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Potential Agreement with the IMF: Great News

The government has finally published the DNU. The decree does not provide much detail about the agreement with the IMF, but in our view, it leaves plenty of room for optimism. Let's break it down.

First, it is confirmed that the program will be an Extended Fund Facility (EFF). This type of agreement is typically approved for periods of three to four years to implement structural reforms. The most important aspect is the repayment period, which ranges from 4.5 to 10 years, with payments in 12 semiannual installments. Notably, the grace period is quite favorable for the Central Bank's fragile net reserves (currently negative by approximately USD 4 billion).

Between 2025 and 2028, inclusive, Argentina must pay capital of USD 12 billion to the IMF, with the total amount to be paid reaching USD 14 billion by March 2029. However, when including other international organizations, the disbursements exceed USD 20 billion. The agreement with the IMF not only allows for the refinancing of its maturities, but it also facilitates refinancing with the other organizations (CAF, WB, and IDB). The DNU does not specify whether there will be upfront funds or if the disbursements will be received as the principal matures. We believe the latter scenario is the most likely.

The big question for the market is whether or not new funds will be available for Argentina. We believe that the DNU provides several indications that there will be. This is where the "Letras Intransferibles" (bills) come into play. Remember that for many years, the Treasury paid off debt using international reserves. To do so, it issued several bills to the Central Bank. The BCRA's asset shifted from holding dollars to holding public bonds with no market value. Last year, the BCRA recognized an accounting loss and stopped valuing these bills at their residual value, opting instead to value them at their recoverable value.

Until now, this had no significance beyond the BCRA's accounting. However, now the bills have become part of the negotiation between the Government and the IMF, as they could be an elegant way to circumvent the Guzmán Law to refinance debt.

The DNU is unclear regarding the disbursement of fresh funds to recapitalize the BCRA through the cancellation of intransferable bills. However, if the intention is to reduce the consolidated debt, as the Government has stated on several occasions, we believe the most likely scenario is that the IMF will disburse as an advance the amount of the first bill due in June of this year, for USD 10.562 billion (the next significant maturity of intransferable bills is not until 2029).

In this way, the consolidated Treasury's debt decreases and the BCRA is capitalized in dollars, as it reduces a liability valued at its recoverable value, currently around one-third. Initially, it is just an accounting adjustment with little importance, but through fresh funds, it becomes a significant operation. The second option would be for the IMF to only disburse the recoverable value of these bills, an amount close to USD 3 billion.

We believe the most likely scenario is some kind of mixed scheme, with a partial initial disbursement. Advancing the USD 14 billion of maturities with the IMF itself, plus the USD 10.5 billion from this year's intransferable bills, seems unlikely to us.

However, given the emphasis the Government has placed on the recapitalization of the BCRA and the reduction in consolidated debt that the operation implies (mainly due to the creative accounting to avoid issues in Congress), we believe the USD 10.5 billion from the first letra intransferible would be the initial disbursement, a valuable upfront that goes directly to strengthening net reserves. The disbursement of the other USD 14 billion is likely still under negotiation.

Our reading is that the news is very positive, and the market's reaction has been too muted. Clearly, the correction of global markets did not help these days. The upfront disbursement could be very valuable. Contrary to other reports we've seen from investment banks, we believe that conditioning part of the future disbursements on a new economic program is also, to some extent, a positive factor. At the end of the day, the Government will easily meet the fiscal target, as it has been much more aggressive than any program from the IMF itself. On the other hand, the IMF will likely demand some exchange rate flexibility and, gradually, move towards a framework that will make it easier to absorb external shocks, which, for us, is more than welcome.

As we explained in other reports (see here), we believe that the current exchange rate regime (tablita or active crawling peg) could create balance of payments issues in the future if not phased out in time. Therefore, if the new program with the IMF involves increasing exchange rate flexibility over the coming months, we also see that as good news.

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