

PUERTO RICO

CHANGING THE GUARD

Bouncing back after the 2006 budgetary crisis, Puerto Rico's investment platform is once again attracting foreign interest at the same time as tourism and construction are on the rise

Nearly two years after a budget crisis shut down schools and government agencies across Puerto Rico, business and fiscal leaders are brimming with confidence and have no doubt that economic order is being restored.

The 2006 crisis, brought on by disputes between the island's main opposing political parties, set off a two-week closure of nearly all government services. The debacle cast negative global attention on Puerto Rico, causing stock values to plummet and triggering poor credit ratings for banking institutions.

Fiscal policy leaders, with help from the private sector, have been able to retool the banking sector, reduce debt and offer incentives to bring investors back to the Commonwealth. This sense of poise is bolstered by Puerto Rico's tax exemptions for banking transactions, a highly educated workforce and the convenience of access to the United States without a passport, leaders say.

"You can carry out almost any kind of business transaction without worrying about taxes," Commissioner of Financial Institutions Alfredo Padilla says of banking transactions. "It is a mutually beneficial arrangement for the country and the international banks."

The restructuring of debt at a major Puerto Rican bank is an encouraging example of fiscal change. Doral Financial Corporation, the island's seventh-largest bank based on deposits, faced insolvency in 2005 and hired investment bank Bear Stearns to recapitalize its assets. Bear Stearns found investors to pump new life into the bank, eventually acquiring 90 percent of the company so it could service its debt.

Doral ultimately sold 95 percent of its shares to offshore interests. "To have a debt of \$625 million and be able to convince foreign entities to take that risk and make a substantial investment in the institution says a lot about the faith people have in their organization and the market or country that they are in," Mr Padilla says.

Boosting tourism in Puerto Rico is another objective. While neighboring Caribbean islands depend largely on tourism, the sector accounts for only 7 percent of



Alfredo Padilla
Commissioner for
Financial
Institutions



Rick Newman
President of Puerto
Rico Hotel and
Tourism Association
/ Holiday Inn

Puerto Rico's gross domestic product. And as business travelers make up 40 percent of the total, tourism advocates are adapting their message to draw more leisure visitors.

Puerto Rico has historically been a top destination for tourists of Puerto Rican heritage living in New York and other East Coast cities. Rick Newman, chairman of the board of directors of the Puerto Rico Hotel and Tourism Association, says it's time to cast a wider net.

"As you move inland, going West, we are not that strong, so we need to continue building on that," Mr Newman says. "We also have to look at Latin America and Europe as potential growth opportunities."

Mr Newman is the general manager of the Holiday Inn San Juan. The hotel was built in the 1960s, closed after three decades and was reopened with a new look in 2004, reflecting traditional Puerto Rican and contemporary décor. Corporate guests make up 60 percent of weekday guests. The hotel is located near the airport and has easy beach access.

Across the island, hoteliers aim to build 5,000 additional rooms a year for the next four years. "We have proven that we can create the demand to absorb the rooms," Mr Newman says. "What we need to do right now is to continue building rooms and filling them."

Mr Newman emphasizes the ease with which mainland U.S. visitors can access the island. No passport is needed to visit, and goods can be transferred with ease across borders.

President of the Puerto Rican Chamber of Commerce, Bartolomé Gamundi, highlights the diverse opportunities for both investors and tourists.

"For investors, we offer a number of opportunities in terms of tourism, medical devices, biotechnology, electronics, textiles, and real estate," Mr Gamundi says. "For visitors, it is a perfect destination that offers a picturesque landscape, a lot of beaches, activities, attractions and entertainment." ■

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PUERTO RICO

PUERTO RICAN PUBLIC SECTOR ADOPTS REFINANCING TECHNIQUES

Sectoral performance has exceeded analysts' expectations and rebuilt investor confidence in the Commonwealth

Affecting change in any government's public fiscal policies requires tenacity and a good case. The latter is often the most difficult to provide. Officials want sure bets that will not jeopardize political standing, employment, and the economy. Recently, the Puerto Rican government launched a series of initiatives, based on major successes in the private sector, that have significantly reduced the country's outstanding debt. Officials believe improvements in public finances will stimulate growth in the economy and help encourage investment in the Commonwealth.

For hard proof that refinancing large debts was feasible and could save a significant amount of money, officials turned to a major Puerto Rican institution. Doral Financial, the island's seventh-largest bank in terms of deposits and its largest mortgage servicer was a prime example. The institution, teetering on the edge of insolvency in 2005, hired an external firm, Bear Stearns, for advice on how to recapitalize. Bear Stearns found a diverse group of investors willing to put up the capital Doral needed to get back on its feet.



Glen Wakeman
Chief Executive
Officer, Doral
Financial Group

Convincing the various investors required shrewd planning by Doral executives and an overhaul of procedure. "Our plan was to take serious senior executives with multimarket global experience and bring them to Puerto Rico with the objective of imparting their knowledge to an already great workforce, in turn increasing both their performance and marketability," recounted Glen Wakeman, C.E.O. of Doral Financial.

Mr. Wakeman's strategy paid off. An investment group led by Bear Stearns Merchant Banking agreed to acquire 90 percent of the company and to provide the capital Doral needed to pay off a large debt that was approaching maturity. Since then, share prices are up and the bank has received an upgraded ranking. "It is a tremendous vote of confidence in Puerto Rico," Mr. Wakeman went on to say.



Doral's revival has restored investor confidence in Puerto Rico

The Puerto Rican government took note of the success and adopted similar strategies. In July 2006 a group of experts was approached to form the Puerto Rico Sales Tax Financing Corporation (COFINA, by its Spanish acronym) and given the authority to issue bonds and use other financing mechanisms to pay off existing longstanding extraconstitutional debt.

The newly formed group has already saved the government significant money. With the help of COFINA, the Puerto Rico Public Buildings Authority placed \$900 million into a new set of bonds, the proceeds of which will be used to refinance \$573 million in debt at lower rates and will generate over \$300 million in new money to continue implementing its capital improvements program.

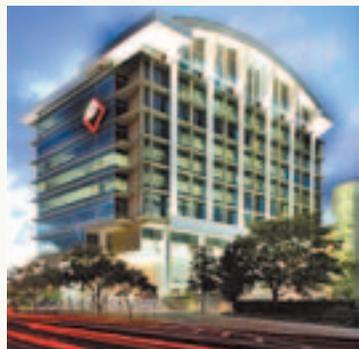
The news has caused optimism among officials regarding Puerto Rico's future. According to the governor, the bond issues "have been classified by the credit rating agencies as a milestone in the history of our fiscal and economic development. They received the highest credit rating in the last 30 years, serving as an indicator that our economic course is back on track." ■

"PUERTO RICO BONDS RECEIVED THE HIGHEST CREDIT RATING IN 30 YEARS, SERVING AS AN INDICATOR THAT OUR ECONOMIC COURSE IS BACK ON TRACK"

BEAR STEARNS BUYOUT AND FITCH UPGRADE REVIVE PUERTO RICAN INSTITUTION

The ratings company has raised Doral Financial Corporation's status to stable, easing concerns and restoring investor and shareholder confidence

Fall can be an uneasy season for Puerto Ricans. The threat of hurricanes still lingers and most residents keep a cautious eye on weather reports. In November 2006, shareholders of the island's largest residential mortgage company, Doral Financial, found themselves fearing not only warnings of high winds and heavy rains but an even more alarming report, one detailing its company's annual performance. The eventual outcome was not good: significant losses and a plummeting



Fitch's upgrade of Doral's rating has seen share prices jump from \$12.60 to \$20

share price. Company executives blamed the slowdown on the island's economy and reduced returns on mortgage sales. The news could not have come at a worse time. With signifi-

cant outstanding debt scheduled to mature the following year, shareholders and executives at Doral agreed they needed to act fast.

Doral executives sounded out potential partners and Bear Stearns Merchant Banking responded. The bank assembled a group of hedge funds and private equity firms, including Goldman Sachs Inc., Marathon Asset Management, and Perry Capital, and orchestrated a deal that gave investors a 90 percent stake in the company, who bought shares at 63 cents apiece, while keeping them free from regulation by the Federal Reserve. The fresh capital allowed Doral to immediately pay off \$625 million it owed in outstanding debts, settle a class action lawsuit, and ease any immediate liquidity pressure.

The deal did not go unseen. The highly influential Fitch Ratings announced it had upgraded Doral Financial's rating, based on the equity sale and payment of the impending debt maturity, and had given a particularly positive rating to the company's long-term issuer default rating and its long-term deposits rating. Since the deal, the company has regained its foothold in the island's mortgage market, driven its share price up to around \$20, and diversified the financial services it offers. Furthermore, the company has avoided the American sub-prime crisis because as Glen Wakeman, C.E.O. said, "Puerto Rico is a long-term 15- to 30-year, fixed rate market." Mr. Wakeman and investors are convinced they have ridden out the worst of the storm.

PONCE IS CHANGING...

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and see it for yourself?*

Puerto Rico's second city, Ponce, is not only a beautiful colonial town, but it's also extremely business-oriented.

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PUERTO RICO

THE FIRST PORT OF CALL FOR INGENUITY

Situated on Puerto Rico's central west coast, Mayagüez holds an historically significant past and is mapping out equally big plans for the future.

As the island's third busiest shipping destination after San Juan and Ponce, Mayagüez has embarked on a massive redevelopment of its port to bring more tourists and cargo to western Puerto Rico. Government and business leaders hope to return Mayagüez to its former splendor and brand the city as the "New Cruise Port" of Puerto Rico.

The city was established in 1760 by Spanish explorers from the Canary Islands. Mayagüez was a pioneer in rum production and became an important scientific center with the founding of the University of Puerto Rico-Mayagüez, a leading engineering institution.

Mayagüez gained industrial importance in the 1960s with major tuna canning and textile operations, employing thousands of workers. But as both industries cut jobs during the 1990s, leaders sought to supplant losses by focusing on shipping.

The Holland Group, a Puerto Rico-based development company comprised of Dutch and US interests, holds a 60-year-concession to redevelop the Mayagüez port. The group also plans to develop nearby industrial land to be able to handle more cargo.

Developers want to create better links between the island's seaports and air-



The campus of engineering at the University of Puerto Rico-Mayagüez is a production line for skilled graduates, many of whom go on to work at NASA

ports. Mayor of Mayagüez José Guillermo Rodríguez says work is underway on new air connections to Aguadilla in the north, and plans to lobby for a freeway between Mayagüez and Ponce, the island's second largest city.

Business leaders also point out that the city produces some of the best-prepared college graduates in Puerto Rico. The University of Puerto Rico-Mayagüez ranks first in producing Latin American engineers in the United States, sending many of its graduates to jobs at NASA.

Mayagüez, which will host the 21st Central American and Caribbean Games in 2010, is one of the cities that make up the Porta del Sol, or "Doorway to the Sun." The brand is an effort by municipalities in the region to promote tourism by taking advantage of the area's sea-side, cultural and artistic offerings.

The Porta del Sol region begins with the Atlantic beaches of Isabela in the north and continues through Mayagüez. The dry coastal forest found in Guánica, the area with the richest bird population on the island, lies along the Caribbean.

Surfers and windsurfers favor the northwest coast near Isabela because of the strong trade winds present in the tropics. There are eight scuba diving spots in the region with an average water temperature of 81 degrees Fahrenheit and 75 feet of visibility.

The Porta del Sol also offers a gastronomy circuit of 13 restaurants reflecting the island's Taino Indian, Spanish and African influences. ■

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PUERTO RICO

DEEP DEVOTION TO PONCE'S MARITIME EXPANSION

\$700 million Port of the Americas project aims to deepen access points to allow passage for Panamax class vessels



Francisco Zayas Seijo
Mayor of Ponce

A massive expansion of the Port of Ponce is destined to turn the dockyard into Puerto Rico's busiest maritime thoroughfare and catapult the island's second-largest city to international shipping prominence, municipal and state leaders say.

When completed, the Port of the Americas project will allow for storage of 1.4 million 20-foot containers, according to the Port of the Americas Authority, which is overseeing the work.

Mayor Francisco Zayas, a key backer of the estimated \$700 million project, says work is on schedule to be completed by 2009, and predicts that the port could eventually dwarf the cargo handling capacity of San Juan, currently the Commonwealth's chief sea access point.

"The main advantage that Ponce can offer is the port," Mr Zayas says. "We are confident that in a few years' time Ponce is going to be the most important port in Puerto Rico in terms of cargo."

Work on the Port of the Americas began in 2005 with the construction of a 1,200-foot quay. Dredging followed, allowing ships with a depth of up to 50 feet (15.24 meters) to access the port, making it the deepest harbour in the Caribbean region.

This depth alone gives Ponce an advantage over San Juan, which can only permit ships of up to 36 feet in depth, Mr Zayas says. With the San Juan region expected to grow, "sooner or later they had to start moving the cargo somewhere else."

Puerto Rico had not been able to accept such large ships because of the relatively shallow depths of its entry channels. The expansion allows ships meeting Panama Canal size specifications to enter the Port of the Americas.

Puerto Rico's chief exports include electronics, apparel, rum, beverage concentrates and medical equipment. Mr Zayas says a modern port facility with adequate storage space is essential for attracting business: "Easy access to a port facility would be in their best interest." ■

'WE ARE CONFIDENT THAT IN A FEW YEARS' TIME PONCE IS GOING TO BE THE MOST IMPORTANT PORT IN PUERTO RICO IN TERMS OF CARGO'

A CARNIVAL OF UNIQUE CURIOSITY

Puerto Rico's oldest carnival turned 150 years old this winter as the City of Ponce celebrated a week of revelry led by masked "vejigantes."

These colorful demons roamed Ponce's streets – clad in elaborate costumes – to terrorize children with their spiky horns, striking them with dried cow bladders. The term "vejigante" is derived from the Spanish for bladder, vejiga.

The weeklong celebration started Jan. 30 with a dance in front of City Hall. Sunday's main parade was followed by the annual burial of the sardine – coinciding with another big parade – which brought the party to a close (until next year) on Tuesday, Feb. 5.



The Pearl of the South: Ponce's colorful history and vibrant present combine to great effect to form a beautiful, fascinating and welcoming city

COURTING THE DIASPORA BY RETURNING TO THE ROOTS OF PONCE

Juan Ponce de León's city is embarking on a conquest of its own - the 'Porta Caribe' promotional drive

Civic leaders in Ponce, the city regarded by Puerto Ricans as the "Pearl of the South," are waging a tenacious battle to revamp the colonial gem into an economic hub to rival the capital, San Juan.

Ponce's mayor, tourism officials and business leaders are leveraging colonial charm in a drive to lure investment to this city of 190,000.

An airport expansion in 2005 yielded a fivefold jump in passenger traffic. U.S. residents of Puerto Rican descent are actively being courted to return to the island – as tourists – and spend dollars in the region. Plans for a convention center to anchor a convention district would generate hundreds of jobs, says Mayor Francisco Zayas.

"This powerful investment will help us improve quality of life in an economically distressed area," Mr Zayas said during the announcement of the \$21 million funding package.

Ponce was founded in 1692 by the great-grandson of Spanish conquistador Juan Ponce de León. It is the second-largest city in Puerto Rico after San Juan and lies three miles from the island's south-central coast. The historic center is dotted with colonial-era buildings and the renowned Ponce Museum of Art, the leading fine arts museum in the Caribbean.

Both government and private partnerships have been forged to improve infrastructure, draw investment and entice tourists to visit the region.

The U.S. Department of Housing and Urban Development approved the fund-

ing to develop the convention center, which will house 92,000 square feet of convention space, at least two hotels and sufficient room for 3,000 exhibitors and attendees.

The expansion of Merceditas Airport has already opened additional connections to U.S. mainland cities, with Jet Blue and Spirit Airlines adding services to New York and Fort Lauderdale, Fla., respectively.

Ponce has joined forces with 14 surrounding municipalities to create the brand "Porta Caribe" to promote the region. Mr Zayas, jubilant after a recent New York trip to champion the Ponce region, says there exists an emotional element to the sales pitch.

Many visitors of Puerto Rican descent have been living in the United States for three generations, he says: "They want to go back to their roots, and Ponce resembles the old Puerto Rico – its ambience, the towns around Ponce, and the pace of living."

Efforts are also underway to take advantage of vacant properties in the city center, transforming the units into housing for limited-income buyers. Historically, these residents have been concentrated in poorer quarters along the city's edge.

"This had a negative effect on Ponce because its most important resource, its people, lived outside of Ponce," Mr Zayas explains.

An additional \$2.9 million project calls for a total of 238 homes to be built and rehabilitated along the waterfront, the mayor concludes.



PUERTO RICO



THE INGENIOUS DON Q GETS MINDS AND GILLS TILTING

Fueling the US market will be an easier task with an instantly recognizable brand and growing consumer interest



Puerto Rican rum producer Serrallés is betting that Don Q – the signature beverage bearing the name of Cervantes' legendary knight-errant – will boost its market share in the United States and beyond.

Mainland U.S. sales of Don Q rum have doubled in the United States in the past year, says Executive Vice President and Secretary of Destilería Serrallés, Inc. Alberto J. Torruella Serrallos. The company is targeting key U.S. cities for promotional rum tastings and making special efforts

to reach customers of Puerto Rican heritage.

The Ponce-based company has taken top honors at recent rum-tasting contests in San Francisco and Brussels, Belgium, and was lauded in Barcelona, Spain, for its production methods. Serrallés has also expanded into tourism, purchasing the Hilton Ponce in 2000 with plans to develop the property into a resort. "We hope to be able to bring in a substantial amount of tourists from the U.S.," Mr Torruella says.

Serrallés has been in the sugar business since the 1840s and has been making rum since 1865. Rum consumption increased more than any other spirit in the United States between 2005 and 2006, growing by 23 percent, according to the 2006 Adams report. ■

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TALKING A GOOD GAME

Increased competition and a range of gimmick-free services attract record numbers of subscribers

Ambitious new players are entering the fiercely competitive telecommunications market in Puerto Rico as wireless telephone operators vie for customers in an increasingly crowded sector.

Cell phone use in the Commonwealth has spiked 60 percent since 2000, according to the Telecommunications Regulatory Board of Puerto Rico. Prepaid service plans and handsets with video capabilities are among the most sought-after features for the island's estimated 1.9 million customers.

Open Mobile, which replaced the former Spanish-American operator Movistar, launched prepaid services in June 2007. Open Mobile led a \$40 million overhaul of the beleaguered Movistar network and has promoted a range of ready-to-use phones. There are no credit checks or cancellation fees, says Open Mobile's General Manager, Frank Bell.

"Because of that, we do not need a gimmick of giving away free phones and then tying someone to a contract for two years," Mr Bell says of some long-term agreements.

Open Mobile's basic service starts at \$35 per month. The company beams text messages to users as the current period ends, inquiring whether the user wants to renew service. "We are very simple to do business with," Mr Bell asserts.

The company surpassed its sales goals by 30 percent during its first two months of operation. Open Mobile is currently the Commonwealth's smallest operator, but aims to open enough stores to be within reach of 95 percent of the population, Mr Bell says.

American giant AT&T, formerly known as Cingular Wireless, is the biggest player in the industry with 30 percent of Puerto Rico's cell phone subscribers. AT&T was the first operator to offer mobile video technology on the island, says Vice President and General Manager of AT&T Puerto Rico José Juan Dávila.

"Real estate, insurance, construction – any industry where you would need to simultaneously talk and see something in real time has great use for this technology," Mr Dávila says of the latest video capabilities.

AT&T offers Smart Links, a service allowing parents to control their children's talk time, text messaging and mobile Internet access. Users can also access content from El Nuevo Día newspaper on their handsets. Pricing plans start at around \$10 for 60 minutes of airtime.

The head of the Telecommunications Regulatory Board of Puerto Rico says bridging the telecommunications gap with the United States mainland in a rapidly changing sector is the group's key challenge.

"The high level of competition and public policy are reducing that gap," says Miguel Reyes Dávila, the board's president. "These developments promise the emergence of even more telecommunications services to the community, and what is even more important – active competition." ■



José Juan Dávila
Vice President and
General Manager
of AT&T
Puerto Rico



Frank Bell
General Manager
of Open Mobile

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