

Fitch Assigns Guatemala 'BB+' Rating; Outlook Stable

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Fitch Ratings-New York-22 February 2006: Fitch Ratings today assigned Guatemala sovereign ratings of 'BB+' with a Stable Rating Outlook. These ratings are supported by the country's low external and public debt burdens, the government's track record of fiscal discipline and moderate inflation, as well as a solid commercial debt repayment history. The 'BB+' ratings apply to the long-term foreign and local currency issuer default ratings as well as to Guatemala's global bonds maturing in 2007, 2011, 2013 and 2034. Fitch has also assigned a short-term rating of 'B' and a country ceiling of 'BB+'. Fiscal prudence, combined with steady, though sluggish, GDP growth, has resulted in one of the lowest government debt/GDP ratios among peers. Fitch recognizes the government's efforts to manage its fiscal accounts in a prudent manner through various external shocks. Fitch estimates that Guatemala's general government debt burden will approach just 17% by the end of this year, compared with a 'BB' median of 48%. However, GDP measures of public debt understate Guatemala's debt burden due to the narrowness of the country's tax base. Guatemala's debt/revenues ratio approached 160.0% last year, compared with a 'BB' median of 198.4%. At around 10%, Guatemala has one of the lowest tax/GDP ratios of its peers and the government has encountered significant obstacles to increasing its tax take. Furthermore, Fitch views the country's low tax/GDP ratio as a key structural challenge given the country's high levels of poverty, poor social indicators and vulnerability to natural disasters. Limited public debt and a manageable fiscal deficit also drive the sovereign's low financing requirement, which is expected to approach 4% of GDP this year if the budget is fully executed. A positive balance of payments performance, underpinned by remittance growth and increased private capital inflows, has been reflected in international reserve accumulation of US\$250 million in 2005. This, combined with low debt service, will boost Guatemala's liquidity ratio to a projected 187% at the beginning of 2006 compared with a median of 157% for 'BB'-rated sovereigns. Even when adjusting the liquidity ratio to exclude banks' foreign assets and include banks' resident foreign currency deposits, the ratio remains above 100%. However, Guatemala runs a persistent current account deficit (estimated at 4.1% in 2005), about half of which is financed by short-term capital inflows. The newly approved free trade agreement with the US (DR-CAFTA) could reduce this vulnerability over the medium term. Net external debt represented 31.5% of current external receipts in 2005, versus the 'BB' median of 32.5%. Although economic risks appear contained due to the government's favorable balance sheet, high levels of poverty and inequality, as well as the country's poor social indicators, will likely constrain Guatemala's ratings for some time. Guatemala's per capita income is on a par with similarly rated peers, however this masks the country's extreme wealth disparity. The proportion of the population living in poverty was 59.9% in 2002, a rate that is significantly higher than that in poorer countries such as Nicaragua (50.3%) and Honduras (53.0%) and approaching that of Bolivia (63%), which Fitch assigns a 'B-' foreign currency issuer default rating. Other comparative social indicators, such as infant mortality, life expectancy, access to healthcare, literacy rates and school enrollment rates also do not compare favorably to the regional average in Latin America, to similarly rated sovereigns, or to poorer countries. While maintaining a small government is prudent and has helped minimize the country's exposure to economic vulnerabilities, this policy makes tackling the poverty issue difficult due to a lack of resources. The government will have to implement a more comprehensive tax reform to increase the tax take if it is to address its social challenges. Yet political opposition to tax reform remains formidable. As a result, Fitch believes the current policy framework could be vulnerable to the erosion of public support if progress on these fronts is not forthcoming. A copy of the sovereign report on Guatemala will be available shortly on Fitch's website 'www.fitchratings.com'. A teleconference on the country's 'BB+' ratings will be held on Thursday, Feb. 23, at 10:30am (EST). Contact: Theresa Paiz Fredel +1-212-908-0534, Roger M. Scher

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