

Emerging Markets Faxable

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Dominican Republic:

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More to the Bondholder Presentation Than Meets the Eye.

We have taken a closer look at the "Presentation to Bondholders" that the Dominican Central Bank published yesterday and think the environment is becoming increasingly complicated for a debt exchange. Our main conclusions are:

1. Domestic Creditors Are Not Pulling Their Weight in 2005 Financing

- The financing gap the Government cites of US\$186 million reflects a domestic not external shortfall. In addition to the US\$81 million overall deficit, there is a domestic financing gap of US\$424 million and an external financing surplus of US\$238 million. Part of this domestic shortfall is understandable as the significant needs of the electricity sector are considered a domestic responsibility. However, the government was unable to get the domestic commercial banks and suppliers to rollover their exposure at 100% which was a critical assumption in our original model. It is not clear why this was so and may indicate a political unwillingness to take on domestic agents.

2. Multilateral Creditors Are Also Not Playing a Major Role

- The World Bank and the IDB are providing only US\$210 million in gross budget support. It is not clear why this number is so low: unwillingness on the part of the multilaterals based on the Dominican track record or inadequate gaming of the official sector by the authorities.

NFPS Financing

	USD Millions
Overall Balance	-181.1
Net Domestic Financing	-251.4
Net Commercial Banks	-24.3
Net Arrears to Suppliers	-78.4
Net Other	-148.6
Net External Financing	239.0
Disbursements	887.0
WB	150.0
IDB	60.0
Caracas Agreement	226.0
Project Financing	451.0
Amortizations	-648.0
Central Government	-610.0
Other	-38.0
Current Financing Gap	-193.4
Total Arrears	288.4
IFI	52
Bilateral	174
o/w post Cut-Off Paris Club	80
Commercial Banks	37
Bonds	3.4
Suppliers	22
Minus Reschedulable Arrears	123
Net Arrears	165.4
Total Financing Gap	-358.8

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The official sector could of course argue that its loans in 2004 were substantial and that participation should be seen in a cumulative sense. But in the context of the new IMF program, the reality is that this participation is very small.

3. The Real Financing Gap is Much Larger at Around US\$350 million - Though the government says the financing gap left over is only US\$186 million, it also notes that the stock of arrears expected at end-2004 will be US\$290 million. This means the shortfall in gross terms is closer to US\$475 million. Admittedly, some of this can be rescheduled. Of the US\$290 million in arrears, US\$145 million is to the Paris Club of which all but US\$80 million is pre-cutoff and can be rescheduled. We also think that the US\$35 million in arrears to Commercial Banks and US\$22 million to Suppliers can be rescheduled. This leaves actual arrears that need to be paid on the order of US\$165 million meaning the real financing gap for investors to use is US\$350 million, broadly consistent with the amount cited in our November 4 report. The size of this gap

increases the likelihood that the authorities would need to capitalize bond coupons.

Given these themes, what can the message be that the bondholders are sending to the government this week in their meetings?

In our view, the combination of very high prices on the bonds, large financing gap that likely necessitates capitalizing coupon payments, and inadequate pressure on other creditors to play a sufficient role in the financing process makes the environment increasingly complicated for a successful debt exchange.

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