



Latin American Sovereigns

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Latin American Sovereign Ratings (LTFC)

↗	Chile	A-	Stable
↗	Aruba	BBB	Stable
↗	Mexico	BBB-	Stable
↗	El Salvador	BB+	Negative
↗	Panama	BB+	Negative
↗	Costa Rica	BB	Negative
↗	Colombia	BB	Negative
↗	Peru	BB-	Negative
↗	Dominican Republic	B+	Stable
↗	Brazil	B	Positive
↗	Venezuela	B-	Stable
↗	Uruguay	B-	Stable
↗	Ecuador	CCC+	Stable
↗	Argentina	DDD	n/a

Key Latin Sovereign Rating Actions Last 6 mo.

- Brazil Revised Outlook to Positive June 3
- Venezuela Upgrade to B-
- Colombia BB Negative affirmed in May
- Uruguay Default in May; New bonds B-
- Ecuador Pos Outlook revised to Stable; CCC+
- Chile Affirmed in February
- Mexico BBB- affirmed in September

Three Latin Rating Groups

➤ Investment grade

- Higher savings rates & lower debt levels
- Stronger GDP and export growth
- Stable politics

➤ BB

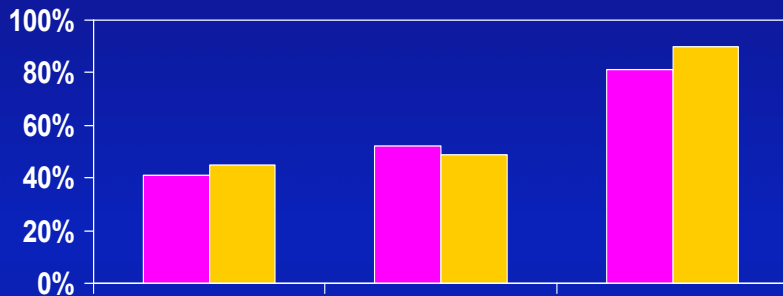
- Modest public and external financing needs
- Less reliance on market finance than 'B's
- Mixed record on politics

➤ B and lower

- Countries in financial and/or political crisis
- Heavy public and external debt and fiscal imbalances
- Low GDP and export growth prospects

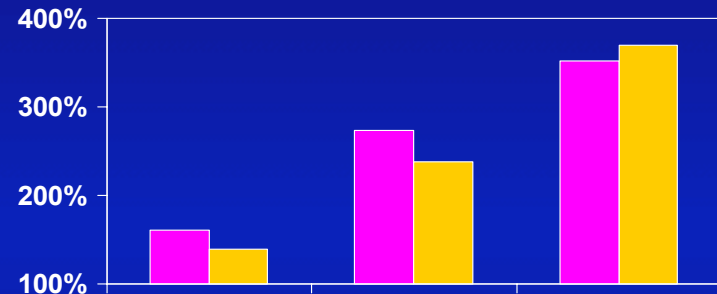
Comparative Fiscal Indicators - 2003

Gen govt debt / GDP

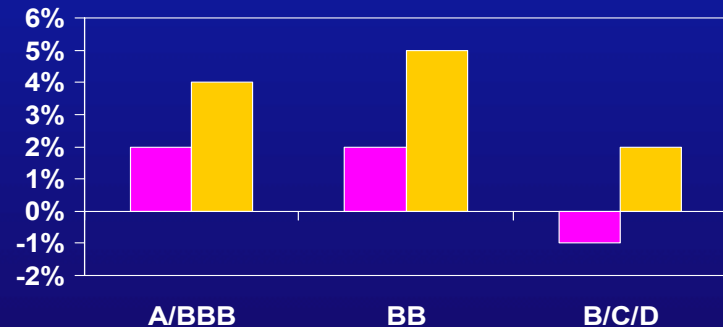
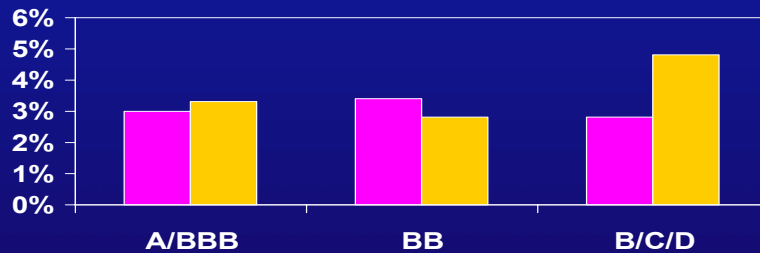


LATAM **World**

Gen Govt Debt / Revenue

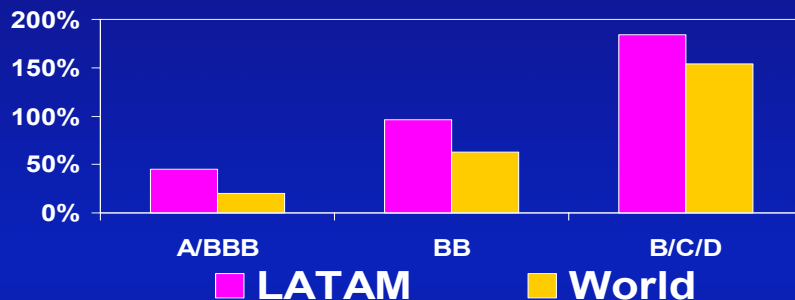


Econ Growth (5 yr avg)



Comparative External Indicators - 2003

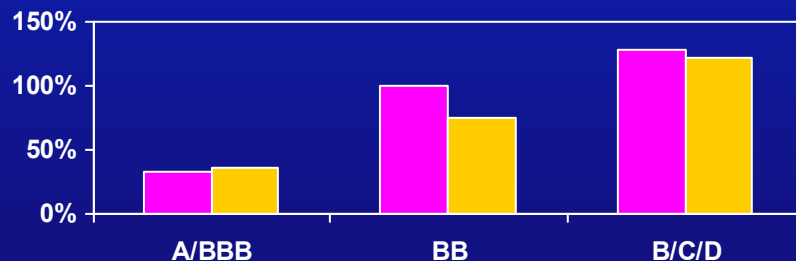
Net External Debt / CXR



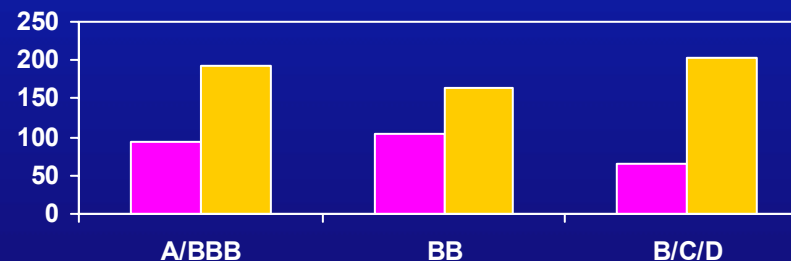
CAB Plus Net FDI / GDP (5 yr avg)



Gross Public External Debt / CXR

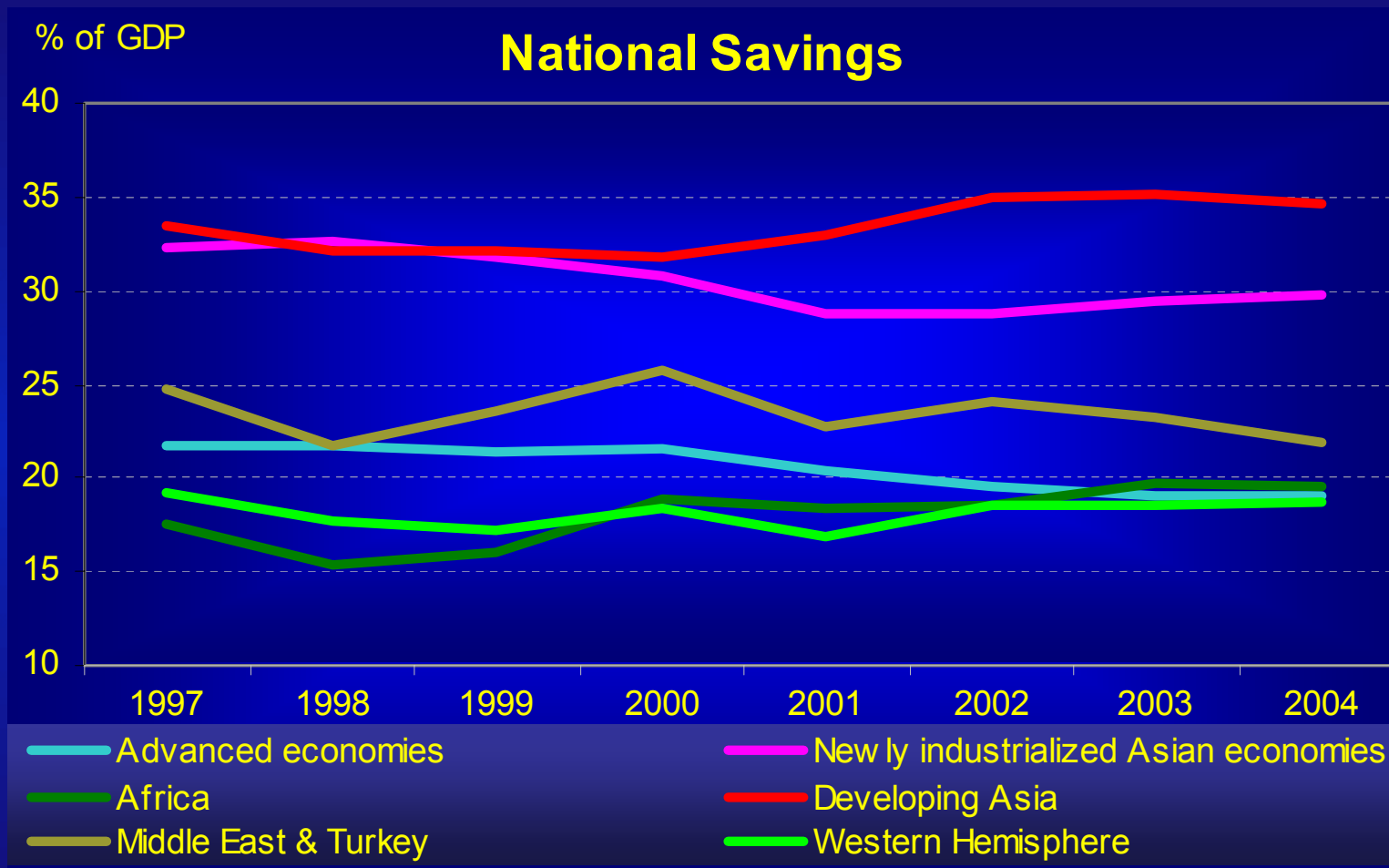


Fitch Liquidity Ratio



Public Finances are the Problem. . .

- With low capital flows, higher savings will have to fund investment in order to boost growth
- 1/2 of difference in savings vs. Asia is public savings
- Public investment already low –need to cut public operating expenditures and, in certain cases, raise taxes
- If demand increases, growth could be limited by capacity constraints, and inflation could accelerate



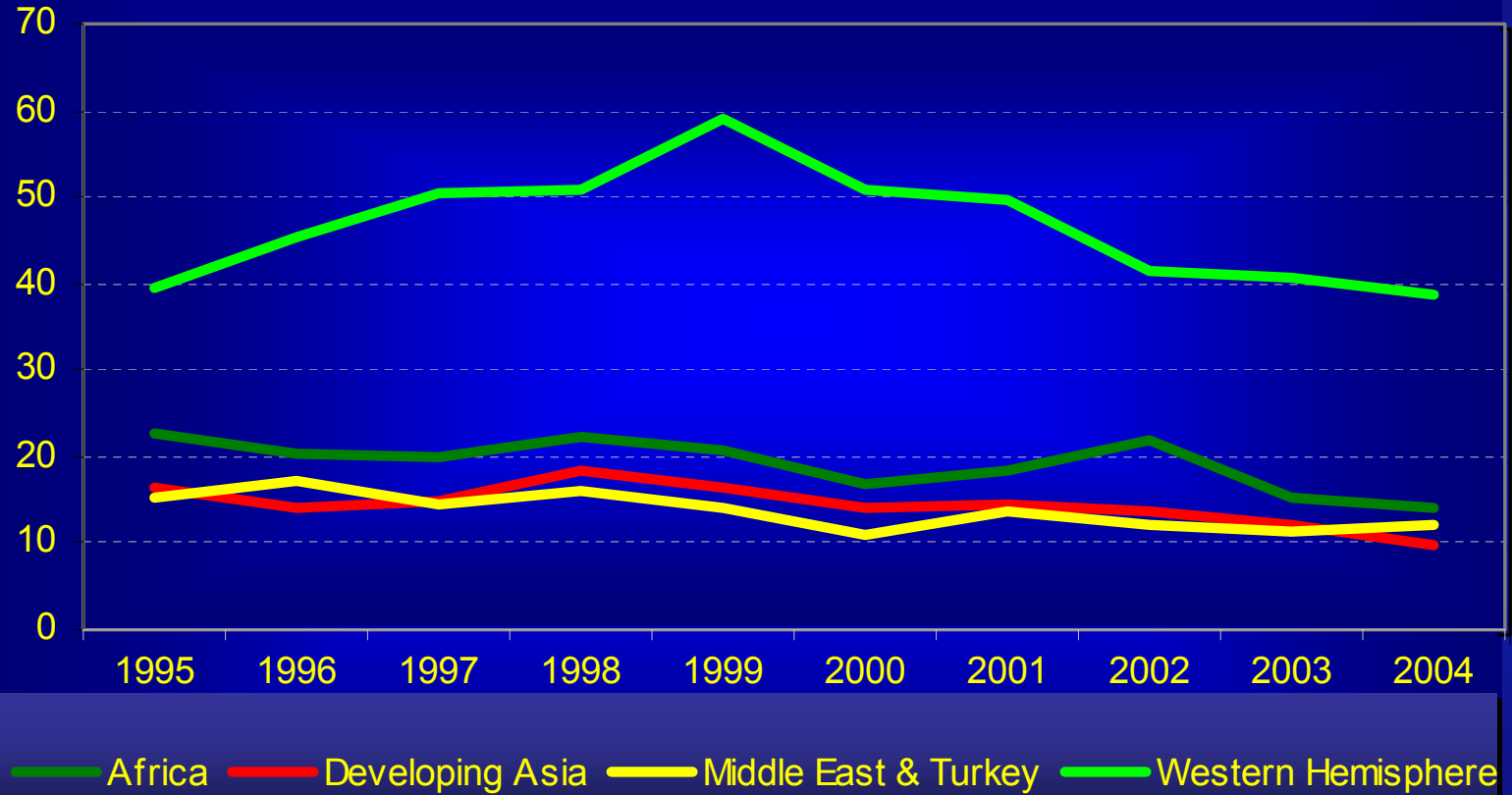
Source: IMF



Source: IMF

% of Exports

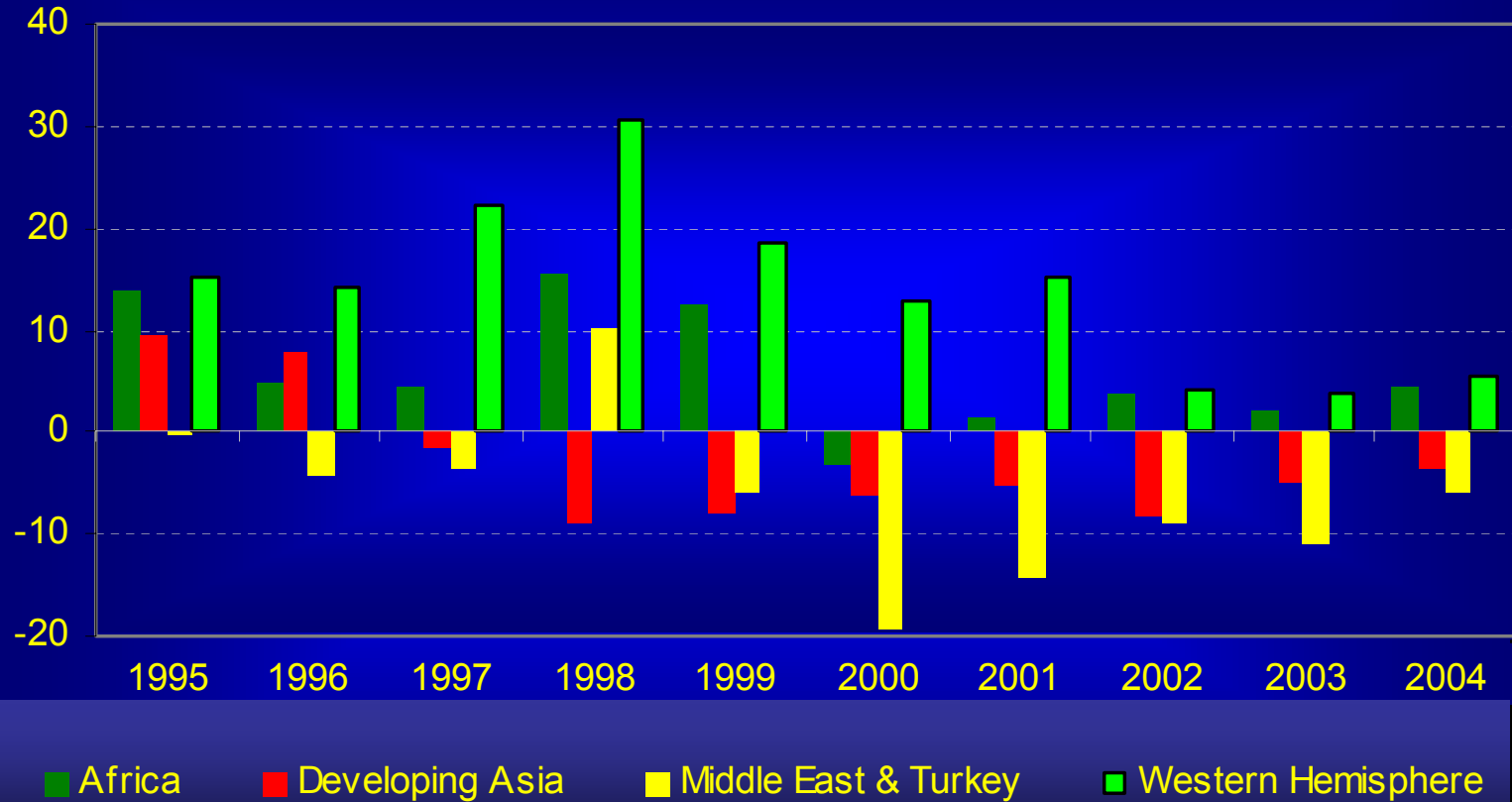
External Debt Service



Source: IMF

% of Exports

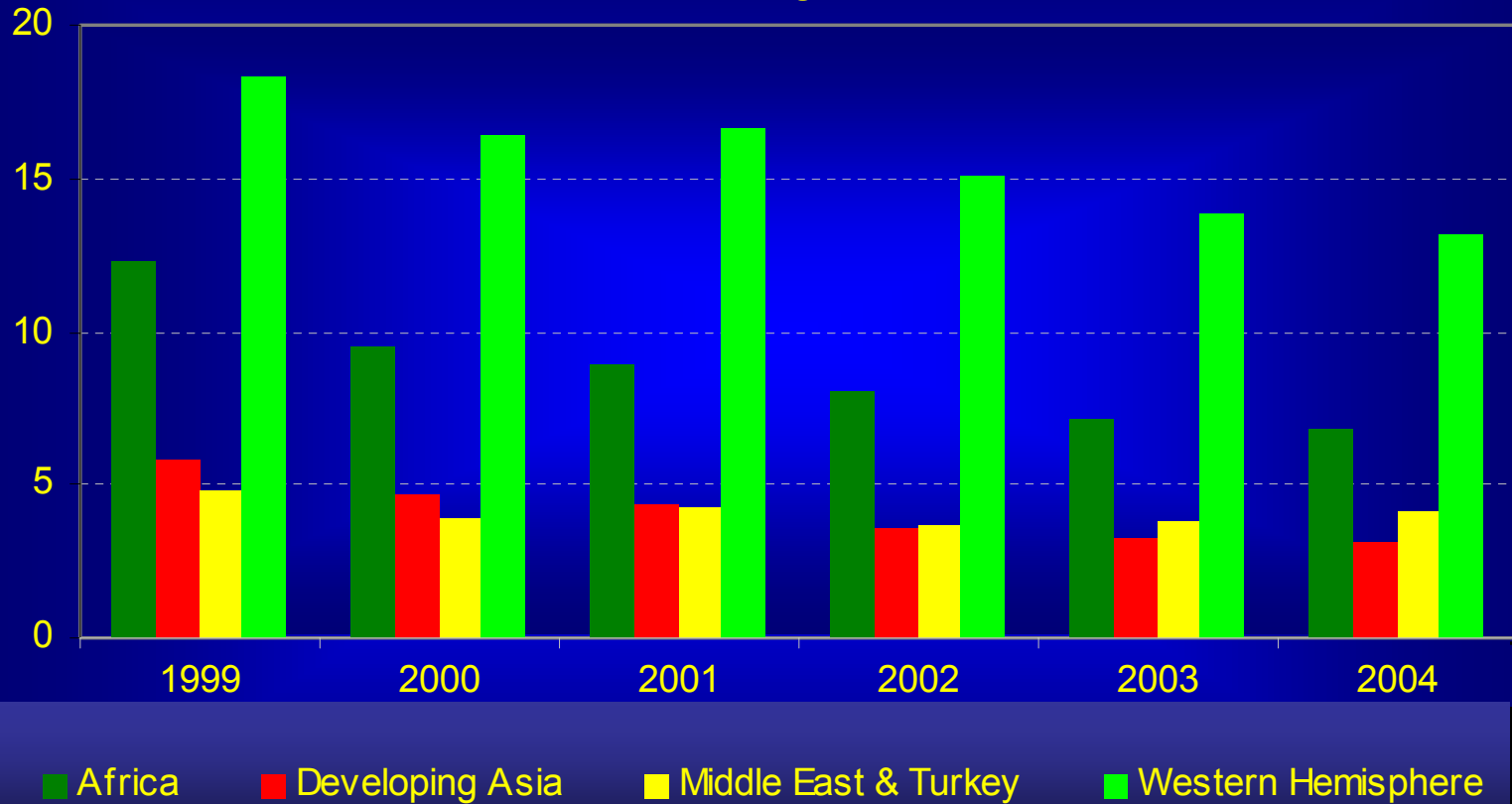
Current Account Deficit



Source: IMF

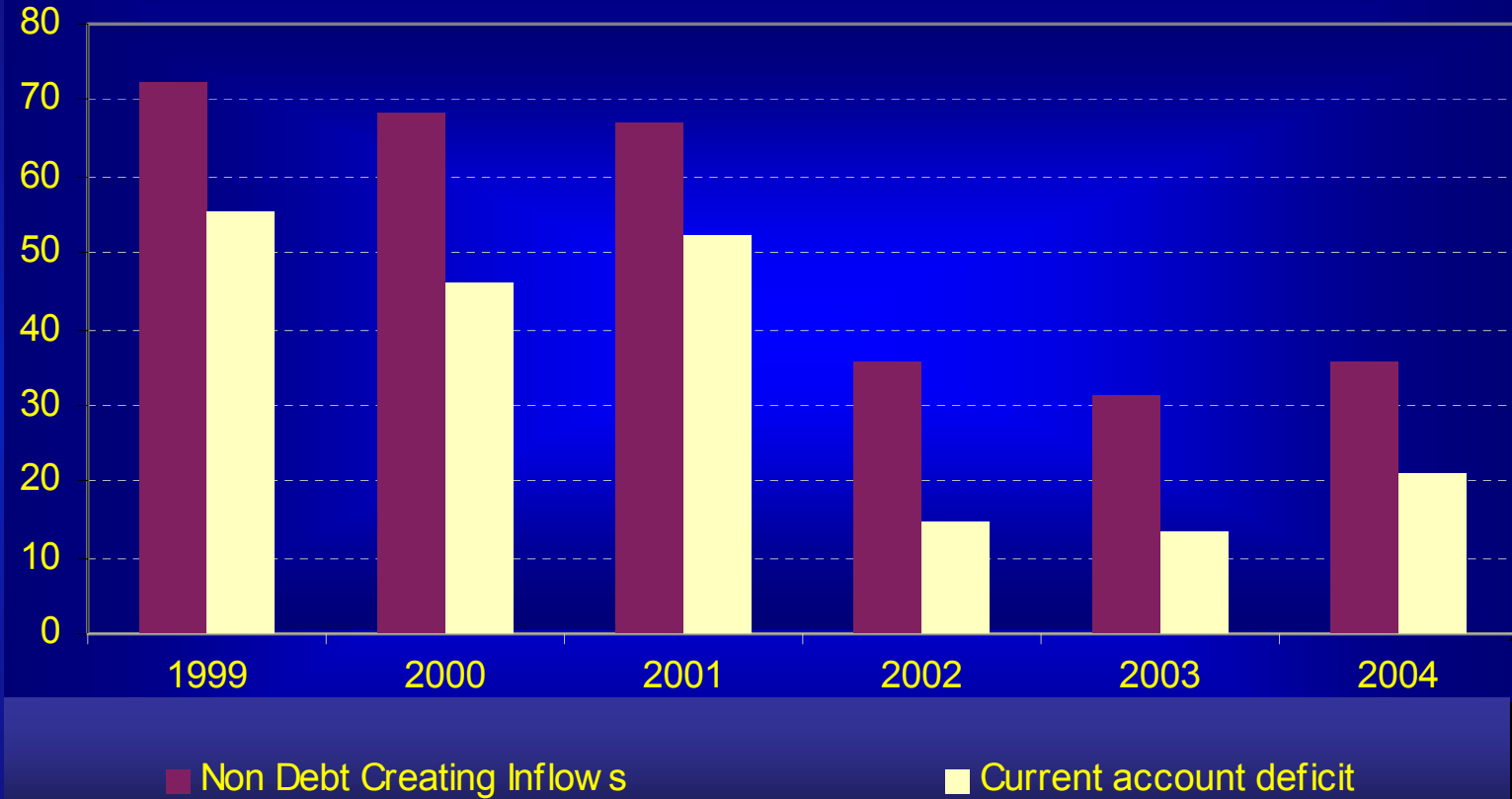
% of Exports

Interest Payments



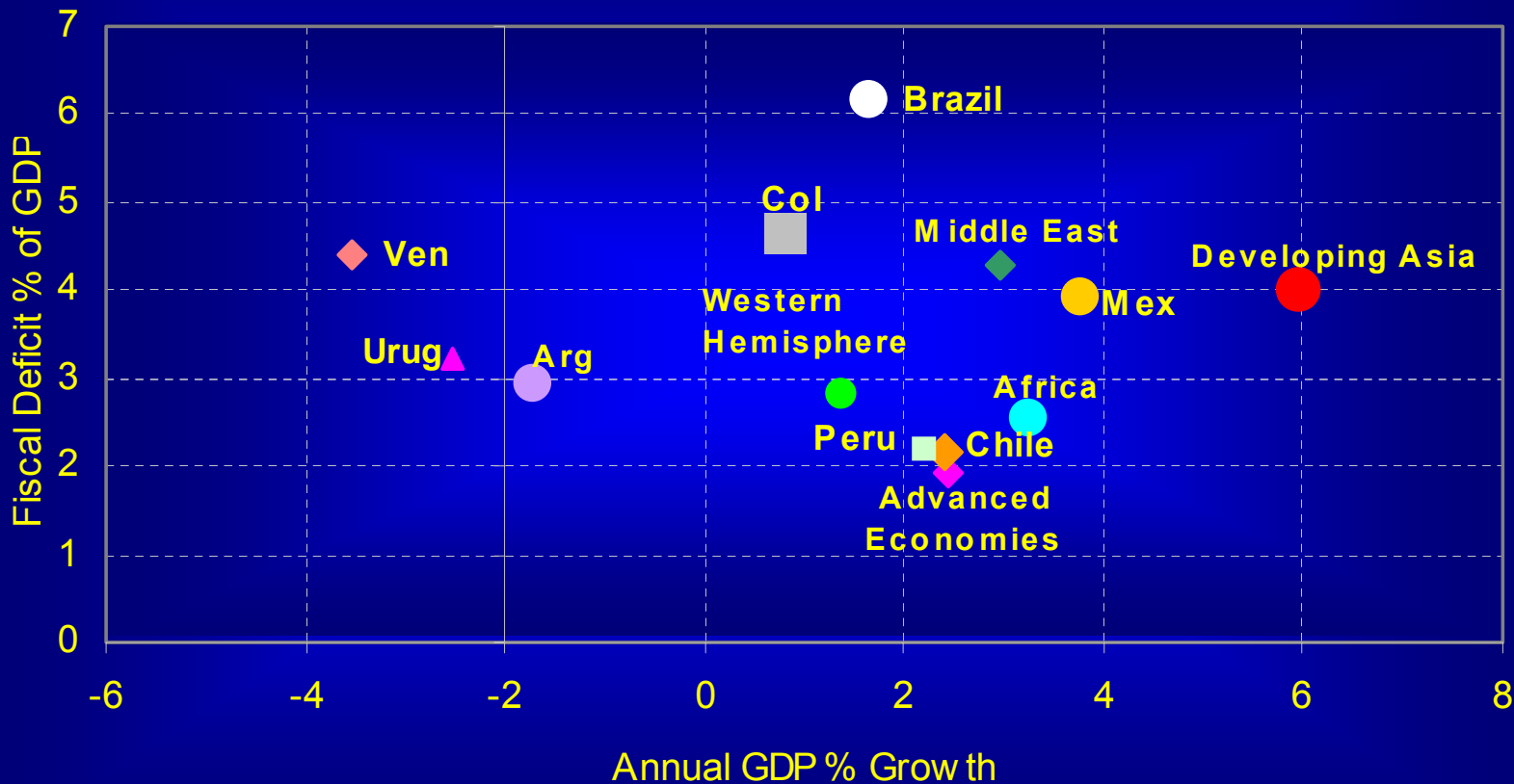
Source: IMF

bln of USD **Net External Borrowing-Western Hemisphere**



Source: IMF

Growth and Fiscal Performance. Avg 1997-2002



Source: IMF and Fitch Ratings

Economic and Credit Outlook

Economic:

- Regional GDP growth of 1-3.5% in 2003-05, up from recessionary conditions in 2001-02
- US\$90-100 bln of external financing needs in 2004-05, vs. US\$140 bln in 2001
- Potential public debt to GDP improvement from currency strength and tighter fiscal policies

Credit events to watch:

- Brazil's tax revenue performance and new IMF program
- Argentina - debt deal, budget performance
- Politics and reforms throughout the region
- Continued market access
- Global events: U.S. economy, high-yield flows

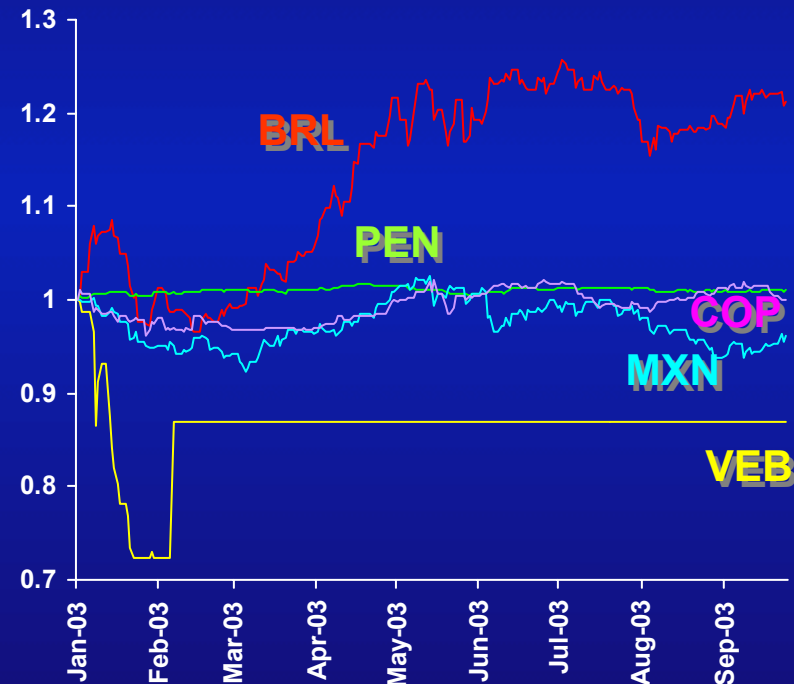
Strong Market Performance In 2003

Sov Spread Over UST
(bps through 9-23-03)



Source: Deutsche Bank

Currency Performance



Source: Bloomberg

Which Countries Most Vulnerable to Reversal of Rally?

- Those with the heaviest external financing needs and thin domestic markets
 - External vulnerability as a function of reserves to CA balance, public and private amortization, ST debt
 - Domestic vulnerability using ratios of debt and deficits to broad money
1. Brazil
 2. Uruguay
 3. Colombia
 4. Venezuela
 5. Panama
 6. El Salvador
 7. Mexico

FitchRatings

Mexico

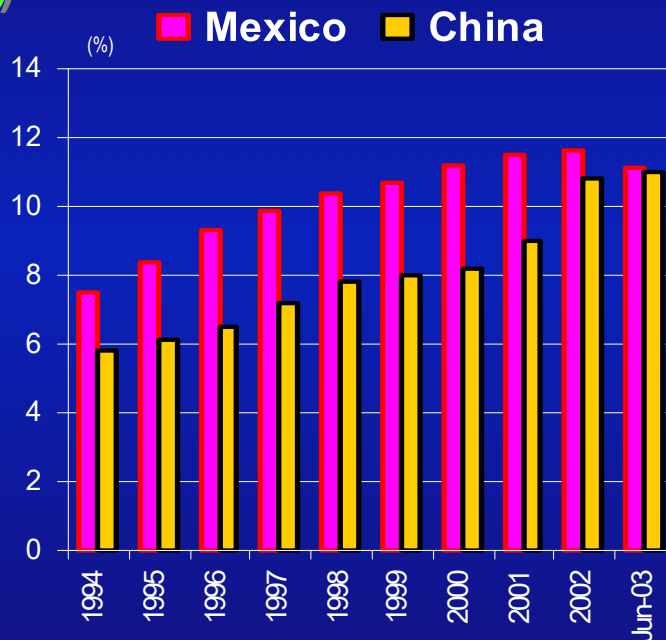
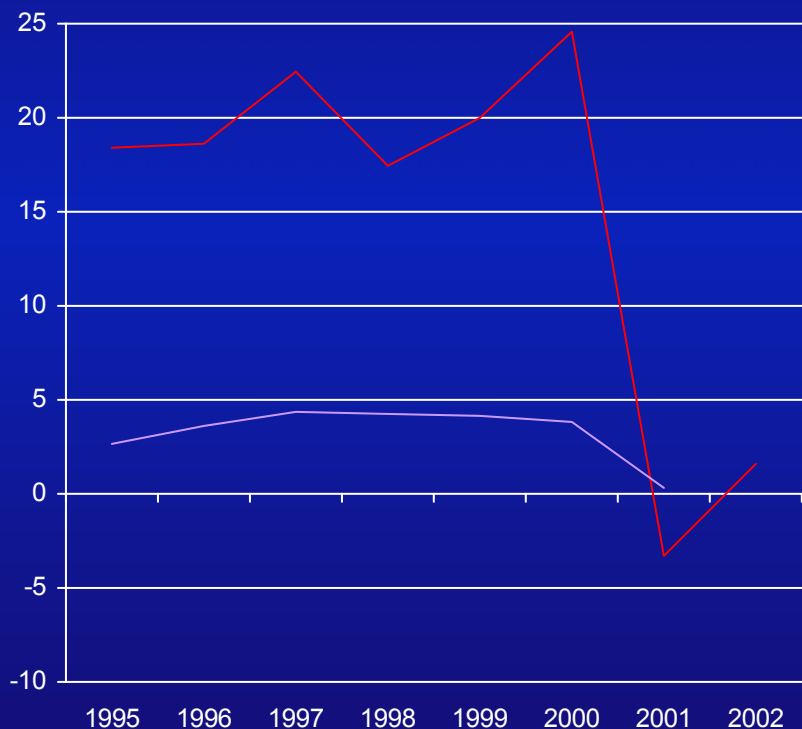
Can Mexico Advance up the
Investment Grade Scale?

Rating lacks dynamism because of:

- Structural weaknesses in public finances
- Lack of structural reforms
- Issues related to competitiveness
- Challenging political environment

Weakness in Maquiladoras: Cyclical or Structural?

Maquila and U.S. GDP Growth (%)



Mexico & China's share in U.S. imports

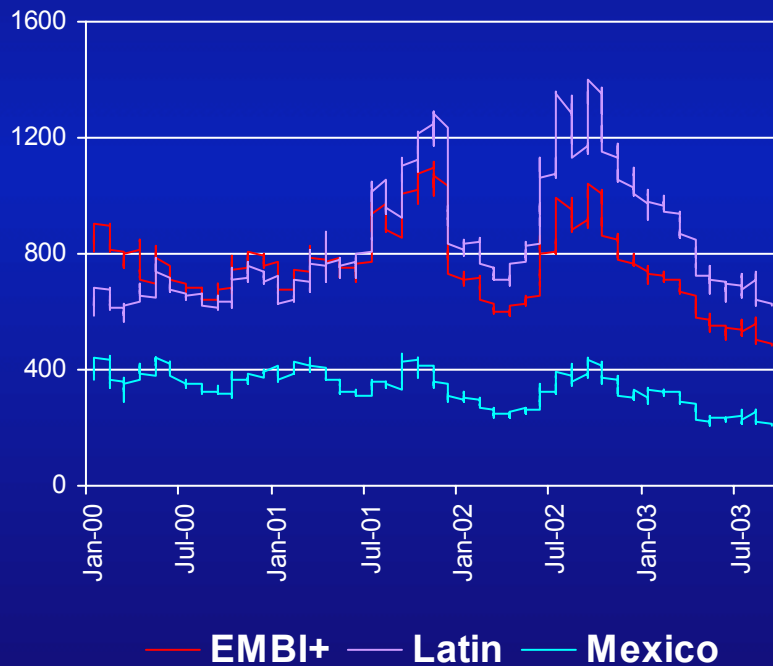
— Maquila — U.S. GDP

Maquila weakness a concern:

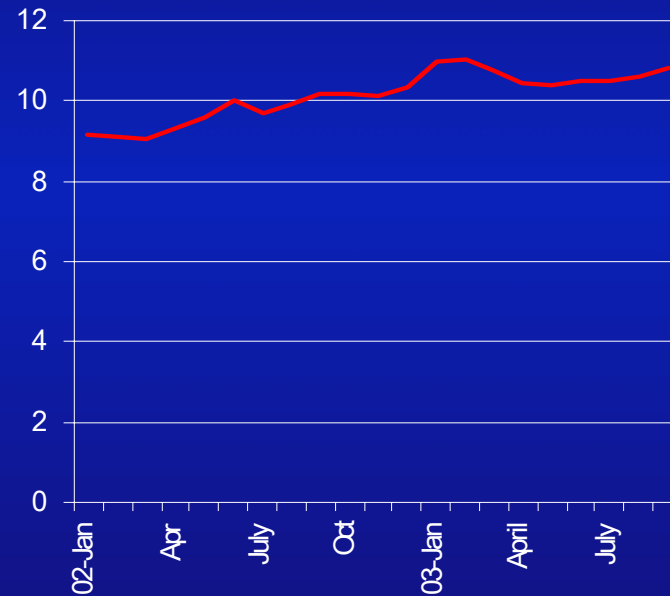
- 50% of the export base
- A good source of employment
- Good for a capital scarce country
- Lack of skilled labor force to move up VA Chain
- High income and regional inequality
- Low export growth prevents reduction of external debt burden

The burden of adjustment on the exchange rate

Credit Spreads over UST
(bps through 9-08-03)



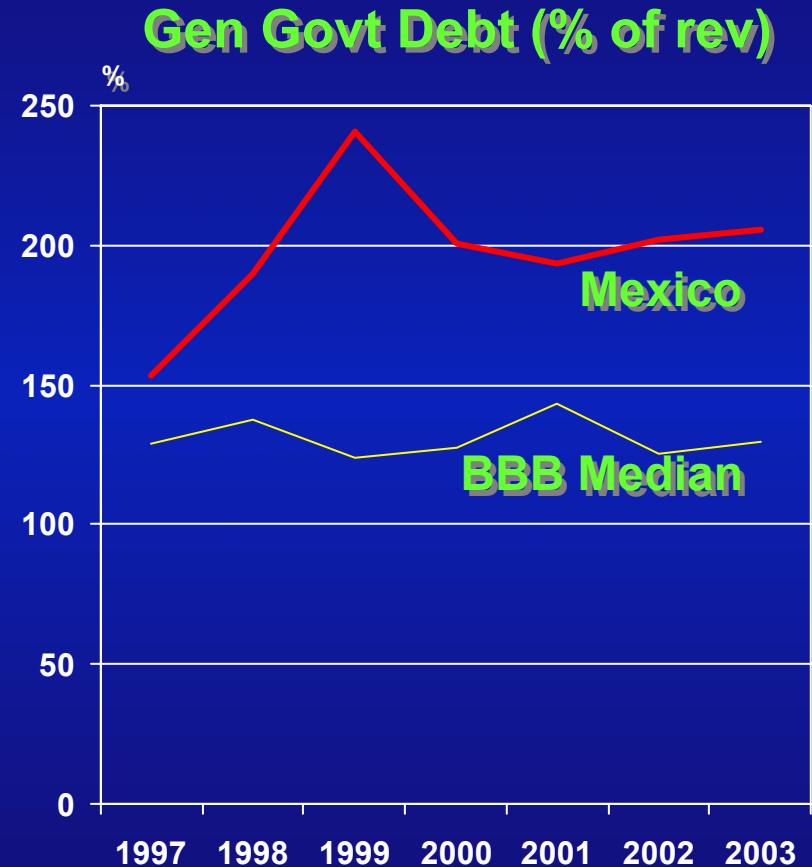
P/USD (eop)



Real appreciation of 25% 1997-02

Structural weaknesses in Mexico's Public Finances

- Low tax to GDP ratio
- High dependence on oil revenues
- High government debt / revenue ratio
- Relatively high PSBR / GDP ratio

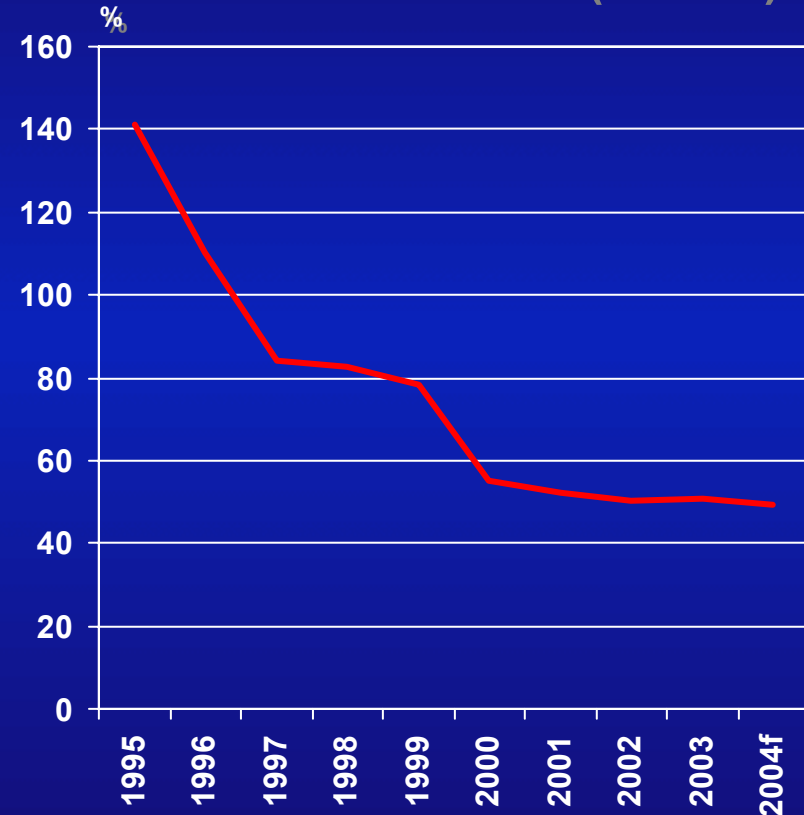


Source: Fitch Ratings.

Investment Grade Intact

- Declining external debt burden
- Robust policy framework
- Integration with the U.S., a net positive
- Relatively strong FDI in an uncertain global environment
- Greater political maturity

Net external debt (%CXR)



Source: Fitch Ratings. (f) forecasts.

FitchRatings

The next six months are crucial

- Can PRI & PAN come together?
- A narrow window of opportunity to pass reforms
- 2004 Budget discussion
- Tax reform and/or Electricity reform

FitchRatings

The Outlook for Brazil

Fundamental credit concerns

- Heavy debt burden (82.5% of GDP)
- Unfavorable debt profile
- Structural BOP vulnerabilities
- Slow economic growth
- Fiscal pressure of interest burden and social needs
- LTFC Rating = B Positive Outlook

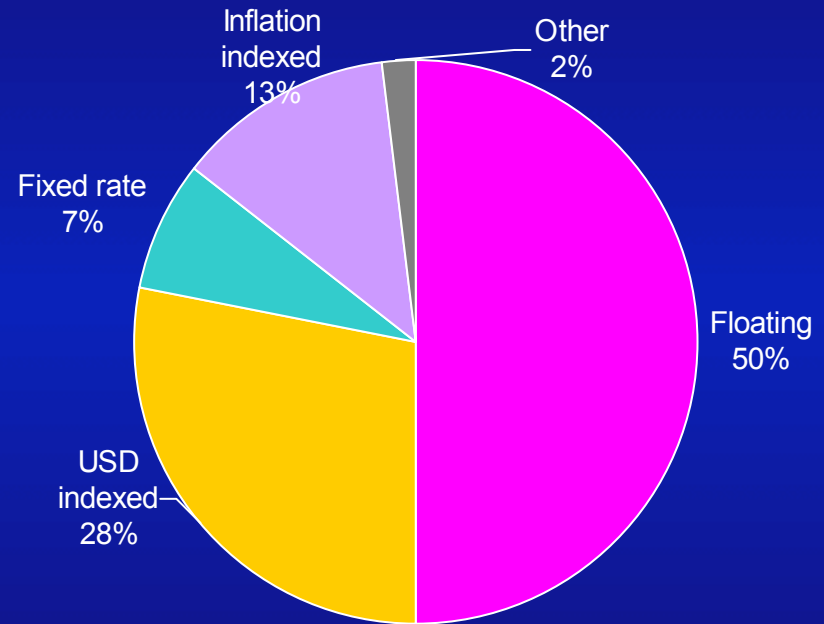
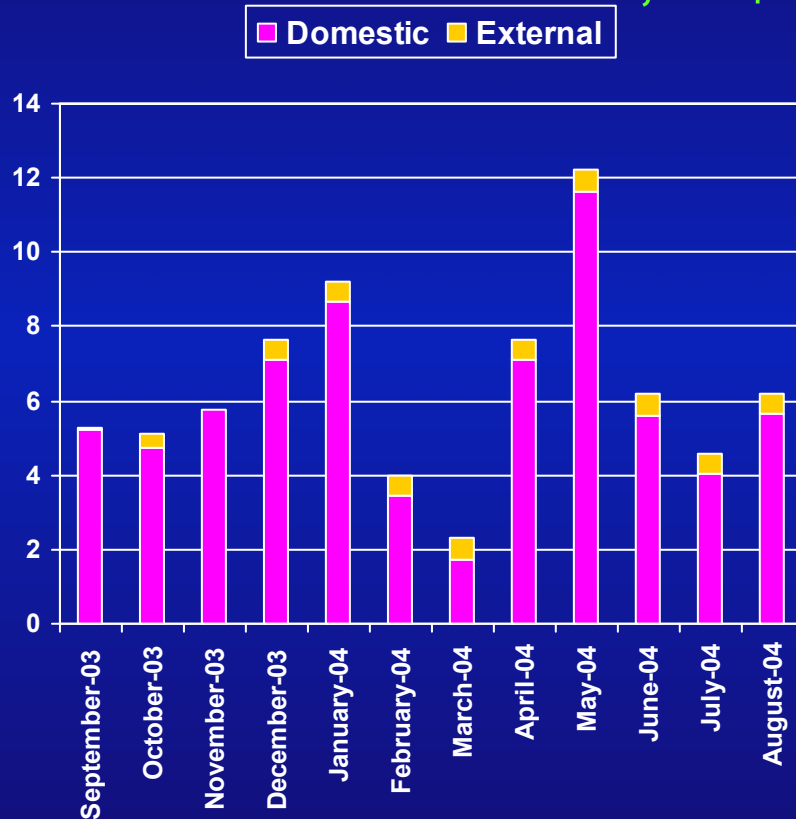
Revised Outlook to Positive June 3

- Alliance with PMDB gives government coalition >60% in congress to pass reforms
- Commitment to 4.25% primary surplus through 2006
- Domestic debt auctions functioning
- Current account continues to improve, but capital account remains a concern
- Monetary policy easing, with inflation expectations falling, underpins future growth

Demanding Debt Burden

Federal debt amortizations, US\$bns

Profile of domestic debt



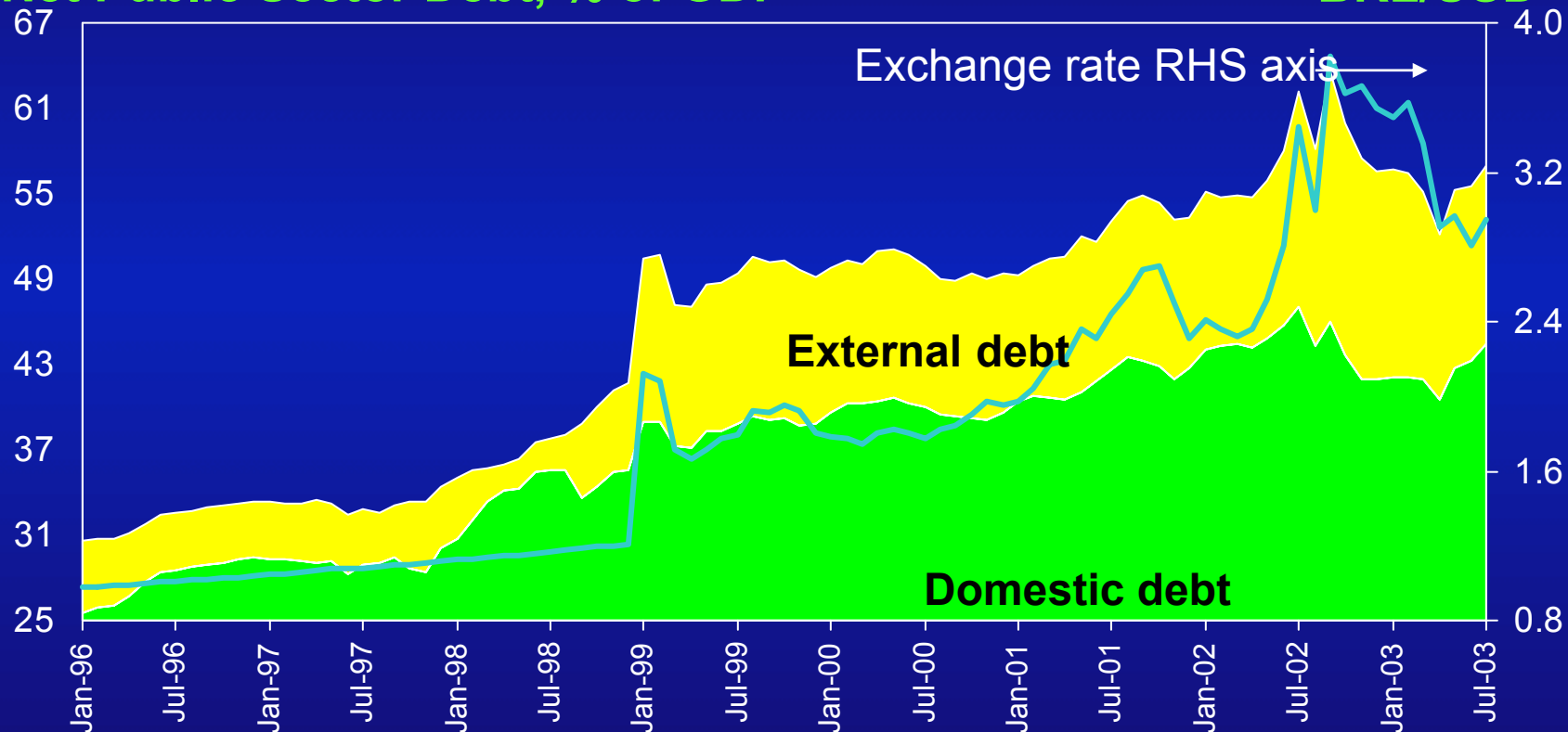
34% of dom debt due in 12 mo
August 2003

Source: BCB and Fitch estimates

Vulnerable to Market Sentiment

Net Public Sector Debt, % of GDP

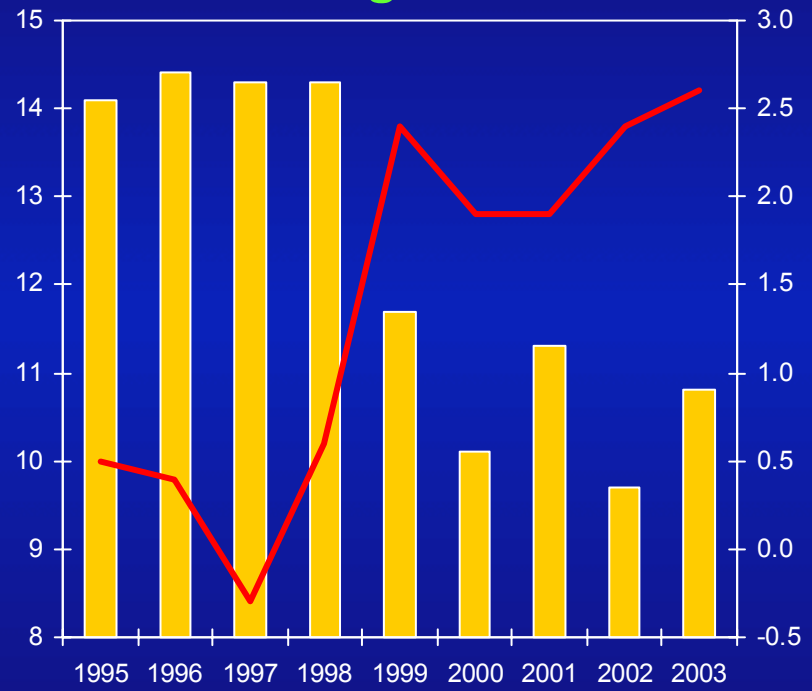
BRL/USD



Source: BCB

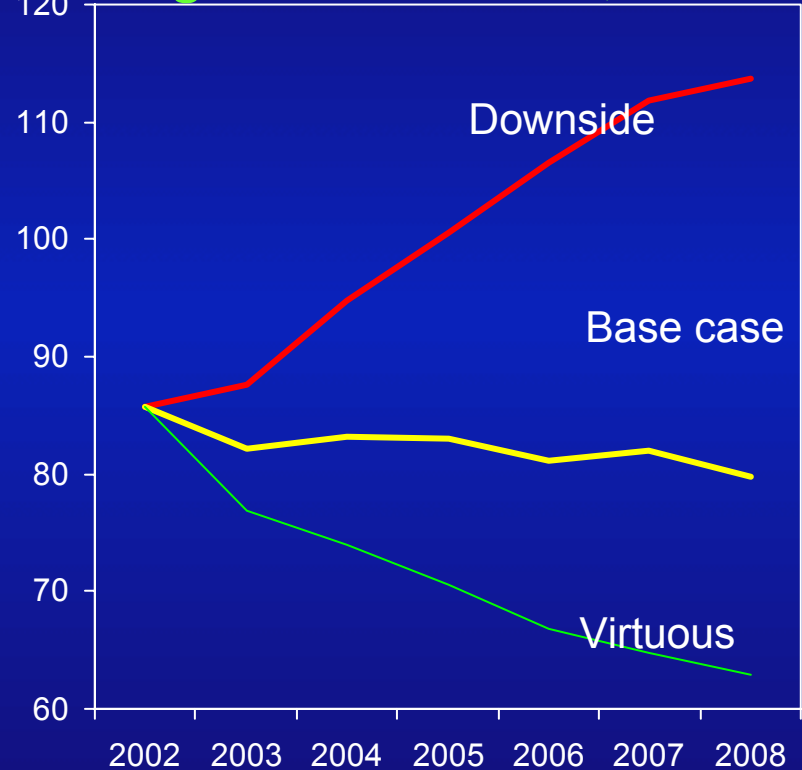
Limited Room for Maneuver

Central government



■ Discretionary spending % of total spending (LHS axis)
— Primary surplus, % of GDP (RHS axis)

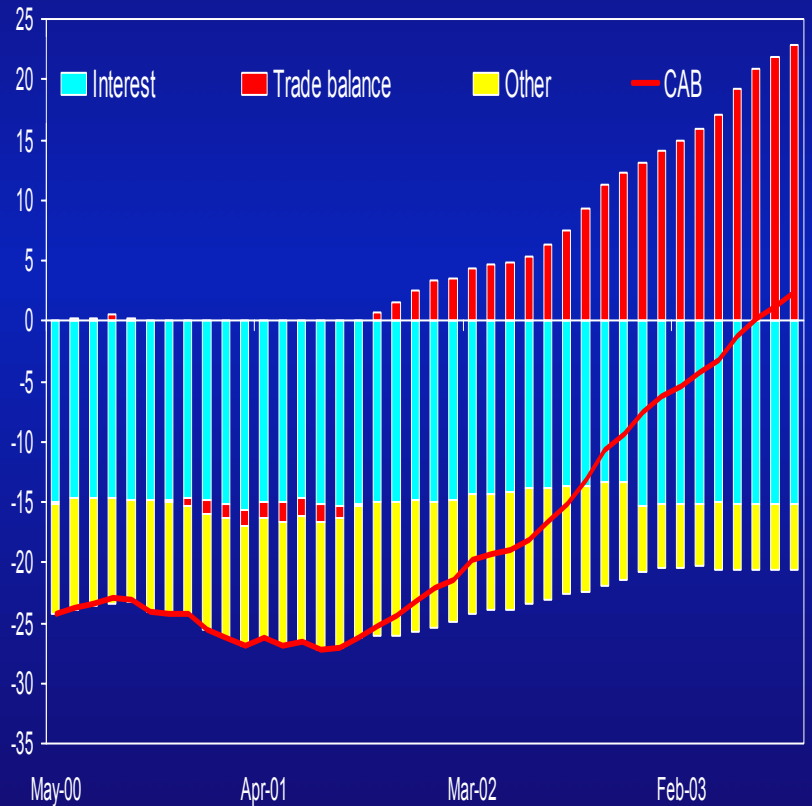
Gen. government debt, % of GDP



Source: CSFB and Fitch

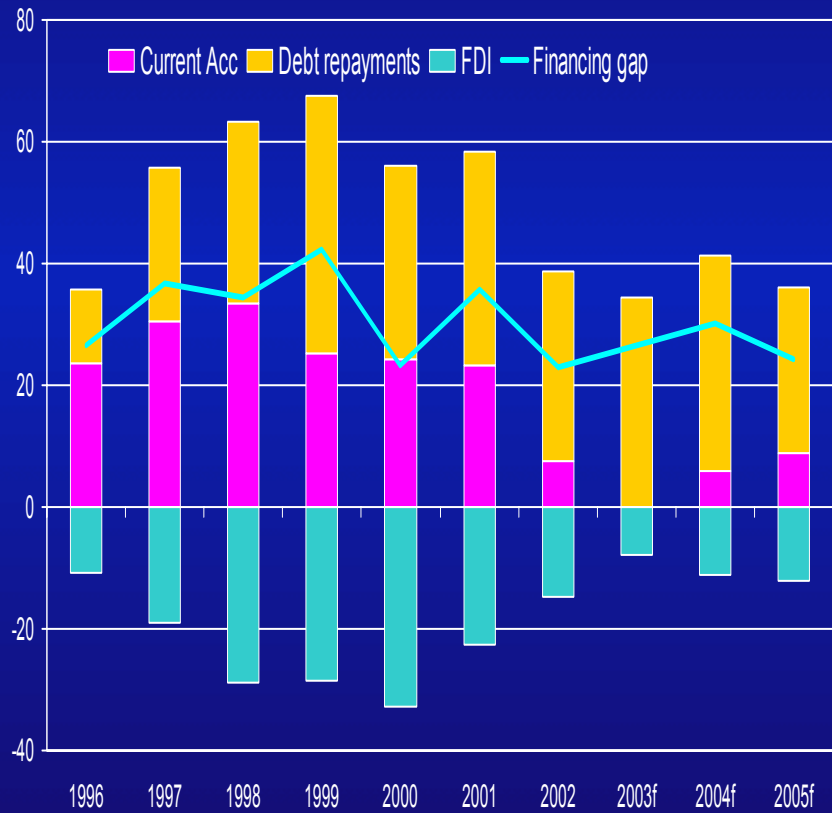
External Adjustment Underway

Current account balance, \$bns

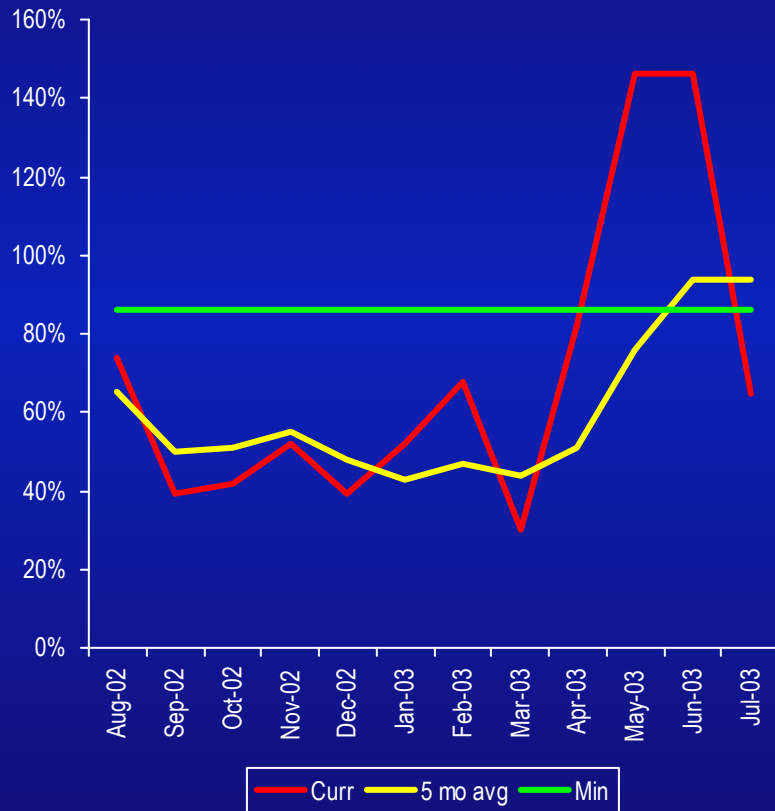


Source: BCB and Fitch estimates

Financing requirement, \$bns



Capital Flows Improving, but Small Cushion



US\$bIn

14	End-02 Net Int'l Resvs
0	Current account
+8	FDI
-35	MLT Amortization
-23	S-T Debt
<u>+50</u>	Gross Borrowing
14	End-03 Net Int'l Res

Rollover rate required = 86%

MLT rollover rate achieved through July 03 = 83%

Brazil: the Need to Avoid Complacency

2003-04 Reforms

- Social security
- Watered-down tax reform
- Bankruptcy reform
- Central bank independence

New IMF Program

- Don't repeat 2000-01 and 2002 experiences

Future Reforms

- Revenue earmarking
- Deeper social security and tax reforms
- Privatization
- Free trade agreements
- Transparent regulatory environment