Fitch: Peru's Election Results Could Affect Its Investment Climate

19 de abril de 2006

Fitch Ratings-New York-17 April 2006: The outcome of Peru's first round of national elections last week could put at risk a deepening of structural reforms that would support export and investment growth, according to Fitch Ratings. Recent strong export and GDP growth and the consequent improvement in external and public debt dynamics underpinned Fitch's revision of the Outlook on Peru's sovereign ratings to Positive from Stable in November 2005. Fitch currently rates Peru's foreign and local currency Issuer Default Ratings 'BB' and 'BB+'. With 90% of the vote counted, Ollanta Humala, of the 'Union por el Peru' party, was in the lead in the first round of the presidential election, securing 26.3% of the vote, followed by APRA party leader, Alan Garcia, with 20.8%, and the center-right's Lourdes Flores with 20.2%. Humala and either Garcia or Flores will move to a second-round vote in late May or early June. Furthermore, whoever is elected will likely face a fragmented Congress, making it difficult to push through reform legislation. Although Mr. Humala has stated that if elected he would maintain public debt service and fiscal discipline while increasing social expenditure, concerns about Peru's post-election investment climate persist given the candidate's campaign stance regarding the role of the state in Peru's extractive sectors and a free trade agreement with the U.S. Alan Garcia has been campaigning on a more moderate platform than Mr. Humala; however, doubts about his policy direction persist given his heterodox policy record as president in the 1980s. Nevertheless, Garcia's APRA party has in recent years supported prudent policy settings and modest reforms in Congress in order to enhance the party's credibility with the electorate. Based on preliminary election results, APRA will have the second largest block of seats in Congress, behind Mr. Humala's party. And, even if Lourdes Flores, perceived by market participants as more market-friendly than her opponents, triumphs in the second round of elections, her political skill will be tested, as her center-right party will only have about 15% of the seats in Congress. 'No matter who ultimately becomes Peru's next president,' said Theresa Paiz Fredel, Director of Latin American Sovereign Ratings at Fitch, 'the marked improvement in Peru's external solvency indicators is expected to continue near-term given the favorable external environment for commodity prices. However, a departure from the current policy framework could negatively affect medium-term trends for investment and export growth,' said Paiz Fredel. Peru's next president takes office on July 28, 2006. Although GDP and export growth have already begun to decelerate, growth remains robust by Latin American standards and continues to support Peru's sovereign creditworthiness, which should provide a sufficient buffer to deal with possible adverse shocks over the near term, whether election-related or externally driven. Fitch is projecting real GDP growth of 4.8% this year compared with 6.7% in 2005. Solid balance of payments performance has been reflected in international reserve accumulation of US$375 million during the first three months of 2006 and Peru's low external financing needs of about 8% of reserves. Similarly, reserve accumulation, combined with the reduction of debt service achieved through the government's debt reprofiling operations, boosted Peru's liquidity ratio to 214% at the beginning of 2006. While this compares favorably to a median of 165% for 'BB' rated sovereigns, when adjusting the liquidity ratio to include resident foreign currency bank deposits in the denominator, the liquidity ratio falls to around 93%, highlighting the risks associated with high, albeit declining, dollarization. The government's debt reprofiling operations have also reduced the public sector's financing requirement to a manageable 3% of GDP over the medium term if the current fiscal stance is maintained. Furthermore, the authorities do not intend to tap international debt markets in 2006. Factors that could trigger an upgrade of Peru's sovereign ratings include evidence that export volume and investment growth trends are sustainable over the medium term, as well as an improvement in fiscal trends, such as the conversion of temporary tax measures into more permanent revenue sources. A smooth transition to the next government and maintenance of prudent macroeconomic policy settings after the election would also be positive for creditworthiness. On the other hand, a populist departure from the current policy framework could have a negative impact on Peru's sovereign credit story. Contact: Theresa Paiz Fredel +1-212-908-0534 or Roger M. Scher +1-212-908-0240, New York. Media Relations: Christopher Kimble, New York, Tel: +1 212-908-0226. Fitch's rating definitions and the terms of use of such ratings are available on the agency's public site, 'www.fitchratings.com'. Published ratings, criteria and methodologies are available from this site, at all times. Fitch's code of conduct, confidentiality, conflicts of interest, affiliate firewall, compliance and other relevant policies and procedures are also available from the 'Code of Conduct' section of this site.