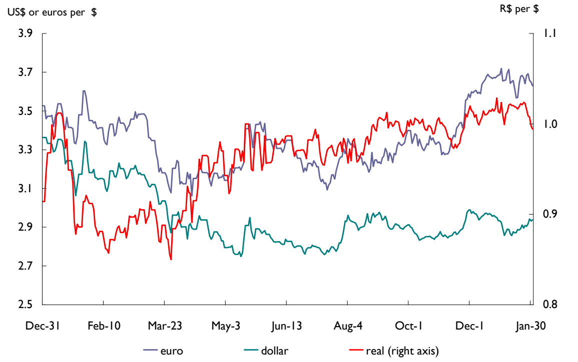
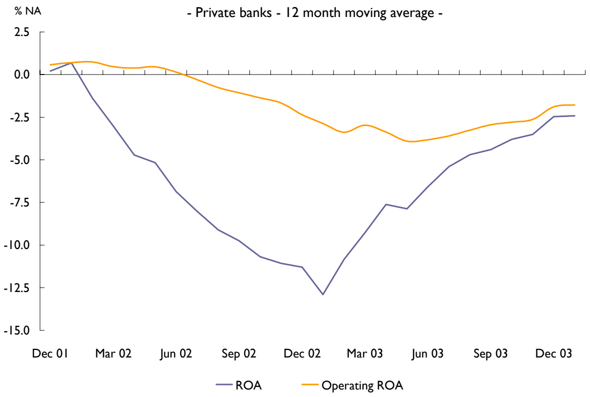


Chart 2

Profitability

- Private banks - 12 month moving average -



Context

1- **During January financial institutions operated in a context noted for stable prices and a downward trend in interest rates. The Consumer Price Index (CPI) went up 0.42% in the month, and the Reference Stabilization Coefficient**[1] (CER) rose 0.2%. The peso appreciated against the euro by 1.9% in nominal terms, taking the exchange rate to $3.64 per euro. The local currency also appreciated against the real by 2.6%, while remaining almost unchanged against the US dollar, ending January at $2.93 per US$ (see Chart 1). The cut-off rate for Central Bank bills (LEBAC) in pesos not adjusted by CER fell from 3.7% to 3.2% for 6-month maturities, while the one-year rate dropped from 8.5% to 7.85%. Interest rates for time deposits with 30- to 44-day terms fell from 3.6% to 2.9%, while those for terms of 60 days or longer fell from 3.8% to 3.4%. Lastly, call money rates remained at similar levels to those of previous months, at 1.6%.

Profitability[2]

2- As foreseen in the previous report, **private banks did not record positive results in January 2004. Losses totaled almost $300 million, a monthly return of –0.3% of netted assets (ROA) and –2.1% of net worth (ROE).** In annualized terms, these figures were a ROA of –3.2% and a ROE of –25.3%. Annual ROA has thus recorded a deterioration of over 6 percentage points (p.p.) in relation to the genuine but non-recurring profits in the previous months, although recording an improvement of almost half a percentage point compared to year-on-year losses. This level of losses took place in the context of a significant recovery in the profitability of private banks in recent months (see Chart 2). In the first half of the previous year these banks posted annualized losses for 4.5% of NA, while losses in the second half were virtually nil. If results for December and January are corrected for the variations of a non-recurring nature, both positive and negative, which, as will be seen in the following points, affected those months, it can be seen that bank profitability has remained stable at a level of close to –0.5% of NA.

3- In the case of the system as a whole profitability on NA was **–0.2% in the month and –2.3% in annualized terms; in relation to net worth it was –1.6% in the month and –18.7% on an annualized basis.** These indicators should be treated as preliminary, given that data from a leading public bank was unavailable at the time of writing.

4- **The loss recorded in January in the line for gains from securities was a result of the cost of the gradual correction to the valuation of government securities to mark them at market prices.** Com. "A" 4084,[3] when referring to government securities, established that securities for which prices are not routinely quoted (securities for which the Central Bank does not inform daily volatility), should be treated as "not traded", and valued at the latest available price for up to a month after volatility ceased to be published, subsequently setting up a provision for impairment risk. If non-recurring variations are

[1] Compiled on the basis of the geometric mean rate calculated on the change in CPI in the previous month.
[2] Unless otherwise specified, profitability figures are stated in annualized terms (See point f of the Methodology section)
[3] Modifying Com. "A" 3911.

disregarded, the result for January is 1.4% of NA, similar to the corrected result under this heading for December, in harmony with the result on securities for the whole of 2003 (1.7% of NA).

5- The decline in private bank profitability compared to December is mainly explained by the existence during that month of large non-recurring gains from the completion by a leading private bank of its debt restructuring process[4] (see Report on Banks for December). In addition, in January there was a drop in CER and CVS restatement, and a negative impact from the enforcement of the regulation on the valuation of government securities, only partly offset by a seasonal decline in operating costs.

6- Another impact of the policy for the gradual shift towards the marking to market of government securities, as required by Com. "A" 3911 and its subsequent modifications, **has been the increase as from January 2004 of 0.25 p.p. (to 3.25%) in the discount rate used to value these assets (secured loans and others). This resulted in the recording of losses from the valuation of government securities,** leading the "Other financial results" heading (which in December recorded an almost nil value) to record a loss of –0.4% in January in terms of NA, erasing the modest gains recorded the appreciation of other assets.

7- CER and CVS restatement, corrected for non-recurring adjustments, dropped slightly, from 1.3% to 1%, reflecting a slowing in the CER restatement rate during January. Nevertheless, given the presence of a major national bank that recorded a significant extraordinary correction to the amount it had accrued for CER and CVS in December (see the previous Report) **the final unadjusted amount showed a drop of almost 2 p.p. in January, recording a level of 1% of NA** (see Chart 3).

8- Traditional sources of banking income (interest and service income) remained relatively stable between December 2003 and January 2004. Income from services recorded a slight drop to a level of 2.2% of NA. **For the fourth month running, interest income was positive, although still low.** In January, the interest rate margin reached 0.4% of NA, 1 p.p. below the rate recorded in December, which recorded the positive, non-recurring effects of the restructuring of the debt of the institution referred to above. The improvement in interest income recorded in recent months is mainly a reflection of the drop in the cost of funding. Comparison between the monthly levels recorded during the first half of 2003 and those for the last months of that year and the first month of 2004 shows that whereas interest income fell by 1 p.p. to a level of an annualized 3% of NA, outlays under the same heading went from around 4.5% to 5% of NA down to a level of close to 2.8% of NA (see Chart 4).

9. Following the seasonal increase recorded in December, operating costs dropped in January by almost 1 p.p. to 4.3% of NA. This level is 0.2 p.p. lower than in the same month of the previous year, so it can be assumed that there is still a slight downward trend in the cost

Chart 3

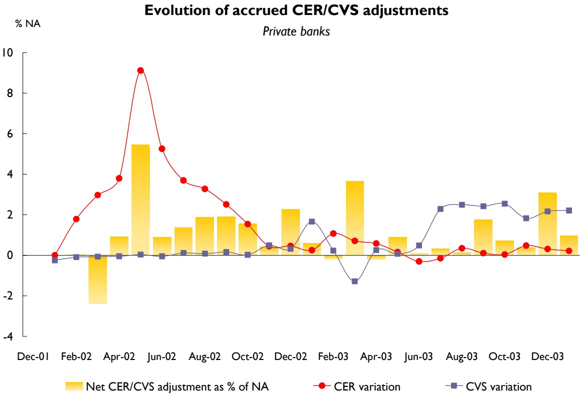


Chart 4

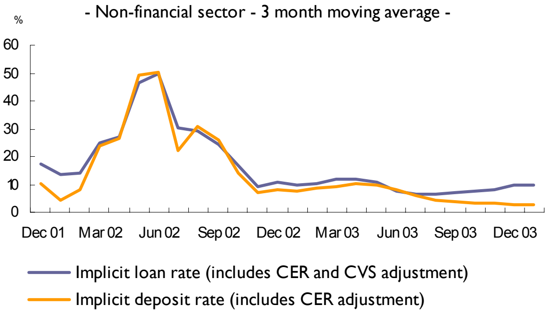
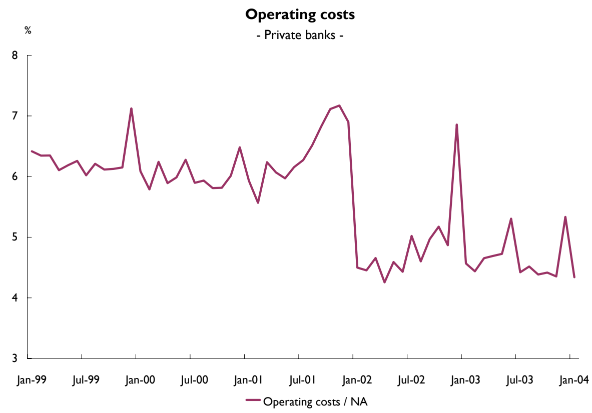


Chart 5

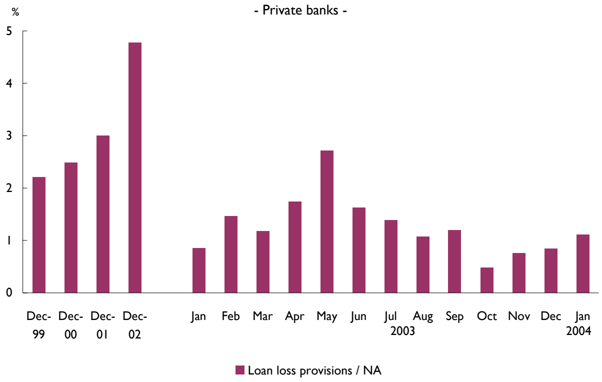


[4] It should be noted that the bank in question corrected the data submitted in December, reclassifying profits it had originally included under "Others" as gains from securities, and to a lesser extent, as interest income.

Chart 6

Loan loss provisions

- Private banks -



structure, coinciding with a certain drop in the number of employees, although this decline could lose strength as a result of the process of wage recovery (see Chart 5). Furthermore, **in January almost 82% of operating costs were met out of recurring revenue** (interest income, CER and CVS accrual and income from services). Although this represents a certain deterioration compared to the level in December 2003 (when cover was in excess of 100% as a result of the extraordinary nature of the CER accruals), coverage in the order of 80% is still high compared to that recorded during much of the previous year, when the monthly coverage ratio during the first three quarters was barely able to rise above 50%.

10- Loan loss provisions rose 0.3 p.p. to an annualized level of 1.1% of NA (see Chart 6). **In spite of this slight increase, they remain at a level of close to 1% of NA, which is low in historical terms,** after a period in which provisions were at a high level. Looking forward, given the favorable outlook for economic activity and the granting of new loans, it is expected that provisions -barring possible corrections of a non-recurring nature- will continue at a low level.

Table 1

Profitability by group

Annualized ROA in % - by type and area coverage

	2003	3-Dec	4-Jan	% share of NA (Jan)*
Public	-2.9	2.4	-0.5	*29.3*
Private	-2.5	3.1	-3.2	*69.7*
Retail	-2.6	2.9	-3.5	*66.3*
National coverage	-3.2	2.3	-4.3	*54.4*
Regional coverage	0.7	6.5	0.6	*11.6*
Specialized	0.8	-11.1	-3.8	*0.4*
Wholesale	-1.2	6.9	1.9	*3.4*
Non-bank institutions	-4.6	-7.0	3.1	*0.9*
TOTAL	**-2.6**	**2.8**	**-2.3**	*100*

(*) Percentage share of total NA according to January figures.

11- Lastly, **the other items heading improved in January, given the drop in charges for other provisions,** which had increased considerably in December in view of the closing of the accounting year. In January there were very moderate sundry gains leading to an improvement of almost 2 p.p. compared to the losses recorded in December.

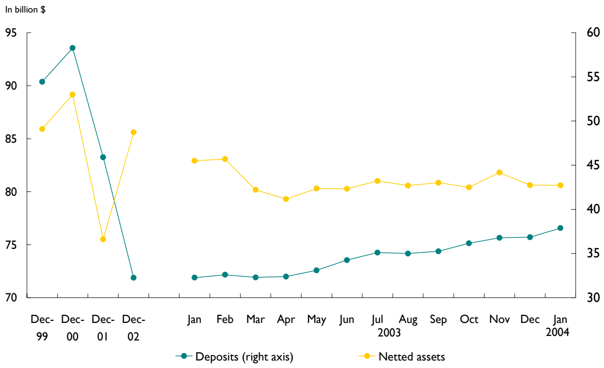
12- **Retail banks with a nationwide coverage (which have the largest weighting) and regional banks were the sub-groups showing the largest drop in their ROA**, with a decline of close to 6 p.p. in both cases (see Chart 1). Wholesale banks also recorded a worsening in their profitability, although of a lesser magnitude, mainly as a result of the positive impact in December from the reversal of the conversion into pesos (*pesificación*) of the current accounts held by banks at the Central Bank and abroad. Specialized retail banks recorded lower losses than in the previous month as a result of the seasonal decline in their operating costs (given the importance of these costs for this sub-group). Public banks also recorded a worsening in their results, although in this case data should be viewed as preliminary.

13- In terms of the individual banks, of the 60 institutions for which data was available for the month of January, 27 recorded losses, and **in 12 of these cases the losses were lower than in December.**

Chart 7

Netted assets and deposits

- Private banks - at Dec 99 prices -



Activity level and flow of funds

14- The financial system's activity level increased again in the first month of the year. NA for all banks rose by $2.0 billion, an increase in real terms of 1%. **Total deposits continued the upward trend they have been recording for several months, growing in January by 3%.** Deposits in foreign currency increased by 6% measured in dollars. In the case of the private bank group, NA remained stable compared to December, and total deposits recorded the same increase as for the entire system (see Chart 7).

Table 2

Estimated sources and uses of funds

Private banks - Jan-2004

In million pesos

Source		Uses	
Private sector deposits	1,800	Liquid assets [1]	1,070
Public sector deposits	190	LEBAC	210
Loans to the Public Sector	150	CEDRO	210
		Financial sector (net)	180
		Trusts	75
		Loans to the private sector	60
		Other	335

[1] Minimum cash compliance (cash, current accounts with the BCRA and special collateral accounts) and other liquid assets (with foreign branches or head offices).

Chart 8

CEDRO and deposits

- Private banks - Includes CER adjustment -

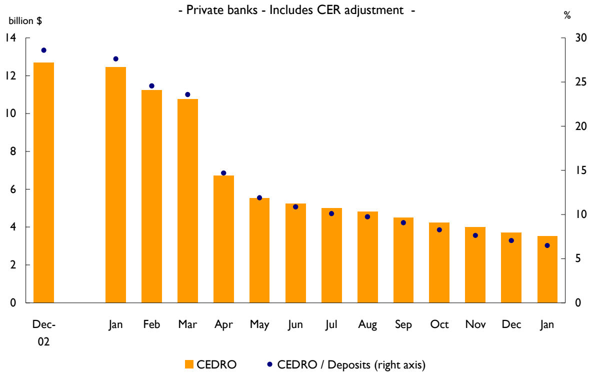
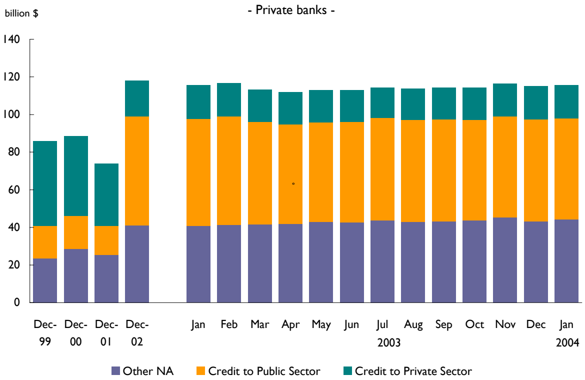


Chart 9

Asset portfolio

- Private banks -



15- Analysis of the main changes to balance sheet structure according to the flow of funds shows that private banks made use of funds totaling $2.14 billion, mainly acquiring liquid assets and LEBAC, and settling CEDRO liabilities. These funds came mainly from deposits by the private sector (see Table 2).

16- **Deposits were by far the largest source of funds during the month, having grown by $2.0 billion, well in excess of the positive flow in the last months of 2003.** Private sector savings accounts led the way, with new deposits for $1.1 billion, 9% of which were in dollars. In January 2004 the private financial system held deposits for $41.6 billion in pesos from the private sector (not including CEDRO or accrued interest), $14.2 billion more than in January 2003; deposits in dollars were US$830 higher, ending January at US$1.31 billion.

17- **A smaller source of funds was provided by government securities, with sales on the market for US$50 million ($150 million approximately) in BODEN 2012.** In terms of NA, public sector financing[5] fell 1 p.p., a result of both these sales and the impact of regulations on the valuation of these securities during the month and the settlement of debt abroad using BODEN 2012 in US$ - which is still underway as part of the debt restructuring process referred to in previous issues of this Report[6].

18- Among uses of funds, **liquid assets grew by $1.1 billion, driven by the greater volume of funds in the current accounts held by banks at the Central Bank as a result of a higher volume of deposits.** Of this increase, 20% corresponded to holdings in dollars.

19- **Investment in LEBAC rose by $210 million, a significantly larger investment than recorded in December** despite the steady drop in the yield on these securities, particularly in the case of the longer terms. These securities represented 5% of NA in January, with a growth in the last 12 months of 3 p.p.

20- It is estimated that **CEDRO repayments required disbursements for $210 million in January** (this calculation includes CER adjustments and the exchange difference from the settlement of certificates under the terms of court orders) a significantly lower amount than in previous months. As can be seen from Chart 8, these deposits accounted for 6.5% of deposits in January, a drop of 0.6 p.p. compared to December, as a consequence of the amortization of certain series falling due during the month and, to a lesser extent, as a result of outflows from court-ordered releases.

21- **As has been the case since October 2003, in January lending to the private sector has again registered as a use of funds,** rising by $60 million during the month[7], with an increase in short-term lending (credit cards, consumer loans, and to a lesser extent, current account overdrafts), which was partially offset by a drop in longer-term lending. **Regional retail banks and specialized institutions (the lending of which accounts for 20% of total loans to the private sector) increased**

[5] Includes government securities, financial system loans to the public sector and compensation from the federal government.
[6] These latter factors are not included in the calculation of the sources and uses of funds as they do not represent a movement of funds.
[7] This calculation eliminates the distortion generated by the writing-off of unrecoverable loans, now recorded in memorandum accounts.

their credit facilities by 4% and 5% respectively, with a notable increase in credit card lending and consumer loans by both groups, as well as in current account overdrafts in the case of regional banks and promissory notes in the case of specialized institutions. Lastly in this analysis of flows of funds, the net financial sector (loans, deposits and other obligations due to the financial sector) have meant a use of funds for $180 million.

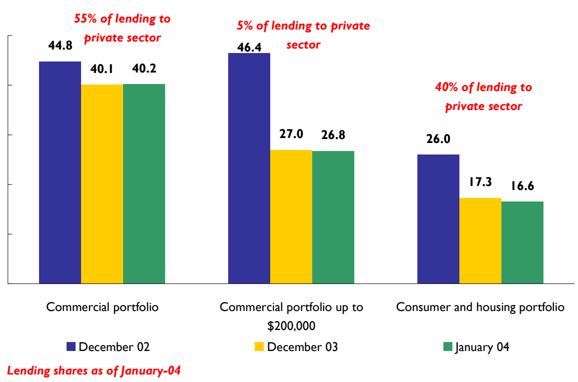
Credit[8] and liquidity risk

22- In January the quality of loans to the private sector remained stable at a level of close to 30% in the case of private banks, with a very slight drop (barely 0.3 p.p.) compared to the previous month, although 7.5 p.p. below the level recorded six months earlier. The level of non-performance by the private sector portfolio of the financial system aggregate remained at around 34%, reflecting the larger (but also declining) level of non-performance recorded by public banks (close to 44%).

Chart 10

Non-performing portfolio by type of lending

Private bank lending to private sector



23- As in previous months, the slight improvement in the level of non-performance in private banks took place as a result of the behavior of the consumer and housing loan portfolio (see Chart 10). This segment of the portfolio continued to record the lowest non-performance level (16.6%), as well as showing the greatest change since the previous month (with a drop of close to one percentage point). This result was due to a drop in the amount of non-performing loans in a context in which total loans to the segment recorded a moderate increase. Commercial loans continued to show a high level of non-performance -close to 40%- with a slower rate of recovery.

24- The non-performance of loans to the private sector for the various groups making up the private bank sector continued to evolve unevenly, as can be seen from the analysis of non-performance among the various bank sub-groups in the sector (see Table 3). **The banks with the greatest weighting (retail institutions with a nationwide coverage) retained as a sub-group the highest level of non-performance (although it remains below the level recorded by public banks)**, as there was no significant change from the previous month. Regional banks, with a lower weighting, recorded a slight decline in their non-performance, which stands at almost half the average level for the private bank sector. Lastly, specialized retailers and wholesalers -with a marginal weighting in total lending- continued to record non-performance levels close to the average for private banks, with a decline of between 1.5 p.p. and 2 p.p. compared to the previous month.

Table 3

Non-performing portfolio by group

As a % of non-financial private sector lending

	Dec-02	Dec-03	Jan-04	Share of lending to private sector(*)
Public	44.9	45.2	44.4	*29.0*
Private	37.5	30.5	30.2	*68.9*
Retail	37.7	30.5	30.2	*66.1*
National coverage	38.8	33.5	33.6	*53.1*
Regional coverage	27.7	15.9	14.9	*11.6*
Specialized	36.5	31.2	29.8	*1.4*
Wholesale	33.7	32.0	30.2	*2.7*
Non-bank institutions	36.6	16.3	16.2	*2.1*
TOTAL	**39.6**	**34.5**	**34.0**	*100.0*

(*) As of the last month.

25- In terms of individual banks, out of the 46 private institutions for which new data was available for January, **in 24 cases there was an improvement in the quality of lending to the private sector compared to December,** while in 8 cases there was no change.

26- In addition, collateral coverage for private bank loans also remained stable from December to January; **the percentage of non-performing loans to the private sector covered by preferred**

[8] Unless otherwise specified, this section refers to the quality of loans to the private non-financial sector.

Chart 11

Deposits and liquidity

- Private banks -

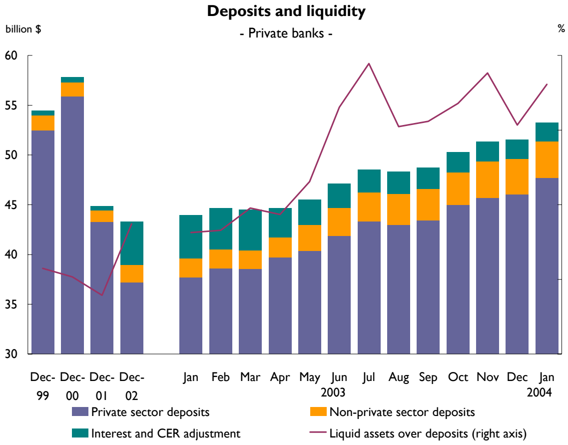


Chart 12

Netted assets and net worth

- Private banks -

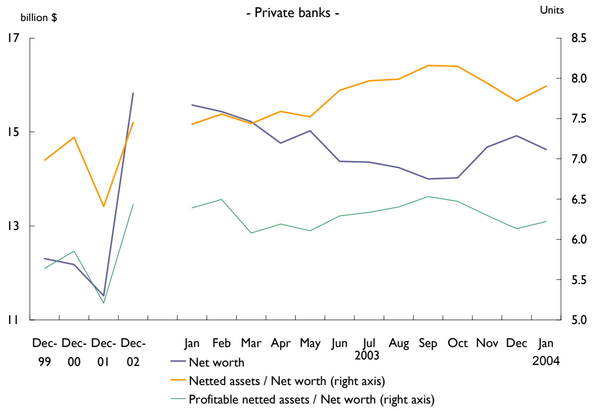
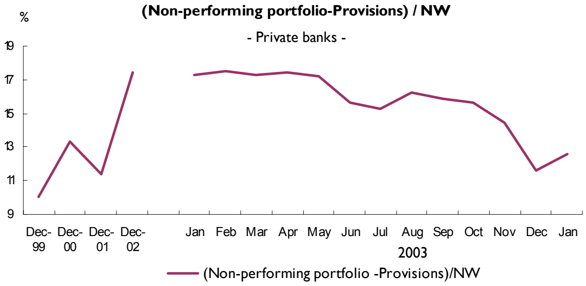


Chart 13

(Non-performing portfolio-Provisions) / NW

- Private banks -



guarantees remained at 23% (barely 2 p.p. below the level recorded in the same month of the previous year)**.** In the case of public banks, this ratio dropped by almost 3 p.p. from December to January to a level of 33.5%. Coverage by means of provisions remained at a level of 80% for private banks, with a notable performance by regional and specialized banks, with a ratio of provisions on their non-performing portfolios of close to 100%.

27- In view of the mentioned development of liquid assets and the monthly change in total deposit levels, the liquidity ratio for private banks (liquid assets as a percentage of total deposits) rose by 1 p.p., ending January at 29% and returning to its November level after the seasonal drop in the final month of 2003 (see Chart 11). In the last two months there has been a notable increase in sight accounts (savings accounts went up by 15% and current accounts rose by 10%), with a slight drop in time deposits (-2%) as a result of lower interest rates, causing the liquidity ratio on the more liquid deposits to fall by 6 p.p. Nevertheless, **the lengthening of time deposit maturities is a sign of the considerable improvement in the confidence of users of the financial system; deposits in the 30- to 59-day segment dropped 4 p.p. over the last two months (–14 p.p. in the last year), with deposits for longer terms gaining ground.**

28- On the matter of prudential regulations, **surplus liquidity returned to its November levels.** Excess compliance in terms of total deposits for private banks increased by 1 p.p., reaching 6% (variation between the various sub-groups was minimal; only wholesale banks, given the nature of their funding, recorded values much higher than the rest of the system). Public banks recorded the same monthly increase, with a January level of 11%.

Solvency

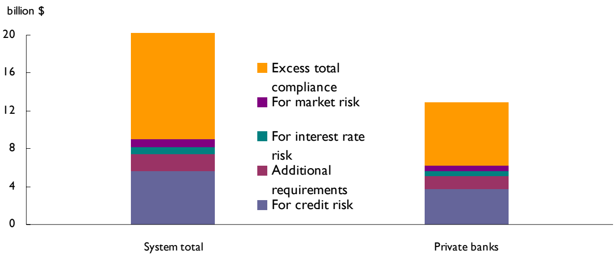
29- The net worth of private banks fell $290 million in the month (-2%) as a result of the losses recorded in January (see Chart 12). The leverage ratio (defined here as netted assets / net worth) returned to its November values, ending the month at 7.9 (from a level of 7.7 in December). In the case of public banks, the ratio rose from 9.8 to 10. For details of capital requirement compliance, see the next section.

30- In January, exposure of private bank net worth to private sector credit risk remained mostly unchanged. Non-performing loans to the private sector not covered by provisions as a percentage of net worth increased by barely 0.3 p.p. between December and January, remaining at a level of close to 10% (almost 7 p.p. below the level for the same month of the previous year, see Chart 13). This slight monthly increase was caused by the behavior of retail banks with nationwide coverage, which recorded an increase in exposure of close to one percentage point from a fall in the level of provisions higher than that recorded in their non-performing loans. Public banks recorded a drop of almost 2 p.p. in their exposure to credit risk from the private sector, which in terms of net worth reached a level similar to that of private banks in January.

Chart 14

Minimum capital requirements and compliance

January 2004 - Columns add to total capital compliance



New minimum capital regulations

31- As mentioned in previous issues of this Report, **since January 2004 compliance has been required with new regulations on minimum capital levels,** following the repeal of the previous system in December 2001, as a consequence of the serious domestic crisis that had a particular impact on the financial system.

32- The main changes since December 2001 to financial institution minimum capital regulations introduced by Communication "A" 3959 and subsequent communications are as follows:

a- **The requirements for credit risk on risk assets was cut to 8%,** in line with the international standard established by the Basel Committee;

b- **Suspension of the risk index** (IR) used to adjust capital requirements upward on the basis of the rate of interest on the loans granted by financial institutions;

c- **Application of the correction factor to the capital requirement based on ratings assigned to financial institutions by the Superintendence of Financial and Exchange Institutions** was suspended until June 2004;

d- **The dollar was included within the market risk requirements, as well as the CER and CVS indexes;**

e- **An additional requirement was set up for the risk of mismatching between inflation and market interest rates;**

f- **The same percentage was applied to the credit risk on holdings of public sector assets (securities and loans);**

h- **Risk weights were adjusted** to make them consistent with the changes in relation to guarantees and public sector assets.

i- **A temporary coefficient for calculating the requirement** for credit risk and interest rates was introduced, initially at levels of 0.05 and 0.2 respectively, with a schedule for convergence towards unity.

33- In January 2004, the first month in which the regulation was applied, **capital compliance ratios were well in excess of requirement.** Compliance in terms of risk-weighted assets reached 14%, both for the system as a whole and for private banks. Excess total compliance in terms of the total requirement[9] for January was 134% for all banks and 110% for private banks (with a certain dispersion among sub-groups for the total for private banks, although all show ratios in excess of 95%).

34- As can be seen from Chart 14, the capital requirement for credit risk and interest rates stood at $6.4 billion for the system as a whole. **Compliance measured in terms of the Adjusted Stockholders' Equity (or *Responsabilidad Patrimonial Computable*) totaled $19.4 million (measured in current pesos) recording a positive trend since the last quarter of 2003,** as a result of the increase in net worth from the capitalization of foreign debt and the improved results that have been recorded.

[9] This includes the capital requirement for credit risk, interest rate risk and market risk and the additional requirement for the role as custodian and/or registration agent, and for failure to comply with technical ratios. It also includes forbearances.

Outlook for February

35- In February it is expected that profitability will improve in comparison to January. **This will be due mainly to the lower impact of negative adjustments required by the schedule for marking government securities to market** in accordance with Com. "A" 3911 and the changes to the valuation of government securities made by Communication "A" 4084.

36- **The CER index has recorded no significant change in February, so no material changes are expected in the accrual of CER and CVS adjustments in that month.** The daily CER index series went from 1.46 at the end of January to 1.465 at the end of February, a percentage change only slightly higher to that recorded between December and January (see Table 4). In February the CVS should record a similar increase to that of previous months, with the inclusion of the last of the 8 installments laid down by Decree 392/03 increasing the wages of employees in the private sector. As a result, it is expected that as long as there are no extraordinary adjustments, the accrual for CER and CVS will remain around 1% of NA.

Table 4
Main developments in February

	Jan	Feb	Chg. (%)
Prices			
Exchange Rate ($/US$)[1]	2.93	2.92	-0.31
CPI	143.20	143.34	0.10
CER[1]	146.00	146.55	0.38
	%		Chg. (p.p.)
Average percentage rates			
Lending	21.5	20.5	-1.0
Private banks	21.5	20.4	-1.0
Overdraft	23.6	22.4	-1.2
Promissory notes	10.0	9.4	-0.6
Mortgage	10.4	9.9	-0.5
Pledge-backed	16.7	12.8	-4.0
Personal	42.1	44.9	2.8
Public banks	24.0	22.2	-1.8
Overdraft	24.8	22.6	-2.2
Promissory notes	13.9	12.8	-1.1
Mortgage	8.3	7.4	-0.9
Pledge-backed	16.8	15.1	-1.7
Personal	14.8	14.7	-0.1
30- to 44-day time deposit	2.8	2.2	-0.6
6-month LEBAC in pesos, w/o CER	3.2	3.1	-0.1
	In millions		Chg. (%)
Balance[1] - Private banks			
Peso deposits - Private sector	43,363	43,104	-0.6
Sight deposits	23,582	23,882	1.3
Time deposits	17,631	17,200	-2.4
Peso loans - Private sector	17,920	18,256	1.9
Overdraft	3,694	4,117	11.5
Promissory notes	3,150	3,190	1.3
Mortgage	5,436	5,377	-1.1
Pledge-backed	463	461	-0.3
Personal	1,534	1,512	-1.4

(1) End of month figure.

37- Analysis of **the evolution of balances and their corresponding interest rates makes it possible to predict that interest income will be positive and slightly higher.** In the case of interest revenue, in February there has been an increase in total loans granted, with significant growth in outstanding overdrafts. Although the rates of interest for this latter type of lending have continued to show a downward trend, overdrafts carry a high relative yield (with rates at close to 22%), so that the application of funds to such lines has a positive effect on the interest rate profit margin. On the matter of the cost of funding, once again in February there was an increase in the balance of sight deposits and a drop in that of time deposits; given the slight decline in the interest rates paid on time deposits - close to half a percentage point in the case of time deposits for terms of between 30 and 44 days. It is therefore expected that the cost of funding will fall, leading to further improvement in interest income.

38- **The remaining current income lines are expected to show stability, in line with the behavior recorded in recent months.** Income from services in particular should remain above 2% of NA, while operating costs will remain at slightly over 4% of NA. It is estimated that loan loss provisions will continue at low levels (around 1% of NA), given the improved prospects for economic activity and the steady increase in new (better-quality) lending.

Latest regulations

This section contains a summary of the main regulations related to the business of financial intermediation issued during the month (taking as a reference the date on which they came into force).

Due to its effect in January, mention is made first of **Communication "A" 3911** issued in March 2003, establishing the valuation method to be applied to holdings of government securities. This regulation set the schedule for the nominal interest rate used to discount such bonds; including adjustments to their value in six-month periods, the first of which fell due in December 2003. As from January 2004 the rate to be used was set at 3.25%, an increase of 0.25% form the previous period.

By means of **Communication "A" 4084** dated January 30, 2004 changes were made to the valuation of public sector assets. It established that "secured bonds" received by financial institutions in replacement of provincial debts should receive similar valuation treatment to that applied to notes issued under the terms of Decree 1579/02.
Guidelines were set for determining the "theoretical value" of the securities acquired as from February 28, 2003.
In addition, it was established that the "patriotic bonds" (Argentine Republic External Bills in Dollars), "Certificates for Option of Fiscal Credit" and the "Certificates for Option of Tax Credit" are to be stated at the book value, taking as a reference the current value of the securities which, because of their rate and term, were to record the lowest parity in relation to their nominal value. The differences arising from the application of this procedure are to be applied against the balance of a regularizing account.

In addition, a special treatment has been defined for those securities assigned in guarantee of advances granted by the Central Bank for the subscription of bonds (Decree 905/02). It this case, banks recording such assistance could opt irrevocably, to exclude these bonds from the general valuation criterion, in which case they were to be recorded according to the value admitted for the purpose of the setting up of the guarantees.
Furthermore, clarification was provided regarding the treatment to be granted to the securities held by banks in their treasury stock that were originally subject to minimum capital requirements for market risk, which, at the time the regulation was published did not have a regular market price. If the Central Bank does not publish the corresponding volatility, they should therefore be treated as securities without trading.

Lastly, as a new security known as "Central Bank Notes" has become available, it was established that these Notes are to be excluded from the limits in relation to the diversification of credit risk, granting them the same treatments as is given to Central Bank Bills.

Notes on methodology

(a) Aggregate balance sheet information is taken from the Monthly Accounting Information System (non-consolidated balances). To calculate data for the system aggregate, for institutions not providing data for the month under review, the latest information available is repeated in the aggregate balance sheet. When estimating income flows, however, consideration is given exclusively to those institutions providing data on the month in question.

(b) Due to the possible lack of data for a number of banks at the time of writing this Report, and given the possibility of subsequent corrections to the data provided by financial institutions, the data included – particularly for the last month mentioned – is of a preliminary nature. As the latest available data is always used, data related to earlier periods may not coincide with what had been previously mentioned in earlier issues of the Report. In these cases, the latter version should be considered as that of the best quality.

(c) Data on deposits and loans relate to balance sheet information and do not necessarily agree with those gathered by the centralized System of Information Requirements (SISCEN). Reasons for discrepancies include the exact date taken into account for the calculation of monthly variances and the items included in the definition adopted in each case.

(d) Qualitative information on specific transactions involving specific banks has been taken from the notes to the financial statements of the banks, or obtained on the basis of inquiries made of the supervisors at the Superintendence of Financial and Exchange Institutions.

(e) Estimates of the main sources and uses of funds: this table summarizes the aggregate principal movements of funds in the corresponding period, derived mainly from the institutions assets and liabilities management policies. In view of the source of this information – the main variations in the aggregate balance sheet headings for the institution aggregate – and the purpose of the table, when preparing it certain changes have been made, mainly on the grounds that changes related to the revaluation of items (for exchange rate or inflation adjustment, etc.) should be eliminated, as should those related to the accrual of provisions, depreciation and amortization, changes in the way certain transactions are recorded and the elimination from the balance sheet of assets for which recovery is doubtful (with 100% provisioning). In particular, balances of foreign currency items at the end of the period are restated at the exchange rate at the beginning of the period.

(f) The profitability indicators provided have been calculated on the basis of monthly results estimated on the basis of the changes in the amount of accumulated results during the year in progress. Unless otherwise indicated, profitability ratios have been annualized.

(g) Initially, the breakdown by group of banks was determined on the basis of the majority existing in decision-making – in terms of shareholders' meeting votes – distinguishing between privately-owned institutions and public institutions. With the aim of deepening the analysis, private institutions were further broken down according to their geographical and commercial coverage. As a result, wholesale banks were defined as those specializing in the large corporation and investor segment, which usually do not depend for their funding on deposits from the private non-financial sector. Retail banks were divided into those carrying out business at national level, those located in specific geographical regions – municipal, provincial or regional institutions – and institutions specializing in a financial sector niche market – generally smaller institutions. Lastly, it should be noted that this grouping has been carried out solely for analytical purposes and does not represent the only methodological criterion for grouping, while in addition, the detailing of the characteristics of each group of institutions has been established in a general manner.

Glossary

Consolidated (or aggregate) assets and liabilities: Those arising from excluding operations between financial system institutions.

Gains from securities: Includes income from government securities, short-term investments, corporate bonds, subordinated debt and options. In the case of government securities, it includes the results accrued from income, quotation differences, exponential increase on the basis of the internal rate of return (IRR), and from sales, as well as the charge for impairment to value.

Income from services: Commissions collected less commissions paid. Includes commissions on liabilities, credits, securities, guarantees granted, rental of safe deposit boxes and foreign trade and exchange transactions, excluding in the case of the latter results from the trading of foreign currency, which are recorded in the "Exchange difference" accounts (here included under the heading "Other financial results"). Outflows include commissions paid, contributions to the Banking Social Services Institute (ISSB), other contributions on service income and charges accrued for gross income tax.

Interest income (interest margin): Interest collected less interest paid on financial intermediation, on an accrual basis – taken from balance sheet – rather than on a cash basis. Includes interest on loans of government securities and premiums on repos and reverse repos.

Liquid assets: Minimum cash compliance – cash, current account at Central Bank and special accounts in guarantee – and other liquid items, including correspondent accounts.

MAE: Mercado Abierto Electrónico. Electronic over-the-counter market.

Net operating revenue: Interest income plus net adjustments according to the CER and CVS indexes in relation to financial intermediation plus service income.

Net worth exposure to counterpart risk: :Non-performing portfolio net of allowances in terms of net worth.

Netted assets and liabilities (NA): Those net of accounting duplications inherent to the recording of swaps, whether term or unsettled spot transactions.

NFPS: Non financial private sector.

Non-performing portfolio: Portfolio in categories 3 to 6, as per the debtor classification system.

Operating costs: Includes remuneration, social security payments, services and fees, sundry expenses, taxes and amortization.

Operating profits: Result from interest and net adjustments according to the CER and CVS indexes in relation to intermediation plus service income, less tax charges in relation to interest and services and operating costs.

Other financial results: Income from financial leasing, adjustments to valuation of credit to the public sector, contribution to the deposit guarantee fund, interest on liquid funds, difference in market price of gold and foreign exchange, premiums on the sale of foreign currency and other unidentified income (net).

Private sector credit: Loans to the private sector and private sector securities.

Public sector credit: Loans to the public sector, holdings of government securities and compensation receivable from the Federal Government.

ROA: Net profits as a percentage of netted assets. When referring to accumulated results the denominator includes the average netted assets for the reference months.

ROE: Net profits as a percentage of net worth. When referring to accumulated results the denominator includes the average net worth for the reference months.

Other: In the profitability structure, sundry gains – including gains from long-term investments, loan recoveries and release of allowances – and sundry losses – including losses on long-term investments, amortization of differences from court orders, loss on sale or impairment of fixed assets, amortization of goodwill.

SEFyC: Superintendence of Financial and Exchange Institutions.

Statistical exhibit

Balance sheet

Private banks

In current pesos (millions)	Dec 99	Dec 00	Dec 01	Dec 02	Jan 03	Dec 03	Jan 04	Change (%) Month-on-month	Change (%) 2004 End to end	Change (%) Year-on-year
Netted assets	**85,918**	**88,501**	**73,796**	**117,928**	**115,723**	**115,118**	**115,584**	**0.4**	**0.4**	**-0.1**
Liquid assets	13,228	13,920	10,576	11,044	11,107	14,500	15,565	7.3	7.3	40.1
Public bonds	6,433	7,583	1,627	19,751	19,155	22,047	21,776	-1.2	-1.2	13.7
Private bonds	410	563	451	273	216	172	167	-2.8	-2.8	-22.5
Loans	56,916	56,035	52,319	51,774	50,767	47,230	46,956	-0.6	-0.6	-7.5
Public sector	6,389	8,172	13,803	25,056	25,029	23,784	23,605	-0.7	-0.7	-5.7
Private sector	47,705	45,103	36,636	26,074	24,979	22,816	22,718	-0.4	-0.4	-9.0
Financial sector	2,823	2,760	1,880	644	760	630	633	0.4	0.4	-16.7
Provisions over loans	-3,119	-3,248	-3,957	-7,463	-7,194	-5,222	-5,116	-2.0	-2.0	-28.9
Other netted credits due to financial intermediation	4,470	5,730	4,489	26,235	25,426	20,673	20,711	0.2	0.2	-18.5
Purchases (net)	487	1,103	807	380	354	698	649	-7.0	-7.0	83.4
Corporate bonds and subordinated debt	1,022	724	665	1,514	1,413	1,394	1,390	-0.3	-0.3	-1.6
Unquoted trusts	958	1,609	1,637	6,205	6,232	3,573	3,749	4.9	4.9	-39.8
Compensation receivable	0	0	0	15,971	15,351	13,503	13,500	0.0	0.0	-12.1
BCRA	12	35	865	377	363	415	415	0.0	0.0	14.5
Assets under financial leases	796	776	752	553	538	387	384	-0.8	-0.8	-28.7
Shares and participation	1,371	1,651	1,703	3,123	3,118	2,790	2,881	3.3	3.3	-7.6
Fixed assets and sundry	3,246	3,225	3,150	5,198	5,173	4,903	4,875	-0.6	-0.6	-5.8
Foreign branches	48	75	112	-109	-107	-136	-137	0.6	0.6	28.0
Other assets	2,120	2,190	2,574	7,549	7,523	7,775	7,521	-3.3	-3.3	0.0
Netted liabilities	**73,615**	**76,322**	**62,281**	**102,101**	**100,148**	**100,200**	**100,958**	**0.8**	**0.8**	**0.8**
Deposits	54,447	57,833	44,863	44,445	45,044	52,625	54,318	3.2	3.2	20.6
Public sector (1)	1,342	1,276	950	1,636	1,765	3,076	3,263	6.1	6.1	84.9
Private sector (1)	52,460	55,917	43,270	38,289	38,764	47,097	48,738	3.5	3.5	25.7
Current account	5,022	4,960	7,158	8,905	8,292	11,588	11,939	3.0	3.0	44.0
Savings account	9,702	9,409	14,757	6,309	6,370	10,547	11,644	10.4	10.4	82.8
Time deposit	35,218	39,030	18,012	11,083	12,436	18,710	19,031	1.7	1.7	53.0
CEDRO	0	0	0	9,016	8,791	2,409	2,276	-5.5	-5.5	-74.1
Other netted liabilities due to financial intermediation	16,185	15,401	14,082	48,364	46,317	40,825	40,128	-1.7	-1.7	-13.4
Call money	2,146	2,293	1,514	836	905	726	647	-10.9	-10.9	-28.5
BCRA lines	274	83	1,758	16,624	16,242	17,030	17,052	0.1	0.1	5.0
Outstanding bonds	4,990	4,939	3,703	9,073	8,503	6,674	6,666	-0.1	-0.1	-21.6
Foreign lines of credit	6,680	5,491	4,644	15,434	14,378	9,998	9,788	-2.1	-2.1	-31.9
Sales (net)	492	510	99	349	340	168	183	8.8	8.8	-46.1
Subordinated debts	1,683	1,668	1,700	3,622	3,418	1,850	1,830	-1.1	-1.1	-46.5
Other liabilities	1,299	1,420	1,637	5,671	5,369	4,899	4,681	-4.4	-4.4	-12.8
Net worth	**12,304**	**12,178**	**11,515**	**15,827**	**15,575**	**14,919**	**14,626**	**-2.0**	**-2.0**	**-6.1**

(1) Does not include accrual on interest or CER.

Profitability structure

Private banks - in annualized terms

As % of	Yearly						2003	2004	Monthly	
netted assets	1999	2000	2001	2002	2003	2004	H2	H1	Dec-03	Jan-04
Net interest income	4.5	4.1	4.3	-0.2	0.1	0.4	0.3	0.4	1.4	0.4
Restatement by CER and CVS	0.0	0.0	0.0	1.1	0.9	1.0	1.1	1.0	3.1	1.0
Other financial income	0.5	0.7	1.0	4.3	-1.0	-0.4	0.8	-0.4	-0.2	-0.4
Service income margin	3.1	2.9	3.2	2.0	2.0	2.2	2.1	2.2	2.3	2.2
Gains on securities	1.1	1.4	1.2	2.5	1.7	-0.7	2.1	-0.7	5.4	-0.7
Operating costs	-6.3	-6.0	-6.4	-4.8	-4.6	-4.3	-4.6	-4.3	-5.3	-4.3
Loan-loss provisions	-2.2	-2.5	-3.0	-5.0	-1.3	-1.1	-1.0	-1.1	-0.8	-1.1
Tax charges	-0.4	-0.4	-0.5	-0.4	-0.3	-0.3	-0.3	-0.3	-0.4	-0.3
Income tax	-0.5	-0.4	-0.3	-0.2	-0.3	0.0	-0.1	0.0	-0.3	0.0
Other	0.5	0.4	0.7	-3.0	0.3	0.1	-1.6	0.1	-2.0	0.1
Monetary results	0.0	0.0	0.0	-7.5	0.0	0.0	0.0	0.0	0.0	0.0
ROA before income tax	0.8	0.6	0.5	-11.1	-2.2	-3.1	-0.3	-3.1	3.4	-3.1
ROA before monetary results	0.3	0.1	0.2	-3.8	-2.4	-3.2	-0.4	-3.2	3.1	-3.2
ROA	**0.3**	**0.1**	**0.2**	**-11.3**	**-2.4**	**-3.2**	**-0.4**	**-3.2**	**3.1**	**-3.2**
Indicators (%)										
ROE	**2.3**	**0.8**	**1.4**	**-79.0**	**-19.0**	**-25.3**	**-3.5**	**-25.3**	**23.8**	**-25.3**
Operating profit / NA	0.9	0.6	0.6	-2.4	-1.9	-1.1	-1.4	-1.1	1.0	-1.1
Operating revenue / operating costs	120.5	116.9	117.1	58.8	66.5	81.6	77.3	81.6	127.8	81.6
Interest income (with CER and CVS) / loans	..	13.9	16.1	24.7	8.9	7.5	8.3	7.5	13.6	7.5
Interest payments (with CER and CVS) / deposits	..	5.7	7.8	21.9	5.8	2.3	3.2	2.3	2.7	2.3

Note: interest income and the loan balances correspond to non-financial sector transactions.

Portfolio quality

Private banks

As percentages	Dec 99	Dec 00	Dec 01	Dec 02	Dec 03	Jan 04
Non-performing loans (overall)	7.6	8.3	9.9	19.9	15.7	15.6
Loans to the non-financial private sector	8.9	9.8	14.0	37.4	30.5	30.2
Commercial portfolio	6.2	7.6	15.2	44.5	40.1	40.3
Commercial portfolio up to $200,000	11.7	14.6	16.4	47.1	27.0	26.8
Consumption and housing portfolio	12.5	11.9	12.4	26.1	17.3	16.6
Provisions / Non-performing loans	69.4	67.7	75.7	73.3	77.3	77.4
(Non-performing - Provisions) / Overall financing	2.3	2.7	2.4	5.3	3.6	3.5
(Non-performing - Provisions) / Net worth	11.5	13.4	11.4	18.7	12.1	12.1