

CREDIT OPINION

21 November 2023

Update



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RATINGS

Chubut, Province of

Domicile	Argentina
Long Term Rating	Ca
Type	LT Issuer Rating - Fgn Curr
Outlook	Stable

Please see the [ratings section](#) at the end of this report for more information. The ratings and outlook shown reflect information as of the publication date.

Contacts

Philipp Toculescu +54.11.5129.2644
 Analyst
 philipp.toculescu@moody's.com

Cristiane Spercel +55.11.3043.7333
 Senior Vice President/Manager
 cristiane.spercel@moody's.com

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Chubut, Province of

Update to credit analysis

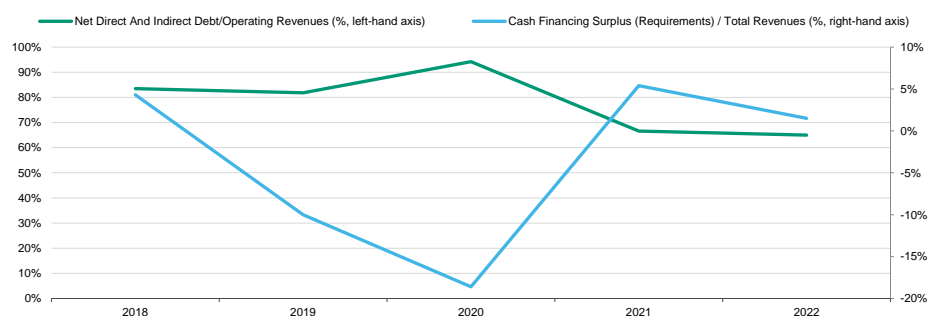
Summary

The credit profile of the [Province of Chubut](#) (Ca stable) reflects its history of volatile operating and financial results, tight liquidity, inflexible expenditure and high leverage. While the debt exchange completed in late 2020 brought a temporary relief to the province's finances, debt payments increased in 2023 and are set to rise materially in 2024. The risk of future debt restructuring remains high because of Chubut's persistent idiosyncratic risks and a difficult operating environment.

Like all Argentine regional and local governments (RLGs), the province has significant macroeconomic and financial links with the [Government of Argentina](#) (Ca stable). The credit profiles of the RLGs incorporate our expectation of continued elevated systemic risks marked by macroeconomic imbalances and constrained market access.

Exhibit 1

High leverage amid volatile financial results



Source: Moody's Investors Service and Province of Chubut's financial statements

Credit strengths

- » US dollar-linked revenue stream from hydrocarbon royalties, driven by the fact that Chubut is the largest oil-producing province in Argentina

Credit challenges

- » Track record of volatile operating and financial results
- » Exposure to foreign currency debt
- » Difficult operating environment

Rating outlook

The stable rating outlook captures our expectation that the economic and financial strain faced by the province will not differ significantly over the next 12-18 months. At the same time, the stable outlook incorporates our expectation that bondholders will not face losses exceeding that captured in the Ca rating (35%-65%).

Factors that could lead to an upgrade

Given the stable outlook, we do not anticipate upward pressure for the Province of Chubut. Nevertheless, an upgrade of the sovereign rating would increase upgrade rating pressure to the province's rating. For an upgrade, we would also consider if financing conditions stabilize. Upgrade pressure could also derive from a perception of lower than expected losses to private creditors in future debt restructurings.

Factors that could lead to a downgrade

A downgrade in Argentina's bond ratings or further systemic deterioration, or both, would exert downward pressure on the ratings. Increased idiosyncratic risks would also translate into a downgrade. We would also downgrade the ratings if a debt restructuring results in losses greater than those reflected in the current ratings.

Key indicators

Exhibit 2

Chubut, Province of Year ending December 31

	2018	2019	2020	2021	2022
Net Direct and Indirect Debt / Operating Revenue	83.5	81.8	94.2	66.6	65.0
Cash Financing Surplus (Deficit) / Total Revenue	4.3	-10.0	-18.6	5.4	1.5
Interest Expense / Operating Revenue	6.7	6.1	4.3	3.9	3.7
Gross Operating Balance / Operating Revenue	12.9	-2.7	-11.7	12.0	9.1
Capital Spending / Total Expenditures	11.7	7.8	6.8	8.5	9.0
Intergovernmental Transfers / Operating Revenue	31.4	29.9	35.7	34.7	34.6
Local GDP per capita/National Average	130.8	129.0	131.0	129.2	N / A

Source: Moody's Investors Service and Province of Chubut's financial statements

Detailed credit considerations

The credit profile of the Province of Chubut, as expressed in its Ca stable ratings, reflects a Baseline Credit Assessment (BCA) of Ca and a low likelihood of extraordinary support from the Argentine government in the event of acute liquidity stress.

Baseline Credit Assessment

US dollar-linked revenue stream from hydrocarbon royalties

Chubut is one of the largest crude oil-producing province in Argentina and it derives a large portion of its revenue from hydrocarbon royalties (see exhibit 3). The hydrocarbons law stipulates that oil and gas concessionaires must pay royalties to the provinces where they operate. The percentage of the hydrocarbon production payable by each concessionaire to each province as hydrocarbon royalties is set forth in each applicable concession. The amount of hydrocarbon royalties payable under Chubut's concessions is fixed at 12% of commercialized oil and gas production, and valued at the wellhead price. But this percentage may be reduced to 5% depending on the productivity, conditions and location of the wells.

The royalties revenue stream, which was equivalent to 19% of Chubut's total revenue in 2022, provides a natural hedge to the province's US dollar-denominated debt. This is an important credit consideration in the current environment of significant currency depreciation. However, royalties are paid in pesos at the selling exchange rate on the business day, immediately before the date on

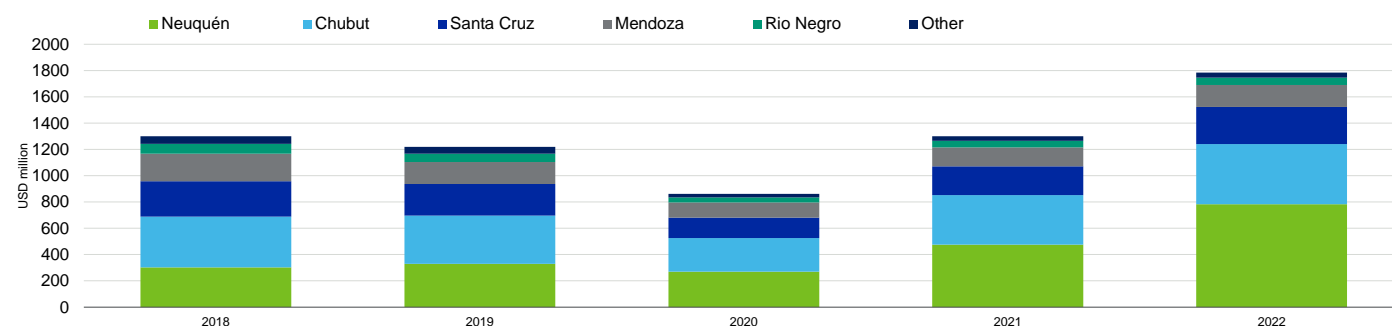
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which the payment is due. This means that while debt is partially hedged, royalties do not completely eliminate conversion risk in case that access to foreign currency becomes more restrictive.

Exhibit 3

Chubut is the third largest crude oil-producing province in Argentina

Annual crude oil royalties (\$ millions)



Source: Argentina's Energy Secretariat

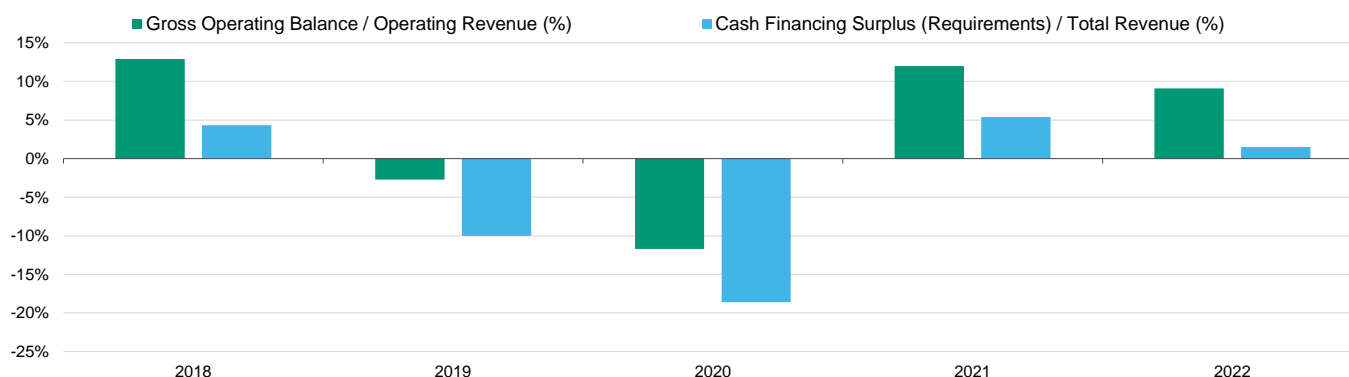
Track record of volatile operating and financial results

The Province of Chubut has historically presented a volatile financial performance (see exhibit 4). The recent improvement in credit metrics is primarily related to higher revenues intake, as a result of an accelerating local inflation and expenses that remained below the general increase in prices. During 2022, the province recorded a gross operating surplus of 9.1% and a cash financing surplus of 1.5%.

We do not expect the recent improvement in fiscal results to be sustainable in the long run, because the worsening economy will hit revenues. In addition, we expect social demands will keep adding pressure on the province to increase levels of spending. We anticipate Argentina's economy to contract by around 3.5% in 2023 and an additional 2.5% in 2024, after expanding by 5.2% in 2022. Meanwhile, Chubut will face greater social pressure to correct the accumulated delay of wages because of high inflation — to the detriment of fiscal results. We expect local inflation will accelerate to around 200% in 2023, up from 95% in 2022.

Exhibit 4

Chubut reports volatile operating and financial metrics



Sources: Moody's Investors Service and Province of Chubut's financial statements

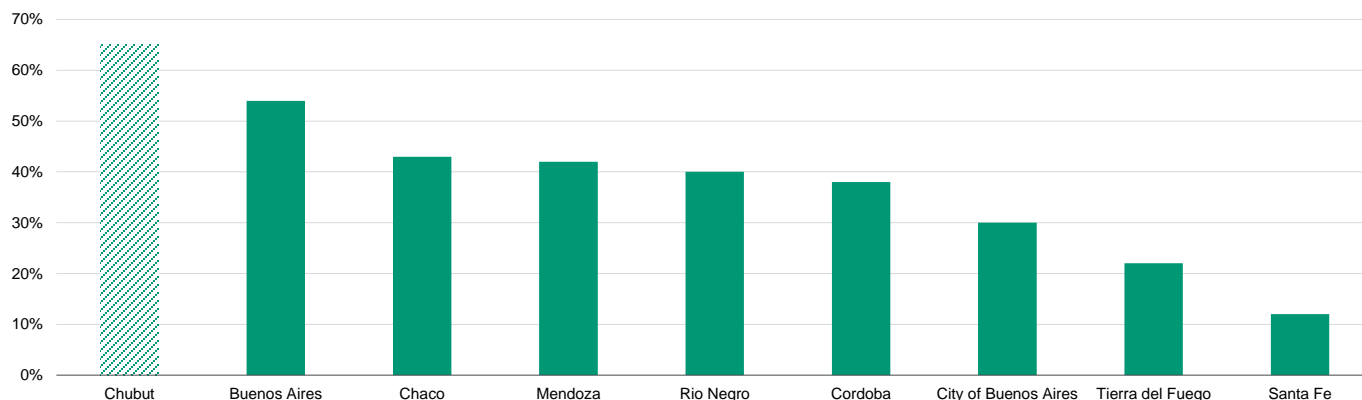
High leverage and exposure to foreign currency debt

Chubut's leverage decreased in the last two years, not only as a result of a controlled official exchange rate that remained below local inflation levels but also because of somewhat stronger fiscal results. However, the province leverage is still the highest among rated peers with net direct and indirect debt representing 65% of its operating revenue in 2022. The province also presents high exposure to foreign-currency debt, representing 66% of total debt for the same period. The rating factors in that a sudden correction in the exchange rate will sharply deteriorate the province's financial metrics.

Exhibit 5

Chubut presents the highest leverage among rated peers

Debt to operating revenue (%) as of December 2022



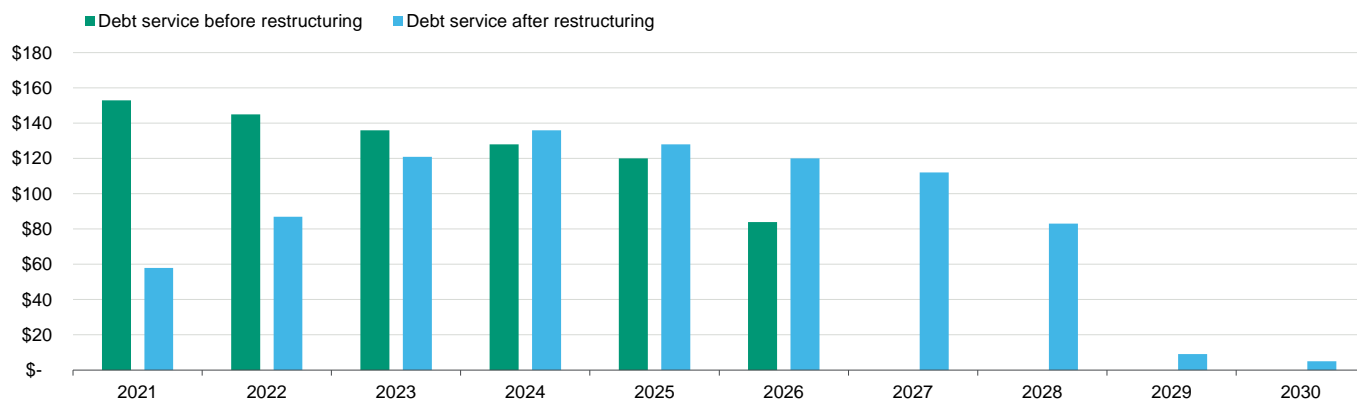
Source: Argentina's economy ministry

Despite the restructuring of the \$650 million notes, the risk of future debt restructuring remains high. While the exchange significantly eased the scheduled debt repayment for 2021 and 2022, in 2023 Chubut faced similar repayments to those before the restructuring. Furthermore, the province will face debt service payments of \$136 million in 2024 and \$128 the year after. Chubut's ability to meet those payments is uncertain given its low levels of foreign currency deposits, difficult operating environment and restricted access to both capital markets and foreign currency.

Exhibit 6

Following the restructuring, Chubut still faces significant principal debt payments

Debt service before and after restructuring (\$ million)



Source: Argentina's economy ministry

Difficult operating environment

We expect Argentine RLGs to continue enduring elevated systemic risk. Argentina presents high economic volatility, virtual lockout from international market-based sources of financing and significant reliance on the central bank to fund the government's large fiscal deficit. The large fiscal deficit increases short term macroeconomic imbalances. Despite the significant tightening of capital controls, pressure will persist on the country's currency and foreign exchange reserves.

Earlier this year the central bank said it [would restrict RLGs' access to foreign currency](#), requiring them to extend the maturity of at least 60% of their foreign-denominated debt by at least two years. While enforcement has been ambiguous, restrictions will become more severe if foreign reserves continue dwindling. Provinces had \$1.1 billion of foreign-currency deposits available as of August 2023, but their debt-service payments increase to \$1.6 billion in 2024 before surging to \$2.1 billion in 2025.

We also expect the fiscal strength of Argentine RLGs to deteriorate, as economic activity slows and inflation pressures remain high. Consequently, RLGs will have to maintain high levels of spending amid falling purchasing power leading to weaker operating results. A lack of external funding and restrictions on foreign currency access, further increase the risk of RLG debt restructurings through 2024.

Extraordinary support assumptions

We assess that there is a low probability of the Province of Chubut receiving extraordinary support from the national government, reflecting the lack of a history of timely intervention by the national government.

ESG considerations

Chubut, Province of's ESG credit impact score is CIS-4

Exhibit 7

ESG credit impact score

CIS-4



ESG considerations have a discernible impact on the current rating, which is lower than it would have been if ESG risks did not exist. The negative impact of ESG considerations on the rating is higher than for an issuer scored CIS-3.

Source: Moody's Investors Service

The Province of Chubut ESG Credit Impact Score is **CIS-4** reflecting its exposure to social and environmental risks and weak governance profile.

Exhibit 8

ESG issuer profile scores

ENVIRONMENTAL

E-4



SOCIAL

S-4



GOVERNANCE

G-4



Source: Moody's Investors Service

Environmental

E-4. Chubut's exposure to environmental risks reflects the risk that the loss of natural capital, physical climate risks and water stress pose to this province. Environmental risks would deeply impact relevant industries for Chubut's economic output such as oil and gas and mining. We also acknowledge that carbon transition risks are low because there is no significant pressure for decarbonization in the near term.

Social

S-4. Our overall assessment of social risk indicates high levels of exposure to labor and income and access to basic services related risks with moderate demographic, housing and health and safety pressures. Argentina has history of low job creation and macroeconomic instability that has increased domestic poverty but the country benefits from comparatively strong educational outcomes.

Governance

G-4. Chubut's governance score reflects the province's aggressive approach regarding debt and investment management because there has been acceptance of debt structures that pose significant risks. The province has exhibited exposure to foreign currency debt and a debt maturity profile concentrated in the short term. Chubut also presents weak transparency and disclosure practices as information is delivered with delays and with less level of detail. Balancing those risks is the province's overall stable institutional framework, with a relatively defined revenue profile supported by a federal tax sharing regime established by law.

ESG Issuer Profile Scores and Credit Impact Scores for the rated entity/transaction are available on Moodys.com. To view the latest scores, please click [here](#) to go to the landing page for the entity/transaction on MDC and view the ESG Scores section.

Rating methodology and scorecard factors

In the case of the Province of Chubut, the BCA matrix generates an estimated BCA of ca, which is in line with the BCA of ca assigned by the Rating Committee. The matrix-generated BCA of ca reflects an Idiosyncratic Risk score of 6 (presented below) on a 1-9 scale, where 1 represents the strongest relative credit quality and 9 the weakest. It also incorporates a Systemic Risk score of Ca, as reflected in the sovereign bond rating.

For details about our rating approach, please refer to the [Regional and Local Governments](#) rating methodology, published on January 16, 2018.

Exhibit 9

Chubut, Province of Regional and Local Governments

Baseline Credit Assessment – Scorecard	Score	Value	Sub-factor Weighting	Sub-factor Total	Factor Weighting	Total
Factor 1: Economic Fundamentals				3.4	20%	0.68
Economic Strength	1	129.20%	70%			
Economic Volatility	9		30%			
Factor 2: Institutional Framework				5.0	20%	1.00
Legislative Background	5		50%			
Financial Flexibility	5		50%			
Factor 3: Financial Position				5.3	30%	1.58
Operating Margin	3	6.96%	12.50%			
Interest Burden	5	3.84%	12.50%			
Liquidity	9		25%			
Debt Burden	5	66.24%	25%			
Debt Structure	3	19.50%	25%			
Factor 4: Governance and Management				9.0	30%	2.70
Risk Controls and Financial Management	5					
Investment and Debt Management	9					
Transparency and Disclosure	9					
Idiosyncratic Risk Assessment						5.95 (6)
Systemic Risk Assessment						Ca
Suggested BCA						ca
Assigned BCA						ca

[1] Local GDP per capita as a % of national GDP per capita

[2] Gross operating balance / operating revenue

[3] Interest payments / operating revenue

[4] Net direct and indirect debt / operating revenue

[5] Short-term direct debt / total direct debt

Source: Moody's Investors Service; Fiscal 2022

Ratings

Exhibit 10

Category	Moody's Rating
CHUBUT, PROVINCE OF	
Outlook	Stable
Baseline Credit Assessment	ca
Issuer Rating	Ca
Senior Secured	Ca

Source: Moody's Investors Service

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