CENTRAL BANK OF THE DOMINICAN REPUBLIC

Executive Summary of the Central Bank Monetary Program 2014

(December 2013)

INTRODUCTION

Since 2012, the Central Bank of the Dominican Republic (CBDR) has been following an Inflation Targeting Framework (ITF). Accordingly, policy decisions are designed to minimize future inflation deviations from the announced targets. Within this framework, the main instrument is the monetary policy rate (MPR) also the standing facility expansion rate, which aims to influence the interbank rate and possibly other market rates in order to affect the decisions related to consumption, savings, and investment among private agents.

Under this monetary policy framework, the performance of the monetary base and of other monetary aggregates become indicative variables, rather than intermediate or control variables, as was the case under the old monetary targeting framework (MTF).

Under the ITF, the elaboration of the Monetary Program is based on a macroeconomic consistency model that takes into account the forecasts for the main variables of the monetary, fiscal, real and external sectors. These forecasts are conditioned by the implementation of monetary policy measures designed to accomplish the inflation target within the stipulated time horizon.

The Central Bank Monetary Program for 2014 is based on the provisions contained in Article 26 of the Monetary and Financial Law Number 183-02, and the Monetary Program and Monetary Policy Instruments Regulation derived from that law. Under this regulatory framework, price stability is the main objective of monetary policy in the Dominican Republic.

b. Inflation should remain within the target range during the year

The growth of the Dominican economy accelerated during the final quarters of 2013, indicating that annual growth would exceed 3.0% by year end. It is also expected that growth will accelerate further in the first semester of 2014, leading to a real GDP growth rate in the range of 4.5-5.0%. With this result, the output gap, although still negative, would narrow and is expected to close in the first half of 2016. Inflation would settle toward the lower limit of the year-on-year (y-o-y) target of 5.0% ±1.0% for year-end 2013, and for 2014 would remain within the target range of 4.5% ±1.0%.

The global economy has slowed in 2013, influenced by a moderating economic activity in the emerging economies. For the year, we expect a global GDP expansion rate of 2.4%, down from 2.7% in 2012. In 2014, we expect increased activity as a result of improved economic performance in the United States (USA) and a recovery of the Euro Area (EA).

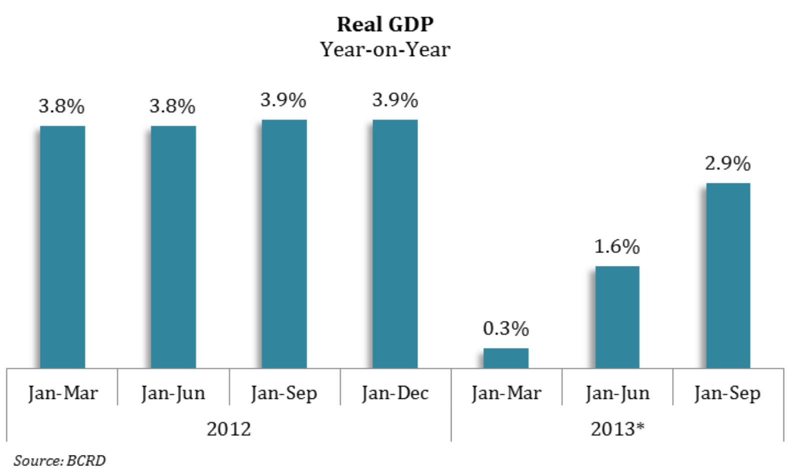
PRELIMINARY MACROECONOMIC RESULTS 2013

During 2013, there has been a rebalancing of global growth. Developed economies, led by the U.S., have experienced an improved performance, while economic activity in most emerging economies began to slow down. Indeed, annual growth reached 2.0% in the U.S. as of September, in spite of this the unemployment rate remains high -reaching 7.0% in November- and slightly higher than the Federal Reserves (FED) estimates consistent with its long-term inflation target. Meanwhile, the rate of decline in y-o-y terms of real GDP in the Euro Zone has slowed, standing at -0.4% in September. Measured on a quarterly basis, this real GDP growth was positive for the first time in Q4 2013, thus effectively ending the recession. On the other hand, in Latin America a slowdown in the pace of expansion is observed in most economies, and is especially pronounced in the case of Brazil, the largest economy in the region.

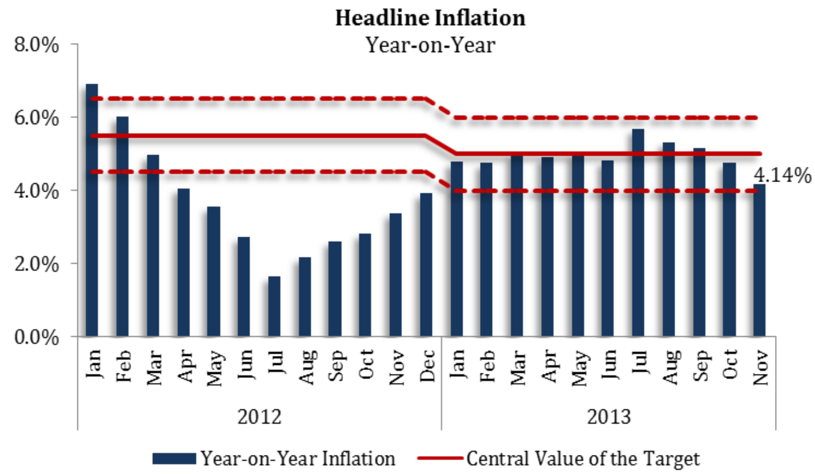
In the developed economies, inflationary pressures are under control, growth rates remain subdued, and unemployment remains high, leading their central banks to maintain expansionary policy positions. In particular, the Federal Reserve is holding its policy rate near zero and maintaining its quantitative easing program although gradually reducing it since December. Meanwhile, the European Central Bank (ECB) recently reduced its policy rate in order to counter deflationary pressures and help lessen unemployment. Latin American central banks are maintaining neutral to expansionary policy stances, with the exception of Brazil, which has adjusted its policy rate upward in the face of strong inflationary pressures notwithstanding its slow growth.

Oil prices are currently at levels similar to those observed at year-end 2012. This is largely explained by the moderate growth in worldwide economic activity. Additionally, gold prices are below US$1,300.00 per Troy ounce, due to decreased inflationary expectations and improved US economic performance expectations that led investors to liquidate their gold positions.

Locally, real GDP expanded at a rate of 2.9% in the first three quarters of 2013, showing a recovery from the levels seen earlier in the year. During the third quarter, there was a recovery in domestic demand, primarily explained by an increase in private consumption and a sustained growth in exports, particularly of gold. For year-end 2013, economic growth should be higher than the 3.0% originally projected in the Macroeconomic Framework.

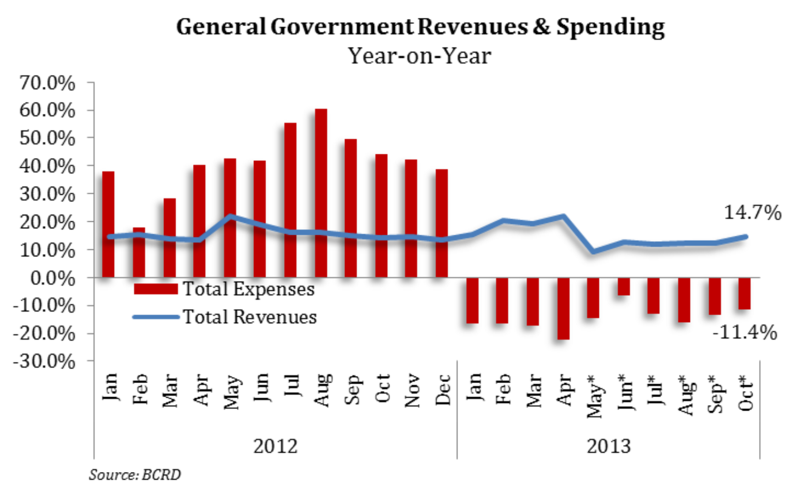


At the same time, the output gap is still negative, allowing domestic inflationary pressures to remain subdued. Internationally, oil and other commodities have not registered important price increases that would have led to major external inflationary pressures. Accordingly, inflation has stayed within the y-o-y target range of 5.0±1.0%, for the year. Similarly, core inflation has remained stable in 2013, standing at 4.5% y-o-y in November.



As of September 2013, total exports experienced a growth rate of 8.0%, driven by gold exports. Total imports decreased as a result of a moderation in consumption and domestic demand. In this regard, the current account deficit remained at US$1,853.0 million, maintaining the correction observed since earlier in the year. By year-end 2013, it is expected that the current account deficit will stand at 4.7% of GDP, an improvement over the deficit of 6.7% of GDP experienced in 2012.

Fiscal policy maintained a restrictive bias throughout the year. With the approval in late 2012 of a tax reform package aimed at increasing revenue, as well as a spending rationalization plan, it has been possible to reduce the Non-Financial Public Sector (NFPS) deficit to 1.8% of GDP as of October 2013. Thus, total revenues increased 14.7% y-o-y by October, while expenses decreased 11.4% for the same period. Recent estimates suggest that the NFPS deficit at year-end should be around 2.8% of GDP, as forecasted in the 2013 Budget.



With regard to the monetary sector, in February 2013 the CBDR modified the operation of monetary policy by introducing a new interest rate band defined around the Monetary Policy Rate (MPR). Under this new approach, the CBDR undertakes daily interventions by means of auctions of overnight CBDR Bills and/or Repos, with interest rates equivalent to MPR±200 basis points. This modification did not involve a change in the stance of monetary policy, as the MPR remained unchanged at 5.0% per annum during the January-April 2013 period.

During the first quarter, economic activity evolved slowly, due to the impact of the fiscal adjustment measures keeping inflation under control. Also, due to the impact of the fiscal adjustment, economic activity evolved slowly during the first quarter keeping inflation under control. This allowed for the adoption of a set of measures designed to stimulate credit to the private sector and aggregate demand. In May, the CBRD lowered the MPR 75 basis points (to 4.25% annually), while the legal reserve requirement ratio on local currency deposits was reduced for multiple service (commercial) banks (from 15.6% to 12.3%) and for savings and loan associations, savings banks and credit cooperatives and credit corporations (from 11.1% to 8.1%). These measures freed up approximately RD$20,000.0 million for productive sectors, home mortgage, and consumer lending.

As a result, between May and August 2013 interest rates declined gradually, while about RD$15,000.0 million of the former legal reserve funds (75.0% of the approved total) were disbursed. Between May and August 2013 about RD$15,000.0 million of the former legal reserve funds (75.0% of the approved total) were disbursed, leading to a gradual decline in interest rates. This had a spillover effect on lending to other sectors, further increasing private credit. Indeed, local currency lending to the private sector grew by 15.4% y-o-y in August 2013, and had increased by RD$29,664.3 million since month-end April 2013.

The improvement in credit growth – and the increase in public spending in May and June – led to a recovery in economic activity, which registered growth of 2.8% in the second quarter, supported by increases in private consumption and metals exports.

However, international conditions became less favorable to the Dominican economy after the U.S. Federal Reserve (FED) Chairman announced the possibility of reductions in the securities purchase program. As a result, a gradual process of capital outflows from emerging economies began, leading to faster currency depreciation in those countries. At the same time, growth forecasts for both the U.S. economy and Latin American were consistently revised downward, while international commodity prices showed an upward bias, especially oil prices. This implied additional risks for the external sector of the Dominican economy.

In the domestic environment, foreign direct investment and national exports excluding gold recorded significant declines from the levels seen in 2012, which caused a reduction in the supply of currency in the foreign exchange market. Additionally, foreign exchange-generating activities, such as remittances and tourism revenues, although positive showed a moderation in growth during the first six months of 2013.

The combination of these international and domestic factors had an impact on the depreciation of the peso beyond that foreseen in the Macroeconomic Framework. Also, expectations of further depreciation and increasing dollarization of savings led to greater volatility in the exchange rate.

Considering that periods of high exchange rate volatility represent a risk for the accomplishment of the inflation target, the CBDR announced a set of measures aimed at reducing excess volatility in this variable. In August, the CBDR increased the MPR by 200 basis points, from 4.25% to 6.25%, and the interest rate band was narrowed by 50 basis points, to MPR ±150 basis points.

The nominal and real market interest rates increased in accordance with the transmission mechanism of monetary policy. Indeed, the weighted average nominal lending interest rate reached 14.96% annually as of December 20th, while the weighted average nominal deposit rate stood at 6.87% per annum in the same period, equivalent to increases of 206 and 238 basis points, respectively, since year-end 2012. In real terms, the deposit rate attained a positive level – for the first time since May 2013 –, encouraging savings in local currency and acting as a disincentive to the dollarization of deposits that had been observed in recent months.

Nonetheless, loans to the private sector in domestic currency maintained their dynamism due to a higher demand for credit. In fact, local currency loans to the private sector reached RD$478,074.2 million, representing a y-o-y growth of 13.9% in November 2013. This is an increase of RD$54,924.7 million over December 2012. In November, local currency loans to the private sector rose by RD$8,574.7 million, despite the fact that the freeing up of legal reserve funds barely reached RD$369.6 million.

INTERNATIONAL ENVIRONMENT OUTLOOK

It is expected that the rebalancing of global economic growth experienced in 2013 will continue, to the extent that there is further expansion of economic activity in developed economies and moderate growth in emerging economies. In this regard, the most recent estimates from Consensus Forecasts (CFC) indicate that the world economy will grow by 2.4% annually in 2013, and they forecast an expansion of around 3.1% annually for 2014.

It is expected that the U.S. economy will grow about 1.7% annually by year-end 2013, supported by the good performance of the private sector during the year. By 2014, the recovery process should strengthen, and the economy should grow around 2.6%.

In the Euro Area there has been an improved performance that has enabled those countries to overcome their recession after the second quarter of 2013. The rate of decline has slowed, measured on a year-on-year basis, while in quarter-on-quarter terms there have been two successive quarters of positive growth. Therefore, it is expected that by year-end the economy will show a fall off of 0.4% in cumulative terms. In 2014 growth would gather strength, since most Euro Area countries should exhibit positive growth rates except Greece, where GDP is expected to contract by 0.7%. Given the above, the Area as a whole would record a growth rate of 0.9% annually.

For 2013, growth in emerging economies has been based on the performance of developing Asia. At year-end 2013, that region is expected to register growth of 6.3%, while in 2014 it should grow around 6.5%, remaining at the forefront of growth in the emerging economies.

Latin American economies have slowed down over the course of 2013, due to lower prices of its main exports, coupled with weaknesses in domestic supply. As a consequence, the region should show cumulative growth of 2.6% for 2013. An improvement in performance is expected for 2014, although the rate of expansion would remain moderate, around 3.0% by year-end 2014.
Commodity prices in 2013 have been influenced by moderate growth in emerging economies and political instability in the Middle East and North Africa, particularly with regard to oil prices. The IMF forecasts a price of US$104.5/bbl for its oil basket for 2013. A reduction of the oil basket price is foreseen for 2014, to US$101.4/bbl.

Outlook for External Variables

Variables	2012	2013*	2014*
GDP – World Economy (Growth)	2.7%	2.4%	3.1%
Real GDP - USA (Growth)	2.8%	1.7%	2.6%
GDP - Euro Zone (Growth)	-0.6%	-0.4%	0.9%
GDP - Latin America (Growth)	2.8%	2.6%	3.0%
Oil Prices (US$/Bbl)**	105.0	104.5	101.4

**Forecasts*

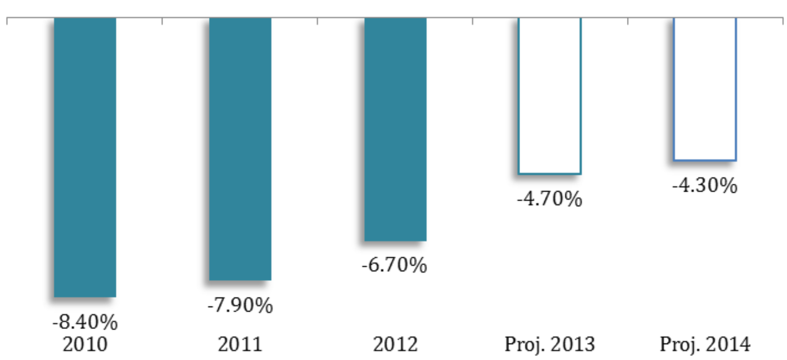
*Source: Consensus Forecast./**IMF*

MACROECONOMIC OUTLOOK FOR THE DOMINICAN REPUBLIC

The tightening of the monetary policy stance applied in August has had the expected effects, moderating the volatility of the exchange rate and increasing market interest rates in a manner consistent with the monetary policy transmission mechanism. This, coupled with the reduction of the funds available from the freeing up of legal reserves in May, would moderate the growth of private sector credit. The latest forecasts show that local currency loans to the private sector would grow at an expected rate of 12.0% - 14.0% y-o-y by the end of 2013, and should scale back to a range of 8.0% -10.0% for 2014.

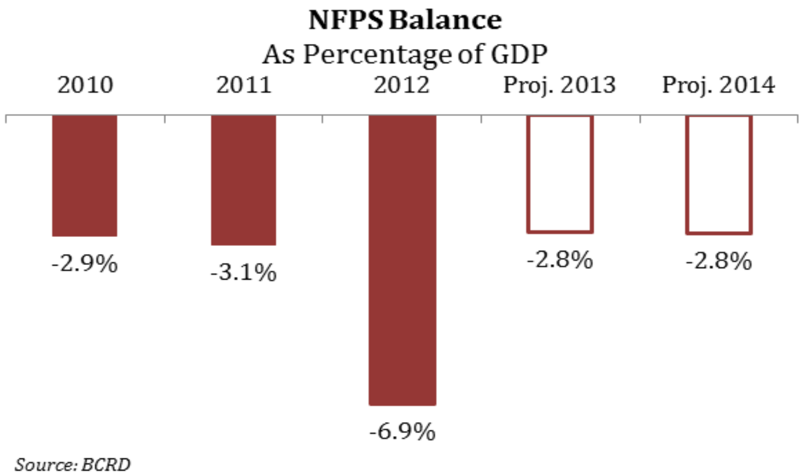
Regarding the external sector, the rise in exports together with a falloff in imports contributed to the adjustment process of the current account deficit that began in 2011. Therefore, a deficit equal to 4.7% of GDP is expected by the end of 2013. In 2014, a 7.7% growth in exports combined with a recovery of 6.0% in import growth should lead to an estimated deficit of 4.3% of GDP.

Current Account Balance
As Percentage of GDP



Source: BCRD

As concerns the fiscal sector, the approved 2014 budget foresees a y-o-y increase in revenue of 10.2% and an increase of 10.3% in expenses, which would place the Non-Financial Public Sector (NFPS) deficit at around 2.8% of GDP. Accordingly, fiscal policy would assume a neutral stance throughout 2014, prolonging the effects of the tax reform measures that were approved in 2012 and the public spending adjustments undertaken in 2013. Moreover, the forecasts suggest that the CBDR quasi-fiscal deficit would reach 1.4% of GDP in 2014. As a result, the Consolidated Public Sector balance would show a deficit of 4.2% of GDP at year-end, thus remaining at a level similar to the estimated deficit for 2013.



Economic activities have undergone an upturn as a result of the expansionary measures implemented during the first half of 2013, and it is expected that this momentum will continue through the first half of 2014. Beginning in the second half, a slowdown is expected due to the delayed effect of the MPR increase implemented in August. Thus, real GDP would grow by more than 3.0% in 2013, and should accelerate in 2014 to 4.5% - 5.0%. Despite these results, the output gap would still be negative but is expected to close in the first half of 2016.

In addition to domestic risks, growth expectations in the United States remain a source of concern. While further strengthening of U.S. economic growth is expected, lower than expected results could have repercussions on Dominican economic performance.

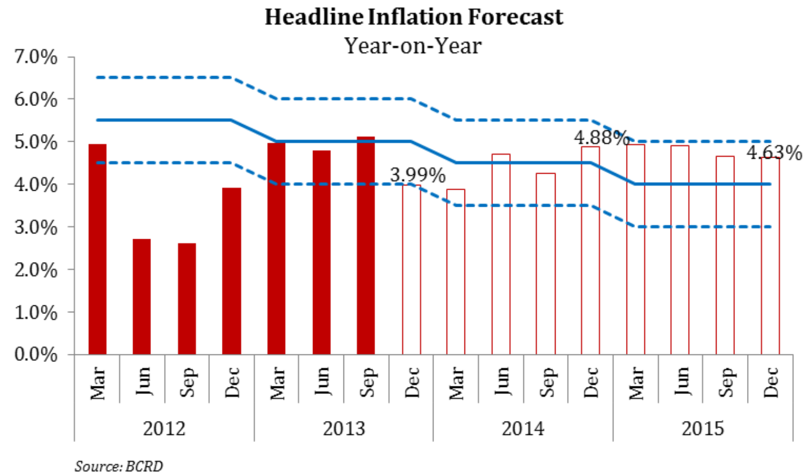
Outlook for Domestic Variables

Variables	2012	2013	2014
Real GDP (Growth)	3.9%	3.0%	4.5%-5.0%
Inflation (year-end)	3.9%	4.0%	4.5%±1.0%
Current Account (% of GDP)	-6.7%	-4.7%	-4.3%
Fiscal Balance (% of GDP)	-6.9%	-2.8%	-2.8%

Source: CBDR

INFLATION FORECAST AND EXPECTATIONS

Throughout 2013 inflation pressures have remained under control and no deviations from the target are expected in the foreseeable short term. Thus, at the end of 2013 y-o-y inflation is estimated to stand at 4.7%, near the lower limit of its 5.0% ±1.0% target.. In (For?) 2014, since the output gap would remain negative, sources of domestic pressures would still be moderate, so it is expected that inflation will stay within the target range of 4.5% ±1.0% during the year.



Regarding core inflation, its behavior has closely followed that of overall inflation. It is expected to average 4.8% at year-end 2013, and in 2014 it should stand at around 4.1%.

The balance of risk factors for the inflation forecast remains stable; thus there is no apparent bias in this variable although there are some tax increases contemplated in the Tax Reform of 2012 scheduled to become effective at the beginning of 2014. At the same time, the Government Budget includes some wage increases for specific groups. These adjustments would have a temporary effect on price levels but are expected to dissipate quickly. Despite the expected rebound in economic activity for 2014, the economy would still operate below its potential capacity, and this would ease domestic inflationary pressures. At the same time, there are risks associated with the international environment related to the gradual dismantling by the FED of its Quantitative Easing program. Nevertheless, the current outlook assumes a reduction in oil prices for next year, which, in that case, would generate less external inflationary pressures.

OUTLINE OF MONETARY POLICY: GOALS, INSTRUMENTS AND INDICATORS

Considering that the CBDR establishes its monetary policy according to an inflation targeting framework, where monetary aggregates are indicative variables, we describe below the expected path for such variables. For 2014, forecasts show that the growth of the Narrow Money Base (NMB), consistent with the inflation target of 4.5% ±1.0%, would be approximately 10.5%, which is slightly above the projected growth of nominal GDP.

Variables	2014			
	Mar.	Jun.	Sep.	Dic.
Narrow Money Base (MM of RD$)	161,579.3	166,146.0	168,740.3	184,349.8
Y-o-y Var. (%) Narrow Money Base	*-1.1%*	*1.4%*	*13.1%*	*10.5%*
Net International Reserves (MM of US$)	3,486.0	3,579.5	3,729.4	3,897.6
Y-o-y Var. Net International Reserves (MM US$)	*-14.5*	*-261.9*	*385.6*	*350.0*
Local Currency Loans to Private Sector (MM of RD$)	483,581.3	492,219.2	502,832.1	524,289.9
Y-o-y Var. (%)Local Currency Loans to Private Sector	*12.7%*	*9.9%*	*8.0%*	*8.7%*

The behavior of the NMB would be influenced by the projected US$350.0 million increase in Net International Reserves (NIR) during 2014. If this is achieved, NIR would reach US$3,897.6 million.

These forecasts contemplate revenues estimated for 2014, derived from the CBRD Recapitalization Plan, equal to 0.7% of nominal GDP. Given these revenues, as well as interest payments for open market operations and other items, the quasi-fiscal deficit would amount to 1.4% of GDP at year-end 2014.

SUMMARY MAIN MACROECONOMIC INDICATORS
2013 PRELIMINARY FIGURES - 2014 FORECAST

Below is a summary of the main macroeconomic indicators:

CENTRAL BANK OF THE DOMINICAN REPUBLIC
MONETARY PROGRAMMING AND ECONOMIC RESERARCH DEPARTMENT

MAIN MACROECONOMIC INDICATORS - MONETARY PROGRAM 2014

Variables	Forecast 2013	Forecast 2014
Real Sector:		
Real GDP Growth	3.0%	4.5%-5.0%
Inflation Rate, End of Period	4.0%	4.5% ± 1.0%
Inflation Rate, Annual Average	4.7%	4.4%
Growth of the Implicit GDP Deflactor	5.0%	4.5%
Fiscal Sector:		
Tax Burden	14.6%	14.8%
% Var. Central Government Total Revenues	20.3%	10.2%
% Var. Central Government Tax Revenues	17.6%	10.6%
% Var. Central Government Total Spending	-4.0%	10.3%
NFPS Balance as % of GDP	-2.8%	-2.8%
Quasi-Fiscal Balance as % of GDP	-1.4%	-1.4%
Consolidated Public Sector Balance as % of GDP	-4.3%	-4.2%
External Sector:		
Balance of Payments Current Account (MM of US$)	-2,812.1	-2,628.1
Balance of Payments Current Account (% of GDP)	-4.7%	-4.3%
% Var. – Total Exports	9.9%	7.7%
% Var. – Total Imports	-2.8%	6.0%
Oil Imports Bill (MM of US$)	4,587.4	4,509.2
Foreign Direct Investment (MM of US$)	2,078.6	2,152.1
Overall Balance of Payments Deficit	938.7	300.0
Monetary Sector:		
Net International Reserves (MM of US$)	3,547.6	3,897.6
% Var. – Narrow Money Base	-0.6%	10.5%
% Var. – Local Currency Loans to Private Sector	14.0%	8.7%