Statement by the Staff Representative on Argentina
June 20, 2018

This statement provides additional information that has become available since the Staff Report (EBS/18/53) was circulated to the Executive Board on June 13, 2018. The information does not alter the thrust of the staff appraisal.

Pressures on the FX have intensified since the Staff Report was sent to the Board. On Thursday June 14, the peso depreciated by 6.5 percent, at the end of a day where markets operated with very low levels of liquidity and without any intervention of the BCRA.

On the evening of Thursday June 14, the Governor of the Central Bank, Federico Sturzenegger, resigned, and was replaced by the Finance Minister, Luis Caputo. Sturzenegger motivated his decision with the loss of confidence in his stewardship by the markets. Together with Sturzenegger, other key members of the Monetary Policy Committee presented their resignation. The Finance Ministry will be reabsorbed into the Treasury. The Minister of Energy and the Minister of Production were also replaced.

On Monday, June 18, the authorities announced a series of measures to help stabilize FX markets. The measures aimed at absorbing liquidity and reducing the risk of a disorderly auction of the LEBACs, scheduled for Tuesday June 19. They included:

- Increasing the reserve requirements by 3 percentage points on June 21 (and a further 2 percentage points on July 18). The incremental part of this reserve requirement could be satisfied through holdings of fixed rate, peso Treasury bonds maturing in 2020.

- Relaxing the restrictions on banks' ability to purchase US$-denominated, domestic law debt in the secondary market.

- Reducing the limit on banks' net open FX position from 10 to 5 percent of regulatory capital. However, an additional 25 percent of regulatory capital could be held in these US$-denominated Treasury instruments.

- Announcing the mechanism (although not the volumes) for the central bank to auction the Treasury's FX holdings (arising from Fund budget support), based on a multiple-price auction set to begin on Thursday of this week.

- Announcing a process (but without an indication of volumes) for central bank auctions of foreign currency, to be implemented after market close, in cases where there are clear signs of market dysfunction (in terms of bid-ask spread, market volumes, or intraday volatility). An after trading-hours FX intervention, such as this one, is a highly unusual practice and possibly could prejudice price discovery during the trading day.

- Announcing the intention to auction FX for an amount up to US$ 400 million, only on Monday and Tuesday of this week, based on a multiple price auction that would take place after market close.

The measures contributed to stabilize the peso. The peso appreciated about 2 percent on Monday and was relatively stable on Tuesday, two days with still relatively low traded volumes. After market closed on Monday, the central bank sold US$ 175mn at a rate of AR$ 27.5, slightly more appreciated than the market close. The bank did not sell any FX on Tuesday.

The authorities also successfully issued USD 4 billion equivalent in peso bonds on Monday, although at relatively high rates. Treasury placed US$ 2 billion equivalent in a 28-month peso bonds (at a yield of 27.7 percent) and another US$ 2 billion (1.7 of which in US dollars) in a 12- month dual currency bond (that gives the investor a choice between a US$ yield of 4.5 percent or peso yield of 33 percent). The revenues from the issuance would finance the buyback of non-marketable, low interest, Treasury papers held by the BCRA. This would in turn allow the BCRA to roll off LEBACs by an equivalent amount.

Equity and bond markets have been suffering heavy losses over the past few days. The stock market lost 4½ percent since last week with a pronounced decline in utility companies and banks. The equity markets were affected by both political uncertainty (including the changes in the cabinet) and reports that Argentina would not be included as part of the MSCI emerging market index. The EMBI spread has increased by around 70 bps over the last week and reached its highest level (590 bps) since 2015. Bonds prices have also fallen since last Wednesday, (by about 1½ percent for 3-year US dollar denominated bonds).

On Tuesday, the BCRA completed its monthly LEBAC auction. With the peso equivalent of US$ 18.5 billion in LEBAC coming to maturity on Thursday, the BCRA accepted offers for a total of US$ 11.5 billion, with a cut-off interest rate of 47% for the 1-month bills.