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Fitch Upgrades Panama's L-T Foreign & Local Currency IDRs to 'BBB-'; Positive Outlook [Ratings](#)

23 Mar 2010 4:51 PM (EDT)

Fitch Ratings-New York-23 March 2010: Fitch Ratings has upgraded the Republic of Panama's long-term foreign currency and local currency Issuer Default Ratings (IDRs) to 'BBB-' from 'BB+'. Both Rating Outlooks remain Positive. Fitch has also upgraded the short-term foreign currency IDR to 'F3' from 'B' and the country ceiling to 'A-' from 'BBB+'.

The upgrades reflect a sustained improvement in public finances, underpinned by recent tax reforms, and the economy's resilience to the global financial crisis and associated recession. Although economic growth decelerated to 2.4% in 2009 from 10.7% in 2008, it was one of the strongest rates of growth in Latin America and among 'BBB' rated peers. Similarly, fiscal deterioration was moderate, especially by international standards while Panama's general government debt/GDP ratio stabilized around 45%. The Positive Outlook reflects the expectation that government debt/GDP ratio will further decline as the growth accelerates and fiscal discipline is maintained despite an ambitious public investment program.

'Panama's key credit metrics have been on an improving trend since the middle of the last decade and held up well to the worst global downturn since World War II. Recent tax and fiscal reforms signaled a continuing commitment to fiscal discipline and enhancing the flexibility and quality of public finances,' said Theresa Paiz Fredel, Senior Director in Fitch's Sovereign Ratings team. 'Further upgrades will depend on additional measures to strengthen the management of public finances, successful implementation of the government's ambitious public investment program and sustainable economic recovery,' added Paiz Fredel.

Sustained growth in investment, underpinned by rising domestic savings as well as inflows of foreign direct investment, have supported rapid economic growth in recent years, while increases in real income and employment bode well for private consumption over Fitch's rating horizon. The Panama Canal expansion project and other public works projects will also raise the economy's potential output and sustainable rate of growth. Nonetheless, continued fiscal discipline and effective management of government assets and the public investment program, as well as the expansion of the Canal, will be required to ensure that the Outlook for the economy and public finances remains Positive.

'The passage of two tax reforms in the first nine months of the Martinelli Administration, which are expected to yield around 1.6% of GDP in additional revenue this year, underpin the government's commitment to sustainable fiscal policies,' said Paiz Fredel.

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Panama's per capita GDP, governance and human development indicators, as well as a stable financial system support the sovereign's IDR of 'BBB-'. Furthermore, dollarization underpins an established record of macroeconomic stability that compares favorably with peers, as illustrated by an extended period of high growth in conjunction with low inflation.

Although Panama's gross public debt ratios remain high relative to 'BBB' peers, official dollarization, a favorable amortization profile and the government's considerable financial and land assets offset this weakness. Fiscal consolidation and vigorous growth reduced the government debt to GDP ratio to an estimated 45% last year, from a peak of 70% in 2004. Under conservative assumptions of a 1% of GDP fiscal deficit and average growth of 5%, Panama's government debt/GDP ratio will converge with the current 10-year 'BBB' category median of 35% by 2014 at the latest. Furthermore, net government debt, at 29% of GDP, is in line with the 10-year 'BBB' median. Given the moderate debt burden and Fitch's expectation that the non-financial public sector will maintain a deficit of close to 1% of GDP, the government's financing needs remain manageable at an estimated 2.6% of GDP this year, among the lowest of 'BBB' rated sovereigns and further supporting creditworthiness.

While the net sovereign external debt to current account receipts ratio remains high at 22.5% compared with a 10-year peer median of -8.1% in 2009, this partly reflects Panama's monetary regime whereby the authorities do not technically maintain international reserves. However, the overall level of foreign indebtedness of the economy is very low - net debt is equivalent to less than 2% of GDP, substantially less than the 10-year 'BBB' median of around 10%.

Evidence that the economy can sustain high growth without internal or external imbalances emerging would underpin confidence in sovereign creditworthiness, as would further measures to improve the management of public finances, including greater fiscal and funding flexibility. Successful execution of the government's public investment program, including the Panama Canal expansion project, without endangering Panama's favorable debt dynamics would also be positive for creditworthiness. By contrast, Fitch could revise the Outlook to Stable if unexpected fiscal deterioration beyond the scope of the Fiscal Responsibility Law or the realization of contingent liabilities lead to a sustained deterioration in the government's debt dynamics.

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