Comment

Rating Corporates Above the Country Ceiling

Analysts

Corporates
Daniel R. Kastholm, CFA
1 312 368-2070
daniel.kastholm@fitchratings.com

Sovereign
Roger M. Scher
1 212 908-0240
roger.scher@fitchratings.com

Introduction

In June 2004, Fitch Ratings assigned "Country Ceiling" ratings to its rated sovereigns and published criteria for how these country ceilings would be assessed (see "Country Ceiling Ratings and Rating Above the Sovereign," June 17, 2004). With the process of globalization reducing incentives for sovereigns to impose exchange controls or a moratorium on private external debt service, and given the experience in recent sovereign crises in which such measures were often not taken, slightly more than a third of Fitch's 90 rated sovereigns have country ceilings above their long-term foreign currency (LTFC) sovereign ratings. To determine what differential, if any, a sovereign can have between these ratings, Fitch employs a risk model designed to capture the cost and benefits to the sovereign of imposing exchange and capital controls. The more open to trade and capital flows and the lower the exposure of private sector liabilities to exchange rate risk, the more likely the country ceiling will exceed the LTFC sovereign rating. In such countries, most private sector entities' ratings would be constrained either by their long term local currency (LTLC) ratings or the country ceiling, whichever is lower.

Structured finance transactions that incorporate credit enhancements mitigating transfer and convertibility (T&C) risks, often by trapping foreign currency cash flows offshore, can be rated above the country ceiling. Likewise, multilateral development banks, such as the Asian and African Development Banks and Corporación Andina de Fomento, can have higher ratings than the sovereigns where they are domiciled, given their status as preferred creditors, including being exempt from exchange controls, and the fact that they often have sizable liquid assets deposited with banks offshore. And, exceptionally strong corporates, or less frequently financial institutions, that are shielded from T&C constraints may be rated above the country ceiling. Such considerations as substantial export earnings, foreign assets and offshore production, foreign parents or strategic partners that would provide financial support could enable corporate entities to be rated above the country ceiling, though these cases remain comparatively rare. The purpose of this paper is to provide in detail the factors that support rating certain entities above the country ceiling.

In some cases, private companies may possess characteristics that, similar to financial "structures" and incentives that characterize structured finance transactions, limit the sovereign's capacity or willingness to impede these companies' external debt service. These characteristics include:

- A strong credit profile for the company;
- Substantial foreign exchange earnings relative to a company's foreign currency debt burden;

- Production facilities and cash generation ability from subsidiaries or operations offshore, especially those domiciled in highly rated sovereigns, i.e. multinational enterprises;
- A foreign owner or a strategic partner that could be relied on as a source of financial support in the absence of a formal guarantee;
- A history of preferential treatment of the company by the sovereign, including exemption from T&C constraints and surrender requirements for export proceeds, and favorable tax treatment;
- Committed credit lines from highly rated international banks, especially credit lines without a material adverse change (MAC) clause which enable banks to withdraw committed facilities in the event of a sovereign crisis or other risk events; and,
- Assets held offshore, especially liquid assets, often as a result of rules allowing exporters to trap and maintain cash balances offshore that are available for debt service.

The following table shows the corporates which Fitch rates above the country ceiling and where they are domiciled. See Appendix A for a summary profile and rationale for going above the country ceiling for each of the companies listed below.

Corporates Rated Above the Country Ceiling by Fitch

Company	LTFC	Domicile	Sovereign LTFC	Country Ceiling
YPF S.A.	BB	Argentina	DDD	B
PAE	B+	Argentina	DDD	B
CVRD	BB	Brazil	BB–	BB–
CST	BB	Brazil	BB–	BB–
AmBev	BB+	Brazil	BB–	BB–
CocaCola Femsa	BBB+	Mexico	BBB–	BBB
KCM	BBB+	Mexico	BBB–	BBB
Southern Peru Copper	BB+	Peru	BB	BB

In all cases, these companies possess two or more of the characteristics outlined above. For instance, YPF and Companhia Siderurgica de Tubarao (CST) are owned by financially strong parent companies, generate substantial hard currency from exports and maintain cash balances (liquid assets) abroad. AmBev and Coca Cola Femsa (KOF) are also owned by strong parent companies (albeit minority owned in the case of KOF) and have multi-national operations that mitigate T&C risk. Companhia Vale do Rio Doce (CVRD) is a good example of an exporter that generates substantial hard currency, maintains substantial amounts of cash abroad and has been exempt from past government restructurings and T&C constraints.

To assess if a company has a sufficient mitigation of T&C risks to warrant a rating above the country ceiling, Fitch employs a case-by-case approach. In the analysis, Fitch implicitly considers the probabilities of a number of events occurring. The first event considered is a local currency default by an entity, the probability of which is represented by the entity's long-term local currency rating (LTLC). The second event considered would be a sovereign crisis that causes the authorities to impose a debt moratorium or T&C constraints preventing entities domiciled in the country from servicing foreign currency obligations. This probability is contained in a country's 'country ceiling' rating, and in sovereigns in which the country ceiling exceeds the sovereign's LTFC rating, Fitch believes that the likelihood of a broad debt moratorium is lower than that of a sovereign FC default. If the LTLC rating of an entity and the country ceiling are both higher than the sovereign LTFC rating, then the entity's LTFC rating could be higher than the sovereign LTFC rating[1]. The third event considered is the conditional probability that, given a sovereign-imposed debt moratorium, the entity concerned is affected by said moratorium and cannot service its FC debts. If this latter probability is less than one, i.e. it is conceivable that a sovereign-imposed debt moratorium would not always ensnare the entity, then the entity could be rated higher than the country ceiling. The probability of a debt service interruption resulting from a sovereign-imposed debt moratorium could differ across entities domiciled in a given country according to the factors listed on pages 1-2.

[1] It is important to note that an entity's LTFC rating would also be affected by the likelihood that factors other than sovereign-imposed T&C constraints, such as the vulnerability to a sharp currency depreciation, would affect FC debt service capacity.

Of the characteristics listed on pp. 1-2 that could substantially mitigate sovereign T&C risks, alone any one of these may not be sufficient to lower the probability the entity will not get ensnared in a sovereign-imposed debt moratorium, and therefore not sufficient to rate the entity above the country ceiling. Usually, there must be a combination these characteristics that will drive a rating above the country ceiling. Likewise, a corporate rated above the country ceiling where it is domiciled will nevertheless be linked to the country ceiling by virtue of it not being totally immune to sovereign balance of payments pressures. When an entity is rated above the country ceiling, Fitch is not suggesting that sovereign interference with an entity's FC debt service cannot occur, but merely that it is a lower probability event than it is for most other entities domiciled in that country. Fitch does not impose a limit of notches above the country ceiling, as the level of risk mitigation could be sufficient in some cases to warrant a rating multiple notches above. Such substantial risk mitigation can occur, for example, in the case of a company with a highly-rated foreign parent deemed very likely to support its subsidiary's debt service obligations.

■ The 'Long Term Local Currency' Rating

Considering a corporate's LTLC rating, it incorporates the business and financial risks of the company, as well as sovereign risk, including factors affecting the general economy and public policy (i.e. tax, labor and regulatory policies). Although the LTLC rating may be rated above the sovereign's LTLC rating, sovereign factors can often limit or constrain a financially strong corporate's rating at or above the sovereign's LTLC rating. The degree to which the corporate LTLC ratings are constrained by the sovereign LTLC rating depends on a diverse set of factors and circumstances including:

- Type of business and industry position.
- Exposure to the local economy.
- Product destination and customer location.
- Cost structure, local vs. imported supplies.
- Degree of regulation and importance to public policy goals.
- Ownership structure.
- Financial strength.
- Debt Profile, i.e. capital market debt versus bank debt and hard currency versus local currency debt.

During periods of acute sovereign stress and/or default, the domestic economy of a particular country can substantially contract, the local currency can experience a sharp devaluation and inflation could accelerate, forcing the government to impose price controls on certain goods and services. The financial markets and banking system would likely be disrupted, limiting access to credit. For instance, bank debt could be extended or rolled over only for the best corporate credits, even as capital markets shut down, thus making a corporate's debt structure, composition and denomination key items to consider in judging its ability to withstand a sovereign crisis.

Clearly, sovereign stress scenarios will create a difficult operating environment for all corporates, but to varying degrees. An exporter, for example, would likely do significantly better than a company more dependent on the local economy, such as a food retailer. An exporter generally competes on a global basis and usually benefits from a depreciating local currency, which could lower its cost structure and reduce the burden of its local currency debt obligations. Fitch believes that such entities often have a higher degree of insulation from the government, and their local currency ratings can exceed the local currency rating of the sovereign by several notches. See Appendix B for a list of Fitch's LTLC ratings above the sovereign.

In contrast to exporters, food retailers, for instance, are more likely to be exposed to recessionary pressures of the local economy. One food retailer may perform better than a similar food retailer in the same market if that company has a majority of its debt in local currency rather than foreign currency and the other does not, or if one of the companies has very little debt and is well capitalized versus the other entity.

For regulated entities, the linkage to the sovereign is much greater due to government oversight, including tariff and price-setting. Regulated entities tend to be dependent on local economic conditions, and the public policy significance of the services they provide can affect sovereign interference. As a result, barring exceptional support features from a strong foreign parent, such entities' ratings would likely remain at or close to the sovereign ratings. Such factors as clear laws and regulations enforced by a reasonably independent regulatory commission, high capital investment needs in the sector, and conservative financials could likewise support an argument for some notching of a regulated entity's LTLC rating above the sovereign.

As mentioned above, if an entity's LTLC rating exceeds the country ceiling, then the next step is for Fitch to assess the probability that the entity will get ensnared in sovereign-imposed T&C constraints.

Being an Exporter: Sufficient for Rating Above the Country Ceiling?

Many companies with ratings above the country ceiling are exporters with foreign currency-denominated income streams, which are generally captured and retained offshore, and from a practical perspective, could be used to service external debt. Foreign currency trapped and held abroad can be an important driver of ratings above the country ceiling. Fitch stresses that being an exporter alone is not sufficient to have a rating above the country ceiling. This rationale is based on the premise that during a sovereign balance of payments crisis, the government has an incentive to acquire scarce foreign exchange from the private sector in order to forestall its own foreign currency debt default and meet other key sovereign foreign currency needs. Hence, the authorities might look to the country's major exporters as a source of foreign exchange. Through surrender requirements, export taxes, the outright imposition of T&C controls or a private debt moratorium, the sovereign could force exporters to default. Furthermore, government-owned exporters (e.g. natural resource producers) are particularly prone to sovereign interference.

Despite these risks of interference with foreign currency flows, recent history has shown that certain governments seem to understand the importance of striking a balance between appropriating an exporter's hard currency and allowing it to maintain sufficient hard currency to meet obligations in order to avoid injury to the country's export capacity. For instance, the sovereign could permit important exporters a degree of financial flexibility, e.g. by allowing them to hold a portion of export proceeds offshore or quickly authorizing transfer of funds to meet bona fide financing and operating requirements during periods of exchange controls. This may explain the government of Argentina's less harsh treatment of the hard currency-generating hydrocarbon exporters, which are funding a substantial portion of the federal government by way of export taxes, versus the foreign-owned utilities that sell public services domestically to a population living under challenging economic conditions. All of the hydrocarbon exporters in Argentina, Repsol YPF, PanAmerican Energy, Petrobras Energia and Compania Mega, are allowed to keep 70% of export proceeds offshore, whereas other exporters must repatriate 100% of export proceeds. These differing policies and incentives for sovereign interference are what necessitate Fitch's case-by-case approach.

The track record of a sovereign government's treatment of specific companies with regard to surrender requirements, taxation, exemption from T&C constraints or debt moratoria can be a pivotal factor in determining whether a company can pierce the country ceiling, though one has to be careful about using past history as a predictor of the future. For example, in the case of the Brazilian iron company, CVRD, the company, like the state-owned oil company Petrobras, was exempt from remittance constraints in past debt moratoria declared by the Brazilian authorities (in the 1980s and 1990s). Yet CVRD, which was partially privatized in 1997, was a state-owned enterprise back then, suggesting that the government could treat CVRD differently than in the past. On the other hand, through a "golden" shareholding, the Brazilian government still plays an important role in CVRD, and the degree to which this role could impact the firm's financial decisions in a balance of payments crisis limits the divergence between CVRD's LTFC rating and the country ceiling. Petrobras, still majority state-owned, remains at Brazil's country ceiling rating of 'BB–'.

While an exporter is in one of the best positions to stave-off a default due to T&C issues, some combination of the characteristics that mitigate risk outlined on pages 1-2 are necessary to yield corporate ratings above the country ceiling. The corporates that Fitch currently rates above the country ceiling are generally exporters and multinational companies, several with financially strong foreign parent companies, and by and large are domiciled in Latin America, specifically, in Argentina, Mexico, Peru and Brazil. Nevertheless, Fitch does consider an exporter's inherent strength to generate hard currency relative to its debt burden, comparing the ratios of foreign currency earnings to foreign currency debt and debt service and the proportion of revenues that are exported, as well as an exporter's other strengths, such as access to secured bank financing or the ability to securitize future export flows.

The "Metric": 12 Months Debt Service Coverage

Sovereign balance of payments crises usually have a duration. Sovereigns sometimes come close to running out of foreign exchange (i.e. defending an exchange rate or providing support to suffering private companies with large external debts) and in some cases this results in a sovereign default[2]. Exchange and capital controls, a private debt moratorium, bank holidays, high export revenue surrender requirements and/or punitive export taxes may be imposed to shore up the foreign exchange position of the sovereign. In the past, these measures have all had a duration, ranging from weeks and months to two years, though controls remained in place for longer in some countries in the 1980s following Mexico's default in 1982. See Appendix C for an overview of recent sovereign financial crises.

For this reason and to put this in perspective, Fitch's Emerging Market Structured Finance Group routinely requires an offshore debt service reserve fund that covers at least six to eighteen months of debt service to allow the foreign currency rating of a specific transaction to be rated one or more notches above the country ceiling. This reserve buys an entity time to service debt until the sovereign eases exchange controls for private sector debt service and/or alternative mechanisms for obtaining foreign exchange become available. In Malaysia during the late 1990s Asian financial crisis, external debt service was exempted from exchange controls. Even when debt service is not formally exempted, it has often been the case that after an initial period of disruption, the exchange authorities routinely approve foreign exchange needed for external debt service.

In the Venezuelan crisis of 2003, when oil production was sharply curtailed for more than a month, Fitch downgraded Venezuela's LTFC sovereign rating to 'CCC+', but lowered the rating of PDVSA Finance, a future flow oil receivables transaction with a three-month reserve fund, only to 'BB–'. The Venezuelan authorities have maintained exchange controls since February 2003, though private entities can apply for foreign exchange for debt service and other reasons. In addition, government-issued foreign currency bonds for the local market and trading in ADRs have provided mechanisms in Venezuela for companies to obtain foreign exchange. Likewise, during the 1994-96 foreign exchange control period in Venezuela, the Brady bond market provided a similar mechanism. In Argentina in 2002, foreign exchange controls were imposed and private companies had to apply to the central bank to obtain foreign exchange for debt service. The central bank was initially selective about approving foreign exchange transactions, but eased this policy after a couple of months. Nevertheless, sharp currency depreciations often cause corporate bond defaults during sovereign crises, as occurred in Argentina, so it is sometimes difficult to discern whether a private sector default is a result of sovereign-imposed T&C constraints or a currency depreciation.

Certainly, a balance of payments crisis and the controls imposed as a result could last longer than 6-18 months, but there is a high enough probability that the duration of such a crisis or of the interruption of private sector debt service associated with it will be short. With this in mind, Fitch has developed a "metric" for assessing the adequacy of an offshore cash reserve to warrant rating an entity above the country ceiling. Generally, if cash abroad covers at least 12 months of external debt service (including debt amortization and interest), and other characteristics that mitigate T&C risk, found on pages 1-2 are present, then a rating above the country ceiling is possible. Likewise, should the coverage of debt service fall short of 12 months, and other factors strongly mitigate T&C risks, Fitch could still rate a company above the country ceiling. Furthermore, debt service coverage in excess of 12 months, especially in conjunction with other risk mitigants, could warrant a greater than one notch uplift from the country ceiling, though beyond 2-3x coverage, risk mitigation would diminish, given that most sovereign crises do not go beyond 2-3 years. A multiple notch uplift above the country ceiling is reserved for those credits with a strong, supportive foreign parent and/or substantial multinational operations that ensure that the company has clear financing sources outside the purview of the sovereign where it is domiciled.

It is important to underscore as well that Fitch monitors the size of assets held offshore *over time*. Adequate debt service coverage should be maintained over time, at a minimum the most recent two year period. The quality and liquidity of offshore funds are likewise critical, with cash and cash equivalents held in highly rated financial institutions and instruments qualifying as the best investment vehicles. Finally, Fitch considers any changes to laws and regulations that allow or prohibit companies from maintaining adequate funds offshore, i.e. surrender requirements. In Brazil's case for example, exporters are required to surrender or repatriate export proceeds within 180 days of export, which in and of itself, after a 30-40

[2] Sovereigns often have the option of turning to multilateral or other official creditors for balance of payments support.

day payment lag is factored in, provides a 4-5 month cash cushion that could be used for debt service in a crisis. In addition, Brazilian companies, as a result of a transfer pricing rule, can keep 10% of gross export proceeds permanently abroad and can do the same with proceeds from any overseas asset sales.

Appendix A: Profiles of Select Corporates With LTFC Ratings Above the Country Ceiling

YPF S.A.

Fitch LTFC Rating: BB

Key Factors in Rating YPF Above the 'Country Ceiling'

- Strong Foreign Parent.
- Substantial Exporter and Generator of Hard Currency.
- High Levels of Cash Consistently Kept Abroad.
- Low Debt Levels.
- Lower Surrender Requirement Embodied in Law.
- Important tax payer/collector for Government.

Repsol YPF's Argentine subsidiary (YPF) has a LTFC rating of 'BB', three notches above Argentina's country ceiling of 'B'. YPF is 100% owned and controlled by Repsol YPF, the Spanish-owned integrated oil company rated 'BBB+' by Fitch. YPF's ratings benefit from its strong foreign shareholder, strong stand-alone financial strength, and reliance on significant dollar-denominated oil exports. The Argentine government has allowed the company as well as all hydrocarbon (oil) producers to maintain up to 70% of export proceeds abroad and repatriate at least 30% of export revenues to Argentina. These surrender requirements are embodied in Argentina's hydrocarbon law that was ratified in December 2002 during the sovereign crisis; exporters of all other products must repatriate 100% of all export proceeds. This unique constellation of almost all the characteristics noted above has allowed Repsol YPF to be rated well above Argentina's sovereign rating and country ceiling, despite the Argentine debt default and accompanying crisis.

Repsol YPF (Argentine Subsidiary) Financial Profile 2004

USD mn	
Revenues	6,688
% Export Sales	37%
EBITDA	3,671
Cash	1,346
Total Debt	648
% Total Debt in Foreign Currency	69%
ST Debt Service (excl. bank rollovers)	30
Total Debt/EBITDA	0.2
EBITDA/Interest Expense	49.5
Months of offshore cash	significant

Heightened sovereign interference risk and the imposition of a tax on crude oil exports, among other factors, led to a four-notch downgrade of YPF between December 2001 and March 2002 (three-notch downgrade for parent, Repsol YPF), followed by a two-notch upgrade to 'BB' in October 2003 (one-notch upgrade for parent, Repsol YPF).

YPF's strong financial position allowed it the flexibility to absorb the substantially higher oil export taxes imposed during the sovereign crisis and provided a large portion of total government collections (YPF represented 3% of exports and 17% of government revenues in 2003). Following the sovereign default, YPF has repaid approximately USD 1.8 billion in debt as well as maintained access to the bank and bond markets. YPF also benefited from the devaluation of the Argentine Peso which lowered its cost structure. The company was never denied sovereign authorization to pay debt obligations.

PANAMERICAN ENERGY (PAE)

Fitch LTFC Rating: B+

Key Factors in Rating PAE Above the 'Country Ceiling'

- Strong Foreign Parent; 60% BP.
- Substantial Exporter and Generator of Hard Currency.
- High Levels of US Dollar Cash Generation Relative to Debt.
- Consistently High Levels of Cash.
- Low Surrender Requirement Embodied in Law.

The rating reflects PAE's strong and expanding asset base of hydrocarbon reserves, its position as the second largest hydrocarbon producer in Argentina, strong U.S. dollar revenues from exports of oil and gas, ability to retain a material amount of export revenues offshore, benefits related to its ownership by BP plc (Fitch LTFC rating of 'AA+'), strong credit protection measures, conservative financial position, and manageable debt maturity profile. The rating also reflects concentration of assets in Argentina, potential for increased interference in Argentine export taxes or remittance requirements, political concerns in Bolivia, inherent risks of commodity price volatility, and small size relative to BP's consolidated operations.

PAE

Financial Profile 2004

USD mn

Revenues	1,546
% Export Sales	43%
EBITDA	915
Cash	160
Total Debt	644
% Total Debt in Foreign Currency	96%
Debt Service (excl. bank rollovers)	52
Total Debt/EBITDA	0.7
EBITDA/Interest Expense	26
Months of offshore cash	38

The Argentine branch, rated 'AA(arg)' on the national scale by Fitch, has historically been the primary PAE subsidiary both in terms of assets and revenues and the entity that assumes the financial debt for the whole group. The company has demonstrated its success in navigating the Argentine environment to date. PAE's ability to generate sufficient cash flow to repay dollar denominated debt coupled with its right to maintain 70% of export proceeds outside Argentina has mitigated the risks associated with having the majority of its assets and cash generating activities concentrated in Argentina. Due to the combination of maintaining its export revenues abroad and the company's prudent financial strategy, PAE never failed to meet scheduled debt service despite currency controls imposed during the height of the Argentine crisis.

Total financial debt at December 2004 was approximately US$644 million, with a total financial debt-to-EBITDA of 0.7 and debt-to-total capital of 15%. While PAE's leverage may increase in the future, the company's financial strategy is to maintain a conservative capital structure in the current environment. Core borrowing facilities are generally held at the Argentine branch level. Given PAE's conservative balance sheet, the company is expected to continue to issue debt on a periodic basis to refinance maturities, extend the average life of its debt and maintain a relatively stable debt-to-capitalization ratio. The company faces maturities of approximately US$204 million in 2005 and US$52 million in 2006. Short-term cash needs should be adequately covered through cash balances, cash from operations plus access to working capital financing.

PAE has demonstrated its ability to access financial markets and refinance outstanding debt, which has been supported by a combination of conservative capital structure, increasing levels of cash generation, and a manageable debt amortization schedule. During 2002 and 2003, at a time when financial and capital markets were closed for most Argentine companies, PAE was able to raise funds multiple times for refinancing and working capital purposes. For the year ended- 2004, PAE reported a total EBITDA of US$915 million, compared with a total EBITDA of US$685 million for the same period in 2003, reflecting increased production of oil, gas, and liquid petroleum gas (LPG) and higher prices.

AMBEV (SUBSIDIARY OF INBEV)

Fitch LTFC Rating: BB+

Key Factors in Rating Ambev Above the Country Ceiling

- Geographic Diversification of Cash Flows.
- Strong International Parent Company.

AmBev's BB+ FC rating reflects its geographic diversification of operations and cash flow and implicit support from its new parent company, InBev. As part of the Inbev acquisition, AmBev now directly owns 100% of Labatt Canada (Labatt), the second-largest brewer in Canada. This subsidiary, which was merged into AmBev on August 27, 2004, accounted for about 13% of AmBev's 2004 EBITDA and 35% of its debt. If Labatt had been part of AmBev for all of 2004, it would have accounted for about 30% of its consolidated EBITDA. In 2003, AmBev's Brazilian operations, pre-acquisition, accounted for about 92% of the company's consolidated EBITDA. With the addition of Labatt, plus the growth of its other investments in Latin America, on a pro forma basis, in 2004 Brazilian operations should have accounted for less than 65% of its consolidated EBITDA.

Ambev's FC rating also incorporates the overall strategic importance of the company to InBev. As a result of the acquisition and a mandatory tender offer, InBev now owns 81% of the voting shares in AmBev and has a 56% economic stake. On a pro forma basis, Ambev should have accounted for about 50% of InBev's consolidated EBITDA in 2004. The former controlling shareholders of AmBev now share control of InBev. These shareholders built AmBev into a diversified multinational beverage company over the past 15 years through a series of investments in Latin America. Given its comfort for operating in emerging markets, Fitch believes InBev's level of financial support for AmBev would be high during a political or economic crisis in Brazil.

AmBEV

Financial Profile 2004

Reais mn

Revenues	12,007
% Export Sales	n.a.
EBITDA	4,537
EBITDA (Foreign Ops)	1,136
Cash	1,505
Total Debt	7,810
% Total Debt in Foreign Currency	87%
Brazil subsidiary ST FC debt	450
Total Debt/EBITDA	1.7
EBITDA/Interest Expense	7.7
Months of offshore cash	6

N.a. = Not available.

In addition to 6 months cash offshore, AmBev could cover annual dollar debt service by more than 1 times (x) with hard currency from Labatt; about $250 million of LaBatt's cash flow is available to upstream to AmBev under the existing debt arrangements. This compares with annual U.S. dollar debt obligations of about $275 million per year by AmBev's Brazilian operating subsidiary. This debt service consists of approximately $170 million of amortizing debt and $100 million of annual interest expense on the notes due in 2011 and 2013. Alternatives are also available to provide hard currency and financial support from the shareholder through intercompany loans during times of sovereign stress. It is important to note that the foreign currency rating of AmBev is below the local currency rating of 'BBB' due to negative covenants on debt at Labatt that restrict the distribution of cash from it to AmBev by the following formula: EBITDA less interest charges, capital expenditures and cash taxes.

COMPANHIA VALE DO RIO DOCE (CVRD)

Fitch LTFC Rating: BB

Key Factors in Rating CVRD Above the Country Ceiling

- Substantial Exporter and Generator of Hard Currency.
- High Levels of US Dollar Cash Generation Relative to Debt.
- High Levels of Cash, Portion Held Offshore, Bolstered by Committed LOC.
- Preferred T&C Access Given in Past by Government.

CVRD is the world's largest exporter of iron products and is rated 'BB', one notch above Brazil's LTFC rating and country ceiling, both 'BB–'. While CVRD does not have a strong foreign parent like in the cases of Repsol YPF and several others, CVRD has strong and growing foreign-currency denominated earnings streams, cash abroad and rules that allow them to trap enough cash offshore to meet a substantial portion of annual external debt service. In addition, CVRD has a track record of favorable treatment by the government. CVRD was government-owned until its 1997 privatization and operates relatively autonomously from the government although the government continues to own a "golden share" as well as ownership stakes held through government pension funds and the state development bank. As a quasi-government-owned company, CVRD, like the state-owned oil company, Petrobras, was exempt from remittance constraints in past debt moratoria declared by the Brazilian authorities (in the 1980s and 1990s). This continuing government role in CVRD, and the degree to which this role could impact the firm's financial decisions in a balance of payments crisis, limit the divergence between this company's LTFC rating and the country ceiling.

CVRD

Financial Profile 2004

USD mn

Net Revenues	8,066
% Export Sales	72%
EBITDA	3,722
Cash	1,249
Total Debt	4,095
% Total Debt in Foreign Currency	97%
Debt Service (excl. bank rollovers)	1,113
Total Debt/EBITDA	1.1
EBITDA/Interest Expense	11.4
Months of offshore cash	9

As of Dec. 31, 2004, CVRD held US$1.2 bln in assets offshore, as against US$1.1 bln in 2004 debt service. Of these assets, roughly US$876 million was cash and net accounts receivable, and the balance equity positions in foreign companies in investment grade countries. In addition, the company had US$750 million in committed credit lines from highly rated international banks, which lacked material adverse change (MAC) clauses that could allow the banks to withdraw their line of credit in a crisis (only a forced debt acceleration of US$50 million or more could enable the banks to cancel these lines); offshore cash plus committed LOC cover current debt service by close to 18 months.

CVRD's pure cash position abroad has fluctuated between $227 million and $1.4 billion over the last three years. In conjunction with CVRD's other risk mitigants – history of exemption from remittance requirements, strategic role as world's largest iron ore exporter, other overseas assets, and strong stand-alone financials -- the company's mitigants of T&C risks warrant a one-notch uplift above the country ceiling.

COMPANHIA SIDERURGICA DE TUBARAO (CST)

Fitch LTFC Rating: BB

Key Factors in Rating CST Above the Country Ceiling

- Strong Foreign Parent; more than 60% owned by Arcelor.
- Substantial Exporter and Generator of Hard Currency.
- High Levels of US Dollar Cash Generation Relative to Debt.
- High Levels of Cash; Portion Held Offshore.

CST, the Brazilian steel company, benefits from a 62% ownership stake held by Arcelor, the world's second largest steel producer based in Luxembourg which has strong financials. In addition to Arcelor's support, CST's ability to trap foreign exchange offshore in amounts sufficient to meet a major portion of debt service, according to Brazilian rules on transfer pricing and export proceed surrender requirements, warrant a one-notch uplift from the country ceiling.

CST

Financial Profile 2004

USD mn

Net Revenues	1,823
% Export Sales	63%
EBITDA	842
Cash	132
Total Debt	517
% Total Debt in Foreign Currency	62%
Debt Service (excl. bank rollovers)	232
Total Debt/EBITDA	0.5
EBITDA/Interest Expense	22.5
Months of offshore cash	6

As of Dec. 31, 2004, CST held cash offshore of US$119 million that partially covers a year's debt service. CST's ratings are supported by the company's favorable competitive position as one of the world's lowest cost producers and exporters of steel slabs. Consequently, CST is able to generate positive cash flows during troughs in the industry cycle. The rating is also supported by the company's U.S. dollar-denominated revenues, as approximately 65% of CST's sales are generated outside of Brazil. The U.S. dollar cash flow mitigates Brazilian risk and protects the company from a mismatch between the currency of its debt and that of its revenues. The ratings also take into consideration the cyclical nature of the steel industry. CST's annual average per-ton slab prices have fluctuated significantly over the last several years to $340 in 2004 from $172 in 2001 but, over the long term, average in the US$210–230 range. Such price volatility has a significant effect on credit-protection measures.

COCA-COLA FEMSA

Fitch LTFC Rating: BBB+

Key Factors in Rating Coca Cola Femsa Above the Country Ceiling

- Strong Foreign Owner, The Coca Cola Company, rated 'A+'.
- Moderate Levels of Cash Relative to Debt.
- Substantial International Operations in a number of low-rated countries.
- No Surrender Requirements.

In Mexico, where the country ceiling of 'BBB' exceeds the sovereign LTFC rating of 'BBB–',

Coca Cola Femsa

Financial Profile 2004

USD mn

Revenues	4,118
Non-Mexico Revenues	1,757
EBITDA	887
Non-Mexico EBITDA	281
Cash	322
Total Debt	2,239
Total Debt in Foreign Currency	23%
Short-term debt	293
Total Debt/EBITDA	2.5
EBITDA/Interest Expense	4
Months of Offshore Cash	0

Coca-Cola Femsa (KOF), a soft drinks company 39.6% owned by The Coca-Cola Company (KO), is rated 'BBB+', one notch above the country ceiling and three notches below KO's 'A+' rating. Coca-Cola Femsa is the second largest bottler of Coke products in the world, accounting for approximately 40% of Coca-Cola's sales to Latin America and about 50% of its sales in Mexico. KOF's rating reflects its strategic importance to Coca-Cola. It also reflects Coke's track record of financially supporting its key bottlers. So, in this case, the strength and support of the parent is likewise key to the uplift above Mexico's country ceiling, along with the company's international operations.

KOF's rating above the country ceiling further reflects the balance between the currencies of its debt obligations and the geographic diversification of its cash flow. It also reflects the fact that during the next four years the company never faces a year with debt amortizations of more than $333 million. During the past twelve months KOF generated $887 million of EBITDA. Approximately 68%, or $606 million, was generated in Mexico. The balance of KOF's cash flow from operations was generated almost evenly between Venezuela, Argentina, Brazil and Costa Rica. At December 31, 2004, 77% of the company's debt was denominated in Pesos and 23% was denominated in U.S. dollars. As a result of the geographic breakdown of KOF's cash flow and debt, the company could service its Mexican peso denominated interest expense due in the next 12 months with EBITDA generated in pesos in Mexico by a ratio of 3.5x and it could service its dollar interest expense by EBITDA generated outside of Mexico by 5.5x.

KIMBERLY CLARK DE MEXICO

Fitch LTFC Rating: BBB+

Key Factors in Rating Kimberly Clark de Mexico Above the Country Ceiling

- Strong Foreign Owner (48%), Kimberly Clark, rated 'AA'.
- High Levels of Cash Relative to Debt.
- No Surrender Requirements.

KCM's foreign currency rating of 'BBB+', which is one notch above Mexico's country ceiling of 'BBB', is based on the company's debt-payment track record, export sales and implicit support from Kimberly-Clark. The company maintains large cash balances relative to debt levels to ensure liquidity in the event of economic downturns or other unforeseen events.

Kimberly Clark de Mexico Financial Profile 2004

USDmn

Revenues	1,774
% Export Sales	7%
EBITDA	543
Cash	191
Total Debt	530
% Total Debt in Foreign Currency	57%
Debt Service (excl. bank rollovers)	70
Total Debt/EBITDA	1
EBITDA/Interest Expense	11.7
Months of Offshore Cash	33

KCM's long-term strategy is to maintain a conservative debt profile. The company's low debt levels, coupled with a strong and stable cash flow generating ability, have resulted in interest coverage ratios in the range of 12 times (x)–13x over the past several years. At Dec. 31, 2004, KCM's debt totaled $530 million, of which only $59 million is due over the next 12 months. KCM's credit-protection measures remain strong, with EBITDA/interest expense at 11.7 times (x) and net debt to EBITDA of 0.6x during 2004, consistent with the rating category. The company pays important cash dividends that average slightly more than $200 million per year and has also continued to buy back shares on a discretionary basis.

KCM also maintains large cash balances to ensure liquidity. At Dec. 31, 2004, KCM's balance of cash and marketable securities was $191 million. A majority of the cash balances are held outside Mexico in dollar accounts to ensure the availability of hard-currency needs. Over the past three years, KCM has maintained average cash balances of close to US$200 million.

SOUTHERN PERU COPPER COMPANY (SPCC)

Fitch LTFC Rating: BB+

Key Factors in Rating SPCC Above the Country Ceiling

- Geographic Diversification of Cash Flows.
- Substantial Exporter and Generator of Hard Currency.
- High Levels of US Dollar Cash Generation Relative to Debt.
- High Levels of Cash; Portion Held Offshore.

SPCC's foreign currency rating reflects enhanced geographic diversification of operations and cash flow following the completion of SPCC's acquisition of affiliate company, Minera Mexico from SPCC's parent company, Americas Mining Corporation (AMC) on April 1, 2005. SPCC now owns 99% of Minera Mexico, Mexico's largest copper producer. SPCC's cash flow should become more diversified as Minera Mexico is expected to account for approximately 50% of the company's consolidated EBITDA going forward. SPCC and Minera Mexico together generated US$1.7 billion of EBITDA in 2004 (SPCC with US$1.0 billion and Minera Mexico with US$676 million). In addition, the rating reflects the company's improved capital structure and reduced consolidated debt levels on a pro forma basis. In 2004, strong financial performance and cash flow generation allowed the company to reduce debt and net debt levels by 20% and 56%, respectively, on a pro forma basis.

SPCC's foreign currency rating of 'BB+' exceeds Peru's 'BB' country ceiling by one notch due to the cash flow generated by its Mexican subsidiary, Minera Mexico. In the event of a sovereign crisis in Peru, in which transfer and convertibility restrictions were imposed, the free cash flow of Minera Mexico should be able to cover SPCC's future debt service by approximately 1.0 times (x) to 4.0x depending on copper prices. On a consolidated basis, SPCC also generates about US$2.0 billion in exports outside of Latin America, which would provide the company with access to hard currency in the event of transfer and convertibility restrictions in Peru. SPCC, a Delaware-incorporated company, has historically held most of its cash in the United States. Cash balances outside of Peru would provide additional sources of liquidity to the company in the event of foreign currency restrictions. The downgrade of SPCC's local currency rating to 'BB+' from 'BBB–' and the upgrade of Minera Mexico's local and foreign currency rating to 'BB+' from 'BB–' reflects the consolidated credit quality of SPCC and Minera Mexico, the new ownership structure and the rebalancing and support of the debt by the two entities on a combined basis.

SPCC (Pro forma)

Financial Profile 2004

USD mn	
Revenues	3,097
% Export Sales	67
EBITDA	1,681
EBITDA (Foreign Ops)	676
Cash	756
Total Debt	1,330
% Total Debt in Foreign Currency	100%
Debt Service	278
Total Debt/EBITDA	0.8
EBITDA/Interest Expense	13.3
Months of offshore cash	33

The combined entity has a strong capital structure and is expected to generate EBITDA of more than US$2.0 billion in 2005, resulting in a consolidated total debt-to-EBITDA ratio of about 0.5x. Management of SPCC believes that a consolidated debt of between US$1.1 billion and US$1.2 billion is appropriate. Therefore, it does not intend to use any excess cash flow in the future to reduce debt. In 2004, SPCC generated EBITDA of US$1.0 billion and had total debt of US$289 million, resulting in a total debt-to-EBITDA ratio of about 0.3x. In 2004, Minera Mexico generated EBITDA of US$676 million and had total debt of US$1.0 billion, resulting in a total debt-to-EBITDA ratio of about 1.5x. Although SPCC's proforma consolidated leverage is low for the rating category, the company's management has yet to demonstrate a long-term commitment to a conservative capital structure that would enable it to grow during the trough in the pricing cycle, which somewhat constrains the rating.

Appendix B: Corporate LTLC Ratings Above the Sovereign LTLC Rating

Company	Country	LTLC Rating	Sovereign LTLC Rating	Notches
Petrobras Energia S.A.	Argentina	B	B–	1
YPF S.A.	Argentina	BB	B–	4
Alcoa Aluminio S.A.	Brazil	BBB–	BB–	3
Aracruz Celulose S.A.	Brazil	BBB–	BB–	3
Banco Bradesco S.A.	Brazil	BB+	BB–	2
Banco Itau BBA S.A.	Brazil	BB+	BB–	2
Banco Itau Holding Financeira S.A.	Brazil	BB+	BB–	2
Banco Itau S.A.	Brazil	BB+	BB–	2
Banco Safra S.A.	Brazil	BB	BB–	1
Banco Santander Brasil S.A.	Brazil	BB+	BB–	2
Banco Santander Meridional S.A.	Brazil	BB+	BB–	2
Banco Votorantim S.A.	Brazil	BB	BB–	1
Banco do Brasil S.A.	Brazil	BB	BB–	1
Banco do Estado de Sao Paulo S.A. (Banespa)	Brazil	BB+	BB–	2
Brasil Telecom Participacoes S.A.	Brazil	BB+	BB–	2
Brasil Telecom S.A.	Brazil	BBB–	BB–	3
Braskem	Brazil	BB+	BB–	2
Companhia Siderurgica Nacional (CSN)	Brazil	BBB–	BB–	3
Companhia Siderurgica de Tubarao (CST)	Brazil	BBB–	BB–	3
Companhia Vale do Rio Doce (CVRD)	Brazil	BBB	BB–	4
Companhia de Bebidas das Americas (AmBev)	Brazil	BBB	BB–	4
Gerdau Acominas	Brazil	BBB–	BB–	3
MRS Logistica S.A. (MRS)	Brazil	BB	BB–	1
Ripasa S.A. Celulose e Papel	Brazil	BB+	BB–	2
Samarco Mineracao S.A.	Brazil	BBB–	BB–	3
Tele Norte Leste Participacoes S.A.	Brazil	BB+	BB–	2
Telemar Norte Leste S.A.	Brazil	BBB–	BB–	3
Unibanco-Uniao de Bancos Brasileiros S.A.	Brazil	BB	BB–	1
Bank Buana Indonesia	Indonesia	BB– OP	B+ OP	1
Bank Nisp	Indonesia	BB– OP	B+ OP	1
P.T. Telekomunikasi Selular	Indonesia	BB+	B+ OP	3
Bolzano, Autonomous Province of	Italy	AA+	AA	1
Trento, Autonomous Province of	Italy	AA+	AA	1
Canon Inc.	Japan	AA	AA– ON	1
America Movil, S.A. de C.V.	Mexico	BBB+ OP	BBB	1
Banca Serfin	Mexico	BBB+	BBB	1
Banco Nacional de Mexico (Banamex)	Mexico	A–	BBB	2
Banco Santander Mexicano	Mexico	BBB+	BBB	1
BBVA Bancomer	Mexico	BBB+	BBB	1
Coca-Cola Femsa, SA de CV	Mexico	BBB+	BBB	1
Corporacion Interamericana de Bebidas	Mexico	BBB+	BBB	1
Kimberly-Clark de Mexico (KCM)	Mexico	A	BBB	3
Telefonos de Mexico S.A. de C.V. (Telmex)	Mexico	A–	BBB	2
Empresa de Generacion Electrica Fortuna S.A.	Panama	BBB–	BB+	1
Telefonica del Peru, S.A.A. (TDP)	Peru	BBB+	BB+	3
Akbank	Turkey	BB+	BB–	2
Anadolu Efes Biracilik ve Malt Sanayii A.S.	Turkey	BB+	BB–	2
Ford Otosan	Turkey	BBB–	BB–	3
HSBC Bank A.S.	Turkey	BB+	BB–	2
Kocbank A.S.	Turkey	BB+	BB–	2
Kuwait Turkish Evkaf Finance House	Turkey	BB	BB–	1
Turkiye Petrol Refinerileri A.S. (TUPRAS)	Turkey	BB+	BB–	2
ProCredit Bank (Ukraine)	Ukraine	BB–	B+	1
C.A. La Electricidad de Caracas S.A.	Venezuela	BB–	B+	1
Summary				
Total LTLC Ratings Above Sovereign LTLC	54			
Average Notches	1.9			

Appendix C

Overview of Sovereign Crises

Crisis Country	Year	Sovereign Debt Default	Pre-Crisis Exchange Rate Regime	Exchange and Capital Controls Imposed During Crisis
Mexico	1994-5	No	Crawling peg	Additional exchange and capital controls were not imposed during the crisis, though there was a major banking crisis and bank failures.
Venezuela	1994-5	Domestic debt only	Managed	Extensive controls on current account as well as capital account transactions were imposed, including export surrender requirements and restrictions on the availability of foreign exchange for imports. Capital outflows were prohibited except for foreign debt repayments.
Romania	1996-7	No	Managed	Banks had their fx dealer licenses revoked except for 4 state-owned banks. Limits were placed on foreign exchange bureaus. Consequently, the inter-bank fx market effectively closed and the private sector had difficulty obtaining foreign exchange.
Korea	1997-8	No	Managed	Additional exchange and capital controls were not imposed during the crisis. However, Korean banks' short-term foreign debt obligations were restructured into new obligations with a sovereign guarantee. Although the corporate sector was not prevented from meeting foreign debt obligations, there were several major corporate defaults.
Indonesia	1998	Bilateral external debt to official creditors was restructured. Single sovereign Yankee bond unaffected.	Managed	The Indonesian authorities did not impose additional exchange and capital controls during the crisis. Nonetheless, there were widespread bank and corporate defaults following the collapse of the rupiah. Bank Indonesia provided a US dollar guarantee in support of a swap of inter-bank debt owed to foreign banks for medium and long-term obligations. The government also supported a voluntary restructuring of external obligations of the corporate sector, providing a foreign exchange guarantee.
Russia	1998-9	Rouble denominated government securities; "Soviet-era" foreign currency denominated debt owed to official and private creditors. Remained current on Russian Federation Eurobonds.	Crawling peg	Capital controls were tightened significantly, including enforcement of export surrender requirements. A 90-day moratorium on private sector external obligations (including fx forward contracts) was announced by the authorities suspending payments by residents to non-residents of principal on loans with a maturity exceeding 180 days. According to the authorities, only $400m payments of non-bank debt were due over this period compared to $2.7bn of bank obligations. Moreover, many corporates and even some banks circumvented the moratorium to make payments to foreign creditors by using foreign assets or earnings or making deposits with the Russian branches of foreign creditor banks.
Ecuador	1999	Brady bonds, Eurobonds and official bilateral debt were all rescheduled.	Fixed	Bank holiday was imposed, followed by deposit freeze. Capital controls were imposed, including export surrender requirements and advance deposits for import payments. However, the servicing of private sector external debt was not prohibited.
Pakistan	1999	Official bilateral debt was rescheduled. Sovereign Eurobond debt was also restructured as was some domestic debt.	Fixed	Controls on capital account transactions were imposed, particularly with respect to capital outflows (such as on foreign investment abroad, loans to non-residents) as well as export surrender requirements and controls on import financing. US dollar bank deposits were frozen.
Ukraine	1998-2000	Selective restructuring of domestic public debt followed by external debt restructuring.	Fixed	Additional exchange controls were imposed, including export surrender requirements and controls on import financing. However, controls did not cover private external debt service and there were no indications that the private sector incurred arrears to foreign creditors due to capital controls.

Source: Fitch Ratings

Overview of Sovereign Crises

Crisis Country	Year	Sovereign Debt Default	Pre-crisis Exchange Rate regime	Exchange and Capital Controls Imposed During Crisis
Argentina	2001	Exchange of domestic and external sovereign debt held by private creditors concluded in December 2001 judged to be distressed debt exchange and hence an event of default by Fitch. Argentine authorities announced a moratorium in January 2002 on debt not previously exchanged.	Fixed	Restrictions on bank deposit withdrawals imposed in December 2001 – the “corralito” which imposed restrictions on the withdrawal of deposits from the banking system. All currency transfers abroad had to be approved by the central bank, including payments to foreign creditors. The central bank was very selective in granting permission to the private sector to transfer fx abroad to foreign creditors, but this was relaxed after a couple of months. Exchange control regulations were subject to a multitude of ad hoc changes in the months following the abandonment of “convertibility”, though generally exporters and those companies with offshore assets were not prevented from meeting their obligations. In January, dollar deposits were forcibly pesoized and the maturity of time deposits extended. Following the moratorium on sovereign external debt, surrender requirements on export proceeds were also imposed along with strict limitations on interbank currency trading. Widespread bank and corporate defaults due to direct sovereign intervention (deposit freeze/pesoification/tariffs) and the huge depreciation of the peso and contraction of the economy. Nonetheless, some Argentine corporates did manage to remain current on their external obligations during this period.
Uruguay	2002	Yes	Crawling peg	One week bank holiday imposed to stem deposit flight. Subsequently, US dollar denominated time deposits of state banks were forcibly restructured. Access to deposits in foreign banks was unrestricted following the end of the bank holiday. Additional exchange and capital controls were not imposed. Severe banking crisis. Corporate sector debt payments largely unaffected.
Moldova	2002	Yes	Managed	The authorities did not impose additional capital and exchange controls as a result of the restructuring of its sovereign Eurobond and official bilateral debt. The sovereign bond restructuring, which was expected, had few macroeconomic ramifications.
Dominican Republic	2003-05	Yes	Dual – Managed and Floating	Fraudulent activities resulted in the collapse of the second largest bank in the country and the subsequent contagion and failure of other smaller banks. Inadequate management of public finances also contributed to the crisis that began in 2003; however, additional exchange and capital controls were not imposed during this period. While the servicing of private sector external debt was not prohibited, a lack of confidence in the authorities’ ability to manage the banking crisis led to a vicious cycle of currency weakness, inflation and capital flight. As a result, access to foreign exchange was scarce.

Source: Fitch Ratings