

REPORT ON THE DOMINICAN ECONOMY 2010 EXECUTIVE SUMMARY

The Dominican economy grew by 7.8% in 2010, thus consolidating the recovery process within the framework of the stand-by agreement with the International Monetary Fund (IMF). This enabled the country to successfully implement countercyclical policies necessary to overcome the effects of the unfavorable international environment. During 2010, all economic activities continued to expand, including the industrial free zones that were able to reverse a contractionary trend they had been experiencing since 2005. The growth rates for the different sectors are as follows: Trade, 13.6%; Financial Intermediation and Insurance, 12.5%; Construction, 11.0%; Communications, 8.3%; Local Manufacturing, 7.7%; Transportation and Storage, 6.3%; Education, 5.9%; Agriculture, 5.5%; Energy and Water, 5.4%; Tourism and Hospitality, 4.7%; Health, 4.6%; Other Service Activities, 4.3%; Industrial Free Zones, 3.4%; Rental Housing, 3.1%; Mining, 2.9 %; Public Administration, 1.2%.

On the expenditure side, real GDP growth was sustained primarily by domestic demand, which was 9.2% higher than the previous year. Accordingly, private final consumption, gross capital formation (investment) and government consumption increased by 7.7%, 17.5% and 3.3%, respectively. Additionally, exports increased by 11.6%, while imports were higher by 14.4% over the 2009 figure.

Growth in the financial sector was led by a rise of 21.3% in multiple service banks' and other lenders' total loans to the private sector in 2010. This was achieved through monetary policy measures implemented by the authorities, resulting in a drop in the weighted average lending rate, from 17.69% in 2009 to 12.15% in 2010. This significant expansion in the channeling of resources was directed primarily to finance working capital and toward the acquisition of machinery, equipment and supplies for the construction, agriculture, local manufacturing and trade sectors.

In addition to the growth registered in 2010, which was higher than the 6.1% average for Latin America and the Caribbean according to IMF World Economic Outlook figures, inflation reached 6.24%. This is within the lower limit of the target range of 6-7.0% set in the Monetary Program. A significant proportion of the variance in the Consumer Price Index (CPI) was explained by increases in transport, fuel and electricity prices. Core inflation, which measures inflationary trends leaving out the effects of non-monetary exogenous factors, ended the year at 4.17%; this in part reflects the renewal of economic activity.

Insofar as the labor market is concerned, the expanded unemployment rate, which takes into account both the unemployed actively seeking work during the period in question (openly unemployed) and those who did not seek but would accept and are available for work (hidden unemployed), continues to decline. It stood at 14.1% in October, 2010. This is 5.6 percentage points below the 19.7% unemployment rate registered in October, 2004, following the banking crisis of 2003-2004. The open unemployment rate, as recommended by the International Labor Organization (ILO) for purposes of international comparison, was 4.5% in October 2010, down from 5.1% the previous October. This decline was reflected in an expansion in the rate of employed individuals, with a net increase of 160,208 new jobs due to the economic recovery throughout 2010.

In the external sector, preliminary figures show that the country's balance of payments closed 2010 with a surplus of US\$57.8 million. This indicates that, despite the unfavorable international environment characterized by a slower than expected global economic recovery and the increases in oil prices and key raw materials in the last months of 2010, the country received adequate resources through foreign direct investment, portfolio investment, and loans to cover the current account deficit of 8.5% of GDP. At the same time, external debt obligations were honored and there was an increase in international reserves. All this took place in an environment of exchange rate stability, which is crucial for private sector activity.

One of the most important factors bearing on the outcome of the balance of payments current account is the price of oil. In fact, fuel imports totaled US\$3.43 billion. This is higher by US\$786.5 million (29.8%) than the fuel bill for 2009 due to an increase of US\$11.30 per barrel (20.6%) in the average import price and an increase of 7.6% in imported volume.

The fiscal operations of the Central Government on an accrual basis ended 2010 with a deficit of RD\$47.29 billion, or 2.5% of GDP. This is lower than the previous year, in which the deficit equaled 3.5 % of GDP. This reflects a significant adjustment in public spending that took place in the second half of 2010. The strong fiscal contraction limited the variance from the target in the IMF standby agreement to 0.2% of GDP.

During the first three quarters of 2010, a flexible monetary policy remained in effect, which led to historically low interest rate levels, accompanied by a recovery of GDP growth and low inflation. However, in September and October there was a shift in the policy stance, as the overnight rate was increased by 0.75 and 0.25%, respectively, in those two months. The purpose of these increases was to transition to a more neutral monetary policy stance, thus avoiding significant variances from the inflation target for 2011.

Regarding the financial sector, it reflected good operational performance, supported by sustained growth in the key variables, as well as adequate levels among performance indicators, despite the continued presence of certain disruptions in international markets.