

May 2016

Low Leverage

Over the last decade, Argentinian provincial debt has constantly declined as a percentage of current revenues, closing 2015 at an estimated aggregate 29.8%. According to Fitch Ratings' criteria, this metric is considered a strong indication of the debt burden and capacity to pay. Although there is no solvency risk at the consolidated level, the market constraints and difficulties accessing long-term financing have been constantly pressuring liquidity, leaving provinces exposed to refinancing risk. Provincial debt as a percentage of GDP remains very low, closing 2014 at 4.7%, which compares favorably with Latin American countries, such as Mexico (3.1%), Colombia (1.4%) and Brazil (11%).

High Inflation and Currency Depreciation

High inflation presents a challenge to healthy fiscal performance. Provinces have rigid expenditure structures, where personnel expenses represent close to 60% of current revenues. Salary and price adjustments have pressured operational expenditures, driving volatile operating margins since 2009. Debt service and growth in debt stock have also been affected by currency depreciation, as 64% of the consolidated provincial debt is denominated or linked to foreign currency (USD). Some provinces with revenues linked to commodities and royalties have a natural hedge to some extent. Despite these challenges, Fitch believes Argentinian provinces' fiscal performance is manageable.

Ratings Constrained at the Country Ceiling

Compared with international peers, the key debt and fiscal metrics of the majority of Argentinian provinces suggest an intrinsic credit profile higher than the country ceiling of 'B'. Fitch currently rates two provinces — Salta and Neuquen — and the cities of Buenos Aires and La Plata at long-term foreign and local currency Issuer Default Ratings of 'B'.

Positive Outlook for Federal Transfers, but Negotiation Still in Progress

Fitch believes the devolution of the 15% federal transfer share from Argentina to the provinces is a credit positive. Decree 408/2016 establishes a gradual devolution over five years. Negotiations are underway regarding the progressive nature of the devolution and debt recognition in years the withholding was effective. Federal transfers currently represent 50% of provinces' consolidated revenues. Other topics under negotiation include a new coparticipation system; using funds to increase investment in education and basic infrastructure; establishing a regime to sustain fiscal and financial recovery for the national and local governments; and transferring assignments, goods and services.

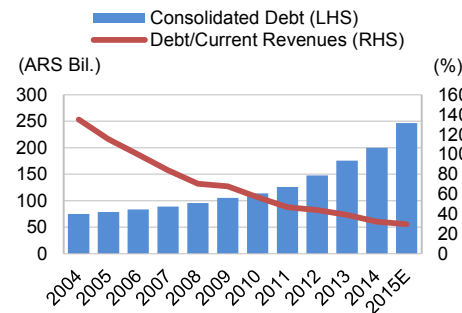
2016 Provincial Financing Needs

Provinces' 2016 borrowing requirements amount to ARS66 billion (USD4.6 billion), which could be higher, as some provinces also have authorization to refinance existing debt to get better terms and conditions. Fitch recently assigned an expected rating of 'B(EXP)' to a bond issuance from Neuquen of up to USD526.2 million, which will be backed by a share of gas and oil royalties.

Humberto Panti
+52 81 8399-9152
humberto.panti@fitchratings.com

Gerardo Carrillo
+52 55 5955-1600
gerardo.carrillo@fitchratings.com

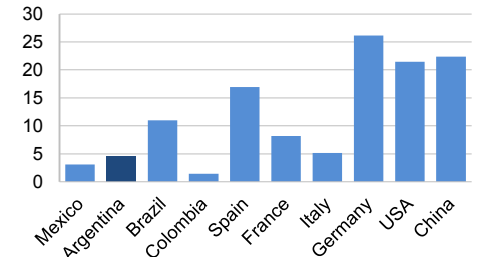
Provinces Debt



E – Estimate.
Source: E&R, Fitch calculations.

LRG Debt/GDP

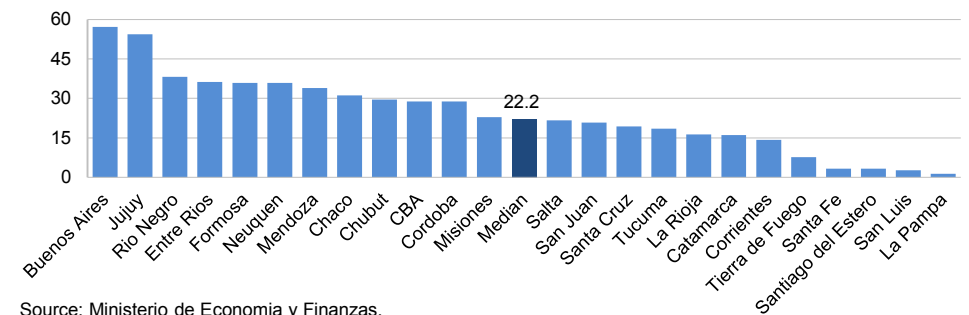
(%, Select Countries, 2015)



LRG – Local and regional government. Note: As of 2014, Argentina includes only provincial debt.
Source: Fitch.

Debt/Current Revenues

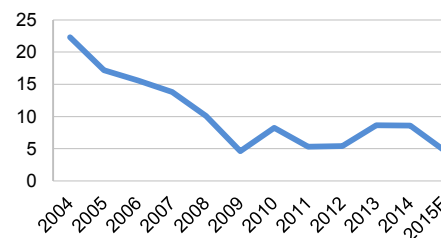
(%, 2014)



Source: Ministerio de Economia y Finanzas.

Operating Margin

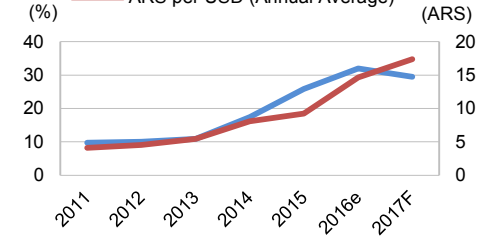
(%, Consolidated Provinces)



E – Estimate.
Source: E&R, Fitch calculations.

Inflation and FX

(%) Consumer Prices (Annual % Change)
(ARS) ARS per USD (Annual Average)



F – Forecast.
Source: Fitch.

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