

Euromoney Conference Panama

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Good morning,

Your Excellency, Martín Torrijos Espino, President of the Republic of Panama. Ladies and gentlemen.

I appreciate the opportunity to speak at this conference and thank the organisers. Today I wish to share with you HSBC's views on the strategic importance of Latin America for the Group, particularly Panama, as well as our vision for the region in the coming years.

At HSBC we know the region well. We have had a presence in Latin America since the 1950s, through various representative offices. In recent years the Group has made important investments and acquisitions in Argentina, Brazil, Mexico and Panama, among other countries. In Panama we have had operations since 1972 and in Mexico since 1971. Today, HSBC is the fifth largest commercial bank in Panama and we are one of the leading financial groups in Mexico, Brazil and Argentina.

This presence is strengthened by our recent agreement to acquire Banistmo, the leading financial group in Central America, which offers us an excellent opportunity to expand our presence in the region, including Colombia, and provides us with a strong platform for growth.

Among the main opportunities that these markets offer, is the high degree of political and economic stability that has evolved in the last 10 years due, to a great extent, to the favourable macroeconomic policies that have been implemented in these countries which have led to sustainable economic growth.

Lets look at the region. In Colombia, the economic indicators are very favourable; growth perspectives are optimistic, and consumption and private investment continue to grow robustly. The economy grew at a rate of 5.23 per cent in annual terms during the first quarter of the year. economic activity in Costa Rica continues being strong and it does not seem to be affected by the uncertainty that surrounds its entrance to the CAFTA. For the first half of the year, the economic activity in El Salvador gave very positive signs and the central bank estimates that GDP growth in 2006 will be 3.5 per cent. In Honduras, the economy continues to experience healthy growth, and some economists estimate that Panama's GDP could grow one percentage point faster, if the extension of the Canal is approved.

These growth factors reflect HSBC's belief that in the coming decades, a majority of the world's growth opportunities will originate in rapidly developing emerging markets.

This view is based on trends that are now very clear. As populations age in developed countries, especially in Europe and Japan, the economic growth of those economies will slow. Therefore, investors in those countries will look for better returns in fast growth, emerging markets where young populations will demand more goods and services as their purchasing power increases.

Among these emerging economies are Brazil, China, India, and Mexico, as well as other economies in Asia, Latin America, and Central America. In this group, it will be of great importance for nations to remain competitive in a globalised world; to continue with stable macroeconomic policies, healthy public finances and the processes of deregulation where required, as well as to encourage competition in domestic markets. It will also be essential to invest in areas such as education and technology, which contribute to the human and intellectual capital of a country and which are fundamental for the development of any nation.

Equally, each country will have to take advantage and exploit their competitive advantages. Without a doubt, Panama possesses important differentiators; its strategic geographic location, and being at a nexus of strong international trade flows, namely China, USA and Latin America.

I was reminded yesterday of Panama's geographic importance by Joseph Salterio, CEO HSBC Bank (Panama) S.A., who told me the fact that William Patterson, the founder of the Bank of England, embarked in setting a major Financial and Commercial Centre in Punta Escocia in Darién, Panamá in 1698. This ended in disaster, 'mainly due to poor planning' and whose negative repercussions eventually resulted in the Scots joined up with the English in the Union of the Crown in 1707. This is an example of how working together and consulting local knowledge is better than working alone. For HSBC, working closely with the local expertise in the region is important. Being able to successfully connect the parts and linking up of the region as a whole makes HSBC 'The world's local bank.'

Central America and Colombia is a market with 83 million people, in which a great part of the population does not use banking services. The population is just starting to benefit from economic growth, stability and lower inflation, which translates to an increase in living standards. Growing family incomes in many of these countries will create viable new customers for the banking system, increasing the demand for more competitive financial products and services. This will benefit consumption and the development of manufacturing sectors, as many young people will seek to acquire goods, automobiles and homes. And banks will provide the financing.

Unfortunately, not all emerging economies will benefit from this trend to the same extent, but those that do will see the economies and the living standards of their populations transformed.

There is no doubt that investment, economic growth and stability are important catalysts that help improve family's income, as well as reduce poverty. Two examples come to mind, which I wish to share with you:

Let us take the case of Chile, where the country has registered spectacular growth since 1990, as a result of favourable macroeconomic policies, deregulation, trade liberalization and attractive rules for foreign investment. This has led to robust development of many sectors of the economy, and has led to a strong increase in the living standards of most Chileans. Furthermore, Chile has a strong and competitive financial services market where foreign and local banks compete, where people have access to mortgages and credit at very accessible costs, and where inflation is under control.

The second example is China, which has had an annual GDP growth of 9 percent or more since 1980. This growth has reduced China's poverty to an extraordinary degree. According to the United Nations, the proportion of the Chinese population that lived in absolute poverty decreased from 25 percent in 1979 to 2 percent today. That is quite outstanding and has created a growing middle-class and led to an increase in internal consumption and financial services. The size of China's financial sector, in which we participate actively as the main foreign investor, is enormous and presents great opportunities for banking.

In my opinion, there are two more examples that are very relevant to Panama. Throughout my career at HSBC, I have witnessed several emerging economies that have managed to establish themselves as important commercial centres in their region as well as examples of how strong and sustained economic development can be achieved.

When I worked in Dubai, in the mid seventies, the streets of the city were not even paved. There were few hotels and only one airport which was really just a stop over and refuelling point. Today Dubai has come a long way, and is now a free port with a very dynamic and fast

growing economy, mainly in the sectors of port services, transport, tourism and trade, with one of the most advanced airports in the world and with one of the world's most highly recommended airlines 'Emirates'. It also has a developed and very active banking sector. Let there be no doubt, Dubai is now one of the main business centres of the Middle East, if not the principal one.

Moreover, when I worked in Asia I visited Singapore on many occasions. I witnessed how free trade, the simplification of the legal and tax systems, combined with strong investment, especially in education and technology, as well as in the telecommunications, ports and financial services sectors helped transform Singapore into a developed economy and important corporate and commercial centre.

And it is not by chance that some people consider Panama as "the Singapore of the Americas." These two countries, although distant, share much in common. Mainly, these countries have taken advantage of very unique historical circumstances and, through the implementation of intelligent policies with a long term perspective, have managed to exploit their geographic advantages to generate the right conditions for accelerated economic development and a high degree of sustainable prosperity.

During the past decade, Panama has attracted foreign investment that helped to generate a modern and dynamic economy. This process began in the mid 90s, when the Panamanian government initiated a process of privatization of public companies, including utilities, and transportation, aiming to generate greater efficiency in their management.

The reversion of the Panama Canal and all its land on December 31, 1999, opened the way for new international investment in Ports, Railroad, Telecommunications, and real estate. The present site of Playa Bonita where this conference is being held is a vivid example of the utilization of areas previously unused. The Panamanian administration of the Canal has demonstrated itself to be very efficient and profitable in running the operation for the benefit of the country and its citizens.

Also, the passage of the Banking Law in 1972 which was modified in 1999 has allowed Panama to become a Regional Financial Centre mainly catering to the Andean, Central America and Caribbean nations. As a result of this, a number of major Central American financial companies have set up operations to cater to the regional market.

As a result of the increase in foreign investment, through liberalisation, the industrial sectors that have most benefited have been power generation and distribution; telecommunications, including mobile and fixed lines; seaports on both sides of the Canal; shipyards, Call centres, tourism, the construction of

shopping centres, and the growth of service operations such as aircraft maintenance, tourism and of course, a regional high quality airline, COPA, very much like Emirates or Singapore Airlines but serving the region.

In terms of trade, Panama has enjoyed important growth due to the businesses originating in the Colon Free Trade Zone and the expansion of its ports. Today, the country has world class operators, among them, Hutchinson Whampoa, under the name of Panama Ports Company, Grupo Evergreen, as well as Stevedoring Services of America, that have turned it into the largest port region of Latin America.

In the tourism sector, Panama is growing at a rate of 12% per year and furthermore, this country has been identified as one of the five best places to retire for foreigners, mainly from the United States, Canada and Spain, who are arriving to live in the country and to enjoy the advantages of a dollar based economy with an inflation rate that has remained below 2% annually on average for the past 35 to 40 years.

In addition, one of the most important events for the development of this country may be about to happen namely the expansion of the Panama Canal. It is estimated that the project will cost between five to six billion dollars and will take 10 to 12 years to be completed, and will contribute significantly to economic growth in the country in the years to come and build on the success that the Panamanian people have had in managing an asset of such global importance.

Let me say a little more about the impact this might have on the economy. So far the Canal contributions have improved the Treasury's accounts. Direct contributions during the fiscal year 2005 reached almost 490 million US dollars, representing around 60 per cent of the total budget for public investment. For 2006, Canal contributions are expected to surpass 500 million dollars. With the third set of locks, Canal net income will grow up to 4.3 billion in 2025, equivalent to an average annual growth of over 11.6 percent. In 2025, the expanded Canal will be able to generate total contributions of up to 4.2 billion to the National Treasury, which will consist of 670 million in net tonnage fees and public services fees, and up to 3.5 billion in surplus after reserves for investments are made. In cumulative terms, during the first 11 years of operation of the third set of locks, the expanded Canal will be able to generate contributions to the National Treasury of 8.5 billion more than it would if it were not expanded, an amount which, by itself, exceeds the amount that will be invested on the third set of locks.

The benefits of the Canal expansion will not only come from direct income generated by the waterway, but also from the entire conglomerate's economic activity level. It is estimated that the Canal expansion will allow the Canal economic system exports to be tripled by the year 2025. Additionally, the Canal expansion will stimulate a 40 per cent increase in the rest of the conglomerate's

investments, which will rise to 1.1 billion per year by 2025.

The Canal expansion will allow Panama to attain a gross domestic product of 31.7 billion by 2025 in 2005 dollars. This represents almost 2.5 times the gross domestic product of the country in 2005, and equals an average annual growth rate of over 5 percent for the next 20 years. However, other estimates project that GDP would grow between 1 and 1.2 percentage points faster with the expansion, which means that by 2025 Panama's GDP would have expanded an additional 22 percent. Also, exports of services directly and indirectly associated with the Canal and its expansion would triple by 2025.

The Canal expansion's impact on employment will first be observed in the jobs directly generated by the economic boom that will be experienced during the years of the construction. The project would create 44,500 more direct and indirect jobs by 2010, 61,000 by 2015, and 88,700 by 2020. These include 6,500 and 7,000 additional jobs that will be directly related to the works during the construction's peak years. Finally, the unemployment rate would be 5 percent by 2025 down from 9.6 per cent in 2005.

What if the expansion is rejected? Canal officials argue that, if the expansion is rejected, more global transportation would shift to alternative routes, such as the Suez Canal and by land across the United States, leaving Panama uncompetitive and robbing it of future volume growth. The Canal is already reaching its full capacity, and there are important risks of losing market share in expanding global trade, especially of Chinese manufactured exports bound for the United States. In fact, failure to approve Canal expansion now, could delay a new referendum by as long as three years or indefinitely, and deliver a serious hit to the economy. Real growth from 2007-2009 could in that case average less than 4 per cent per year, and could deepen even further after 2010.

These facts look to me like very compelling reasons that support the expansion for project. It will be necessary for Panama to remain competitive and to enhance an earning asset for the benefit of future generations of Panamanians.

Nevertheless, the decision on this expansion rightfully will be made by the citizens of Panama and their representatives. Whatever the outcome of the referendum, HSBC is here for the long term. We have confidence in the economy of the country and we have optimistic expectations for its future.

In HSBC's view, Panama is taking firm steps to become the Singapore of the Americas and, in addition to the extension of the Canal; we see numerous opportunities on the horizon that must be taken advantage of, to create even more development opportunities for the nation;

First, the Free Trade agreements with Singapore, Taiwan, Chile, and in the near future, with the United States.

Second, the Creation of Special Economic Processing Zones, that are attracting industries such as Singapore 's Technology Aerospace, for the repair and maintenance of aircraft for the region. Additionally, repair and maintenance facilities for ships, boats and heavy equipment, as well as oil refineries and oil warehousing facilities can be established in these zones.

These developments represent a source of opportunity for banks such as ours, and are an important potential market for our services. Our vision is to be 'Latin America's and Panama's leading financial services company in the eyes of our customers.' And to achieve this objective, our strategy is simple; to continue being competitive, always being a step ahead of our competitors, and to offer always our customers a fair value and the highest standards of customer service.

Also, we recognize that as one of the world's leading financial services organisations, we play a fundamental role in the social and economic development of the countries in which we operate by providing a safe place

for the savings of the country, as well as an efficient intermediation system between savings, loans and investments.

As client driven organisation, we need to demonstrate a strong emphasis on ethics and social responsibility. It pleases me to say that HSBC has been very active in financing Corporate Social Responsibility programmes in Panama. The Group is providing financing for irrigation projects that contribute to fight the effects of *El Niño*, as well as other water related projects, and for the construction of bridges both in the city and rural Panama. Finally, with the entry of Grupo Banistmo into the HSBC family we will be better able to support and satisfy the financial needs of Panamanians and our regional as well as global clients in this part of the world.

As I say to my colleagues every day, this region presents one of the most exciting development and growth opportunities in the world and Panama is at the heart of this effort. I look forward to witnessing Panama to achieve its goal of becoming the 'Hub of the Americas' and an example for other countries to follow.

Thank you.