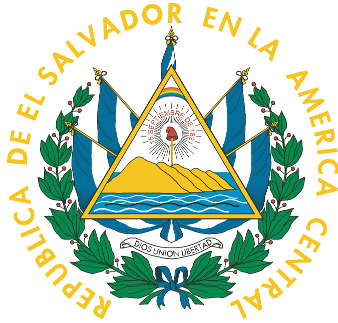
OFFERING CIRCULAR



US$286,458,000

The Republic of El Salvador

7.625% Notes due 2034

Interest will be payable semi-annually in arrears on March 21 and September 21 of each year commencing on March 21, 2005. The Notes will mature on September 21, 2034. Holders will have the right to elect to cause the Republic of El Salvador to redeem the Notes on September 21, 2019 for 100% of the principal amount of the Notes, together with accrued interest to the date of redemption. Such election, which will be irrevocable when made, must be made within the period commencing on July 21, 2019 and ending on the close of business on August 21, 2019.

The Notes will contain provisions, commonly known as "collective action clauses", regarding acceleration and voting on future amendments, modifications and waivers that differ from those applicable to the Republic of El Salvador's outstanding public external indebtedness. Under these provisions, which are described in the sections entitled "Terms and Conditions of the Notes — Events of Default" and "— Modifications, Amendments and Waivers", the Republic of El Salvador may amend the payment provisions of the Notes and certain other terms with the consent of the holders of 75% of the aggregate amount of the outstanding Notes.

Except as described herein, payments on the Notes will be made without deduction for or on account of withholding taxes imposed by the Republic of El Salvador. Application has been made to list the Notes on the Luxembourg Stock Exchange and will be made to list the Notes on the El Salvador Stock Exchange.

Price: 100%

plus accrued interest, if any, from September 21, 2004.

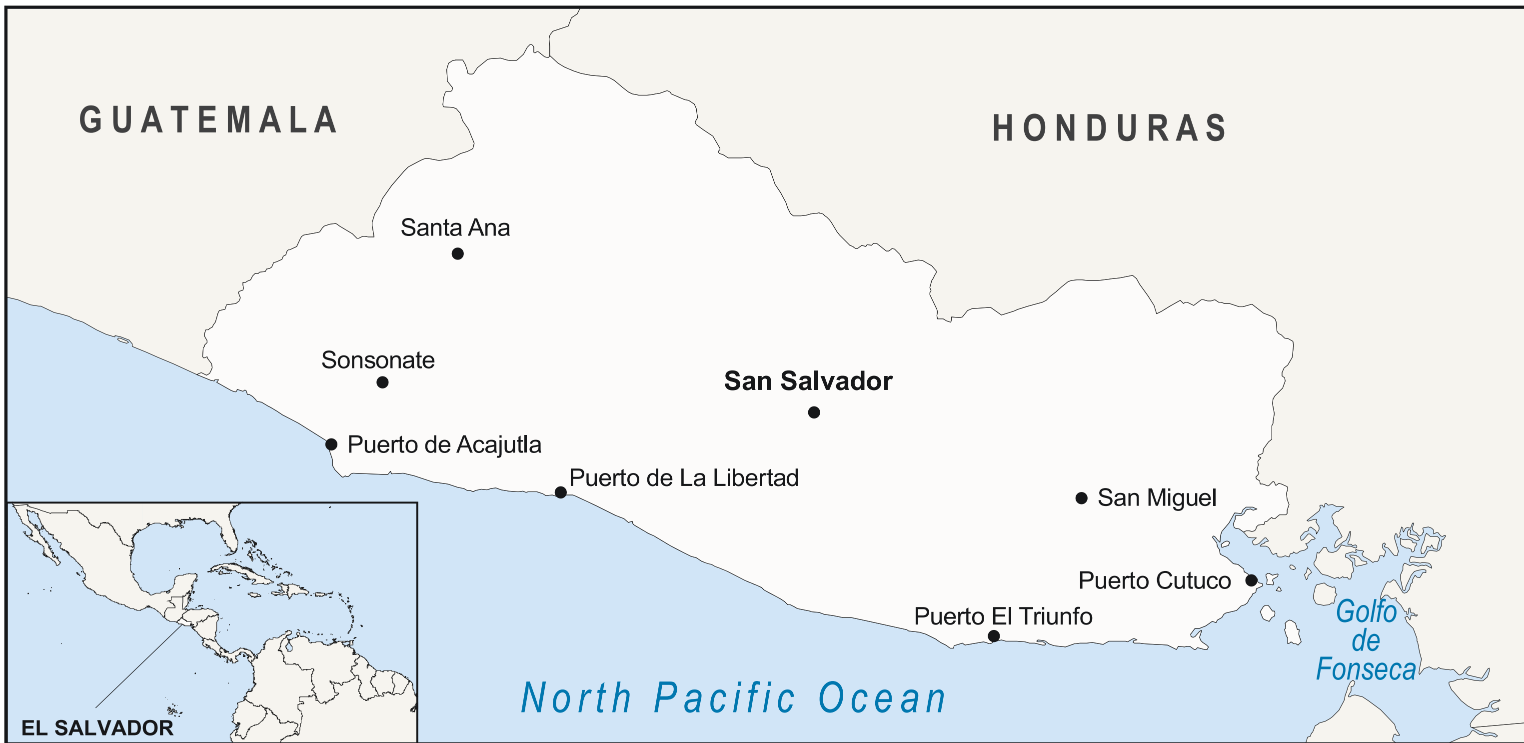
Delivery of the Notes will be made on or about September 21, 2004.

The Notes have not been and will not be registered under the Securities Act. The Notes may not be offered or sold within the United States or to U.S. persons except to qualified institutional buyers in reliance on the exemption from registration provided by Rule 144A and to certain persons in offshore transactions in reliance on Regulation S. You are hereby notified that sellers of the Notes may be relying on the exemption from the provisions of Section 5 of the Securities Act provided by Rule 144A.

Citigroup

September 14, 2004

El Salvador



IN MAKING AN INVESTMENT DECISION, INVESTORS MUST RELY ON THEIR OWN EXAMINATION OF THE REPUBLIC AND THE TERMS OF THE OFFERING, INCLUDING THE MERITS OR THE RISKS INVOLVED.

You should rely only on the information contained in this document or to which we have referred you. We have not authorized anyone to provide you with information that is different. This document may only be used where it is legal to sell these securities. The information in this document may only be accurate on the date of this document.

This Offering Circular may only be used for the purposes for which it has been published.

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Because the Republic or its affiliates may purchase and resell the Notes in certain transactions exempt from registration under the U.S. Securities Act of 1933, as amended (the "Securities Act"), the ability of any subsequent holder of Notes to reoffer, resell, pledge or otherwise transfer the Notes pursuant to the exemption provided by Rule 144 under the Securities Act may be limited.

NOTICE TO NEW HAMPSHIRE RESIDENTS

NEITHER THE FACT THAT A REGISTRATION STATEMENT OR AN APPLICATION FOR A LICENSE HAS BEEN FILED UNDER CHAPTER 421-B OF THE NEW HAMPSHIRE REVISED STATUTES WITH THE STATE OF NEW HAMPSHIRE NOR THE FACT THAT A SECURITY IS EFFECTIVELY REGISTERED OR A PERSON IS LICENSED IN THE STATE OF NEW HAMPSHIRE CONSTITUTES A FINDING BY THE SECRETARY OF STATE THAT ANY DOCUMENT FILED UNDER RA 421-B IS TRUE, COMPLETE AND NOT MISLEADING. NEITHER ANY SUCH FACT NOR THE FACT THAT THE EXEMPTION OR EXCEPTION IS AVAILABLE FOR A SECURITY OR A TRANSACTION MEANS THAT THE SECRETARY OF STATE HAS PASSED IN ANY WAY UPON THE MERITS OR QUALIFICATIONS OF, OR RECOMMENDED OR GIVEN APPROVAL TO, ANY PERSON, SECURITY OR TRANSACTION. IT IS UNLAWFUL TO MAKE, OR CAUSE TO BE MADE, TO ANY PROSPECTIVE

PURCHASER, CUSTOMER OR CLIENT, ANY REPRESENTATION INCONSISTENT WITH THE PROVISIONS OF THIS PARAGRAPH.

The Notes will be direct, general and unconditional obligations of the Republic. The Notes will, at all times, rank equally without any preference among themselves and at least *pari passu* with all other present and future unsecured and unsubordinated Public External Indebtedness (as defined herein) of the Republic.

The Notes will be issued in registered form only. Notes sold in offshore transactions in reliance on Regulation S under the Securities Act ("Regulation S") will be represented by a permanent global Note (which may be subdivided) in fully registered form without interest coupons (the "Regulation S Global Note") deposited with a custodian for, and registered in the name of a nominee of, The Depository Trust Company ("DTC") for the respective accounts at DTC as such subscribers may direct. Notes sold in the United States to qualified institutional buyers (each a "qualified institutional buyer") as defined in, and in reliance on, Rule 144A under the Securities Act ("Rule 144A") will be represented by a permanent global Note (which may be subdivided) in fully registered form without interest coupons (the "Restricted Global Note" and, together with the Regulation S Global Note, the "Global Notes") deposited with a custodian for, and registered in the name of a nominee of, DTC. Beneficial interests of DTC Participants (as defined under "Book-Entry Settlement and Clearance") in the Global Notes will be shown on, and transfers thereof between DTC Participants will be effected only through, records maintained by DTC and its direct and indirect participants, including Euroclear Bank S.A./N.V., as operator of the Euroclear System ("Euroclear") and Clearstream Banking, *société anonyme* ("Clearstream, Luxembourg"), if applicable. See "Book-Entry Settlement and Clearance." Except as described herein, definitive Notes will not be issued in exchange for beneficial interests in the Global Notes. See "Terms and Conditions of the Notes — Form, Denomination and Title." For restrictions on transfer applicable to the Notes, see "Transfer Restrictions" and "Subscription and Sale."

The Republic has taken reasonable care to ensure that the information contained in this Offering Circular is true and correct in all material respects and not misleading as of the date hereof, and that, to the best of the knowledge and belief of the Republic, there has been no omission of information which, in the context of the issue of the Notes, would make this document as a whole or any such information misleading in any material respect. The Republic accepts responsibility accordingly.

This Offering Circular does not constitute an offer by, or an invitation by or on behalf of, the Republic or the Manager to subscribe to or purchase any of the Notes. Each recipient shall be deemed to have made its own investigation and appraisal of the financial condition of the Republic. The distribution of this Offering Circular or any part of it and the offering, possession, sale and delivery of the Notes in certain jurisdictions may be restricted by law. Persons into whose possession this Offering Circular comes are required by the Republic and the Manager to inform themselves about and to observe any such restrictions. See "Subscription and Sale" and "Transfer Restrictions" for a description of further restrictions on the offer, sale and delivery of Notes and on distribution of this Offering Circular and other offering material relating to the Notes.

Each person purchasing Notes pursuant to Rule 144A will be deemed to:

- represent that it is purchasing the Notes for its own account or an account with respect to which it exercises sole investment discretion and that it or such account is a qualified institutional buyer (as defined in Rule 144A); and
- acknowledge that the Notes have not been and will not be registered under the Securities Act or any State securities laws and may not be reofferred, resold, pledged or otherwise transferred except as described under "Transfer Restrictions."

Each purchaser of Notes sold outside the United States in reliance on Regulation S will be deemed to have represented that it is not purchasing Notes with a view to distribution thereof in the United States. Each person purchasing Notes pursuant to Rule 144A also acknowledges that:

- it has been afforded an opportunity to request from the Republic and to review, and it has received, all additional information considered by it to be necessary to verify the accuracy of the information herein;
- it has not relied on the Manager or any person affiliated with the Manager in connection with its investigation of the accuracy of the information contained in this Offering Circular or its investment decision; and
- no person has been authorized to give any information or to make any representation concerning the Republic or the Notes other than those contained in this Offering Circular and, if given or made, such information or representation should not be relied upon as having been authorized by the Republic or the Manager.

IN CONNECTION WITH THIS ISSUE OF NOTES, CITIGROUP GLOBAL MARKETS INC. MAY, ITSELF OR THROUGH ITS AFFILIATES, OVERALLOT OR EFFECT TRANSACTIONS WHICH STABILIZE OR MAINTAIN THE MARKET PRICE OF THE NOTES AT A LEVEL WHICH MIGHT NOT OTHERWISE PREVAIL IN THE OPEN MARKET, TO THE EXTENT PERMITTED BY APPLICABLE LAWS. SUCH STABILIZING, IF COMMENCED, MAY BE DISCONTINUED AT ANY TIME.

PRESENTATION OF INFORMATION

Unless otherwise specified or the context requires, references to "US dollars" and "US$" are to United States dollars and references to the *"colón"* and *"colones"* and "¢" are to Salvadoran *colones.*

References to "FOB" are to exports free on board and to "CIF" are to imports including cost, insurance and freight charges.

Data identified as "preliminary data" reflects an interim calculation and is subject to change.

References to *maquila* are to the assembly of imported goods for re-export.

References to "Central America" and "Central American countries" are to El Salvador, Costa Rica, Guatemala, Honduras and Nicaragua.

Certain economic and financial data in this Offering Circular is derived from information previously published by the *Banco Central de Reserva de El Salvador* (the "Central Bank") and other governmental entities of El Salvador. This data is subject to correction and change in subsequent publications.

Certain other information in this Offering Circular is derived from information made publicly available by the United Nations.

References to "net international reserves" are to foreign currency reserves. The term current account surplus (deficit) as applied to the balance of payments includes foreign aid, unless otherwise specified.

Certain amounts included in this Offering Circular have been subject to rounding adjustments; accordingly, figures shown as totals in certain tables may not be an arithmetic aggregation of the figures which precede them.

FORWARD-LOOKING STATEMENTS

This Offering Circular contains certain forward-looking statements (as such term is defined in the Securities Act) concerning the Republic. These statements are based upon beliefs of certain government officials and others as well as a number of assumptions and estimates which are inherently subject to significant uncertainties, many of which are beyond the control of the Republic. Future events may differ materially from those expressed or implied by such forward-looking statements. Such forward-looking statements are principally contained in the sections "Offering Circular Summary," "The Republic of El Salvador," "The Salvadoran Economy," "Foreign Trade and Balance of Payments," "Monetary System," "Public Sector Finances" and "Public Debt." In addition, in those and other portions of this Offering Circular, the words "anticipates," "believes," "estimates," "expects," "plans," "intends," "projections" and similar expressions, as they relate to the Republic, are intended to identify forward-looking statements. Such statements reflect the current views of the Republic with respect to future events and are subject to certain risks, uncertainties and assumptions. The Republic undertakes no obligation publicly to update or revise any forward-looking statements, whether as a result of new information, future events or otherwise. In light of these risks and uncertainties, there can be no assurances that the events described or implied in the forward-looking statements contained in this Offering Circular will in fact occur.

ENFORCEMENT OF CIVIL LIABILITIES

The Republic is a foreign sovereign state. Consequently, it may be difficult for investors to obtain or realize upon judgments in the courts of the United States. Under its Constitution, the Republic is not permitted to consent to jurisdiction of the courts of any foreign jurisdiction. The Republic has not consented to the jurisdiction of any court outside El Salvador in connection with actions arising out of or based on the Notes or in connection with the enforcement of any judgment arising out of such actions, nor has the Republic appointed an agent for service of process outside El Salvador. The Republic has agreed to the following arbitration provisions as part of the Terms and Conditions of the Notes:

> Any dispute, controversy or claim arising out of or relating to the Notes (other than any action arising out of or based on the United States federal or state securities laws), including the performance, interpretation, construction, breach, termination or invalidity thereof shall be finally settled by arbitration in accordance with the Arbitration Rules of the United Nations Commission on International Trade Law (excluding Article 26 thereof) as in effect on the date of the Fiscal Agency Agreement (the "UNCITRAL Arbitration Rules"). The number of arbitrators shall be three, to be appointed in accordance with Section II of the UNCITRAL Arbitration Rules. The appointing authority shall be the Chairman of the International Court of Arbitration of the International Chamber of Commerce. The third arbitrator may be (but need not be) of the same nationality as any of the parties to the arbitration. The place of arbitration shall be New York, New York. The language to be used in the arbitration proceedings shall be English. Any arbitral tribunal constituted under this paragraph shall make its decisions entirely on the basis of the substantive law of the State of New York.
>
> The decision of any arbitral tribunal shall be final to the fullest extent permitted by law, and a court judgment may be entered thereon by any Salvadoran court lawfully entitled to enter such judgment. In any arbitration or related legal proceedings for the conversion of an arbitral award into a judgment, the Republic will not raise any defense that it could not raise but for the fact that it is a sovereign state. The Republic has not consented to the jurisdiction of any court outside El Salvador, in connection with actions arising out of or based on the Notes or in connection with the enforcement of any judgment arising out of such actions, nor has the Republic appointed an agent for service of process outside El Salvador. The Republic waives any *forum non conveniens* defense in any proceeding in El Salvador.
>
> No arbitration proceedings hereunder shall be binding upon or in any way affect the right or interest of any person other than the claimant or respondent with respect to such arbitration.
>
> The Republic's consent to arbitration shall not preclude a holder of any Note from instituting legal proceedings against the Republic in the courts of El Salvador.

The Republic has represented that it has no right to immunity on the grounds of sovereignty or otherwise, from the execution of any judgment in El Salvador, or from the execution or enforcement in El Salvador of any arbitral award (except, in each case, for the limitation on alienation of public property) in respect of any proceeding or any other matter arising out of or relating to its obligations contained in the Notes. The enforcement by a Salvadoran court of a foreign arbitral award is subject to recognition by the *Corte Suprema de Justicia* (the "Supreme Court") of the Republic, which will recognize such award if all the required formalities are observed and the award does not contravene Salvadoran national sovereignty, public policy and "good morals." Under the laws of the Republic, public property *(bienes de uso público)* of the Republic located in El Salvador is not subject to execution or attachment, either prior to or after judgment. The execution of a judgment against El Salvador in El Salvador is only available in accordance with the procedures set forth in Articles 450 et seq. of the Salvadoran Civil Procedure Code, which envisions registration of the judgment for inclusion in the budget for payment in a subsequent fiscal year of the Republic.

EXCHANGE RATE INFORMATION

From 1989 to December 31, 2000, although El Salvador set no official exchange controls on the *colón* and the exchange rate was permitted to float freely based on market forces, the Central Bank had a policy of purchasing and selling US dollars periodically for the purpose of limiting movement in the *colón*/US dollar exchange rate. No official fluctuation range was established.

On November 30, 2000, the Legislative Assembly approved the *Ley de Integración Monetaria* (the "Monetary Integration Act"), which fixed the *colón* to the US dollar at ¢8.75 to US$1.00, effective January 1, 2001. The Monetary Integration Act allows free circulation of the US dollar in the Salvadoran economy and makes the US dollar the unit of account for the financial system in El Salvador. See "Foreign Trade and Balance of Payments — Exchange Rate Policy and Foreign Exchange Rates."

The following table sets forth the high, low, average and period-end market exchange rates for the periods presented, expressed in *colones* per US dollar and not adjusted for inflation, as published by the Central Bank. The Federal Reserve Bank of New York does not report a noon buying rate for *colones.*

Exchange Rates

Year	High(1)	Low(2)	Average(3)	Period-End(4)
1999	8.79	8.71	8.75	8.79
2000	8.79	8.71	8.75	8.79
2001(5)	8.75	8.75	8.75	8.75
2002(5)	8.75	8.75	8.75	8.75
2003(5)	8.75	8.75	8.75	8.75

(1) High of monthly average prices for the sale of US dollars stated in *colones.*

(2) Low of monthly average prices for the purchase of US dollars stated in *colones.*

(3) The average exchange rate is the average of the purchase and sale prices of US dollars stated in *colones.*

(4) Average price for the sale of US dollars stated in *colones* in the last month of the period presented.

(5) Since January 1, 2001, the *colón*/US dollar exchange rate is fixed at ¢8.75/US$1.00 pursuant to the Monetary Integration Act. As a result, there is no differentiation between the high, low, average and period-end exchange rates.

Source: *Banco Central de Reserva de El Salvador.*

Currency conversions contained in this Offering Circular should not be construed as representations that *colones* have been, could have been or could be converted into US dollars at the indicated or any other rate of exchange.

OFFERING CIRCULAR SUMMARY

The following summary does not purport to be complete and is qualified in its entirety by, and is subject to, the detailed information appearing elsewhere in this Offering Circular.

The Republic of El Salvador

General

El Salvador is a republic and its form of government is a representative democracy. In March 2004, Elias Antonio Saca González was elected President of the Republic. He took office on June 1, 2004, succeeding Francisco Flores, who was elected in 1999. El Salvador is geographically the smallest and also the most densely populated of the five Central American countries. It is bounded on the south by the Pacific Ocean, on the northwest by Guatemala and on the northeast and east by Honduras. El Salvador had a nominal gross domestic product ("GDP") of approximately US$14.9 billion in 2003, an increase of 19.9% from the 1999 nominal GDP of approximately US$12.5 billion. In 2003, real GDP grew at a rate of 1.8%, compared to 2.2% during 2002.

Economy

Beginning in late 1989, the government began to implement a number of measures designed to strengthen the private sector and to minimize the government's role in the economy. The principal steps taken by the government since 1989 to stimulate the economy include the following:

- Adopting the Monetary Integration Act, which went into effect on January 1, 2001 and fixes the *colón* to the US dollar at ¢8.75 to US$1.00, allows free circulation of the US dollar in the Salvadoran economy and makes the US dollar the unit of account for El Salvador's financial sector. The power of the Central Bank to issue new *colones* or coins ceased as of January 1, 2001. All deposits, credits, pensions and other operations of the financial system were redenominated to US dollars on that date. Non-financial firms may use either *colones* or US dollars to express their financial records and accounting. Salaries and wages may be denominated in either *colones* or US dollars and prices can be specified in *colones* or US dollars. See "Foreign Trade and Balance of Payments — Exchange Rate Policy and Foreign Exchange Rates."
- Reducing the role of government in many sectors of the economy through a series of privatizations designed to encourage private investment and foster competition. Since 1998, the government has received net privatization revenues of approximately US$1,123.3 million, through the privatization of the country's electricity distribution companies and telecommunications providers. The government also granted private concessions for certain services and facilities at the international airport and plans to grant additional concessions at a future date. In addition, the government sold an alcohol factory and six state-owned sugar mills to private investors and is in the process of selling its remaining interests in the telecommunications company. The Republic also announced that it may grant concessions at its port facilities at Acajutla. See "The Salvadoran Economy — Privatizations."
- Promoting trade and foreign investment through the elimination of certain tariffs and the application of three tariff rates to approximately 90.0% of imports, the adoption of laws allowing unlimited remittances of earnings by foreign companies, the provision for duty drawbacks on certain exports and the establishment of free trade zones. These measures are intended to stimulate manufacturing, principally by *maquila* plants, which are exempt from import and export duties and enjoy certain income tax exemptions. In addition to implementing the initiatives of the *Mercado Común Centroamericano* (the "Central American Common Market" or "CACM"), the Republic has reached free trade agreements with Mexico, Chile, the Dominican Republic and Panama and has qualified for enhanced, preferential access to the United States market under the Caribbean Basin Initiative (the "CBI"). See "Foreign Trade and Balance of Payments — Regional Integration and Free Trade." On May 28, 2004, the United States signed the U.S. — Central America Free

Trade Agreement ("CAFTA") with the five member countries of the Central America Economic Integration System. On August 5, 2004, the Dominican Republic was added to CAFTA. The treaty will become effective between the United States and one or more other signatories on January 1, 2005, provided that their respective legislatures have approved the agreement. If the agreement does not become effective on January 1, 2005, it will become effective on such later date as the United States and one or more other signatories agree, provided that their respective legislatures have approved the agreement.

- Implementing a comprehensive tax reform that includes the simplification of the tax system and the reduction and elimination of some taxes and tax credits. The reforms commenced with the introduction of a value added tax in 1992 to provide a consistent revenue source. Subsequent amendments increased the value added tax rate from 10.0% to 13.0%, implemented measures to reduce tax avoidance, eliminated exemptions, closed loopholes, provided the tax administration with the tools to enforce tax compliance and to accelerate the imposition of fines and sanctions, introduced a levy on gasoline and diesel fuel and created stricter customs enforcement measures. See "Public Sector Finances — Taxation."
- Decentralizing the government and modernizing, downsizing and closing public sector institutions. The Republic increased by law municipal allocations in the general budget from 6.0% to 7.0% of current revenues to begin in 2005, reduced the size of government by decreasing the number of employees and combining ministries and reduced or eliminated subsidies for electricity, water consumption and public transportation. See "The Salvadoran Economy — Principal Reforms from 1979 to Present."
- Reforming the pay-as-you-go pension system commencing in 1996 by creating a private pension system modeled on the then-existing Chilean system. The prior public pension system remains in place for certain older workers and others who elected to remain in the public system. The reforms have reduced by approximately 50.0% the net present value of the government's obligations with respect to pensions. See "The Salvadoran Economy — Employment and Wages — Pension Reform."
- Privatizing the banking system in 1991, establishing an independent Central Bank and establishing a regulatory framework intended to promote competition among financial institutions. See "The Monetary System."

Benefiting from these measures, El Salvador's real GDP increased at an average annual rate of 4.0% from 1992 to 2003 and 2.3% from 1999 to 2003. El Salvador's rate of inflation decreased from 12.1% in 1993 to 2.5% in 2003. Primarily as a result of the Monetary Integration Act, the average interest rate on short- and long-term loans fell to 6.4% and 7.7% for the month of June 2004, compared to 12.2% and 13.7%, respectively, for the month of December 2000.

Worker remittances from Salvadorans abroad and a strong capital account resulted in the steady growth of foreign currency reserves from 1992 through 1999. Foreign currency reserves declined by approximately 19.3% from December 31, 1999 to December 31, 2002, as the Central Bank provided commercial banks with US dollars in connection with the implementation of the Monetary Integration Act. By year end 2003, however, foreign currency reserves increased by approximately 20.0% from US$1,588.8 million at December 31, 2002 to US$1,905.8 million. By pursuing fiscally conservative policies, the Republic's ratio of public external debt to GDP decreased from 39.3% in 1992 to 37.6% in 2003.

In recent years, *maquila* (assembly for re-export) has been the most dynamic activity within the economy, with *maquila* production increasing 38.9% in real terms from 1999 to 2003. According to the *Ministerio de Economía* (the "Ministry of Economy"), as of December 31, 2003 there were 265 *maquila* plants, 115 of which are located in free-trade zones, with the remaining 150 operating outside the free-trade zones. Over half of the *maquila* plants established in the free-trade zones produce apparel and linens, mainly for export to the United States. In 2003, *maquila* exports represented 60.0% of total exports of goods.

Traditionally, coffee has been the main agricultural product of the Republic and an important sector of the overall Salvadoran economy. As the economy has increasingly come to rely on industrial production, particularly *maquila,* the importance of coffee to the economy has lessened. Coffee accounted for 1.4% of GDP and 12.5% of agricultural production in 2003 compared to 3.8% and 25.5%, respectively, in 1993. Coffee is nevertheless an important source of employment in El Salvador, generating approximately 51,968 jobs in the 2002/2003 harvest, which accounted for 2.1% of employment nationwide. Coffee is also an important source of foreign currency. In 2003, it accounted for 3.4% of total Salvadoran exports of goods.

The Peace Accord

In addition to the economic, monetary and fiscal reforms, the government has implemented a series of initiatives designed to promote social and democratic reforms. These social and democratic reforms flowed from the agreement (the "Peace Accord") signed in 1992 by the government and the *Frente Farabundo Martí para la Liberación Nacional* (the "FMLN") ending 12 years of guerrilla war in the Republic. The three main objectives established by the Peace Accord were:

- the reintegration of former participants in the guerrilla war into the Salvadoran economy and society;
- the implementation of democratic reforms; and
- assistance to rural communities.

The development of programs to achieve these objectives was assisted and monitored by the United Nations. In December 1996, as a result of the implementation of many of these programs, the General Assembly of the United Nations adopted a resolution to withdraw its on-site observers and continue the United Nations verification responsibilities through periodic visits. The General Assembly of the United Nations noted the commitment of the Republic and other parties to the full implementation of the Peace Accord. On January 6, 2003, the United Nations declared that the objectives of the Peace Accord had been accomplished, thus ending the United Nations peace verification process.

Selected Economic Indicators

	For the Year Ended December 31,				
	1999	2000	2001	2002	2003
	(In millions of US dollars, except percentages and where noted)				
The Economy					
Nominal GDP	$12,465	$13,134	$13,813	$14,312(2)	$14,941(2)
Real GDP (in millions of *colones*)(1)	¢56,029	¢57,236	¢58,214	¢59,512(2)	¢60,603(2)
Real GDP growth(1)	3.4%	2.2%	1.7%	2.2%(2)	1.8%(2)
Annual inflation(3)	(1.0)%	4.3%	1.4%	2.8%	2.5%
Balance of Payments					
Exports (FOB goods and services)	$ 3,288	$ 3,803	$ 3,764	$ 3,962(2)	$ 4,127(2)
Imports (CIF goods and services)	5,109	6,031	6,213	6,396(2)	6,978(2)
Trade and services balance	(1,821)	(2,228)	(2,449)	(2,435)(2)	(2,851)(2)
Current account surplus (deficit) of the balance of payments	(239)	(431)	(150)	(412)(2)	(734)(2)
As % of GDP(4)	(1.9)%	(3.3)%	(1.1)%	(2.9)%(2)	(4.9)%(2)
Net international reserves	$ 1,970	$ 1,891	$ 1,710	$ 1,589	$ 1,906
Non-Financial Public Sector					
Total revenues	$ 1,955	$ 2,180	$ 2,147	$ 2,308	$ 2,513(2)
Total expenditures	2,300	2,579	2,649	2,783	2,732(2)
Primary balance surplus	197	123	259	362	526(2)
As % of GDP	1.6%	0.9%	1.9%	2.5%(2)	3.5%(2)
Surplus (deficit)(4)	$ (345)	$ (399)	$ (502)	$ (475)	$ (219)(2)
As % of GDP	(2.8)%	(3.0)%	(3.7)%	(3.3)%(2)	(1.5)%(2)
Public Sector Debt(5)					
Total public debt	$ 4,306	$ 4,782	$ 5,517	$ 6,397	$ 7,119(2)
Internal debt	1,584	1,893	2,127	1,484	1,501(2)
External debt	2,723	2,888	3,390	4,913	5,618(2)
Total public debt (as % of GDP)	34.5%	36.4%	39.9%	44.7%(2)	47.6%(2)
Public internal debt (as % of GDP)	12.7%	14.4%	15.4%	10.4%(2)	10.0%(2)
Public external debt (as % of GDP)	21.8%	22.0%	24.5%	34.3%(2)	37.6%(2)
External debt service (as % of exports of goods and services)(6)	9.0%	6.1%	7.3%	8.2%(2)	11.4%(2)
Average Exchange Rate					
(*colones* per US dollar)(7)	¢ 8.75	¢ 8.75	¢ 8.75	¢ 8.75	¢ 8.75

(1) At constant 1990 prices.

(2) Preliminary data.

(3) As measured by the variation in the *Índice de Precios al Consumidor* (Consumer Price Index or the "CPI") published by the National Bureau of Statistics and Census.

(4) Including foreign aid.

(5) Including debt of the Central Bank.

(6) Exports (FOB goods and services). Calculation does not include Central Bank debt service.

(7) The average exchange rate is the average of the purchase and sale prices of US dollars stated in *colones*. Since January 1, 2001, the *colón*/US dollar has been fixed at ¢8.75/US$1.00 pursuant to the Monetary Integration Act.

Source: *Banco Central de Reserva de El Salvador.*

The Offering

Issuer	The Republic of El Salvador.
Issue Amount	US$286,458,000 principal amount.
Issue Price	100% of the principal amount of the Notes, plus accrued interest, if any, from September 21, 2004.
Maturity Date	September 21, 2034.
Interest	The Notes will bear interest from the date of issue at the rate of 7.625% per annum payable semi-annually in arrears on March 21 and September 21 of each year, commencing on March 21, 2005.
Redemption	Each holder may require that the Republic redeem the Notes on September 21, 2019 at 100% of the principal amount of the Notes to be redeemed plus any accrued and unpaid interest to the redemption date. See "Terms and Conditions of the Notes — Redemption and Purchase; Further Issues."
Withholding Tax; Additional Amounts . .	Principal of and interest on the Notes are payable by the Republic without withholding or deduction for or on account of taxes imposed by El Salvador to the extent described herein. In the event that the Republic is required by law to deduct or withhold taxes, duties, assessments or governmental charges, the Republic will pay Additional Amounts (as defined herein) as necessary to enable holders of Notes to receive such amounts after such deduction or withholding as they would have received absent such deduction or withholding, subject to certain exceptions. See "Terms and Conditions of the Notes — Payment of Additional Amounts."
Status	The Notes will be direct, general, unsecured and unconditional obligations of the Republic. The Notes will at all times rank equally without any preference among themselves and at least equally with all other present and future unsecured and unsubordinated Public External Indebtedness of the Republic. See "Terms and Conditions of the Notes — General," "— Negative Pledge" and "— Covenants."
Negative Pledge and Certain Covenants	The Terms and Conditions of the Notes contain certain covenants and restrictions on the creation or subsistence of any Security (as defined herein) securing Public External Indebtedness, with certain exceptions. See "Terms and Conditions of the Notes — Negative Pledge" and "— Covenants."
Use of Proceeds	Net proceeds from the issuance of the Notes will be used to finance the general activities of the Republic, including, without limitation, capital expenditures, payments of pension obligations and debt servicing.
Collective Action Clauses	The Notes will contain provisions, commonly known as "collective action clauses", regarding acceleration and voting on future amendments, modifications and waivers that differ from those applicable to the Republic's outstanding public external indebt-

	edness. Under these provisions, which are described in the sections entitled "Terms and Conditions of the Notes — Events of Default" and "— Modifications, Amendments and Waivers", the Republic may amend the payment provisions of the Notes and certain other terms with the consent of the holders of 75% of the aggregate amount of the outstanding Notes.
Form of Notes	Registered only, without coupons. No Notes will be issued in bearer form.
Denominations	Each Note will be issued in minimum denominations of US$10,000 and integral multiples of US$1,000 in excess thereof.
Further Issues	The Republic may, without the consent of the holders of the Notes, create and issue additional notes having the same ranking and the same interest rate, maturity and other terms as the Notes (or the same except for the amount of the first interest payment and the issue price), so that such further notes may be consolidated and form a single series with the Notes, provided that such additional notes do not have, for purposes of U.S. federal income taxation (regardless of whether any holders of such notes are subject to U.S. federal laws), a greater amount of original issue discount than the Notes have as of the date of issuance of such additional notes.
Listing	Application has been made to list the Notes on the Luxembourg Stock Exchange and will be made to list the Notes on the *Bolsa de Valores de El Salvador* (the "El Salvador Stock Exchange").
Governing Law	The Notes shall be governed by, and construed in accordance with, the laws of the State of New York, United States of America, except that all matters concerning authorization and execution by the Republic, as well as the bringing of any actions and the enforcement of any judgment against the Republic in the courts of the Republic will be governed by the laws of the Republic.
Arbitration	Any dispute, controversy or claim arising out of or relating to the Notes, including the performance, interpretation, construction, breach, termination or invalidity thereof, will be finally settled by arbitration in New York, New York, in accordance with the UNCITRAL Arbitration Rules. Any arbitral tribunal constituted under the terms of the Notes will be required to make its decisions entirely on the basis of the substantive law of the State of New York as provided above. The Republic's consent to arbitration will not preclude a holder of any Note from instituting legal proceedings against the Republic in the courts of El Salvador, and the Republic has waived immunity from jurisdiction to which it might otherwise be entitled in any such proceedings or execution of an arbitral award in El Salvador (except for the limitation on alienation of public property).

Fiscal Agent, Principal Paying Agent, Registrar and Transfer Agent	Citibank, N.A., London office.
Luxembourg Transfer and Paying Agent	Kredietbank S.A. Luxembourgeoise.

USE OF PROCEEDS

The net proceeds from the issuance of the Notes, which are expected to amount to approximately US$285,928,052.70 after deduction of fees and expenses, will be used by the Republic to finance the general activities of the Republic, including without limitation, capital expenditures, payments of pension obligations, and debt servicing.

THE REPUBLIC OF EL SALVADOR

Territory, Population and Society

El Salvador is geographically the smallest as well as the most densely populated of the five Central American countries, encompassing 8,124 square miles (21,041 square kilometers). El Salvador is bounded on the south by 210 miles of Pacific Ocean coastline, on the northwest by Guatemala and on the northeast and east by Honduras. In the north, the Sierra Madre mountains rise to over 9,000 feet above sea level. Two major earthquakes struck El Salvador in January and February 2001. Prior to such earthquakes, the last significant earthquake occurred in 1986. Throughout the country, there are 25 distinct volcanoes, most of which are dormant. The most recent major volcanic eruption was in 1946. El Salvador enjoys two seasons, rainy and dry. The rainy season lasts from early May through October, while the dry season lasts from November through April.

In September 1992, the International Court of Justice resolved a border dispute between El Salvador and Honduras and awarded most of the disputed territories in favor of Honduras. At present, both parties are discussing the process of border demarcation in accordance with the decision of the International Court of Justice.

El Salvador's population is currently estimated at 6.6 million people by the *Dirección General de Estadística y Censos* (the "National Bureau of Statistics and Census''), a division of the Ministry of Economy, and is divided almost equally between urban and rural areas. In addition, more than one million Salvadorans are believed to be living and working outside of the country, principally in the United States. These foreign residents make a significant contribution to the Republic's economy through remittances to their families in El Salvador. Over 90.0% of the current population is *mestizo* (of mixed European and Indian descent). According to the 1992 census, San Salvador, the capital and country's largest city, had a population of 416,346. The average annual population growth rate for the Republic is projected to be approximately 2.1% for the period between 1995 and 2025 according to the National Bureau of Statistics and Census. Most of the population is Roman Catholic.

The following table sets forth information on per capita gross domestic product, average life expectancy, adult literacy rates and infant mortality rates in certain countries.

Selected Comparative Social Statistics

	El Salvador	Nicaragua	Honduras	Guatemala	Panama	Costa Rica	United States
Per Capita GDP(1)	$4,890	$2,470	$2,600	$4,080	$6,170	$8,840	$35,750
Average Life Expectancy(2)	70.6	69.4	68.8	65.7	74.6	78.0	77.0
Adult Literacy Rate(3)	79.7%	76.7%	80.0%	69.9%	92.3%	95.8%	99.0%
Infant Mortality(4)	33	32	32	36	19	9	7

(1) Based on 2002 figures, adjusted for purchasing power parity.

(2) In years, at 2002.

(3) At 2002.

(4) Per thousand live births in 2002.

Source: *Human Development Report 2004, United Nations.*

Historical Background

Prior to the Spanish conquest in the early 16th century, the area that is now El Salvador was occupied by various Indian tribes. The Spanish conquest began in 1524 with the arrival of an expedition from Guatemala led by Pedro de Alvarado. A Spanish settlement was permanently established in San Salvador in 1528 and became the agricultural center of the Captaincy General of Guatemala. Under

the Spanish government, the area became a center for the production of several commercial crops including cocoa, indigo and balsam wood.

Following independence from Spain in 1821, El Salvador became a member of the Central American Federation, which was dissolved in 1838 after a military coup in Honduras. Thereafter, as an independent republic, El Salvador slowly shifted its economy from its earlier dependence on indigo, cocoa and balsam wood to one based on coffee.

During the end of the nineteenth and the first quarter of the twentieth century, coffee cultivation on extensive plantations contributed to the establishment of a wealthy landholding minority. Social tensions came to a head in 1932, when an uprising of the landless peasantry led by the recently formed Communist Party was quashed by General Maximiliano Hernández after the loss of 30,000 lives. From 1932 to 1979, El Salvador was governed by a succession of military leaders.

On October 15, 1979, a revolutionary *junta* composed of civilians and members of the military assumed control of the country. Early in 1980, the *Partido Demócrata Cristiano* (the "PDC") joined the *junta* and imposed a program of economic reforms that included the nationalization of the banking system, agrarian reform aimed at the re-distribution of land ownership and the granting of exclusive monopolies to state-owned entities for the international sale of coffee and sugar. In 1982, a popularly elected Constitutional Assembly began drafting a new constitution that became effective in 1983 and that, with amendments, is still in force. In 1984, in the first presidential election under the new Constitution, the PDC leader, José Napoleón Duarte, was elected president.

During this time, several guerrilla organizations unified to form the FMLN. From 1980 until the signing of the Peace Accord in 1992, the Republic faced internal political and military conflicts which caused the loss of approximately 75,000 lives, triggered extensive emigration, displaced hundreds of thousands of persons within the country and caused widespread destruction to the country's infrastructure and economy.

Mr. Duarte was replaced in the 1989 presidential election by Alfredo Cristiani of the *Alianza Republicana Nacionalista* ("ARENA") party. The Cristiani administration implemented a number of changes designed to reinvigorate the economy. The benefits of these measures were evidenced by real GDP growth of 4.8% and 3.6% in 1990 and 1991, respectively, as compared to decreases or minimal growth in the period from 1985 through 1989. Nonetheless, the real benefits for the economy were limited due to the ongoing military conflict.

On January 16, 1992, after 12 years of conflict, the government and the FMLN signed the Peace Accord in Mexico City. The Peace Accord: (i) established the specific requirements for ending the armed conflict; (ii) addressed certain root causes of the conflict by instituting commitments from the parties to follow democratic principles; and (iii) placed specific emphasis on the process of reconstruction as part of the economic and social development of the Republic. Since the signing of the Peace Accord, the Republic has implemented a series of initiatives designed to promote social, economic and democratic reforms establishing a lasting foundation for peace. In December 1996, as a result of the implementation of many of these initiatives, the General Assembly of the United Nations adopted a resolution to withdraw its on-site observers and continue the United Nations verification responsibilities through periodic visits. The General Assembly noted the commitment of the Republic and other parties to the full implementation of the Peace Accord. On January 6, 2003, the United Nations declared that the objectives of the Peace Accord had been completed, thus ending the United Nations peace verification process.

The principal programs established pursuant to the Peace Accord were intended to meet the following goals:

- *Economic and social reintegration of former guerrillas and military personnel into the economy and society.* The immediate aim of the reintegration projects was to generate employment and income for the former combatants and military personnel. The projects included a program to transfer title to rural land to certain beneficiaries, United Nations agricultural training programs, agricultural

credit access programs through the *Banco de Fomento Agropecuario,* vocational training and scholarship programs, and loan programs for the establishment of small business and scholarships.

- *Building public confidence in the government.* Through electoral reforms and voter identification and registration, changes in the judiciary including the evaluation and training of judges, the replacement of internal military police with a trained national civilian police force and the establishment of a human rights commission, the government has sought to restore and build confidence in the government.

- *Assistance to rural communities significantly affected by the conflict.* The Republic provided assistance to rural communities in the short-term through basic municipal services, food and housing and in the medium- and long-term through the promotion of production, infrastructure and capital investment projects in education, health, environmental protection, economic and social infrastructure and municipal development.

The aggregate cost of implementing these programs since 1992 has been approximately US$2.6 billion. In addition, the Republic benefited from the voluntary write-off by the United States of certain of its external debt in 1993 and from the restructuring of the terms of much of its other external debt to finance the costs of such programs. See "Public Debt." The Republic believes that the costs to the Republic of implementing the programs established pursuant to the Peace Accord have been incurred.

Since the signing of the Peace Accord, the Republic has undertaken a number of economic, monetary and fiscal reforms designed to create stability and growth in the economy. For a discussion of these reforms, see "The Salvadoran Economy — Principal Reforms from 1979 to Present."

In recent years, El Salvador's development has been affected by a series of natural disasters including Hurricane Mitch in 1998 and a series of devastating earthquakes in early 2001 that left nearly 2,000 people dead or missing and 8,000 injured, and caused severe dislocations across all sectors of Salvadoran society. The earthquake damage was severe, with the impact concentrated on housing, schools and other basic infrastructure in rural areas that are among the country's poorest regions.

Form of Government

El Salvador is a republic and its form of government is a representative democracy, with powers divided among executive, legislative and judicial branches. Elections are held every five years for president and vice president and every three years for members of the single house of the legislative assembly (the "Legislative Assembly") and local governments. All Salvadoran citizens 18 years or older are entitled to vote. As part of the implementation of democratic reforms under the Peace Accord, there has been a major effort to improve voter identification and registration.

Executive authority is vested in the president and vice president, who are elected for a term of five years, and 12 cabinet ministers. Cabinet ministers are appointed, and may be removed at will, by the president. The president may propose legislation to the Legislative Assembly and has veto power over legislation, which may be overridden by a two-thirds vote of the Legislative Assembly. The president also appoints the regional governors for the 14 departments of El Salvador. The current president of El Salvador, Elias Antonio Saca González of ARENA, was elected in March 2004. President Saca took office on June 1, 2004, succeeding President Francisco Flores. President Saca's plans for his term in office includes the following goals:

- providing public access to government information, services and opportunities by establishing a technology infrastructure;

- creating an efficient government by eliminating, simplifying or redesigning processes that affect private enterprise;

- improving the quality of health services and providing universal health coverage;

- modernizing the educational system by investing in computers;

- supporting the agricultural sector through technical assistance and training;
- improving public security by addressing juvenile delinquency and rehabilitation programs;
- expanding free trade zones and industrial complexes;
- promoting tourism in El Salvador; and
- encouraging the informal sector to register with the government so they can benefit from cheaper financing.

Legislative authority is vested in the Legislative Assembly, which is comprised of a single house of 84 elected members. The Legislative Assembly has the power to enact legislation, ratify treaties and approve the annual budget. Bills must be approved by a majority of the Legislative Assembly to be enacted as laws. Constitutional amendments require approval by the Legislative Assembly in two sessions, the first by a majority of the members of the Legislative Assembly and the second by a two-thirds vote.

In the March 2003 legislative elections, the FMLN won 31 seats and currently is the largest party in the Legislative Assembly, while ARENA won 27 seats. The third largest party, *Partido de Conciliación Nacional* ("PCN"), won 16 seats. Subsequently, two members of PCN switched their political party affiliations by joining ARENA. No one party has control over the Legislative Assembly. As a result, matters are resolved through the creation of coalitions of ARENA or FMLN with one or more of the other minority parties.

The current composition of the Legislative Assembly is described in the following table.

Legislative Assembly
Composition By Political Party

Political Party	Number of Members
FMLN	31
ARENA	29
PCN	14
Partido Demócrata Cristiano ("PDC")	5
Convergencia Democrática/Centro Democrático Unido ("CDU")	5
Total	84

During the 2004 Presidential elections, PCN, PDC and CDU failed to obtain 3.0% of the total number of votes cast, the minimum number required under the Election Code for continued recognition as a political party. Consequently, the *Tribunal Supremo Electoral* ("Supreme Electoral Tribunal") notified such political parties that they would no longer be recognized. Both PCN and PDC have filed a petition with the Supreme Court to overturn the decision of the Supreme Electoral Tribunal. The Supreme Court has admitted the petition, thus, temporarily suspending the effectiveness of the decision of the Supreme Electoral Tribunal.

The next presidential election is scheduled to be held in March 2009. The next legislative and municipal government elections are due to occur in March 2006.

National judicial authority is vested in the Supreme Court and several lower courts. The Supreme Court, the highest judicial authority in the Republic, is composed of 15 justices appointed by the Legislative Assembly from two different lists of nominees separately and independently prepared by the National Council of the Judiciary and the Salvadoran Bar Association. Each Supreme Court justice serves a nine-year term and may be re-appointed. The terms of the Supreme Court justices are staggered such that three justices are appointed every three years. Judges serving on courts of appeal, certain first-instance tribunals and justices of the peace are appointed by the Supreme Court, also from lists prepared by the National Council of the Judiciary. The Constitution provides that the annual national budget must include

appropriations for the Judiciary totaling at least 6.0% of the central government's current revenues. The Judicial Training School was created as part of the implementation of the Peace Accord.

Memberships in International Organizations

El Salvador is a member of the United Nations and the Organization of American States and many of their respective specialized agencies, as well as the International Monetary Fund ("IMF"), the International Bank for Reconstruction and Development, the World Trade Organization (the "WTO"), the Inter-American Development Bank and the *Banco Centroamericano de Integración Económica.* El Salvador is also a beneficiary of the CBI, which, subject to certain exceptions, provides duty-free access to the U.S. markets for certain goods manufactured or processed in CBI beneficiary countries. See "Foreign Trade and Balance of Payments — Regional Integration and Free Trade — Trade Initiatives Involving the United States."

THE SALVADORAN ECONOMY

Principal Reforms from 1979 to Present

The economy of El Salvador has recovered from a series of negative developments during the period from 1979 through the inauguration of President Alfredo Cristiani in 1989, which included the nationalization of the banking system, costly failures in land reform, contraction of the manufacturing and agricultural sectors, the creation of state-owned monopolies in certain industries and extensive government spending related to the civil war. El Salvador experienced a substantial flight of capital from the country and significant emigration of economically active segments of the population to avoid the conflict and the depressed economy. The public sector recorded a substantial fiscal deficit financed by the Central Bank. In addition, as a result of the depressed economy, the Republic fell behind on certain of its external indebtedness, which was restructured after the implementation of the Peace Accord.

Principal Reforms

In 1989, the Republic began to implement a number of economic, monetary and fiscal reforms designed to create stability and growth in the economy. The benefits of these reforms are evidenced by average real GDP growth of 4.0% per year from 1992 to 2003. The reforms have focused on:

- fixing the exchange rate to the US dollar and introducing the US dollar into the Salvadoran economy as legal tender and the unit of account of the financial system through the Monetary Integration Act;
- reforming the pension system through the creation of a private pension system;
- privatizing and modernizing the banking sector;
- restructuring the Central Bank as an autonomous entity with a prohibition on financing of the central government;
- lowering tariff levels and liberalizing trade, including entering into free trade agreements with various trading partners;
- modifying the tax system, including simplification of the tax base;
- decentralizing and reducing the size of the government; and
- privatizing certain state-owned companies.

Monetary Integration Act. Effective as of January 1, 2001, the Legislative Assembly fixed the exchange rate of the *colón* to the US dollar at ¢8.75 to US$1.00, permitted the US dollar to circulate freely in the Salvadoran economy along with the *colón* and designated the US dollar as the unit of account for the Salvadoran financial system. These reforms were intended to stabilize permanently the value of the *colón* against the US dollar, reduce interest rates, increase the local savings rate, control inflation, encourage foreign investment, and simplify the management of the economy. The fixed exchange rate replaced the free floating exchange rate that had been in place since 1989. See "Foreign Trade and Balance of Payments — Exchange Rate Policy and Foreign Exchange."

Reforming the pension system. The government reformed the country's pension system effective on April 15, 1998 with the creation of a new system pursuant to which a substantial portion of the public pay-as-you-go pension system was replaced by a private system based on individual contributions. Under the new system, participating workers make monthly contributions to private pension funds which invest in permitted Salvadoran securities. Subsequent reforms to the pension system law reduced the government's obligations by authorizing the government to make certain payments pursuant to a 15 year annuity rather than in one lump sum and eliminating an employee's option of retiring after 30 years of contributions to the system regardless of age. At March 31, 2004, 1,100,382 Salvadoran workers were participating in the private system and US$1.8 billion in assets, equivalent to 11.9% of 2003 nominal GDP, were managed by

the system's private pension fund administrators. See "The Salvadoran Economy — Employment and Wages — Pension Reform."

Privatizing and modernizing the banking sector. The government modernized the banking sector in El Salvador through the privatization in the early 1990s of commercial banks and the savings and loan associations in order to promote competition and the development of a stronger financial system. The government also created the *Superintendencia del Sistema Financiero* (the "Superintendency of the Financial System") to regulate the banking industry. Further, the Legislative Assembly enacted legislation limiting loans to shareholders, increasing minimum capital requirements in light of the Basle Accord, regulating the supervisory powers and independence of the Superintendency of the Financial System and creating the *Instituto de Garantía de Depósitos* (the "Deposit Guaranty Agency"), which guarantees deposits up to US$7,060.0 and has the authority to provide funding to banks with liquidity problems. See "Monetary System — Financial Sector." Subsequent legislation has provided additional protections to depositors by creating stricter capital and risk management requirements and granting broader authority to the Superintendency of the Financial System.

Restructuring the Central Bank. The Central Bank was restructured as an autonomous institution whose fundamental objective is to protect the stability of the currency and to maintain favorable monetary, credit and financial conditions in the economy. The Central Bank is not permitted to be a funding source for the central government. See "Monetary System — The Central Bank (*Banco Central de Reserva de El Salvador*)."

Promoting trade and foreign investment. In an effort to promote trade and foreign investment, the government has eliminated some tariffs and applied three tariff rates to approximately 90.0% of imports, adopted laws allowing remittances of earnings by foreign companies, provided for rebates of duties on certain exports and encouraged the establishment of free trade zones covering 1,199,489 square meters as of June 30, 2004, which is nearly double the area established at the end of 2002. These measures are intended to stimulate manufacturing, principally by *maquila* plants, which are exempt from import and export duties and enjoy certain income tax exemptions. In addition to implementing the Central American Common Market initiatives, the Republic has reached free trade agreements with Mexico, Chile, the Dominican Republic and Panama and has qualified for enhanced, preferential access to the United States market under the Caribbean Basin Initiative. See "Foreign Trade and Balance of Payments — Tariffs and Other Trade Restrictions" and "— Regional Integration and Free Trade." On May 28, 2004, the United States signed the U.S. — Central America Free Trade Agreement with the five members of the Central American Economic Integration System. On August 5, 2004, the Dominican Republic was added to CAFTA. The treaty will become effective between the United States and one or more other signatories on January 1, 2005, provided that their respective legislatures have approved the agreement. If the agreement does not become effective on January 1, 2005, it will become effective on such later date as the United States and one or more other signatories agree, provided that their respective legislatures have approved the agreement.

Modifying the tax system. The government introduced a value added tax in 1992 in order to provide a consistent revenue source. Subsequent amendments increased the value added tax rate from 10.0% to 13.0%, implemented measures to reduce tax avoidance, eliminated exemptions, closed loopholes, provided the tax administration with the tools to enforce tax compliance and to accelerate the imposition of fines and sanctions, introduced a levy on gasoline and diesel fuel and created stricter customs enforcement measures. See "Public Sector Finances — Taxation."

Decentralizing and reducing the size of government. The government enacted legislation in 2004 aimed at decentralizing the government by increasing municipal allocations in the general budget from 6.0% to 7.0% of current revenues beginning in 2005. Continuing its policy to modernize public sector institutions, the Republic has reduced the size of government by decreasing the number of employees and combining ministries. Since such time, the Republic combined the Justice, Interior and Public Safety ministries into the Ministry of Governance, reduced the number of employees through outsourcing and implemented a hiring freeze. The number of government employees also decreased due to attrition and

voluntary early retirement. To increase efficiency in tax collection and reduce tax evasion, the Ministry of Finance restructured the General Customs Revenue Agency and the General Internal Revenue Agency to operate under a single director. The Government has also amended the *Ley del Servicio Civil* (the "Civil Service Law") to establish a more flexible public sector employment policy which has reduced the government's payroll. The government expects that the flexible policy will continue to reduce its payroll in future years. The Republic has also reduced or eliminated subsidies for electricity, water consumption and public transportation. In July 2004, the government mandated that all public sector entities apply strict measures aimed at increasing public savings.

In order to exert a unified control over the movement in goods, the Ministry of Finance implemented integrated customs facilities with Guatemala and Honduras and established customs facilities in Puerto Quetzal and Puerto Cortez, the main ports in Guatemala and Honduras, respectively.

Privatizing certain state-owned companies. The government reduced its role in many sectors of the economy through a series of privatizations designed to encourage private investment and foster competition. Since 1998, the government has received net privatization revenues of approximately US$1,123.3 million, through the privatization of the country's electricity distribution companies and telecommunications providers. The government also granted private concessions for certain services and facilities at the international airport and plans to grant additional concessions at a future date. In addition, the government sold an alcohol factory and six state-owned sugar mills to private investors and is in the process of selling its remaining interests in the telecommunications company. The Republic also announced that it may grant concessions at its port facilities at Acajutla. See "— Privatizations."

Privatizations

Telecommunications Privatization. Until 1998, *Administración Nacional de Telecomunicaciones* ("ANTEL") was the sole provider of basic telephone service in El Salvador and had sole power to license or grant concessions for related services. In September 1991, ANTEL granted a concession for cellular telecommunications to a company owned by Millicom International Cellular S.A. and local investors. Data transmission facilities have been leased to private operators. In addition, several paging service providers have obtained licenses to provide services.

In July 1998, ANTEL was privatized through a public auction in which France Telecom purchased 51.0% of the capital stock of the entity holding the fixed line telecommunications assets of ANTEL, *Compañía de Telecomunicaciones de El Salvador* ("CTE"), for US$275.0 million and *Telefónica de España* purchased 51.0% of the capital stock of the entity holding ANTEL's wireless telecommunications assets, *Internacional de Telecomunicaciones* ("INTEL"), which subsequently changed its name to *Telefónica El Salvador,* for US$41.0 million. The government sold approximately 6.0% of CTE's capital stock to the company's employees. The government sold its remaining interest in INTEL to the public on October 26, 1999 for US$43.5 million. In September 2003, France Telecom sold its interest in CTE to América Móvil, a Mexican company, and the government currently maintains a 43.0% stake in CTE. The government has begun the process of selling its remaining interests in CTE.

The government transferred the net proceeds from the privatization of ANTEL (US$391.8 million) to the ANTEL Privatization Fund. Interest generated by the ANTEL Privatization Fund is used for the promotion of employment by attracting foreign investment and increasing exports and tourism, for the promotion of handicraft industries and for forest development and protection, school food and scholarships. Since its inception in 1998, the ANTEL Privatization Fund has invested US$61.2 million in such projects and US$200 million of the capital in the ANTEL Privatization Fund has been used for reconstruction efforts related to the 2001 earthquakes as well as other public works.

Electricity Privatization. All planning, regulatory and executive functions concerning power generation, transmission and distribution were vested until 1998 in the *Comisión Ejecutiva Hidroélectrica del Río Lempa* ("CEL"), a state-owned monopoly. Approximately 50.0% of the Republic's electricity is generated by CEL. A private company, *Compañía Nejapa Power,* owns and operates a power plant located in Nejapa on the north side of San Salvador. The plant has a generating capacity of 151.2MW, which represents

approximately 12.6% of the Republic's total approximate generation capacity of 1,200MW. In May 1999, CEL filed for international arbitration of a dispute involving termination of the power purchase agreement executed in 1993 between CEL and *Compañía Nejapa Power.* On June 27, 2002, pursuant to an arbitral award, CEL paid US$90 million to *Compañía Nejapa Power* to compensate it for lost income under the agreement and the parties terminated the agreement effective June 30, 2002. The original term of the agreement was for an additional 13 years, and CEL's future obligations under it totaled approximately US$234 million for power purchases over such period. In addition, many of the large manufacturing enterprises in El Salvador have their own generating capacity. From 1986 to 1998, CEL transmitted and distributed all of the Republic's electricity.

Privatization of Electricity Distribution Facilities. In 1996, the Legislative Assembly approved the *Plan de Gestión del Servicio Público de Distribución de Energía Eléctrica* (the "Electricity Distribution Act") to privatize the electricity distribution companies in El Salvador. Prior to the privatization, CEL controlled the four primary operating electricity distribution companies: *Compañía de Alumbrado Eléctrico de San Salvador* ("CAESS"), *Empresa Eléctrica de Oriente* ("EEO"), *Distribuidora de Electricidad del Sur* ("DELSUR") and *Compañía de Luz Eléctrica de Santa Ana* ("CLESA"). Ownership of a smaller fifth company, *Distribuidora Eléctrica de Usulután* ("DEUSEM"), was divided equally between CEL, local governments and private investors. Pursuant to an auction in January 1998, CEL sold controlling interests in: (i) CAESS and EEO to a joint-venture between *C.A. La Electricidad de Caracas* (Venezuela) and Reliant Energy (United States); (ii) CLESA to AES El Salvador, an affiliate of AES Corporation (USA) ("AES") and (iii) DELSUR to Emel Group (Chile). Net proceeds (including a purchase price adjustment of US$12.5 million paid to AES) from the sale of the four companies were US$573.6 million. CEL retained less than 5.0% of the capital stock of each of the four electricity companies and the remaining capital stock was sold to employees of the companies and the public. During 2002, CEL sold approximately 1.2% of the capital stock of the companies to the public for approximately $3.0 million. In 2004, CEL sold additional shares to the public for US$2.5 million. The government may sell its remaining interests in the distribution companies at a future date.

From the net proceeds of the initial privatization (including sales to employees and the public), which amounted to US$581.4 million, US$320.0 million was used to repay short-term foreign currency debt and US$104.8 million was used to finance certain social and infrastructure projects. Subsequently, CAESS purchased DEUSEM from each one of its original owners in three stages during the second half of 1998. In June 2000, AES, the parent company of CLESA, acquired *C.A. Le Electricidad de Caracas* and, thereby, its indirect interests in CAESS, EEO and DEUSEM, and in the fourth quarter of 2000, AES acquired Reliant Energy's interests in CAESS, EEO and DEUSEM.

Privatization of Electricity Generation Facilities. The Electricity Distribution Act also provides for the restructuring of CEL for the privatization of electricity generation facilities. On July 30, 1999, after a bidding process, Duke Energy International El Salvador acquired 80.0% of the capital stock of the companies holding the thermal assets of CEL for a purchase price of US$125.1 million. In August 1999, the remaining 20.0% of the capital stock was sold to employees. On June 3, 2002, Enel Green Power of Italy entered into an agreement with *Geotérmica de El Salvador,* a wholly owned subsidiary of CEL, for the exploration and testing of geothermal wells. Pursuant to the agreement, Enel Green Power acquired approximately 8.5% of *Geotérmica de El Salvador* and, based on the outcome of the exploration and testing, may acquire additional shares in exchange for an investment in *Geotérmica de El Salvador.*

Transportation Privatization. The Republic has approximately 10,886 kilometers of roads. Two major highways cross the country: the Pan-American highway links the Republic with Guatemala in the west and Honduras in the east; and the *Carretera Litoral,* which runs south of the Pan-American highway, links Sonsonate to the west and Zacatecoluca and Usulután to the east. These roads frequently have been affected by natural disasters. As part of the Peace Accord, the government launched a program to restore the country's roads and bridges with funding of US$195.0 million from the Inter-American Development Bank, US$85.4 million from Japan and US$19.0 million from the *Banco Centroamericano de Integración Económica.* The Republic has outsourced the maintenance of roads to private companies formed by

former Ministry of Public Works employees who purchased the maintenance equipment from the government.

The Republic has two main seaports, Cutuco, to the east of San Salvador, and Acajutla, the major cargo seaport, to the west of San Salvador. The *Comisión Ejecutiva Portuaria Autónoma* (the Autonomous Executive Ports Commission or "CEPA") administers these ports and the international airport. The government has contracted with private companies owned by former port facilities employees for loading and unloading services at port facilities. In September 2002, the Legislative Assembly enacted the *Ley General Marítimo Portuaria* (the General Sea Ports Law) establishing, among other matters, the regulation of the construction, rehabilitation, and operation of the national port facilities. In October 2002, the Legislative Assembly announced the terms of reference for the concession of port facilities at Acajutla. No concessions were awarded out of the bidding process in 2004 since none of the bidding parties met the terms of reference requirements. The government expects the concession of these port facilities to be completed in 2005.

The El Salvador International Airport is located 40 kilometers south of San Salvador and is served by a number of international airlines. In March 1998, the government completed a US$14.5 million expansion program for the airport and concessions have been granted to private companies for a number of facilities and services at and near the airport. The government is currently evaluating a possible public tender for the privatization of other facilities at the airport, possibly through concessions.

Privatization of the Pension System. The government reformed the country's pension system effective on April 15, 1998 with the creation of a new private pension system. See "The Salvadoran Economy — Employment and Wages — Pension Reform."

Effects of Reforms

As a result of the implementation of these laws and programs, the economy experienced increases in consumer spending that caused real GDP to grow at an average annual rate of 6.9% from 1992 to 1995. During the same four-year period, imports increased from US$2.1 billion in 1992 to US$3.7 billion in 1995, funded by a 117.0% increase in lending to the private sector from ¢13.3 billion in 1992 to ¢29.0 billion in 1995. The reforms during the 1992 to 1995 period laid the foundation for stability in future periods. During the period from 1996 to 2003, the average rate of growth of real GDP slowed to 2.6% compared with 4.0% in the period from 1992 to 2003, due in large part to natural phenomena and increases in world oil prices and decreases in coffee prices in the international market as well as the slow-down in the U.S. economy in 2001 and 2002. In 2003, real GDP grew at a rate of 1.8%, compared to 2.2% during 2002.

After reaching 19.9% in 1992, inflation in El Salvador fell to 7.4% for 1996 and to 2.5% for 2003.

Between 1992 and 2003, El Salvador's trade and services deficit grew from US$1.1 billion to US$2.8 billion. This trade gap has been largely offset by the high volume of worker remittances from Salvadorans abroad, which first exceeded US$1.0 billion during 1995 and totaled US$2.1 billion in 2003, an increase of 8.8% from 2002. See "Foreign Trade and Balance of Payments."

Exports of goods and services increased from US$1.4 billion in 1993 to approximately US$4.1 billion in 2003, largely as a result of measures taken to eliminate trade barriers through tariff reductions and to establish free trade zones (areas free from import or export duties and with an income tax exemption) and rebates for nontraditional exported goods manufactured outside of a free-trade zone. Primarily as a result of the Monetary Integration Act, average interest rates on short-term and long-term loans fell to 6.35% and 7.65%, respectively, for the month of June 2004, compared to 12.2% and 13.7%, respectively, for the month of December 2000. As of December 31, 2003, 93.5%, or US$604.1 million, of all cash in circulation was in US dollars. The domestic currency interest rate (passive basic rate — 180 days) decreased from 7.1% at December 31, 2000 to 3.4% at June 30, 2004. Foreign direct investment in the financial system in El Salvador was US$15.8 million in 2000. From January 1, 2001, the effective date of the Monetary Integration Act, to December 31, 2003, the investment level was US$69.1 million.

Gross Domestic Product

The following table sets forth the Republic's real GDP growth for the periods presented.

Real GDP and Real GDP Growth by Economic Sector

	For the Year Ended December 31,				
	1999	2000	2001	2002(1)	2003(1)
Real GDP (in millions of colones)(2)	¢56,029.5	¢57,235.8	¢58,214.1	¢59,512.2	¢60,602.7
Real GDP growth(2)	3.4%	2.2%	1.7%	2.2%	1.8%
Real GDP growth by sector:					
Manufacturing	3.7	4.1	4.0	2.9	2.3
Trade, restaurants and hotels	2.0	3.6	1.9	1.5	1.2
Agriculture, livestock and fishing	7.7	(3.1)	(2.6)	0.1	0.1
Transportation, storage and communications	9.5	6.1	4.3	5.0	2.5
Residential leasing	0.5	1.5	(2.9)	3.8	3.1
Government services(3)	1.6	0.9	0.6	(3.5)	0.0
Community, social, personal, and domestic services(4)	0.3	1.4	(1.1)	1.8	1.3
Construction	(1.8)	(3.4)	9.6	6.7	4.7
Finance and insurance	12.0	7.7	1.6	0.7	1.8
Real estate and business services(5)	0.2	1.5	1.9	2.6	1.5
Electricity, gas and water	2.7	(2.3)	4.7	7.3	3.1
Mining	0.4	(4.7)	11.7	5.5	4.0

(1) Preliminary data.

(2) Based on constant 1990 prices.

(3) Includes wages and fringe benefits paid by the government to its employees.

(4) Includes education and private health care services, entertainment (cinemas and television), and other services such as veterinary services, services provided by commercial, professional, labor and religious associations, and repair and maintenance services provided by electricians, technicians, etc.

(5) Includes leasing and use of non-residential real estate and professional, legal, accounting and similar services.

Source: *Banco Central de Reserva de El Salvador.*

After centuries of dependence upon agricultural products, the Salvadoran economy has increasingly come to rely on industrial production, which accounted for 23.0% of GDP in 2003. In 2003, agricultural products represented 8.5% of Salvadoran GDP compared to 17.5% in 1975. Traditionally, coffee has been the main agricultural product of the Republic and typically represents the largest agricultural component of GDP. See "— Principal Sectors of the Economy."

As measured by real growth in GDP, economic growth in El Salvador averaged 4.0% per year from 1992 to 2003 and 2.3% per year from 1999 to 2003. Following the signing of the Peace Accord, private consumption grew in real terms by 4.6% per year from 1992 to 2003 and 2.9% per year from 1999 to 2003. Increased private consumption was satisfied largely with imports of goods (excluding *maquila*), which increased from US$1.7 billion in 1992 to US$4.4 billion in 2003 and was fueled by an increase in lending by banks to the private sector from US$1.5 billion in 1992 to US$6.0 billion for 2003.

Real GDP increased at a rate of 2.2% in 2000, as compared to 3.4% in 1999. External and internal causes contributed to the slower growth of real GDP experienced in 2000. The rise in international oil prices dampened domestic production by creating additional expenditures for oil derivatives products. In

addition, the fall in international prices of coffee and other agricultural products affected the growth of internal demand and income. For example, the unfavorable international market price of coffee provided less incentive for harvesters to produce coffee in 2000. Further, higher costs in the construction industry caused the delay of many projects leading to a contraction of the agricultural sector.

Real GDP grew at a rate of 1.7% in 2001 and 2.2% in 2002. The growth rate in 2001 was negatively affected by the impact of the earthquakes in January and February 2001, the decrease in the growth rate of the *maquila* sector primarily as a result of the slow-down of the U.S. economy in 2001, continued low international prices of coffee and high international oil prices. These negative factors were offset by investment expenditures relating to the reconstruction after the earthquakes as well as the effect lower interest rates had on consumption and investment. In 2002, the primary sectors contributing to economic growth were the construction sector, including continued investment expenditures relating to the reconstruction effort, the manufacturing sector and the services sector. The increase in the real GDP growth rate in 2002 occurred despite low international coffee prices and a reduction of general external demand, particularly from the United States.

Real GDP growth in 2003 slowed to 1.8%, compared to 2.2% in 2002. The growth rate in 2003 was negatively affected by the decline in international demand for coffee and non-traditional exports and the decrease in public investment following the completion of certain reconstruction projects. These factors had an impact on the manufacturing, construction, transportation, and trade sectors which collectively contributed to 57.0% of real GDP.

Principal Sectors of the Economy

The following table sets forth El Salvador's nominal GDP by economic sector for the periods presented.

Nominal GDP by Economic Sector

	For the Year Ended December 31,									
	1999	% of GDP	2000	% of GDP	2001	% of GDP	2002(1)	% of GDP	2003(1)	% of GDP
	(In millions of US dollars, except for percentages)									
Manufacturing	$ 2,815	22.6%	$ 3,031	23.1%	$ 3,191	23.1%	$ 3,318	23.2%	$ 3,432	23.0%
Trade, restaurants and hotels	2,374	19.0	2,546	19.4	2,660	19.3	2,742	19.2	2,826	18.9
Transportation, storage and communications	1,040	8.3	1,116	8.5	1,202	8.7	1,281	9.0	1,348	9.0
Agriculture, livestock and fishing	1,306	10.5	1,286	9.8	1,301	9.4	1,217	8.5	1,264	8.5
Residential leasing	987	7.9	1,032	7.9	1,036	7.5	1,098	7.7	1,143	7.6
Community, social, personal, and domestic services	820	6.6	882	6.7	947	6.9	1,035	7.2	1,091	7.3
Government services	945	7.6	972	7.4	988	7.2	1,000	7.0	1,038	6.9
Construction	533	4.3	572	4.4	647	4.7	687	4.8	727	4.9
Finance and insurance	519	4.2	571	4.3	603	4.4	621	4.3	646	4.3
Real estate and business services	513	4.1	533	4.1	567	4.1	606	4.2	627	4.2
Electricity, gas and water	248	2.0	222	1.7	237	1.7	256	1.8	256	1.7
Mining	53	0.4	53	0.4	57	0.4	65	0.5	69	0.5
Plus: tariffs and value added tax	811	6.5	862	6.6	953	6.9	980	6.8	1,079	7.2
Less: imputed financial services(2)	501	(4.0)	544	(4.1)	577	(4.2)	593	(4.1)	605	(4.0)
Total	$12,465	100.0%	$13,134	100.0%	$13,813	100.0%	$14,312	100.0%	$14,941	100.0%

(1) Preliminary data.

(2) Imputed financial services include the difference between interest accrued and interest paid by the financial sector.

Source: *Banco Central de Reserva de El Salvador.*

Manufacturing

In recent years, manufacturing has become a key sector of the Salvadoran economy. Since 1999, the manufacturing sector has generated an annual average of 23.3% of the Republic's real GDP and increased from 1999 to 2003 by 14.0% in real terms. Manufacturing was one of the fastest growing sectors of the Salvadoran economy during the period from 1999 to 2003, increasing at an average annual rate of 3.4% in real terms compared to an annual average of 2.3% for real GDP from 1999 to 2003. *Maquila* activity has been the most important component of the manufacturing sector.

The following table sets forth production (at constant 1990 prices) of El Salvador's principal manufacturing activities for the periods presented.

Principal Manufacturing Activities

	For the Year Ended December 31,				
	1999	2000	2001	2002(1)	2003(1)
	(In millions of colones) (2)				
Maquila (assembly for re-export)	¢ 1,416.6	¢ 1,712.0	¢ 1,829.6	¢ 1,871.8	¢ 1,967.3
Baked goods	1,088.2	1,110.2	1,184.6	1,187.7	1,238.8
Chemicals	1,165.0	1,101.6	1,146.7	1,188.6	1,207.6
Beverages	1,089.3	1,146.0	1,211.7	1,220.8	1,135.3
Other processed foods	786.1	839.6	886.2	953.8	988.2
Sugar	896.7	934.9	964.5	946.0	980.1
Printing and related industries	632.1	619.4	666.7	734.7	766.3
Non-metallic mineral products	556.8	569.0	611.6	676.2	727.6
Textiles	751.5	762.9	710.1	703.4	719.6
Refined oil products	682.0	665.1	696.3	711.0	710.2
Metallic mineral products	574.9	593.4	614.1	628.0	641.9
Transport supplies and diverse manufacturing products	436.6	469.5	484.5	503.3	529.0
Leather and related products	500.3	514.8	514.9	510.2	464.8
Milk products	378.5	399.7	412.7	426.9	452.1
Machinery and equipment	436.7	421.0	422.4	440.5	429.1
Paper and cardboard	306.9	328.6	352.3	396.8	407.2
Plastic products	296.8	316.8	333.7	336.2	354.1
Apparel	262.7	267.4	250.3	253.4	265.9
Meat packaging and related products	238.9	247.0	258.8	250.3	264.5
Lumber and related products	156.7	159.0	159.4	166.0	179.1
Other	1.1	0.8	0.9	0.7	0.9
	¢12,654.3	¢13,178.8	¢13,712.0	¢14,106.4	¢14,429.3

(1) Preliminary data.

(2) In constant 1990 prices.

Source: *Banco Central de Reserva de El Salvador.*

Maquila (assembly for re-export) experienced the most dynamic activity within the manufacturing sector, increasing in real terms from ¢1,416.6 million in 1999 to an estimated ¢1,967.3 million in 2003. This represents an increase of 38.9% during that period. *Maquila* increased 5.1% in real terms in 2003 compared with 2.3% for the manufacturing sector as a whole. The *maquila* growth rate slowed in 2002 and 2003, compared to 2000 and 2001, when it grew at a rate of 20.9% and 6.9%, respectively, largely as a result of the slow-down in the U.S. economy. Nonetheless, the level of *maquila* production in 2003 was at its highest historical level.

According to the Ministry of Economy, as of December 31, 2003, there were 265 *maquila* plants, 115 of which are located in free-trade zones, with the remaining 150 operating outside the geographic boundaries of the free-trade zones. Over half of the *maquila* plants established in the free-trade zones produce apparel and linens, mainly for export to the United States. Companies that operate in a free-trade zone are exempt from import and export duties and enjoy a ten-year exemption from income taxes, provided the manufactured goods are exported outside of Central America. Firms that operate outside of a

free-trade zone and that do not export 100.0% of their production are entitled to a 6.0% rebate on exports of non-traditional goods outside of Central America. See "Foreign Trade and Balance of Payments — Composition of Foreign Trade."

Trade, Restaurants and Hotels

Trade, restaurants and hotels accounted for an estimated 18.9% of the Republic's nominal GDP in 2003. From 1999 to 2003, this sector grew by an average annual real rate of 2.0%. Growth in the trade sector slowed during the period from 1999 to 2003, compared with a 6.3% growth rate in the period from 1992 to 1998 due to higher private consumption in the earlier period. Growth in the restaurant and hotel industries largely follows patterns of tourism. Tourism to El Salvador increased after the signing of the Peace Accord in 1992, but has subsequently decreased and was particularly adversely affected by the September 11, 2001 terrorist attacks in the United States. Accordingly, the restaurant and hotel industries' rate of growth has slowed as well. In June 2004, the new government under President Saca created a new ministry within the executive branch, the Ministry of Tourism, that was charged with the task of promoting and revitalizing tourism in El Salvador.

Agriculture, Livestock and Fishing

Agriculture, livestock and fishing accounted for an estimated 8.5% of the Republic's nominal GDP during 2003. In contrast with the 2.3% average annual real growth of the Republic's GDP during the 1999-2003 period, this sector grew at an average real annual rate of 0.4% during the period. The decrease in the percentage that agriculture represents of the Republic's GDP is the result of several factors, including: increases in activity in other sectors of the Salvadoran economy, particularly *maquila;* increasing urbanization of the population; and the volatility of coffee prices. Total land dedicated to the cultivation of traditional products (coffee, sugar, cotton, corn, beans, rice and sorghum) decreased 14.7% from 1980 to 2002. The agriculture, livestock and fishing sector grew by 0.1% in real terms in 2002 primarily as a result of a higher volume of production of basic grains and poultry, especially eggs. Growth in the sector was affected, however, by the decline in the international prices of coffee and sugar and the decrease in activity in the fishing sector. In 2003, the sector grew by 0.1% in real terms primarily as a result of an increase in production in the poultry and fishing sectors. The continued decline in the international price of sugar, a decrease in the volume of coffee produced and a decrease in activity in the basic grains sector contributed to the slow growth in 2003.

Coffee is El Salvador's principal agricultural export. Currently, there are an estimated 160,000 hectares devoted to the cultivation of coffee, representing approximately 7.7% of the country's land. In 2003, coffee accounted for 75.0% of agricultural exports and for 3.4% of total exports of goods. Proceeds from coffee exports decreased to US$105.4 million for 2003 compared with US$106.9 million in 2002 and US$115.1 million in 2001, primarily due to the decline in international coffee prices for 2002 as well as a decrease in volume of coffee produced as a result of coffee farmers' lower levels of investment in their plantations in 2003. Coffee is nevertheless an important source of employment in El Salvador and generated approximately 51,968 jobs in the 2002/2003 harvest, which accounted for 2.1% of employment nationwide. In recent years, coffee growers have experienced difficulties with the coffee pest, *la broca*(coffee berry borer).

In July 2000, the *Fondo de Emergencia para el Café* (the "Coffee Emergency Fund") was created by the Legislative Assembly to revitalize the coffee production industry by extending financing to coffee producers to enable them to repay debts related to their coffee production activity, thereby freeing funds for investment in the coffee industry. The Coffee Emergency Fund obtained US$80 million of proceeds through a December 2000 issuance of zero coupon eurobonds that mature in six month installments over a ten-year period and have an aggregate face amount at maturity of US$123,248,752. The Coffee Emergency Fund distributed the proceeds to coffee producers through the extension of financing. The Coffee Emergency Fund is administered by the Coffee Council, an autonomous public organization consisting of representatives from the government and private trade organizations.

With the exception of coffee, most agricultural production is for domestic consumption. The Republic generally permits the import of most agricultural products which meet established health standards, with the exception of poultry products. Since 1992, the *Ministerio de Salud* (Ministry of Health) has forbidden the import of all poultry products in an effort to limit several common avian diseases such as salmonella.

The following table sets forth the production (at constant 1990 prices) of certain major agricultural, livestock and fishing products for the periods presented.

Main Agricultural, Livestock and Fishing Products

	For the Year Ended December 31,				
	1999	2000	2001	2002(1)	2003(1)
	(In millions of colones) (2)				
Basic grains	¢1,416.6	¢1,301.9	¢1,295.2	¢1,387.7	¢1,376.4
Other agricultural	1,230.1	1,254.8	1,279.9	1,294.1	1,332.9
Livestock	1,219.5	1,249.0	1,250.5	1,266.9	1,289.7
Poultry	846.9	909.8	895.0	953.0	1,011.1
Coffee	1,549.3	1,325.2	1,140.1	981.7	861.0
Forestry	393.9	397.8	399.8	399.8	409.8
Sugar cane	424.2	418.5	408.2	399.6	392.2
Fishing	174.1	166.1	173.9	169.4	186.3
Cotton	5.4	8.9	3.6	3.8	3.8
	¢7,260.0	¢7,032.0	¢6,846.1	¢6,856.0	¢6,863.2

(1) Preliminary data.

(2) Based on constant 1990 prices.

Source: *Banco Central de Reserva de El Salvador.*

Transportation, Storage and Communications

From 1998 to 2003, the average annual real growth rate of 5.5% in the transportation, storage and communications sector was approximately double the 2.3% rate for the economy as a whole during the same period. Prior to the privatization of the telecommunications company, ANTEL, average annual real growth in the sector from 1993 to 1997 was similar to that of the entire economy. Communications was the leading subsector. The privatization program in this sector introduced greater competition to the industry as the multinational corporations acquiring assets of ANTEL made investments in network expansion. In 2003, the transportation, storage and communications sector grew by 2.5% primarily as a result of growth in the communications subsector due to the installation of new telephone lines.

Construction

Growth in the construction sector decreased in 1999 and 2000 by 1.8% and 3.4%, respectively, primarily due to delays in the approval of the general budget for 1999 and environmental regulation that limited the execution of large housing projects, higher construction costs and low growth in purchasing power and the deficiency of certain public institutions in the planning and the administration of projects. In 2001, the construction sector grew by 9.6% primarily as a result of the reconstruction effort following the earthquakes in January and February 2001, as well as increases in housing construction, which were partially attributable to falling interest rates in the country during 2001. Growth in the construction sector slowed to 6.7% in 2002, and to 4.7% in 2003, as a result of a lower level of activity related to the earthquake reconstruction effort.

Finance and Insurance

From 1999 to 2003, the financial services sector grew at an average annual real rate of 4.8%. This growth was primarily the result of an increase in lending to the private sector at an average annual rate of 3.6% during the same period. During 2003, the financial services sector grew by 1.8% compared to 0.7% in 2002. This higher growth rate was primarily due to increased activity in the sector generated by commercial banks and insurance.

Currently, there are 12 private retail banks, two state-owned retail banks, one state-owned mezzanine bank *(Banco Multisectorial de Inversiones)* which lends to commercial banks and financial institutions, and six non-bank financial institutions operating in El Salvador. At December 31, 2003, the Salvadoran commercial banks had total assets of US$10.1 billion, equivalent to approximately 67.8% of nominal GDP for 2003. The financial system also includes broker dealers, insurance companies and the El Salvador Stock Exchange. See "Monetary System — Financial Sector."

Employment and Wages

From 1992 to 2003, the labor force in El Salvador grew at an average annual rate of 3.1%, partly due to the greater participation of women in the labor force. Unemployment decreased from 7.0% in 1999 to 6.9% in 2003. The economic sectors with the greatest job generation during the 1999 to 2003 period were finance (annual average of 6.3%), services (annual average of 2.6%) and commerce (annual average of 2.5%). The percentage of workers in the informal sector of the economy appears to have remained constant during the same period, but the government has no official count of such workers.

El Salvador's labor law provides for a daily minimum wage, which was increased in the industrial sector to US$5.16 for 2003 from US$4.80 at which level it had been set since 1997 and has been set at US$2.47 in the agricultural sector since 1997. Minimum wages are set by a council composed of representatives from the government, the private sector and labor organizations. Minimum wages for each major sector of the economy are set taking into account the evolution of real wages and the overall economic situation. The legal workday is eight hours and the legal workweek is 44 hours. The law prohibits employment of minors under the age of 14 unless such employment is necessary for family sustenance and does not interfere with schooling.

The law prohibits actions against workers seeking to organize. Unions and strikes are only legal in the private sector. Public sector workers may form associations but are not legally allowed to strike. Pursuant to an amendment to the Civil Service Law enacted December 19, 2001, the government has the ability to terminate the appointment of public sector employees.

The following table sets forth daily minimum wages by economic activity in effect for the periods presented.

Daily Minimum Wages by Economic Sector

	Agriculture	Coffee(1)	Sugar(1)	Cotton(1)	Industry	Commerce and Services	Construction
				(In US dollars)			
1999	2.47	2.47	2.47	2.47	4.80	4.80	5.57
2000	2.47	2.47	2.47	2.47	4.80	4.80	6.40
2001	2.47	2.47	2.47	2.47	4.80	4.80	6.70
2002	2.47	2.47	2.47	2.47	4.80	4.80	6.90
2003	2.47	2.47	2.47	2.47	5.16	5.28	7.00

(1) Excluding seasonal workers who are guaranteed minimum wages at different levels.

Source: *Diario Oficial* (Official Gazette of El Salvador).

Social Security

El Salvador's Constitution provides for the guarantee of social security benefits to workers and their families. Social security benefits provide assistance in case of accidents, illness, maternity, disability, retirement and death. Participation in the social security system for coverage for accident, illness, maternity and disability is mandatory for all individuals, except for teachers in the public sector and self-employed individuals. These benefits are administered by the *Instituto Salvadoreño del Seguro Social* (the "Salvadoran Social Security Institute").

Retirement and death benefits for public and private sector workers who remained in the public pension system after the pension reform in 1998 are provided by the *Instituto Nacional de Pensiones de los Empleados Públicos* (the "National Public Pension Institute") and the Salvadoran Social Security Institute through a separate governmental system. The government provides medical services to the population not covered by the Salvadoran Social Security Institute or the National Public Pension Institute through a network of 30 hospitals and 579 health facilities across the country.

The social security system is financed through a combination of contributions from workers and employers. As of January 1, 2003, all employees, except for teachers in the public sector and self-employed individuals, contribute 3.0% of their salary and employers contribute 7.5% of their total payroll for accident, illness, maternity and disability benefits. Teachers in the public sector contribute the same percentage to the *Bienestar Magisterial* for the same benefits provided by the Salvadoran Social Security Institute. For retirement and death benefits, private sector employees contribute 7.0% of their salary and employers contribute 7.0% of their total payroll to the Salvadoran Social Security Institute and public sector employees contribute 7.0% of their salary and their employers contributed 7.0% of their total payroll to the National Public Pension Institute.

During 2003, healthcare unions held strikes at several hospitals demanding that the government guarantee that the Salvadoran Social Security Institute would not be privatized and that the government negotiate a collective bargaining agreement with the healthcare unions and re-hire dismissed and suspended strikers. The strikes ended in the middle of 2003 when the government withdrew the proposed legislation to which healthcare unions objected and agreed to reinstate the strikers with payment for back wages.

The following table sets forth the distribution of workers in the private sector by economic sector and as a percentage of the labor force in the private sector contributing to the Salvadoran Social Security Institute by number and percentage for the periods presented. No comparable information is available for workers in the informal sector of the economy.

Contributors by Sector

	As of December 31,									
	1999		2000		2001		2002		2003(1)	
	Number	%	Number	%	Number	%	Number	%	Number	%
Industry	169,696	37.6%	176,012	38.8%	169,462	37.1%	168,639	36.2%	168,334	35.1%
Commerce	94,615	21.0	94,780	20.9	96,433	21.1	98,019	21.1	104,639	21.8
Finance	67,138	14.9	68,119	15.0	74,049	16.2	78,665	16.9	85,877	17.9
Services	56,449	12.5	56,893	12.5	59,003	12.9	62,022	13.3	62,535	13.0
Construction	29,532	6.5	25,334	5.6	26,155	5.7	27,072	5.8	26,259	5.5
Transport and Communication	20,118	4.5	19,989	4.4	18,380	4.0	17,558	3.8	17,352	3.6
Agriculture	10,493	2.3	9,665	2.1	9,933	2.2	10,030	2.2	10,751	2.2
Electricity, Gas and Water	2,721	0.6	2,781	0.6	3,027	0.7	2,691	0.6	2,846	0.6
Mining	781	0.2	529	0.1	541	0.1	604	0.1	610	0.1
Total	451,543	100.0%	454,102	100.0%	456,983	100.0%	465,300	100.0%	479,203	100.0%

(1) Preliminary data.

Source: *Instituto Salvadoreño del Seguro Social.*

Pension Reform

On December 20, 1996, the Legislative Assembly approved the creation of a private pension system for eligible workers (including both public sector employees and private sector employees) in El Salvador modeled on the then-existing Chilean system. The *Superintendencia de Pensiones* (the "Superintendency of Pensions") is responsible for overseeing both the public pension system and the private pension system. Private pension companies *(Administradoras de Fondos de Pensiones)* were authorized to operate by the pension system law on April 15, 1998. All workers 35 years old or younger were required to affiliate with a private pension company by April 15, 1999. Men between the ages of 36 and 55 and women between the ages of 36 and 50 had the option of continuing with the prior public pension system, or switching to the new private pension system, while women over the age of 50 and men over the age of 55 were not eligible to participate in the new private pension system and were required to remain in the prior public pension system. All workers entering the work force since April 15, 1998 have been required to participate in the private pension system, regardless of age. At March 31, 2004, 1,100,382 workers were covered by this private pension system. At March 31, 2004, there were 42,360 workers participating in the public pension system.

Beginning January 1, 2002, employees participating in the private pension system are required to contribute up to 6.25% of their salary on a monthly basis to a private pension fund (a portion of such amount represents commissions). Employers are required to contribute 6.75% to each worker's private pension fund account on a monthly basis. Only men who are 60 years old and women who are 55 years old, and who have contributed to the pension system for 25 years, are eligible to receive a monthly pension. Beginning July 2004, the option of retiring after contributing to the pension system for 30 years, regardless of age, is no longer available.

When employees who transferred to the private pension system retire, the government issues *Certificados de Traspaso* (Certificates of Transfer or "CTs") to the relevant private pension fund in order to credit the employees for their prior contributions to the public pension system. Beginning in January 2002, the CTs, as a result of reforms to the pension system law, are payable over a 15-year period commencing upon the date of the relevant employee's retirement. CTs were previously payable in one lump sum. In addition, from January 1, 2005, persons who have the option of continuing with the prior public pension system or switching to the new private pension system are eligible to receive a *Certificado de Traspaso Complimentario* (Complimentary Recognition Bond) that would compensate them for any difference between the value of the monthly pensions they would have received had they stayed in the prior public pensions system and the value of the monthly pensions if they shifted to the new private pension system.

The creation of the private pension system reduced by approximately 50.0% the net present value of the government's obligations with respect to pensions. The government currently estimates that the difference between contributions to the public pension system and benefits payable to retirees under the public pension system and partial benefits payable to retirees who switched to the private pension system for the time they were covered by the public pension system was 1.7% of GDP in 2003 and will increase thereafter to reach a projected peak deficit as a percentage of GDP of 2.3% in 2008. The accumulated deficit for the period from 2002-2005 could reach approximately US$1.1 billion.

FOREIGN TRADE AND BALANCE OF PAYMENTS

General

During the 1960s, El Salvador imposed tariff and non-tariff barriers to foreign competition in an effort to encourage the development of a domestic industrial base. By 1970, as a result of the country's shortage of natural resources, El Salvador imported 74.0% of its raw materials and 95.0% of its capital goods from countries outside the CACM. In an effort to reduce this import dependency, El Salvador introduced incentives to foreign investment, and the *maquila* industry developed in free-trade zones to take advantage of El Salvador's comparatively low labor costs.

With the reform programs begun in 1989 and the initiatives implemented after the signing of the Peace Accord, the export sector of the economy began to grow. By 2003, exports of goods and services accounted for 27.6% of nominal GDP. In 2003, imports accounted for 46.7% of nominal GDP, mostly in the form of intermediate goods (32.1% of total imports) and consumer goods (27.7% of total imports). Export earnings have grown 24.9% from 1999 to 2003 primarily as a result of higher *maquila* exports, which have grown steadily by an annual average rate of 8.9% from 1999 to 2003. Based on preliminary information, the trade and services deficit increased from 17.0% of nominal GDP during 2002 to 19.1% of nominal GDP during 2003, and the current account deficit of the balance of payments increased from 2.9% of nominal GDP in 2002 to 4.9% of nominal GDP in 2003 as a result of the increase in the trade and services deficit and the decrease in current account transfers (excluding remittances).

Tariffs and Other Trade Restrictions

Until the late 1980s, El Salvador used tariff barriers to protect its domestic industry against foreign competition. Import duties ranged from zero to 290.0%, with up to 25 different rates. Exports were largely controlled by the government, with the international commercialization of coffee and sugar in the hands of state-owned monopolies.

Since 1989, the Republic has significantly liberalized its foreign trade policy. The tariff structure has been simplified and currently consists of three principal rates: zero for capital goods, between 5.0% and 10.0% for intermediate goods and 15.0% for consumer goods. These three rates apply to approximately 90.0% of imports. There are some products with different rates, such as jewelry, fine arts, guns and ammunition. Import licenses have been eliminated for most goods and export license requirements have been replaced by reporting requirements primarily designed to ensure collection of data relating to foreign trade. The national coffee and sugar boards were dissolved, eliminating government involvement in these industries.

Regional Integration and Free Trade

El Salvador has benefited from regional trade initiatives that have opened up the markets of Central American nations to other nations in the region. Regional integration has been especially beneficial to the manufacturing sector. Increased access to international markets and liberalization of trade barriers are components of El Salvador's plan to increase international competitiveness, to improve export revenues and to encourage foreign investment. In recent years, the Republic has intensified its efforts to strengthen its trade arrangements with its primary trading partners including:

- entering into, along with several other Central American countries, a free trade agreement with the Dominican Republic that became effective on October 1, 2001;
- entering into, along with Guatemala and Honduras, a free trade agreement with Mexico that became effective on March 15, 2001;
- entering into, along with other Central American countries, a free trade agreement with Chile that became effective on June 1, 2002;
- entering into a free trade agreement with Panama that became effective on April 11, 2003;

- entering into, along with the other members of the Central America Economic Integration System, a free trade agreement with the United States on May 28, 2004, which the Dominican Republic also later signed on August 5, 2004 and which will become effective upon exchange of instruments of ratification;
- participating in the Free Trade Area of the Americas negotiations; and
- participating in free trade agreement negotiations with Canada.

Trade Initiatives Involving Central America

The opening of the markets of Central America began in 1960 when El Salvador, Guatemala, Honduras and Nicaragua (joined by Costa Rica in 1963) signed the General Treaty for Central American Economic Integration (the "General Treaty"), which provided the framework for the CACM. The CACM envisioned the creation of a customs union as a temporary step towards the creation of a common market similar to the European Union. In 1995, the five members of the CACM agreed to reduce gradually their external tariff structures for goods produced outside the Central American region. In January 2000, the Central American nations agreed to a tariff structure with, and Salvadoran tariffs are currently set at, three principal rates: 0.0% for capital goods; between 5.0% and 10.0% for intermediate goods; and 15.0% for consumer goods.

In early 1998, El Salvador and several Central American countries signed a free trade agreement with the Dominican Republic intended to create a free trade zone in accordance with WTO regulations. This agreement became effective on October 1, 2001. In October 1999, El Salvador, along with other Central American countries, entered into a free trade agreement with Chile that became effective on June 1, 2002. El Salvador, Guatemala and Honduras reached a free trade agreement with Mexico, which became effective for El Salvador on March 15, 2001. This free trade agreement with Mexico does not apply to trade between El Salvador and Guatemala or Honduras. On March 6, 2002, El Salvador and Panama entered into a free trade agreement that became effective on April 11, 2003.

Trade Initiatives Involving the United States and Canada

El Salvador has been a beneficiary of the CBI since 1983, when the United States government established the CBI to aid Central American and Caribbean countries. The CBI provides duty-free access to the U.S. market for certain goods manufactured and processed in CBI member countries. Excluded from the original list of duty-free products were beef, textiles, clothing, oil and oil derivatives. Sugar remains subject to quotas. The CBI also contains rules of origin which require that products must have at least 35 percent CBI-country content in order to be eligible for duty-free treatment.

On October 2, 2000, the United States declared El Salvador eligible for enhanced CBI benefits available under the Caribbean Basin Trade Partnership Act of 2000 (the "CBTPA"). The CBTPA significantly expands preferential treatment for apparel made in the Caribbean Basin region. Duty/quota-free treatment is provided for apparel made in the Caribbean Basin region from U.S. fabrics formed from U.S. yarns. Duty/quota-free treatment is also available for certain knit apparel made in CBTPA beneficiary countries from fabrics formed in the Caribbean Basin region, provided that U.S. yarns are used in forming the fabric. This "regional fabric" benefit for knit apparel is subject to an overall yearly limit, with a separate limit provided for T-shirts.

New duty/quota-free treatment is also available for apparel made in the Caribbean Basin region from fabrics determined to be in "short supply" in the United States, and for designated "hand-loomed, handmade or folklore" articles. In addition to these apparel preferences, the CBTPA provides NAFTA-equivalent tariff treatment for certain items previously excluded from duty-free treatment under the CBI program (e.g., footwear, canned tuna, oil products, watches and watch parts).

In December 1994, at the Summit of the Americas in Miami, the Presidents of the United States, the five Central American countries, Belize and Panama signed the *Conjunto Centroamericano-USA,* a partnership for sustainable development which commits its signatories to achieving a Free Trade Area of

the Americas by 2005. At the Summit of the Americas in Quebec City in April 2001, the parties reiterated their commitment to achieve a Free Trade Area of the Americas by 2005. On August 1, 2002, the U.S. Congress passed the Trade Act of 2002 which granted Trade Promotion Authority to the President of the United States permitting him to have full authority to negotiate trade agreements. After several rounds of negotiations, the United States signed on May 28, 2004 a free trade agreement with the five members of the Central America Economic Integration System. Subsequently, the Dominican Republic was added as a party to the free trade agreement, now referred to as the U.S.-Dominican Republic-Central America Free Trade Agreement ("DR-CAFTA"). The effectiveness of DR-CAFTA is subject to the approval of the respective legislatures of the parties to the agreement.

Under DR-CAFTA, El Salvador agreed to lower duties on U.S. products over a period of 20 years in the case of agricultural products and over a period of 10 years in the case of industrial products. Approximately 53.0% of U.S. farm exports, including high quality cuts of beef, cotton, wheat, soybeans, key fruits and vegetables, processed food products and wine, will become duty free once the treaty takes effect. Approximately 78.0% of U.S. industrial products, including information technology, agricultural and construction equipment, paper, chemicals and medical and scientific equipment also will enjoy immediate duty free access.

The United States, on the other hand, would immediately grant, once the treaty takes effect, duty free access to approximately 89.0% of El Salvador's agricultural products, including natural honey, certain fruit juices, carbonated drinks, beer, and other ethnic products such as *ajonjilo, loroco, queso duro, quesadillas, tamales,* and *pupusas.* El Salvador's other agricultural products would be granted duty free access within 20 years. In addition, almost all (99.73%) of El Salvador's industrial products exported to the United States would be given duty free access once the treaty takes effect. These products include canned tuna, jewelry, textiles, ready-to-wear clothing, footwear, crates, hooks and other products made of steel or iron.

With respect to sugar, El Salvador's present quota of 27,000 metric tons will be increased by an additional 24,000 metric tons upon effectiveness of the treaty. In succeeding years and until the year 2019, such additional quota will rise annually until 36,000 metric tons is reached. From 2020 onwards, the additional quota will rise annually by 680 metric tons. With respect to coffee products, a strict "rules of origin" will apply whereby only coffee cultivated in Central America or the United States would enjoy duty free access under the agreement. In addition, the benefits under the Caribbean Basin Initiative and other trade preferences with the United States will be maintained.

At the Canada-Central America Summit in Guatemala on September 28, 2000, the Prime Minister of Canada agreed to a request by the leaders of the Central American countries of El Salvador, Guatemala, Honduras and Nicaragua to pursue free trade negotiations. On November 21, 2001, the Canadian Minister for International Trade announced the launch of free trade negotiations. Canadian and Central American officials met for the tenth round of formal negotiations towards a bilateral free trade agreement in February 2004. Further rounds of negotiations may be held at a future date.

In addition, the Central American countries have established a dialogue with representatives of the European Union with a view to establishing an economic association, including a possible free trade agreement, between the two regions.

Composition of Foreign Trade

The Republic's largest trading partners are the United States, Guatemala and Honduras. The following table sets forth the country of destination of the Republic's exports for the periods presented.

Merchandise Exports by Country of Destination

	For the Year Ended December 31, (In millions of US dollars, except percentages)					Percentage of Total Exports	
	1999	2000	2001	2002(1)	2003(1)	1999	2003(1)
North America							
Canada	$ 9.4	$ 6.4	$ 5.0	$ 4.3	$ 6.1	0.4%	0.2%
Mexico	14.3	13.1	24.6	31.9	37.4	0.6	1.2
United States	1,576.5	1,919.6	1,873.6	2,006.9	2,121.1	62.8	67.6
Central America							
Belize	4.3	5.8	7.2	7.5	8.6	0.2	0.3
Costa Rica	91.9	85.7	94.6	106.6	102.0	3.7	3.3
Guatemala	284.1	318.8	323.2	344.0	361.2	11.3	11.5
Honduras	171.6	225.1	184.3	176.6	184.9	6.8	5.9
Nicaragua	91.1	107.5	120.3	113.2	98.1	3.6	3.1
South America and the Caribbean							
Chile	6.0	1.6	1.9	0.3	0.7	0.2	0.0
Dominican Republic	14.2	12.3	12.4	20.8	22.2	0.6	0.7
Panama	35.4	39.0	48.9	45.0	46.3	1.4	1.5
Puerto Rico	4.8	3.6	4.2	3.4	3.8	0.2	0.1
Venezuela	1.6	1.2	6.5	4.6	3.9	0.1	0.1
Europe							
Benelux(2)	24.9	18.0	5.8	5.0	6.6	1.0	0.2
Germany	105.2	94.4	48.8	36.4	31.3	4.2	1.0
Other	74.7	89.2	102.5	89.5	101.9	3.0	3.2
Total	$2,510.0	$2,941.3	$2,863.8	$2,996.0	$3,136.1	100.0%	100.0%

(1) Preliminary data.

(2) Belgium, Netherlands and Luxembourg.

Note: The average exchange rate for each year has been used to translate *colones* into US dollars. See "Offering Circular Summary — Selected Economic Indicators."

Source: *Banco Central de Reserva de El Salvador.*

In 2003, 24.1% of El Salvador's merchandise exports went to Belize and the Central American countries, compared to 25.6% in 1999. Primarily as a result of the free trade agreement with Mexico that became effective in 2001, exports to Mexico in 2003 increased by 185.5% compared to 2000, although they still represented only 1.2% of total exports in 2003. Exports to the United States increased from 62.8% of the Republic's total exports in 1999 to 67.6% in 2003. Exports to the United States consist primarily of *maquila* products, coffee, sugar, shrimp, apparel and textiles.

The following table sets forth the composition of the Republic's major exports for the periods presented.

Merchandise Exports (FOB) by Groups of Products

	For the Year Ended December 31,					Percentage of Total Exports	
	1999	2000	2001	2002(1)	2003(1)	1999	2003(1)
	(In millions of US dollars, except percentages)						
Maquila	$1,333.4	$1,609.0	$1,650.3	$1,757.9	$1,881.2	53.1%	60.0%
Agricultural products							
Coffee	245.1	298.0	115.1	106.9	105.4	9.8	3.4
Other	22.7	35.1	35.8	36.0	34.9	0.9	1.1
Manufacturing							
Paper	80.0	90.2	100.0	128.2	122.9	3.2	3.9
Textiles	145.0	151.2	146.6	157.3	156.7	5.8	5.0
Shoes and footwear	15.0	18.9	19.1	17.7	19.2	0.6	0.6
Food, beverages and tobacco	173.6	182.6	227.5	223.0	239.9	6.9	7.6
Chemicals	151.2	152.11	154.9	157.5	149.8	6.0	4.8
Mineral products	66.9	81.0	85.3	68.6	67.2	2.7	2.1
Animal products							
Shrimp	24.2	15.6	18.9	9.5	10.8	1.0	0.3
Other	22.8	31.8	20.4	23.8	36.1	0.9	1.2
Other	230.1	275.8	289.9	309.6	312.0	9.2	9.9
Total	$2,510.0	$2,941.3	$2,863.8	$2,996.0	$3,136.1	100.0%	100.0%

(1) Preliminary data.

Note: The average exchange rate for each year has been used to translate *colones* into US dollars. See "Offering Circular Summary — Selected Economic Indicators."

Source: *Banco Central de Reserva de El Salvador.*

Maquila exports have been the primary driver of the Republic's increased exports from 1999 to 2003, increasing by 41.1% during such period. By contrast, coffee exports fell by 57.0% during the same period. A decline in international coffee prices as well as a decrease in volume of coffee produced as a result of the earthquakes in the early part of 2001 contributed to decreased coffee exports from 2001 to 2003.

Excluding *maquila* exports, the products which experienced rates of growth in value greater than 25% in 2003 compared to 2002 were electrical energy, denaturalized ethyl alcohol, tuna, milled products and other fish, crustaceans and mollusks products. For the first half of 2004, non-*maquila* exports which experienced rates of growth in value greater than 25% compared with the first half of 2003 were fruits, vegetables and pulses, refined petroleum products, denaturalized ethyl alcohol, other fish, crustaceans and mollusks products, plastic bottles and containers and mineral products.

The following table describes the origin of the Republic's imports during the periods presented.

Merchandise Imports (CIF) by Country of Origin

	For the Year Ended December 31,					Percentage of Total Imports	
	1999	2000	2001	2002(1)	2003(1)	1999	2003(1)
	(In millions of US dollars, except percentages)						
North America							
Canada	$ 29.9	$ 34.8	$ 37.4	$ 34.2	$ 48.8	0.7%	0.8%
Mexico	264.0	257.3	312.4	294.6	315.6	6.4	5.5
United States	2,110.1	2,451.2	2,462.5	2,577.3	2,869.2	51.5	49.8
Central America							
Costa Rica	116.2	143.6	163.4	149.0	157.4	2.8	2.7
Guatemala	384.5	478.1	435.4	418.6	463.6	9.4	8.0
Honduras	87.7	119.5	134.7	155.2	134.9	2.1	2.3
Nicaragua	64.6	69.8	87.5	97.5	111.6	1.6	1.9
South America and the Caribbean							
Argentina	8.9	7.9	11.7	13.6	27.2	0.2	0.5
Brazil	33.5	41.5	52.0	82.2	116.7	0.8	2.0
Colombia	37.5	27.5	35.0	40.1	65.0	0.9	1.1
Chile	13.9	22.0	15.8	22.9	43.8	0.3	0.8
Ecuador	81.6	152.3	127.4	152.5	168.3	2.0	2.9
Panama	98.3	129.7	135.1	156.2	126.0	2.4	2.2
Peru	7.2	7.3	13.1	24.8	12.9	0.2	0.2
Venezuela	43.5	64.9	82.3	78.7	139.3	1.1	2.4
Europe							
Benelux(2)	28.8	25.7	33.0	18.9	35.0	0.7	0.6
Germany	74.5	75.9	89.0	81.0	91.6	1.8	1.6
Japan	126.7	122.5	124.4	136.2	132.8	3.1	2.3
Other	483.3	715.9	674.1	658.6	703.0	11.8	12.2
Total	$4,094.7	$4,947.4	$5,026.6	$5,192.1	$5,762.7	100.0%	100.0%

(1) Preliminary data.

(2) Belgium, Netherlands and Luxembourg.

Note: The average exchange rate for each year has been used to translate *colones* into US dollars. See "Offering Circular Summary — Selected Economic Indicators."

Source: *Banco Central de Reserva de El Salvador.*

The United States is the principal source of El Salvador's imports. Imports from the United States consist primarily of raw materials for *maquila,* automobiles, oil products, paper and corn. Imports from the United States increased by 36.0% from 1999 to 2003, although they decreased from 51.5% of the Republic's total imports in 1999 to 49.8% in 2003. During the same period, the trade deficit of El Salvador with the United States increased from US$533.6 million in 1999 to US$748.1 million in 2003.

The following table sets forth the composition of the Republic's imports for the periods presented.

Merchandise Imports (CIF) by Type of Goods

	For the Year Ended December 31,					Percentage of Total Imports	
	1999	2000	2001	2002(1)	2003(1)	1999	2003(1)
	(In millions of US dollars, except percentages)						
Consumer Goods	$1,004.5	$1,218.4	$1,279.6	$1,368.4	$1,593.5	24.5%	27.7%
Non-durable	837.0	1,041.0	1,104.4	1,183.9	1,321.0	20.4	22.9
Durable	167.5	177.4	175.2	184.5	272.5	4.1	4.7
Intermediate Goods	1,318.4	1,617.8	1,685.1	1,660.0	1,851.0	32.2	32.1
Manufacturing	1,004.5	1,238.4	1,270.1	1283.6	1,444.8	24.5	25.1
Agriculture	85.1	99.0	96.9	88.7	97.1	2.1	1.7
Construction	166.8	192.0	254.4	225.5	249.4	4.1	4.3
Other	62.0	88.4	63.7	62.2	59.7	1.5	1.0
Capital Goods	817.1	958.5	901.3	881.0	937.3	20.0	16.3
Manufacturing	222.9	227.4	280.9	251.8	269.4	5.4	4.7
Transport	396.4	413.3	355.4	349.0	387.7	9.7	6.7
Agriculture	16.4	12.7	13.9	13.7	12.5	0.4	0.2
Construction	53.0	39.1	50.6	81.9	79.9	1.3	1.4
Other	128.4	266.0	200.5	184.7	187.8	3.1	3.3
Maquila	954.7	1,152.7	1,160.6	1,282.7	1,380.9	23.3	24.0
Total	$4,094.7	$4,947.4	$5,026.6	$5,192.1	$5,762.7	100.0%	100.0%

(1) Preliminary data.

Note: The average exchange rate for each year has been used to translate *colones* into US dollars. See "Offering Circular Summary — Selected Economic Indicators."

Source: *Banco Central de Reserva de El Salvador.*

Corresponding to the growth of *maquila* exports during the 1999 to 2003 period, *maquila* imports, as a percentage of total imports of goods, increased from 23.3% in 1999 to 24.0% in 2003. The increase in remittances from abroad during the period helped increase imports of non-durable consumer imports from 20.4% of total imports in 1999 to 22.9% in 2003.

Balance of Payments

The Republic's current account of its balance of payments for the past several years has been characterized by deficits, which have been, except in 2001, substantially offset by capital account surpluses. The negative balances in the current account have been the result of trade deficits and have been partially offset by remittances from Salvadorans working abroad. Capital account surpluses resulted in a positive balance of payments in each year in the eight year period ended on December 31, 1999. The negative balance of payments in 2000 reflected an increase of US$191.2 million of the current account deficit attributable to growth in imports and a fall in capital inflow of US$62.1 million compared to 1999 levels. In 2001, the negative balance of payments was primarily the result of a US$150.3 million deficit in the current account. Unlike prior years, the deficit in the current account in 2001 was not offset by a capital account surplus as the capital account had a US$27.4 million deficit. In 2002, the balance of payments remained negative primarily as a result of a US$261.5 million increase in the current account deficit that was only partially offset by a US$288.3 million capital account surplus.

At the end of 2003, the Republic's current account deficit reached US$733.6 million. However, the balance of payments was positive since capital account inflows from increased debt incurred by all sectors offset the current account deficit.

The following table sets forth the Republic's balance of payments for the periods presented.

Balance of Payments

	For the Year Ended December 31,				
	1999	2000	2001	2002(1)	2003(1)
	(In millions of US dollars, except percentages)				
Current account	$ (239.3)	$ (430.5)	$ (150.3)	$ (411.8)	$ (733.6)
Trade and services balance	(1,820.8)	(2,227.6)	(2,448.6)	(2,434.6)	(2,850.7)
Exports (FOB goods and services)	3,287.8	3,802.9	3,764.1	3,961.7	4,127.0
Imports (CIF goods and services)	5,108.6	6,030.5	6,212.7	6,396.3	6,977.7
Transfers	1,581.5	1,797.1	2,298.3	2,022.8	2,117.1
Private	1,553.4	1,769.0	2,258.9	1,997.5	2,103.5
Remittances	1,373.8	1,750.7	1,910.5	1,935.2	2,105.3
Public(2)	28.1	28.1	39.4	25.3	13.6
Capital account balance	447.1	385.0	(27.4)	288.3	1,049.8
Public sector	188.0	56.6	427.3	776.8	396.0
Central Bank	(15.0)	(10.7)	(40.5)	(27.7)	168.7
Financial sector	30.8	(34.4)	(235.1)	65.9	384.5
Private sector(3)	243.3	373.5	(179.1)	(526.7)	100.6
Change in international reserves	207.8	(45.5)	(177.7)	(123.5)	316.2
Current account surplus (deficit) for the balance of payments/Nominal GDP	(1.9)%	(3.3)%	(1.1)%	(2.9)%	(4.9)%

(1) Preliminary data.

(2) Includes transfers to the central government and other governmental entities.

(3) Includes errors and omissions in the statistical compilation.

Note: The average exchange rate for each year has been used to translate *colones* into US dollars. See "Offering Circular Summary — Selected Economic Indicators."

Source: *Banco Central de Reserva de El Salvador.*

Current Account

In the years following the signing of the Peace Accord, the trade deficit grew from US$1.1 billion for 1992 to approximately US$1.8 billion for 1999 and approximately US$2.8 billion for 2003. The increase in the trade deficit reflects the growth of imports at a higher rate than the growth of exports during the period. Imports have been fueled during the period by increases in remittances from abroad while lower international coffee prices in recent years restrained the growth in exports. In addition, since 2000, higher petroleum prices have had a negative impact on the current account, particularly in 2003.

Transfers from abroad in the form of worker remittances increased from US$858.3 million in 1992 to US$2,105.3 million in 2003. Due to the number of Salvadorans who emigrated to escape the civil war, worker remittances have been a significant factor in the composition of the Republic's current account, and in 2003 represented approximately 33.7% of all current account inflows in the balance of payments.

The impact of these remittances on the Republic's balance of payments has been two-fold. First, by raising national income, worker remittances increase private consumption of foreign and domestic goods and services, thereby creating inflationary pressures. Second, by partially funding the increased demand for

imports, the inflow of worker remittances has reduced the current account deficit. There can be no assurances as to the levels of worker remittances in the future, as the level of remittances is subject to various social and economic factors, such as the return to El Salvador of some of the workers currently in the United States, changes in U.S. immigration policy (including the withdrawal of the temporary protected status afforded to Salvadoran immigrants in the United States), the deaths of older recipients of remittances, the eventual employment of younger recipients of remittances and the establishment of families outside of El Salvador by Salvadorans who remain abroad. Nevertheless, remittances in 2003 outpaced remittances during 2002, rising from US$1,935.2 million to US$2,105.3 million, an increase of 8.8%.

In the years leading up to and immediately following the signing of the Peace Accord, foreign aid (both monetary and in-kind donations) was an important component in the Republic's balance of payments, partially offsetting the trade deficit. The level of this foreign aid reached US$284.1 million for 1994 partially as a result of the implementation of the Peace Accord and fell to US$187.3 million for 2000. The level of foreign aid (both monetary and in-kind donations) in 2001 and 2002 was higher than in 2000 at US$345.0 million and US$302.2 million, respectively, primarily as a result of aid related to the January and February 2001 earthquakes. For 2003, foreign aid (both monetary and in-kind donations) totaled US$173.0 million.

Capital Account

El Salvador registered a positive capital account balance during the eight-year period ended December 31, 2000. In 2001, the capital account balance was negative US$27.4 million, primarily as a result of a US$427.3 million public sector capital account surplus that did not offset a US$40.5 million Central Bank outflow, a US$179.1 million private sector capital account deficit due to an increase in deposits and assets by residents and a US$235.1 million financial sector capital account deficit due mainly to investments by Salvadoran financial institutions in other Central American financial institutions. For 2003, the capital account surplus was US$1,049.8 million which was primarily the result of increased net indebtedness of all sectors within the capital account. Such net indebtedness includes short term debt issuances by the public sector, foreign loans to the private sector and banks and the Republic's issuance of external notes in 2003.

In 1999, the public sector capital account surplus was US$188.0 million, mainly due to the US$150.0 million external notes issued by the Republic in August 1999. In 2000, the public sector capital account surplus was US$56.6 million, mainly due to the US$50.0 million external notes issued by the Republic in January 2000. In 2001, the public sector capital account surplus was US$427.3 million, mainly due to the US$353.5 million external notes issued by the Republic in July 2001. In 2002, the public sector capital account surplus was US$776.8 million, mainly due to the Republic's issuance of US$1,251.5 million of external notes in 2002, which was partially offset by the repayment of externally-held short-term debt with the proceeds of the issuance of such notes. In 2003, the public sector capital account surplus was US$396.0 million mainly as a result of the Republic's issuance of US$348.5 million of external notes in 2003.

The *Ley de Inversiones* (the "Investment Law"), enacted in 1999, implements reporting requirements that permit a more accurate measurement of foreign direct investment in El Salvador. The Investment Law also clarifies certain rules directed to protect foreign investments in El Salvador. Foreign investment must be registered with the National Investment Office of the Ministry of Economy. While the Investment Law recognizes the protection of investor's property rights, expropriation is permitted for public interest reasons with just compensation paid to the investor. There are no limitations on repatriation of profits. Registered foreign investors are entitled to repatriate their investment plus any capital gains and are exempted from withholding tax on dividends. Investors are still liable, however, for tax, labor, social security, bankruptcy and other legal obligations. Foreign direct investment for 2003 was US$156.5 million, compared to US$207.9 million in 2002.

Foreign Currency Reserves

At December 31, 2003, net international reserves were US$1.9 billion, an increase of 20.0% from December 31, 2002. This increase reflected the rise in US Dollar holdings by the Central Bank and commercial banks as a result of the issuance by the Ministry of Finance of short term bonds to pre-fund the 2004 budget and the rise in the reserve requirement for commercial banks. As of December 31, 2003, 4.5% of the Republic's net international reserves was held in cash compared with 3.4% as of December 31, 2002. Both percentages reflected historically high cash reserves to support the implementation of the Monetary Integration Act. Net international reserves at July 31, 2004 were US$1.7 billion.

The following table sets forth the net international reserves of the Central Bank for the periods presented.

Net International Reserves

	At December 31,				
	1999	2000	2001	2002	2003
	(In millions of US dollars, except months)				
Assets:					
Gold (1)	$ 152.5	$ 120.7	$ 117.8	$ 117.8	$ 117.8
Foreign currencies	1,757.2	1,707.0	1,535.3	1,422.3	1,754.4
Cash	1.6	199.0	50.6	54.3	85.3
Deposits abroad	397.3	85.4	181.3	121.6	515.9
Investments	1,358.3	1,422.6	1,303.3	1,246.4	1,153.2
Clearing centers	0.0	0.0	0.0	0.0	0.0
Special drawing rights	34.3	33.0	31.3	33.8	37.0
Other	28.3	33.0	27.1	16.6	0.8
Liabilities:					
Total liabilities	2.8	2.8	2.0	1.7	4.2
Net international reserves	$1,969.5	$1,890.9	$1,709.5	$1,588.8	$1,905.8
Coverage of imports of goods excluding *maquila* (in months) (2)	7.5	6.0	5.3	4.9	5.2

(1) Through 1999, gold was valued at US$325.00/troy ounce. For 2000, gold was valued at US$257.10/troy ounce. For 2001 and 2002, gold was valued at US$251.10/troy ounce. For 2003, gold was valued at US$251.20/troy ounce.

(2) Net international reserves over average monthly imports.

Note: The average exchange rate for each year has been used to translate colones into US dollars. See "Offering Circular Summary — Selected Economic Indicators."

Source: *Banco Central de Reserva de El Salvador.*

Exchange Rate Policy and Foreign Exchange Rates

From 1989 to December 31, 2000, El Salvador set no official exchange controls on the *colón* and the exchange rate was permitted to float freely based on market forces. During this period, the Central Bank had a policy of purchasing and selling US dollars periodically for the purpose of limiting excessive volatility in the *colón*/US dollar exchange rate, although no official fluctuation range was established.

On November 30, 2000, the Legislative Assembly approved the Monetary Integration Act, proposed by President Flores on November 22, 2000, fixing the *colón* to the US dollar at ¢8.75 to US$1.00. This legislation went into effect on January 1, 2001. Pursuant to this legislation, the US dollar is legal tender in El Salvador and is allowed to circulate freely in the Salvadoran economy along with the *colón.* Further,

the US dollar is the unit of account for the financial system in El Salvador and all of the operations and accounting of the financial system are denominated in US dollars. All deposits, credits, pensions and other operations of the financial system were converted to US dollars on January 1, 2001. Non-financial firms may use either *colones* or US dollars to express their financial records and accounting. Salaries and wages may be denominated in either *colones* or US dollars. Prices of products and services can be specified in *colones* or US dollars but were required to be labeled in both currencies until July 1, 2001. Four cases were filed with the Supreme Court challenging the constitutionality of the Monetary Integration Act, however the Supreme Court dismissed the cases and upheld the Monetary Integration Act.

The Central Bank exchanges *colones* for US dollars through the banking system and banks are prohibited from charging commissions for the exchange of *colones* to US dollars and US dollars to *colones.* Each bank must maintain a liquid reserve of US dollars at the Central Bank as a percentage of its obligations. The power of the Central Bank to issue new *colones* or coins ceased as of January 1, 2001.

The benefits that the government sought as a result of the Monetary Integration Act included the following:

- a reduction in interest rates as a result of a reduction in foreign exchange risk;
- the development of a greater variety of financial instruments that are typically not denominated in *colones* but which are common in US dollars;
- an increased level of foreign investment in the financial system, attracted by the protection against devaluation and the attendant improvement in El Salvador's creditworthiness and stability; and
- an increase in the local savings rate due to a reduction in inflation and devaluation risk.

As of December 31, 2003, 93.5%, or US$604.1 million, of all cash in circulation was in US dollars. The domestic currency interest rate (passive basic rate — 180 days) decreased from 10.65% at December 31, 1999 to 3.42% at June 30, 2004. Foreign direct investment in the financial system in El Salvador was US$41.4 million in 2001, US$12.1 million during 2002 and US$15.6 million in 2003.

MONETARY SYSTEM

The Central Bank (Banco Central de Reserva de El Salvador)

Created in 1934, the Central Bank was reorganized in 1991 with the objectives of controlling inflation, preserving the internal and external value of the national currency and maintaining adequate levels of liquidity in the financial system. The Central Bank is prohibited from financing, directly or indirectly, the government or any state-owned entities, or from investing in securities issued by any of them.

The Central Bank is an independent institution governed by a board of six members who are appointed to five-year terms and are removable only for cause. The President of the Central Bank, one of the six board members, is appointed by the President of the Republic. The Executive Cabinet chooses the remaining Board members pursuant to nominations from the banks, the Economic Cabinet, the private sector and professional organizations.

The Central Bank issues *Certificados Negociables de Liquidez* ("CENELIs"), which are US dollar denominated liquidity management instruments that are auctioned by the Central Bank weekly every Tuesday, and *Bonos BC* ("Central Bank Medium Term Bonds"), which are US dollar denominated medium term instruments intended to provide greater stability and liquidity to the Central Bank. As of December 31, 2003, a principal amount of approximately US$375.1 million of CENELIs and US$108.0 million Central Bank Medium Term Bonds were outstanding.

Financial Sector

The entities participating in the financial system in El Salvador include commercial banks, certain state-owned banks specializing in incentive credit, insurance companies, broker/dealers, one security depository, four operating rating agencies, bonded warehouses, financial leasing companies, factoring companies, the El Salvador Stock Exchange and the Deposit Guaranty Institute.

In the early 1980s, the government nationalized all commercial banks and savings and loans associations. During the ensuing years, the operation of the financial system was frequently in the hands of political appointees, and by 1989, the system was essentially insolvent. As the state-owned banks lost public confidence, private entities were formed and accepted deposits and extended credits. Beginning in 1989, the Republic began the modernization of the financial system through the reorganization of the Central Bank, the regulation of financial institutions and the privatization of the banks through the sale of shares to bank employees and individual shareholders.

Following the privatization of the banking system in 1992, the Central Bank recognized an account receivable from the government for approximately US$100.0 million in connection with bad loans the Central Bank had absorbed from the privatized entities. Since such time, the financial sector in El Salvador has grown steadily and, at December 31, 2003, the aggregate value of deposits in the system was US$6.6 billion, including deposits held by the two state-owned banks.

The Central Bank has imposed on financial institutions capital adequacy requirements and other standards corresponding to the Basle Accords. Under applicable law, the current capital adequacy requirement of 11.5% is scheduled to be increased to 12.0% in 2005. The Superintendency of the Financial System supervises compliance with these standards. The Banking Law, enacted in 1999, includes limits on loans to shareholders, establishes minimum capital requirements and regulates supervisory powers and the independence of the Superintendency of the Financial System. The Deposit Guaranty Institute, created by the Banking Law, guarantees deposits up to US$7,060.0 and has the authority to contribute funds to banks with liquidity problems. It was originally funded by the government and currently receives contributions from banks operating in the financial system. The Banking Law also governs the transparency and reporting requirements of banks, imposes audit standards and limits related party loans and other transactions to increase the responsibility of the banks. Subsequent amendments to the Banking Law provide greater protections to depositors by creating stricter capital and risk management requirements and

granting broader authority to the Superintendency of the Financial System with respect to troubled financial institutions.

Commercial Banks

At June 30, 2004, El Salvador had 12 private commercial banks, including two foreign banks. Along with the two foreign banks, five other commercial banks have substantial foreign ownership. At June 30, 2004, the total assets of Salvadoran commercial banks were US$10.4 billion.

Commercial banks are under the supervision of the Superintendency of the Financial System and are subject to periodic reporting requirements and mandatory audits. Commercial banks are required to maintain a certain percentage of their deposits as a reserve deposited at the Central Bank in the form of cash or securities issued by the Central Bank. See "— Interest Rates and Money Supply."

When *Banco de Crédito Inmobilario S.A.* ("CREDISA"), a bank that lent primarily to the construction sector, became insolvent, it underwent a voluntary liquidation process. In connection with the liquidation process, the Central Bank approved a US$141.7 million loan to CREDISA. Upon CREDISA's dissolution on July 16, 2004, the liquidators repaid US$86.0 million to the Central Bank consisting of a US$39.8 million guarantee by commercial banks that absorbed certain assets of CREDISA and a US$46.2 million payment in cash, real estate and other assets owned by CREDISA.

Non-banking Financial Intermediaries

The financial system in El Salvador also includes non-banking financial intermediaries, consisting primarily of cooperatives/credit unions (entities constituted to provide financial services to their members), federations (organizations of cooperatives engaging in the same type of financial activity that provide assessment and technical assistance services to their member cooperatives) and savings and loans associations (non-governmental financial entities that may collect deposits from the public and make loans). The non-banking financial intermediaries are supervised by the Superintendency of the Financial System pursuant to the *Ley de Intermediarios Financieros No Bancarios* (the "Non-Banking Financial Intermediaries Law"), which became effective July 1, 2001. The purpose of the creation of these entities by the Non-Banking Financial Intermediaries Law is to improve access to the financial system for micro and small enterprises through competition.

Pension Funds

In 1996, the Republic enacted a new pension system law, pursuant to which a substantial portion of the public, pay-as-you-go pension system was replaced by a private system based on individual accounts. Under the new system which became effective April 15, 1998, participating workers make monthly contributions to private pension funds which invest in permitted Salvadoran securities. At March 31, 2003, 1,100,382 workers were participating in the private system and US$1.8 billion in assets, equivalent to 11.9% of 2003 GDP, were under the management of the private pension fund managers. Currently, there are three pension funds, one of which is in liquidation and the assets of which will be transferred to the other two funds. See "The Salvadoran Economy — Employment and Wages — Pension Reform."

State-Owned Financial Institutions

In addition to the Central Bank and the mezzanine bank *Banco Multisectorial de Inversiones,* the state owns four other financial institutions, each of which was chartered for the purpose of extending credit to a specific sector of the economy:

- *Banco de Fomento Agropecuario* (Rural Development Bank);
- *Banco Hipotecario de El Salvador, S.A.* (Mortgage Bank of El Salvador);

- *Fondo de Financiamiento y Garantía de la Pequeña Empresa* (Small Business Finance and Guaranty Fund); and
- *Fondo Social para la Vivienda* (Social Housing Fund).

Certain of these institutions extend credit on favorable terms. These state-owned entities are governed by special legislation in addition to the general rules applicable to private financial institutions and, at December 31, 2003, had an aggregate of approximately US$1.2 billion in total assets and approximately US$1.1 billion in total liabilities.

Capital Markets

El Salvador's capital markets have grown in recent years as the financial system has modernized; however, retail trading of debt and equity securities of private Salvadoran issuers is relatively new and has remained limited thus far. Most of the trading on Salvadoran capital markets involves the purchase and sale of government securities. The El Salvador Stock Exchange opened in 1992 and currently lists 45 companies, four public institutions and 16 international entities, sovereign states and foreign central banks. In 2003, US$7.8 billion worth of securities were exchanged on the El Salvador Stock Exchange, an approximately 6.2% decrease from 2002. The Salvadoran capital markets are regulated by the *Ley Orgánica de la Superintendencia de Valores* (Superintendency of Securities Law) enacted in 1996 and are supervised by the Superintendency of Securities.

Interest Rates and Money Supply

The following table sets forth the average annual interest rates for the periods presented.

Average Interest Rates(1)

	1999	2000	2001	2002	2003
	(In percentages)				
Loans					
Short-term	15.5%	14.0%	9.6%	7.1%	6.6%
Long-term	16.1	15.5	10.8	8.7	8.0
Interbank	10.7	6.9	5.3	4.4	3.9
Central Bank(2)	10.5	8.8	4.1	3.5	3.2
Deposits					
30-day	11.4	9.3	5.4	3.1	3.2
180-day	10.8	9.3	5.5	3.4	3.4

(1) Market rates other than with respect to the Central Bank.

(2) Rates are the interest rates charged by the Central Bank to Banco Multisectorial de Inversiones in December of each year.

Source: *Banco Central de Reserva de El Salvador.*

As a result of the Monetary Integration Act and the decrease of interest rates internationally, the average interest rates for the month of June 2004 on short-term and long-term loans fell to 6.4% and 7.7%, respectively, and to 3.1% and 3.4%, respectively, on 30-day and 180-day term deposits.

The following table sets forth the principal monetary indicators for the periods presented.

Principal Monetary Indicators

	At December 31,				
	1999	2000	2001	2002	2003(1)
	(In millions of US dollars)				
Currency in circulation	$ 538.7	$ 449.4	$ 220.8	$ 61.2	$ 36.4
Demand deposits	605.9	611.5	950.4	995.1	1,031.5
M1	1,144.6	1,060.9	1,171.2	1,056.3	1,067.9
Savings	1,308.0	1,452.5	1,781.1	1,915.5	2,005.2
Term deposits	2,988.5	3,018.9	3,248.5	3,044.2	2,974.4
M2 (M1 plus savings plus term deposits)	5,441.1	5,532.2	6,200.8	6,016.0	6,047.5
Deposits in foreign currency	472.0	498.3	0.0	0.0	0.0
Others	244.7	331.1	323.5	340.7	416.7
M3 (M2 plus deposits in foreign currency plus others)	$6,157.8	$6,361.7	$6,524.3	$6,356.7	$6,464.2

(1) Preliminary data.

Source: *Banco Central de Reserva de El Salvador.*

From 1997 to 2000, the Central Bank influenced the money supply through the issuance of *Certificados de Administración Monetaria* at par and, from 1998 to 2000, through the issuance of *Certificados de Administracion Monetaria a Descuento* (CAM-Ds"), both of which were *colones* denominated instruments, that have not been issued since the effectiveness of the Monetary Integration Act in January 2001. In March 1999, the Central Bank began the implementation of a gradual decrease of the reserve requirement *(encaje)* by a total of 3.0%. The reserve requirements applicable to checking accounts, savings accounts and deposit certificates are currently 25.0%, 20.0% and 15.0%, respectively. As a precautionary measure to provide liquidity in anticipation of the presidential elections in 2004, the Superintendency of the Financial System required all commercial banks to gradually increase their reserves to an additional 9.0% of total deposits, 3.0% of which was required to be in cash and 6.0% of which was required to be in the form of securities issued by the Ministry of Finance or the Central Bank. As of July 30, 2004, the 3.0% additional reserve requirement was withdrawn while the 6.0% additional reserve requirement consisting of securities has been maintained.

Effective January 1, 2001, pursuant to the Monetary Integration Act, the US dollar is legal tender in El Salvador and is allowed to circulate freely in El Salvador. Cash in circulation, which is a measure of *colones* in circulation and does not include US dollars in circulation in El Salvador, decreased by approximately 93.1% from December 31, 2000 to June 2004, as the US dollar was integrated into the Salvadoran economy. Further, pursuant to the Monetary Integration Act, all *colones* deposits were converted into US dollars effective January 1, 2001, and the US dollar became the unit of account in the financial system. As a result, US dollar deposits that in prior periods were classified as deposits in foreign currency are for periods from and after January 1, 2001 classified as demand deposits, savings or term deposits, as applicable.

Inflation

Inflation in El Salvador is measured by the CPI, which is computed by the National Bureau of Statistics and Census using a standard basket of goods and services. The basket uses the December 1992 price level as the basis for determining the CPI and is affected by the prices of food staples (fruits and vegetables, basic grains such as corn, rice and beans and others) which comprise 41.6% of the total weight of the basket.

Beginning in 1979, as the fiscal deficit increased and the Central Bank became the government's main source of funds, inflation rates began to increase, reaching a maximum of 31.9% in 1985. In 1991, a comprehensive amendment of the statute governing the Central Bank prohibited it from financing the government, and assigned the responsibility for supporting the *colón* to its board of directors. Pursuant to this authority, the board of directors of the Central Bank adopted monetary policies to control inflation and made active use of a variety of monetary instruments to ensure that such policies were observed.

The following table sets forth the rate of inflation in the Republic as measured by the CPI for the periods presented.

Inflation

	For the Year Ended December 31,				
	1999	2000	2001	2002	2003
Inflation	(1.0)%	4.3%	1.4%	2.8%	2.5%

Source: *Banco Central de Reserva de El Salvador.*

Inflation was a negative rate of 1.0% in 1999, primarily as a result of an increase in food production and the stabilization of prices in the agricultural sector after the inflationary effects of Hurricane Mitch at the end of 1999. In 2000, inflation increased to 4.3% primarily as a result of the elimination in May 2000 of the exemption from the value added tax with respect to food and medicine, the reduction of the subsidy on electricity for residential consumers and the rise in international oil prices.

In 2001, the inflation rate decreased to 1.4%, continuing the post-Peace Accord downward trend that had been interrupted during the 1998-2000 period by the distorting effects that Hurricane Mitch had on prices. Inflation was also influenced by the elimination of a charge to consumers on purchases of gasoline of approximately six *colones* per gallon which had subsidized diesel fuel for public transportation, as well as the decrease in international oil prices during the fourth quarter of 2001.

In 2002, the inflation rate increased to 2.8%. The increase in 2002 was primarily attributable to the increases in gasoline and electricity prices resulting from rising international oil prices, as well as to an increase in rates charged by telecommunication companies. In 2003, inflation was slightly lower than in 2002 at 2.5%, but was still within the target of 2.0% and 3.0% for the year, primarily due to higher food and housing prices.

PUBLIC SECTOR FINANCES

Overview

Budget Process

El Salvador's Constitution requires that for each fiscal year a general budget must be prepared and submitted to the Legislative Assembly for approval. The budget contains estimates of revenues expected to be collected, and authorizes expenditures during the fiscal year. State-owned autonomous entities, other than those in the financial public sector, prepare individual budgets which are also submitted to the Legislative Assembly for approval.

The constitutional principles concerning budgetary matters are set forth in the *Ley Orgánica de Administración Financiera del Estado y su Reglamento* (the State Financial Administration Law or "AFI"), a statute enacted in 1995 to regulate several financial matters of the Republic. Pursuant to the AFI, the Republic's nonfinancial public sector's budget consists of the General Budget (as defined below), budgets for municipalities and the Salvadoran Social Security Institute and budgets for the non-financial autonomous entities (such as CEL and CEPA).

The general budget ("General Budget") is prepared by the Ministry of Finance following budgetary guidelines adopted by the president and the cabinet and consists of the budget for the agencies and ministries of the central government and the budgets for the legislative and judicial branches. The budget for the judicial branch is prepared by the Supreme Court and submitted to the Ministry of Finance for inclusion, without modifications, in the General Budget. The budget for the legislative branch is approved by the Legislative Assembly after consultation with the Executive Branch. Simultaneously with the presentation of the General Budget, the Ministry of Finance submits individual budgets to the Legislative Assembly prepared by each non-financial autonomous entity, with such modifications as the Ministry of Finance deems appropriate. Pursuant to the Constitution, at least 6.0% of the central government's current revenues contained in the General Budget must be allocated to the Judiciary and, pursuant to the Economic and Social Development Fund Law, 6.0% of the current revenues and, beginning in 2005, 7.0% of current revenues must be allocated to municipalities.

The Legislative Assembly must approve the budget for the non-financial public sector before December 31 of each year. In the event the new budget has not been approved by January 1, the budget for the prior year remains in effect until the Legislative Assembly approves the new budget. The Ministry of Finance, however, has authority to make changes to the extended budget by executive decree in order to meet existing obligations, including debt service obligations, of the Republic in excess of those of the prior year. Expenditures are capped at the levels in the budget approved by the Legislative Assembly.

At the end of each fiscal year, the Executive Branch must submit a report on the execution of the budget to the Legislative Assembly and to the *Corte de Cuentas de la República,* the supervisory board in charge of overseeing the Republic's public finances.

Fiscal Policy

During the late 1970s and early 1980s, the economy of El Salvador was in recession due to the civil war, and the fiscal deficit reached 13.9% of nominal GDP in 1981. Loans from the Central Bank became the main source of government financing and resulted in rates of inflation averaging 10.8% from 1970 to 1981. In 1986, the government devalued the *colón* and attempted to eliminate the fiscal deficit with the imposition of new taxes. By the end of 1986, the deficit fell to 0.8% of nominal GDP, while inflation was 30.4%. The expected recovery of the economy did not occur, and by 1988, the fiscal deficit was growing again.

In 1989, the government began to implement numerous economic changes, including the privatization of the banking system, the promulgation of a new statutory framework for the financial sector, and the enactment of a statute prohibiting the Central Bank from directly or indirectly financing the government. As a result of the new policies, the increase in foreign aid that followed the signing of the Peace Accord in

1992 and certain other measures, the fiscal deficit for the non-financial public sector as a percentage of nominal GDP declined from 4.6% in 1992 to 0.1% of GDP in 1995.

During the period from 1996 to 1999, the deficit averaged 2.4% of GDP primarily as a result of the negative impact of the Mexican crisis on the Salvadoran economy, increased social and public safety expenditures and severance payments to employees of privatized public enterprises.

In 2000, the deficit increased to 3.0% of GDP primarily due to an increase in the electricity subsidy during the first half of 2000 in order to lessen the impact of higher electricity rates. Although the current account balance improved from a deficit of US$80.2 million in 2000 to a surplus of US$58.6 million in 2001, the fiscal deficit in 2001 increased to 3.6% of GDP. The increase in the fiscal deficit as a percentage of GDP in 2001 was primarily the result of an investment by the government of US$186.6 million in the earthquake reconstruction effort as well as an expenditure of US$7.9 million for emergency relief relating to the earthquakes.

In 2002, the non-financial public sector deficit was US$474.8 million, equivalent to 3.3% of 2002 GDP, or US$8.3 million lower in nominal terms than set forth in the budget. The non-financial public sector deficit included spending of US$282.0 million, or 2.0% of 2002 GDP, related to the earthquake reconstruction effort. Excluding expenditures relating to the reconstruction effort, the underlying deficit was reduced from US$309.7 million in 2001 to US$192.8 million in 2002. Reconstruction spending increased from US$192.8 million in 2001 to US$282.0 million in 2002, an increase equivalent to 0.8% of GDP.

The budget for 2003 contemplated a deficit of 1.6% of GDP for the non-financial public sector (including expenditures related to the reconstruction then estimated at 1.4% of GDP and excluding obligations relating to the pension system then estimated at 1.3% of GDP). The actual non-financial public sector deficit for 2003 was US$218.9 million, US$24.6 million lower than the target set forth in the budget and equivalent to 1.5% of preliminary 2003 GDP. Excluding expenditures relating to the reconstruction effort, the underlying deficit was reduced from US$192.8 million in 2002 to US$2.6 million in 2003. Reconstruction spending decreased from US$282.0 million in 2002 to US$216.3 million in 2003, a decrease equivalent to 0.5% of GDP.

The 2004 budget submitted to the Legislative Assembly on September 29, 2003 and approved on June 17, 2004 contemplates a deficit of 0.9% of GDP for the non-financial public sector (including expenditures related to the reconstruction effort then estimated at 0.5% of GDP and excluding obligations related to the pension system then estimated at 1.9% of GDP). The main assumptions underlying the 2004 budget include an inflation rate between 3.0% and 5.0%, a real GDP growth rate between 1.5% and 2.5%, remittances from abroad growing at 5.0%, a slight increase in coffee prices and a modest recovery of the U.S. economy.

As of June 30, 2004, total revenues were US$1,316.8 million, equivalent to 8.4% of GDP. Total revenues were greater by 4.5% compared to the first half of 2003. Total expenditures, on the other hand, declined to US$1,229.5 million, 2.5% less than the same period of 2003. The current account surplus was US$220.3 million or US$23.7 million greater than the same period last year. The overall result was a fiscal surplus of US$87.3 million, a reversal of the US$2.0 million deficit in the first six months of 2003. Capital expenditures for the first six months of 2004 are lower compared to the same period of 2003 mainly as a result of the delay in the approval of the 2004 budget that affected new investments in public projects and affected funding for current projects.

Non-Financial Public Sector Revenues and Expenditures

The following table sets forth actual revenues and expenditures for the consolidated non-financial public sector for the periods presented, as well as revenues and expenditures estimated for 2004.

Non-Financial Public Sector
Consolidated Revenues and Expenditures(1)

	For the Year Ended December 31,					
	1999	2000	2001	2002	2003(2)	2004 Estimate(3)
	(In millions of US dollars, except percentages)					
Revenues						
Current revenues(4)	$ 1,920.9	$ 2,062.4	$ 2,075.3	$ 2,193.6	$ 2,442.6	$ 2,478.8
Capital revenues	1.0	7.6	0.9	64.9	0.3	11.4
Foreign aid	33.0	110.1	61.0	49.9	69.7	75.5
Total revenues	$ 1,954.9	$ 2,180.1	$ 2,137.2	$ 2,308.4	$ 2,512.6	$ 2,565.7
Expenditures						
Current expenditures(4)	$ 1,896.4	$ 2,142.6	$ 2,022.0	$ 2,077.2	$ 2,224.1	$ 2,148.8
Consumption	1,391.2	1,491.7	1,512.9	1,526.9	1,617.9	1,614.7
Interest	172.2	203.3	200.2	245.5	307.1	356.9
Transfers	332.9	447.6	308.9	304.8	299.0	177.2
Capital expenditures	403.9	436.3	619.6	706.2	508.1	560.9
Gross investment	389.0	380.3	602.2	609.4	500.2	544.5
Capital transfers	15.0	56.0	17.4	96.9	7.9	16.4
Net lending	(0.3)	(0.3)	(0.2)	(0.2)	(0.6)	(0.5)
Total expenditures	$ 2,300.0	$ 2,578.6	$ 2,641.4	$ 2,783.2	$ 2,731.5	$ 2,709.2
Current account surplus (deficit)(5)	$ 24.6	$ (80.2)	$ 53.3	$ 116.4	$ 218.5	$ 330.0
Surplus (deficit) excluding foreign aid	(378.1)	(508.6)	(565.2)	(524.7)	(288.6)	(219.0)
Surplus (deficit) including foreign aid	(345.1)	(398.5)	(504.2)	(474.8)	(218.9)	(143.6)
External financing	155.1	200.0	614.9	1,253.5	432.1	307.3
Internal financing	191.7	198.7	(110.7)	(778.5)	(213.2)	(163.8)
Current account surplus (deficit)/Nominal GDP	0.2%	(0.6)%	0.4%	0.8%	1.5%	2.1%
Surplus (deficit) excluding foreign aid/Nominal GDP	(3.0)	(3.9)	(4.1)	(3.7)	(1.9)	(1.4)
Surplus (deficit) including foreign aid/Nominal GDP	(2.8)	(3.0)	(3.6)	(3.3)	(1.5)	(0.9)
Nominal GDP	$12,464.7	$13,134.1	$13,812.7	$14,311.9	$14,940.9	$15,685.0

(1) All figures are presented on a cash basis.

(2) Preliminary data.

(3) Estimates are based on amounts contained in the 2004 budget approved by the Legislative Assembly.

(4) Current revenues and current expenditures are presented on a gross basis.

(5) The current account equals current revenues less current expenditures.

Source: *Ministerio de Hacienda.*

Central Government Revenues

The following table shows the composition of the Salvadoran central government's revenues and foreign aid for the periods presented.

Central Government Revenues and Foreign Aid(1)

	For the Year Ended December 31,				
	1999	2000	2001	2002	2003(2)
	(In millions of US dollars)				
Tax revenues(3)					
Income	$ 411.7	$ 451.5	$ 455.4	$ 480.2	$ 530.1
Property transfers	13.7	11.6	11.6	13.0	14.5
Imports	148.1	140.5	146.0	154.8	177.6
Consumption	51.5	48.7	49.3	66.5	61.7
Value added tax	733.9	799.7	866.3	903.9	960.3
Others	0.3	0.1	0.1	1.8	0.9
Special contributions (FOVIAL)(4)	0.0	0.0	1.6	64.8	67.2
Total tax revenues	1,359.2	1,452.1	1,530.3	1,685.0	1,812.4
Non-tax revenues(5)	82.1	103.6	87.0	119.5	123.8
Total current revenues	1,441.3	1,555.7	1,617.3	1,804.5	1,936.2
Capital revenues	0.6	1.2	0.5	2.4	0.4
Foreign aid	13.9	77.1	32.1	18.5	49.4
Total revenues	$1,455.7	$1,633.9	$1,649.9	$1,825.4	$1,985.9

(1) All figures are presented on a cash basis.

(2) Preliminary data.

(3) Tax revenues are presented on a gross basis.

(4) In 2001, the government imposed a levy, the *Fondo de Conservación Vial* ("FOVIAL"), of US$0.20/gallon on gasoline and diesel which is specifically used for road maintenance and improvements.

(5) Includes fines, license fees, plate issuance fees, passport fees, and gasoline related revenues.

Source: *Ministerio de Hacienda.*

One of the challenges facing the government is the collection of income taxes, as evidenced by the dependence of the government on indirect taxes such as the value added tax. To a lesser extent, collection of the value added tax is also a challenge, particularly in connection with transactions related to the informal sector of the economy. Continuing a trend that began in 1992, the value added tax was the principal component of tax revenues in 2003, generating approximately 53.0% of total tax revenues. Income tax revenues accounted for approximately 29.2% of tax revenues during the same year. Import duties, the third largest component of tax revenues, accounted for approximately 9.8% of tax revenues in 2003. The FOVIAL special contributions accounted for 3.7% of tax revenue.

The existence of a large informal sector of the economy inhibits tax collection but the value added tax assists the government in collecting revenues from certain transactions in which that sector engages. Tax revenues increased 7.6% during 2003 as compared to 2002 while current revenues rose by 7.3% in 2003 as compared to 2002. Tax revenues increased 10.1% during 2002 compared to 2001. See "— Taxation."

The government has generated additional revenues and improved customs administration through measures taken to prepare for the planned Central American full customs integration by 2005 and

increased security following the terrorist attacks in the United States in September 2001. Furthermore, in 2002, El Salvador initiated use of a unified Central American customs declaration.

Central Government Expenditures

After the signing of the Peace Accord in 1992, government expenditures on public works, public health, education and human rights and law enforcement increased while defense spending decreased as a result of the termination of the armed conflict and the demobilization of military personnel. Expenditures relating to social goals, including health, education and housing represented approximately 29.5% of government expenditures in 1996 and 36.6% in 2003. The 2004 budget reflects the continued shift from a focus on military spending to the achievement of social goals, with approximately 30.1% of the central government budget allocated to social development which is comparable to the 31.3% and 33.6% budgeted for social spending in 2002 and 2003, respectively.

Between 1995 and 1998, central government expenditures as a percentage of nominal GDP decreased, reflecting the more limited role of the government in the economy. From 1999 to 2002, expenditures as a percentage of nominal GDP increased from 13.5% to 15.5%, reflecting the increase in spending related to social goals, including education, health and other social programs, such as the hiring of new teachers, doctors and nurses, spending on construction and maintenance of roads, as part of the reconstruction program after the 2001 earthquakes, and an increase in expenditures related to public security.

The increases in expenditures relating to social goals and public security were partially affected by reforms undertaken during 2001 in order to reduce central government expenditures. The reforms included:

- the elimination of subsidies for public transportation;
- the reduction or elimination of subsidies for middle- and high-income households and businesses for electricity and water consumption; and
- an amendment to the Civil Service Law which enables the government to implement a more flexible public sector employment policy.

In 2003, central government expenditures as a percentage of nominal GDP decreased to 15.1% from 15.5% in 2002. The decrease was primarily attributable to lower expenditures related to reconstruction and government salaries and wages. Central government expenditures on wages and salaries for 2003 decreased by 2.8% in nominal terms compared to 2002 and were 4.9% of GDP. Overall current expenses remained stable at 12.1% of GDP compared to 2002. The Government believes, however, that higher world oil and liquified gas prices may increase government expenditures for 2004 by increasing the amount of government subsidies for petroleum related products.

The following table shows the actual central government expenditures for the periods presented.

Central Government Expenditures(1)

	For the Year Ended December 31,				
	1999	2000	2001	2002	2003(2)
	(In millions of US dollars, except percentages)				
Education	$ 317.8	$ 334.6	$ 394.1	$ 451.2	$ 451.0
Public health	186.1	197.4	205.0	205.2	232.3
Public security(3)	151.0	158.4	155.9	182.0	188.1
Public works(4)	146.6	66.5	130.2	168.7	165.3
Judiciary	96.9	101.5	106.6	104.2	113.6
Defense	106.4	111.6	130.5	107.1	106.5
Presidency	53.1	56.5	73.0	58.7	61.5
Economy	36.0	35.4	39.7	19.4	51.8
Finance(5)(6)	64.9	69.0	56.6	42.0	43.6
Agriculture	26.3	23.5	25.6	25.0	25.9
Foreign relations	26.7	21.7	23.4	23.8	22.1
Electoral tribunal	20.3	16.9	10.7	25.1	21.0
Attorney General	17.8	18.7	18.5	19.2	19.5
Controller	14.2	13.6	13.0	14.4	18.1
Legislature	13.3	14.4	15.5	16.7	17.5
General Prosecutor	11.5	12.3	12.9	12.5	12.6
Labor	5.5	6.2	6.4	6.2	6.1
Environmental	2.7	3.5	4.1	5.5	5.7
National Judicial Council(7)	0.0	3.2	3.5	3.9	3.6
Defense of human rights	3.8	3.5	3.3	3.6	3.5
Civil service tribunal	0.1	0.1	0.1	0.2	0.2
Justice	18.8	0.0	0.0	0.0	0.0
Interior(3)	18.2	33.0	36.2	0.0	0.0
Housing and urban development	4.7	4.7	7.3	0.0	0.0
Transport	4.3	4.7	5.3	0.0	0.0
Public Treasury(6)	336.0	468.3	491.1	638.7	694.1
Interest payments	122.5	130.6	176.1	222.8	294.8
Current transfers	138.6	195.9	152.1	234.8	234.9
General obligations	129.0	181.1	136.6	154.7	153.5
Other obligations	9.6	14.7	15.5	80.1	81.4
Capital transfers	74.9	96.1	162.9	181.0	164.4
Financial investments	0.0	45.7	0.0	0.0	0.0
Total	$1,683.0	$1,779.3	$1,968.5	$2,133.2	$2,263.4
Central government expenditure/Nominal GDP	13.5%	13.5%	14.3%	15.5%	15.1%

(1) All figures are presented on a cash basis.

(2) Preliminary data.

(3) Includes expenditures of *Policia Nacional Civil* and *Academia Nacional de Seguridad Pública*; starting 2000 includes Justice budget. In June 2001, the Ministry of Justice and Public Safety merged with Ministry of the Interior into the Ministry of Governance.

(4) Includes Housing, Urban Development and Transportation in 2002.

(5) Includes operating expenses of the Ministry of Finance.

(6) Excludes amortizations.

(7) Prior to 2000, expenditures included under Justice.

Source: *Ministerio de Hacienda.*

Taxation

The Salvadoran Constitution authorizes the levy and collection of taxes by tax authorities at the national level. The central government collects taxes on personal and corporate income and on transfers of real estate. In addition, it collects import duties and a 13.0% value added tax on tangible assets and services.

Approximately 93.6% of the central government's current revenues came from various forms of taxation in 2003. The central government's tax revenues were US$1,812.4 million in 2003, an increase of 7.6% over 2002 revenues, which was principally a result of the US$56.4 million increase in value added tax collections. In addition, taxes on income increased 10.4% as a result of the elimination of the ¢75,000 exemption from income tax for corporations as well as the strengthening of the tax auditing process and other tax administration tools.

The value added tax typically is the principal component of tax revenues, generating 53.0% of the total tax revenues in 2003. The value added tax applies to most sales of tangible assets as well as most services except for educational, transportation and cultural services, among others.

The second largest component of tax revenues is the income tax, which accounted for 29.2% of tax revenues during 2003. Personal income tax rates for residents and non-residents who file tax returns in the Republic range from 10.0% to 30.0%. A flat 25.0% rate applies to non-resident taxpayers and corporate entities. Import duties, the third largest component of tax revenues, accounted for 9.8% of tax revenues in 2003.

In addition to changes in the value added tax rates, other tax changes and laws approved as part of the reforms since the Peace Accord include the elimination of property taxes in May 1994, the increase of fees for registration of rights, contracts and other documents in February 1993 and December 2001, and the creation of free trade zones which exempt users from import and export duties and income and real estate transfer taxes. The government has also enacted laws and implemented systems designed to improve the collection of income taxes, which have historically been characterized by high rates of evasion and avoidance. In a series of laws enacted in 1999 and 2000, the Legislative Assembly amended the import tax fraud law and the value added tax and income tax laws. The amendments to the import tax fraud law were primarily directed to reduce tax avoidance by increasing the list of acts considered to constitute import tax fraud and authorizing the imposition of stronger penalties. The amendments to the value added tax law restricted tax credits on items such as basic foods as well as the elimination of exemptions for medicines, fruits and vegetables and basic grains, among others. A loophole in the income tax law was closed by requiring private and public companies and businesses to withhold 10.0% of any amount paid for services provided.

The Legislative Assembly approved a new tax code which became effective in January 2001 and allows the government to unify procedures for different taxes and expedite the process of imposing and collecting fines from taxpayers not complying with the legal framework. In addition, the Legislative Assembly approved a levy of US$0.20/gallon on gasoline and diesel which is used for road maintenance and improvements and, effective January 2002, the elimination of the ¢75,000 exemption from the income tax for corporations.

PUBLIC DEBT

General

Public sector debt, including the internal and external debt of the financial and non-financial public sector and the external Central Bank debt balance, was approximately US$7,119.0 million at December 31, 2003 and US$7,285.3 million at June 30, 2004.

Under the Constitution, the Legislative Assembly has the power to adopt legislation governing the issuance of public debt and to appropriate funds required for debt service. Acting pursuant to this constitutional mandate, the Legislative Assembly approved the AFI, which governs, among other matters, the procedures that must be observed in all matters regarding public debt. AFI rules concerning public debt apply to all state-owned entities, with the exception of the Central Bank and the state-owned financial institutions, as well as to obligations of the municipalities guaranteed by the national government. The Central Bank and the state-owned financial institutions are subject to restrictions in their respective charters regarding the issuance of debt. They are also subject to AFI if they issue obligations guaranteed by the Republic.

Because all AFI-governed public debt must comply with the public indebtedness policies adopted by the Executive Branch, a non-financial public sector entity must obtain the prior written approval of the Ministry of Finance before entering into any negotiations with respect to borrowing. Any contract executed by such entities without the approval of the Ministry of Finance is null and void and unenforceable as against that entity or the Republic and may give rise to civil and criminal liability for the individuals involved. Once approval of the Ministry of Finance is obtained, the entity may proceed to negotiate the terms and conditions of the obligations to be incurred, provided that its own charter gives it the authority to conduct such negotiations on its own behalf; otherwise, the Ministry of Finance conducts the negotiations with the participation of the Ministry of Foreign Relations in the case of transactions with multilateral and bilateral international lenders. Loan proceeds are disbursed to the Republic which, in turn, transfers such proceeds to the ultimate borrower pursuant to an agreement between the Ministry of Finance and such entity.

Although public debt service is the primary responsibility of the entity for whose benefit the loan was received, AFI-governed debt is an obligation of the Republic. Accordingly, transfers from the Central Government to any entity pursuant to the annual budget take into account debt service obligations for the following year.

Treasury Bills ("LETES")

To finance temporary revenue shortages, the Ministry of Finance is authorized to issue short-term debt instruments known as "LETES." LETES are US dollar denominated and are sold at discounts that reflect market conditions at the time of issuance. The maximum maturity of LETES is 360 days. As of June 30, 2004, there was US$326.0 million in LETES outstanding.

External Debt

External debt obligations of El Salvador are to multilateral organizations, bilateral institutions and commercial lenders, including certain external capital markets transactions. The total external debt of the public sector in El Salvador, excluding the Central Bank, was US$5,355.5 million at December 31, 2003 and US$5,314.7 million at June 30, 2004, compared with US$4,817.6 million at December 31, 2002. The increase in public sector external debt since December 31, 2002 is primarily the result of the issuance by the Republic of US$348.5 million of external bonds in March 2003. The Central Bank's external debt at December 31, 2003 was US$262.5 million and at June 30, 2004 was US$257.3.

Since the signing of the Peace Accord in 1992, most of the external debt of the Republic has been contracted with multilateral organizations, and the funds borrowed have been used primarily for the reconstruction and improvement of physical infrastructure. From 1990 to 1999, the Republic entered into

six stand-by arrangements with the IMF, totaling 237.25 million Special Drawing Rights. The Republic did not draw on any of these stand-by arrangements, the last of which expired on February 22, 2000. Since 1999, the Republic has been involved in the following eight note issuances which are included in its external debt:

- US$150.0 million of external notes issued by the Republic in August 1999 that mature on August 15, 2006;
- US$50.0 million of external notes issued by the Republic in January 2000 that mature on January 15, 2007;
- zero coupon notes issued by the Coffee Emergency Fund of El Salvador, with a guaranty of the Republic, for an aggregate issue price of US$80.0 million with an aggregate face amount at maturity of US$123,248,752, that mature from 2001 to 2010;
- US$353.5 million of external notes issued by the Republic in July 2001 that mature on July 25, 2011;
- US$500.0 million of external notes issued by the Republic in April 2002 that mature on April 10, 2032;
- US$300.0 million of external notes issued by the Republic in July 2002 that mature on July 25, 2011 and form a single series with the external notes issued in July 2001;
- US$451.5 million of external notes issued by the Republic in October 2002 that mature on January 24, 2023; and
- US$348.5 million of external notes issued by the Republic in March 2003 that mature on January 24, 2023 and form a single series with the external notes issued in October 2002.

To finance reconstruction associated with the January and February 2001 earthquakes, the Republic received US$327.0 million in new loans from multilateral and bilateral sources, including US$238.0 million in loans from the Inter-American Development Bank, and secured the reprogramming of US$116.4 million of existing loans from such sources to the reconstruction effort. The proceeds of these loans are being disbursed over the period from 2001 to 2005.

The following table sets forth the total public external debt for the periods presented.

Public Sector External Debt

	At December 31,				
	1999	2000	2001	2002	2003(1)
	(In millions of US dollars, except percentages)				
Central government	$2,184.5	$2,293.3	$2,991.1	$4,532.8	$5,008.6
Public financial and non-financial entities	377.0	440.5	278.5	284.8	346.9
Sub-total	2,561.5	2,733.8	3,269.6	4,817.6	5,355.5
Central Bank	161.0	154.3	120.2	95.4	262.5
Total	$2,722.5	$2,888.1	$3,389.8	$4,913.0	$5,618.0
External public debt as a percentage of nominal GDP	21.8%	22.0%	24.5%	34.3%	37.6%

(1) Preliminary data.

Source: *Ministerio de Hacienda.*

The following table shows the composition of the Republic's external public debt by type of creditor for the periods presented.

Public Sector External Debt by Type of Creditor

	At December 31,				
	1999	2000	2001	2002	2003(1)
	(In millions of US dollars)				
Central Government and Public Financial and Non-Financial Entities	$2,561.8	$2,733.8	$3,269.6	$4,817.6	$5,355.5
Multilateral	1,730.6	1,799.7	1,972.0	2,232.6	2,376.7
Bilateral	657.8	645.7	665.0	710.2	763.1
Commercial	173.4	288.4	632.6	1,874.8	2,215.7
Central Bank	160.7	154.3	120.2	95.4	262.5
Multilateral	139.7	127.7	106.3	84.6	177.8
Bilateral	20.0	16.9	13.9	10.8	7.7
Commercial	1.0	9.7	0.0	0.0	77.0
Total Public Sector	$2,722.5	$2,888.1	$3,389.8	$4,913.0	$5,618.0

(1) Preliminary data.

Source: *Ministerio de Hacienda.*

The increases in the multilateral indebtedness of the central government and the public financial and non-financial entities from December 31, 2000 to December 31, 2003 are due primarily to the impact of the disbursement of loans for reconstruction and other infrastructure investments. The increase in commercial indebtedness from December 31, 2000 to December 31, 2003 is due primarily to the Republic's issuance of external notes.

The following table shows the rates of interest applicable to the outstanding principal balance of the Republic's public external debt at June 30, 2004.

Interest on Public Sector External Debt

	At June 30, 2004	
	Amount	Percentage
	(In millions of US dollars, except percentages)	
Fixed Rate		
0-3%	$1,350.3	24.2%
3-6%	209.0	3.8
6-9%	2,451.5	44.0
More than 9%	216.4	3.9
Floating Rate	1,344.8	24.1
Total	$5,572.0	100.0%

Source: *Ministerio de Hacienda.*

The following table sets forth the government's projections as of June 30, 2004 regarding external debt service with respect to debt already disbursed to the public sector, not including the Central Bank, for the years 2004 to 2013.

Public Sector External Debt Service 2004-2013(1)

	For the Year Ending December 31,									
	2004	2005	2006	2007	2008	2009	2010	2011	2012	2013
	(In millions of US dollars)									
Central Government	$487.0	$480.0	$625.0	$500.0	$432.0	$410.0	$397.0	$1,038.0	$315.0	$284.0
Principal	196.0	200.0	353.0	252.0	198.0	184.0	179.0	827.0	166.0	141.0
Interest	291.0	280.0	272.0	248.0	234.0	226.0	218.0	211.0	149.0	143.0
Rest of Public Sector	31.0	30.0	31.0	34.0	29.0	29.0	27.0	16.0	15.0	15.0
Principal	18.0	18.0	21.0	25.0	22.0	23.0	22.0	12.0	12.0	12.0
Interest	13.0	12.0	10.0	9.0	7.0	6.0	5.0	4.0	3.0	3.0
Total Debt Service	$518.0	$510.0	$656.0	$534.0	$461.0	$439.0	$424.0	$1,054.0	$330.0	$299.0

(1) Medium- and Long-Term debt.

Source: *Ministerio de Hacienda.*

Debt Record

During the civil war, El Salvador was unable to service a portion of its international debt. Between 1990 and 1993, the Republic successfully negotiated a rescheduling of certain loans totaling US$382.5 million and forgiveness of certain other obligations with some international creditors. In 1993, the U.S. Agency for International Development, upon its own initiative, forgave US$463.9 million of outstanding debt and Canada converted Cnd$8.1 million of outstanding debt to an obligation of the Republic to use amounts which would have been applied to service this debt for environmental projects. In 1999, the government of France, upon its own initiative, forgave FF133.0 million of outstanding debt. The Republic continued to service such debt until France completed the debt forgiveness process. Since 1993, El Salvador has not rescheduled any loans and has not defaulted on any of its indebtedness.

Internal Debt

The Republic's public sector internal debt, excluding the Central Bank, was US$1,501.0 million at December 31, 2003 and at US$1,713.3 at June 30, 2004. The Republic's public sector debt is denominated in both US dollars and *colones.* As a result of the Monetary Integration Act, all future issuance of public sector internal debt will be in US dollars.

The Republic's central government internal debt consists of obligations to both public sector and private entities. Although pursuant to its charter, the Central Bank is not allowed to finance the government, this restriction became effective only in 1994. Prior to 1994, the Central Bank had extensively financed government operations. At December 31, 2003, the outstanding principal balance of obligations related to such activity was US$704.4 million. No interest obligations were outstanding at such date.

The following table sets forth the public sector internal debt for the periods presented.

Public Sector Internal Debt(1)

	At December 31,				
	1999	2000	2001	2002	2003(2)
	(In millions of US dollars, except percentage)				
Central Government(3)	$ 994.9	$1,249.9	$1,473.9	$ 758.3	$ 844.7
Public non-financial entities	6.1	8.8	14.9	66.4	32.7
Public financial entities	573.1	625.2	631.0	647.4	613.7
Municipalities and other government institutions	9.7	9.5	7.4	11.6	9.9
Total	$1,583.8	$1,893.4	$2,127.2	$1,483.7	$1,501.0
Internal public debt as a percentage of nominal GDP	12.7%	14.4%	15.4%	10.4%	10.0%

(1) Does not include internal debt obligations of the Central Bank.

(2) Preliminary data.

(3) Includes obligations to the Central Bank.

Source: *Ministerio de Hacienda.*

Central government internal debt increased from US$994.9 million at December 31, 1999 to US$1,473.9 million at December 31, 2001 and decreased to US$844.7 million at December 31, 2003. A significant part of this balance is represented by bonds issued by the government for various purposes, including the payment of compensation for lands expropriated prior to 1989 and funding of the fiscal deficit. The decrease in central government internal debt from December 31, 2001 to December 31, 2002 is primarily the result of the Republic's repayment of internal debt with proceeds of its external notes issued in 2002. The internal debt incurred by public financial entities is largely represented by bonds issued by the *Fondo de Saneamiento del Sistema Financiero,* a special purpose public entity created to acquire from state-owned banks and other financial institutions loans in arrears and other assets of a similar nature prior to their privatization. The internal debt obligations of the Central Bank represent, in large part, indebtedness incurred through open market operations.

TERMS AND CONDITIONS OF THE NOTES

The following are the Terms and Conditions of the Notes which will appear on the reverse of each of the Notes (the "Terms and Conditions"). Certain provisions of the Notes refer to and are subject to the Fiscal Agency Agreement to be dated as of September 21, 2004, among the Republic, Citibank, N.A., London office, as Fiscal Agent, Principal Paying Agent, Registrar and Transfer Agent and the paying agents and the transfer agents named therein. The description of the Notes set forth herein does not purport to be complete and is qualified in its entirety by reference to the Notes and the Fiscal Agency Agreement.

1. General. (a) This Note is one of a duly authorized issue of 7.625% Notes due 2034 (the "Notes") of the Republic, limited to the aggregate principal amount of US$286,458,000 (except as otherwise provided below) issued pursuant to a Fiscal Agency Agreement dated as of September 21, 2004 (the "Fiscal Agency Agreement"), among the Republic, Citibank, N.A., London office, as fiscal agent (the "Fiscal Agent"), principal paying agent (the "Principal Paying Agent"), registrar (the "Registrar") and transfer agent (the "Transfer Agent"), which expressions shall include any successors to Citibank, N.A., London office, in its capacity as such, and Kredietbank S.A. Luxembourgeoise, as transfer agent (a "Transfer Agent") and paying agent (a "Paying Agent" and together, the "Agents," which term shall include the Fiscal Agent, the Paying Agents, the Registrar and the Transfer Agents). If not previously redeemed (see Section 7 below), the entire principal amount of the Notes together with accrued interest thereon is payable on September 21, 2034.

(b) The Notes are direct, general and unconditional obligations of the Republic. The Notes shall at all times rank equally without any preference among themselves and at least *pari passu* with all other present and future unsecured and unsubordinated Public External Indebtedness of the Republic.

(c) The holders of the Notes will be entitled to the benefits of, be bound by, and be deemed to have notice of, all of the provisions of the Fiscal Agency Agreement. Copies of the Fiscal Agency Agreement are on file and may be inspected at the office of the Fiscal Agent and at the offices of the paying agents referred to below.

(d) The issue of the Notes is authorized under Legislative Decree No. 349 (as published in the *Diario Oficial* on June 17, 2004) of the Republic's Legislative Assembly.

2. Form, Denomination and Title. (a) Each Note will be issued in minimum denominations of US$10,000 and integral multiples of US$1,000 in excess thereof. The Notes, and the transfer thereof, shall be registered as provided in Section 9 below and in the Fiscal Agency Agreement. In this Note, "Noteholder" and (in relation to a Note) "holder" mean the person in whose name a Note is registered. A Noteholder may (to the fullest extent permitted by law) be treated at all times, by all persons and for all purposes, as the absolute owner of such Note, regardless of any notice of ownership, theft or loss or of any writing thereon.

(b) Notes initially sold within the United States in reliance on Rule 144A under the Securities Act will be represented by the Restricted Global Note and will be deposited with a custodian for, and registered in the name of a nominee of, DTC.

(c) Notes initially sold outside the United States pursuant to Regulation S under the Securities Act will be represented by the Regulation S Global Note deposited with a custodian for, and registered in the name of a nominee of, DTC.

(d) Registration of title to Notes initially represented by the Restricted Global Note in a name other than DTC or a successor depositary or one of their respective nominees will not be permitted unless (i) such depositary notifies the Republic that it is no longer willing or able to discharge properly its responsibilities as depositary with respect to the Restricted Global Note or ceases to be a "clearing agency" registered under the United States Securities Exchange Act of 1934, as amended (the "Exchange Act"), or is at any time no longer eligible to act as such, and the Republic is unable to locate a qualified successor within 90 days of receiving notice of such ineligibility on the part of such depositary or

(ii) following a failure to pay at maturity or upon acceleration of any Note, the Fiscal Agent has received a notice from the registered holder of the Restricted Global Note requesting exchange of a specified amount of the Restricted Global Note for individual note certificates (the "Restricted Note Certificates").

Registration of title to Notes initially represented by the Regulation S Global Note in a name other than DTC or a successor depositary or one of their respective nominees will not be permitted unless (i) such depositary notifies the Republic that it is no longer willing or able to discharge properly its responsibilities as depositary with respect to the Regulation S Global Note or ceases to be a "clearing agency" registered under the Exchange Act, or is at any time no longer eligible to act as such, and the Republic is unable to locate a qualified successor within 90 days of receiving notice of such ineligibility on the part of such depositary or (ii) following a failure to pay principal in respect of any Note at maturity or upon acceleration of any Note, and the Fiscal Agent has received a request from the registered holder of the Regulation S Global Note requesting exchange of the Regulation S Global Note for individual note certificates (the "Regulation S Note Certificates" and together with the Restricted Note Certificates, the "Note Certificates").

(e) The Notes will not be issued in bearer form. So long as Euroclear or Clearstream, Luxembourg, if applicable, or DTC or its nominee is the registered owner of a Global Note, it will be considered the sole owner or holder of the Notes represented thereby for all purposes under the Notes and the Fiscal Agency Agreement. Neither the Republic nor any Agent will have any responsibility or liability for any aspect of the records relating to or payments made by Euroclear, Clearstream, Luxembourg, if applicable, or DTC on account of beneficial interests in a Global Note.

3. Interest. (a) Interest on the Notes will be calculated on the basis of a 360-day year consisting of 12 months of 30 days each and, in the case of an incomplete month, the number of days elapsed.

(b) The Notes will bear interest from and including September 21, 2004 to, but excluding, September 21, 2034 at the rate of 7.625% per annum on the principal amount thereof payable semi-annually in arrears on March 21 and September 21 of each year commencing on March 21, 2005. Each Note will cease to bear interest from and including the due date for redemption unless, upon due presentation and surrender, payment of principal is improperly withheld or refused. In such event it shall continue to bear interest at such rate (both before and after judgment) until the earlier of (i) the day on which all sums due in respect of such Note up to that day are received by or on behalf of the relevant holder and (ii) the day seven days after the Fiscal Agent or the Principal Paying Agent has notified Noteholders of receipt of all sums due in respect of all the Notes (except to the extent that there is failure in the subsequent payment to the relevant holders).

4. Payment and Paying Agents. (a) Payment of principal of the Notes (together with accrued interest) will only be made to the person in whose name such Note is registered as of the close of business on the due date for payment of the principal, following presentation and surrender of such Note at the office of the Principal Paying Agent or any other Paying Agent, by U.S. dollar check drawn on, or by transfer to a U.S. dollar account maintained by the holder with, a bank located in New York City. Payment of interest on a Note will be made to the person in whose name such Note is registered at the close of business on the fifteenth day (if the Notes are represented by Note Certificates) or the third day (if the Notes are represented by Global Notes) (whether or not a business day) (the "Record Date") prior to the relevant due date for the payment of interest. Payment of such interest will be made by a U.S. dollar check drawn on a bank in New York City mailed to the holder at such holder's registered address, or, upon application of the holder to the Principal Paying Agent or any other Paying Agent in New York City or in Luxembourg not later than the relevant Record Date, by transfer of immediately available funds to a U.S. dollar account maintained by the holder with a bank in New York City. If any day for payment of principal or interest in respect of any Note, including the Early Redemption Date ("Payment Date"), is not a Business Day the holder shall not be entitled to payment until the next Business Day following such day in the applicable jurisdiction, with the same force and effect as if made on the date for such payment, and no additional interest in respect of such Payment Date shall accrue as a result of the delay in payment. "Business Day" means a day, other than a Saturday or Sunday, in which

the commercial banks and foreign exchange markets are open, or not authorized to close, in Luxembourg, New York City, San Salvador, or the city of the Paying Agent to which the Note is surrendered for payment.

(b) The Republic agrees that so long as any of the Notes are outstanding, it will maintain (i) a Principal Paying Agent in a Western European or United States city for payments on the Notes, (ii) so long as the Notes are listed on the Luxembourg Stock Exchange and the rules of such Exchange so require, a Paying Agent and Transfer Agent in Luxembourg, (iii) a Registrar having a specified office in London, and (iv) a Paying Agent having a specified office in London. The Republic has initially appointed Citibank, N.A., as fiscal agent and as principal paying agent, registrar and transfer agent and Kredietbank S.A. Luxembourgeoise, as paying agent and transfer agent. Subject to the foregoing, the Republic shall have the right at any time to terminate any such appointments and to appoint any other Agents in such other places as it may deem appropriate upon notice in accordance with Section 13 below.

(c) Payments in respect of the Notes shall be made in such coin or currency of the United States of America as at the time of payment shall be legal tender for the payment of public and private debts.

5. Payment of Additional Amounts. (a) All payments by the Republic in respect of the Notes shall be made without withholding or deduction for or on account of any present or future taxes, duties, fines, penalties, assessments or other governmental charges of whatsoever nature (or interest on any taxes, duties, fines, penalties, assessments or other governmental charges of whatsoever nature) imposed or levied by or on behalf of the Republic or any political subdivision or authority thereof or therein having power to tax, unless the Republic is compelled by law to deduct or withhold such taxes, duties, fines, penalties, assessments or governmental charges (or interest on any taxes, duties, fines, penalties, assessments or other governmental charges). In such event, the Republic shall make such withholding, make payment of the amount so withheld to the appropriate governmental authority (and promptly forward to each holder of a Note an official receipt (or a certified copy) or other documentation evidencing such payment) and forthwith pay such additional amounts ("Additional Amounts") as may be necessary to ensure that the net amounts receivable by the holders of Notes after such withholding or deduction shall equal the respective amounts of principal and interest which would have been receivable in respect of the Notes in the absence of such withholding or deduction. No such Additional Amounts shall be payable:

(i) to, or to a third party on behalf of, a holder who is liable for such taxes, duties, fines, penalties, assessments or governmental charges (or interest thereon) in respect of such Note by reason of such holder's having some connection with the Republic other than the holding of the Note; or

(ii) to, or to a third party on behalf of, a holder who is liable for such taxes, duties, fines, penalties, assessments or governmental charges (or interest thereon) in respect of any Note by reason of such holder's failure to comply with any reasonable certification, identification or other reporting requirement concerning the nationality, residence, identity or connection with the Republic, or any political subdivision or taxing authority thereof or therein, of such holder or the holder of any interest in such Note or rights in respect thereof, if compliance is required by the Republic, or any political subdivision or taxing authority thereof or therein, as a precondition to exemption from such deduction or withholding; provided, however, that the Republic shall be obligated to pay Additional Amounts if such certification, identification or other reporting requirement would be materially more onerous, in form, in procedure, or in substance of information disclosed by the relevant holders or beneficial owners than comparable information or other reporting requirements imposed under United States tax law, regulation and administrative practice; or

(iii) to, or to a third party on behalf of, a holder who is liable for such taxes, duties, fines, penalties, assessments or governmental charges (or interest thereon) in respect of any Note by reason of the failure of such holder to present such holder's Note for payment (where such presentment is required) within 30 calendar days after the date on which such payment thereof became due and payable or is duly provided for and notice thereof is given to the holder, whichever occurs first.

(b) Whenever there is mentioned herein, in any context, the payment of the principal of or interest on, or in respect of, a Note, such mention shall be deemed to include mention of the payment of Additional Amounts provided for in this Section, to the extent that, in such context, Additional Amounts are, were or would be payable in respect thereof pursuant to the provisions of this Section, and express mention of the payment of Additional Amounts (if applicable) in any provisions hereof shall not be construed as excluding Additional Amounts in those provisions hereof where such express mention is not made.

6. The Agents. (a) In acting under the Fiscal Agency Agreement and in connection with the Notes, the Fiscal Agent, the Principal Paying Agent, the Paying Agents, the Registrar, the Transfer Agents and each other Agent are acting solely as agent of the Republic and do not assume any obligation toward or relationship of agency or trust for or with the owner or holder of any Note, except that any funds held by any such Agent for payment of principal of or interest (or any Additional Amounts) on the Notes shall be held in a segregated account by it and applied as set forth herein. For a description of the duties and the immunities and rights of the Fiscal Agent, the Principal Paying Agent, the Paying Agents, the Registrar and the Transfer Agents under the Fiscal Agency Agreement, reference is made to the Fiscal Agency Agreement, and the obligations of the Fiscal Agent, the Principal Paying Agent, the Paying Agents, the Registrar and the Transfer Agents to the owners or holders of Notes are subject to such immunities and rights.

(b) All monies paid by or on behalf of the Republic to the Principal Paying Agent or any other paying agent for the payment of the principal of or interest on any Note which remain unclaimed at the end of two years after such principal or interest shall have become due and payable will be repaid to the Republic upon the Republic's written request therefor and the holder of such Note will thereafter look only to the Republic for payment. Upon such repayment, all liability of the Principal Paying Agent and any other paying agent with respect thereto shall thereupon cease, without, however, limiting in any way the obligation of the Republic in respect of the amount so paid.

7. Redemption and Purchase; Further Issues. (a) If not previously redeemed, the entire principal amount of the Notes together with accrued interest thereon is payable on September 21, 2034. The Notes will not be redeemable prior to maturity at the option of the Republic. The Notes will be redeemable prior to maturity at the option of the Noteholder pursuant to subsection (b) of this Section 7 or on acceleration following an Event of Default.

(b) Each holder may cause the Republic to redeem the Notes held by such holder, in whole or in part in any authorized denomination, on September 21, 2019 (the "Early Redemption Date") at 100% of the principal amount of the Notes to be redeemed plus any accrued and unpaid interest up to, but not including, the Early Redemption Date, *provided that* in order to exercise this redemption option, a holder must take the following steps, as applicable, within the period beginning July 21, 2019 and ending on the close of business on August 21, 2019 (the "Notice Period").

(i) If the Notes are represented by a Global Note, a holder must ensure that, prior to the end of the Notice Period, the Fiscal Agent receives appropriate wire transfer instructions for the payment of the Notes to be redeemed and:

(A) a notice of redemption in the form provided for in Schedule 7 of the Fiscal Agency Agreement (a "Notice of Redemption") together with instructions to the Fiscal Agent for DTC to surrender the holder's interest in the Global Note; or

(B) a telegram, telex, fax transmission or letter from a member of a national securities exchange, the National Association of Securities Dealers, Inc., DTC (in accordance with its normal procedures) or a commercial bank or trust company in the United States, which: (x) contains the name of the holder of the Global Notes, the principal amount of the Global Note to be repaid and the CUSIP number, as appropriate, or (y) describes the terms of the Global Note, states that the redemption is being exercised, and guarantees that a properly completed Notice of Redemption, together with instructions for DTC to surrender the holder's

interest in the Global Note will be received by the Fiscal Agent no later than five business days after the date of the telegram, telex, fax transmission or letter. The Fiscal Agent must receive all of these documents prior to the end of the Notice Period and no later than five business days after the date of the telegram, telex, fax transmission or letter for the Notice of Redemption to be effective.

If a Note is represented by a Global Note, the holder of the Note will be DTC's nominee. Therefore, DTC's nominee will be the only entity that can exercise the early redemption option. In order to ensure that DTC's nominee will timely exercise a right to redemption with respect to a particular Note, the beneficial owner of that Note must instruct the direct participant or indirect participant through which it holds an interest in that Note to notify DTC of its desire to exercise a right of redemption.

(ii) If the Notes are in definitive, certificated form, a holder must ensure that, prior to the end of the Notice Period, the Fiscal Agent receives appropriate wire transfer instructions for the payment of the Notes to be redeemed and:

(A) the certificated Note, together with a duly completed Notice of Redemption; or

(B) a telegram, telex, fax transmission or letter from a member of a national securities exchange, the National Association of Securities Dealers, Inc., DTC (in accordance with its normal procedures) or a commercial bank or trust company in the United States which: (x) contains the name of the registered holder of the certificated Note, the principal amount of the certificated Note to be repaid and the certificate number or description of the terms of the certificated Note, (y) states that the redemption option is being exercised, and (z) guarantees that the certificated Note with the properly completed Notice of Redemption will be received by the Fiscal Agent no later than five business days after the date of the telegram, telex, fax transmission or letter. The Fiscal Agent must receive the certificated Note with the properly completed Notice of Redemption prior to the end of the Notice period and no later than five business days after the date of the telegram, telex, fax or letter for the Notice of Redemption to be effective.

The Fiscal Agent will cancel all Notes and any interest of the holders therein for which holders have validly exercised the redemption option as of the Early Redemption Date once it receives the redemption price from the Republic for the benefit of those holders. The Republic will owe no further obligation relating to the redeemed Notes.

(c) The Republic may at any time, directly or indirectly, purchase Notes in the open market or otherwise at any price. Any purchase by tender shall be made available to all Noteholders alike. The Notes so purchased, while held by or on behalf of the Republic, shall not entitle the holder to vote the Notes and shall not be deemed to be outstanding for purposes of calculating quorums. All Notes so purchased may at the Republic's discretion be held, resold or surrendered to the Fiscal Agent for cancellation.

(d) The Republic may, without the consent of Noteholders, create and issue additional debt securities having the same terms and conditions as the Notes (or the same except for the amount of the first interest payment) in accordance with applicable law; provided that such additional debt securities do not have, for purposes of U.S. federal income taxation (regardless of whether any holders of such debt securities are subject to the U.S. federal tax laws), a greater amount of original issue discount than the Notes have as of the date of the issue of such additional debt securities. The Republic may consolidate the additional debt securities to form a single series with the outstanding Notes.

8. Events of Default. In the event that one or more of the following events (herein referred to as "Events of Default") shall have occurred and be continuing:

(a) the Republic shall default in the payment of principal in respect of the Notes when and as the same are due, and such default shall continue for a period of thirty days thereafter;

(b) the Republic shall default in the payment of interest in respect of any of the Notes when and as the same are due, and such default shall continue for a period of thirty days thereafter;

(c) the Republic shall fail to perform any of its other obligations under the Notes, which default shall continue unremedied within 60 days after notice of such default shall have been given to the Republic by the Fiscal Agent or the Noteholders;

(d) as a result of any default or event of default resulting from the failure to make any payment of principal or of interest thereunder when due contained in any agreement or instrument related to any External Indebtedness (as defined herein) of the Republic in excess of US$25,000,000, such External Indebtedness becomes due and payable prior to the stated maturity thereof or if the Republic defaults in the payment or repayment of any of its External Indebtedness in excess of US$25,000,000 on the maturity thereof as extended by any applicable days of grace or any guarantee or indemnity given by the Republic of any External Indebtedness in excess of US$25,000,000 of others shall not be honored when due and called or within any period of grace applicable thereto;

(e) a moratorium shall be declared on the payment of any Public External Indebtedness of the Republic which does not expressly exclude the Notes; or

(f) the Republic shall deny, repudiate or contest the validity of its obligations under the Notes;

then the holders of not less than 25 percent in principal amount of the Notes outstanding may by written notice to the Republic and the Fiscal Agent declare the Notes then outstanding to be due and payable immediately at their principal face amount plus interest accrued thereon to the date of payment, including any Additional Amounts, unless prior to receipt of such demand by the Republic all such defaults have been cured. If an Event of Default shall give rise to a declaration which shall be effective and all Events of Default shall cease to continue following such declaration, then such declaration may be rescinded and annulled by the affirmative vote or written consent of the holders of not less than 66⅔% in aggregate principal amount of the Notes then outstanding in accordance with the procedures set forth in Paragraph 12 below.

9. Replacement, Exchange and Transfer. (a) If any Note shall become mutilated or defaced or be destroyed, lost or stolen, the Fiscal Agent shall, subject to having received the prior approval of the Republic (such approval not to be unreasonably withheld), authenticate and deliver a new Note at the offices of the Registrar in New York, on such terms as the Republic or the Registrar may require, in exchange and substitution for the mutilated or defaced Note or in lieu of and in substitution for the destroyed, lost or stolen Note. In every case of mutilation or defacement or destruction, loss or theft, the applicant for a substitute Note shall furnish to the Republic, the Fiscal Agent and the Registrar such indemnity as the Republic, the Fiscal Agent or the Registrar, as the case may be, may require and evidence to their satisfaction of the destruction, loss or theft of such Note, and of the ownership thereof. In every case of mutilation or defacement of a Note, the holder shall surrender to the Registrar the Note so mutilated or defaced. In addition, prior to the issuance of any substitute Note, the Republic may require the payment of a sum sufficient to cover any tax or other governmental charge that may be imposed in relation thereto and any other expenses (including the fees and expenses of the Fiscal Agent or the Registrar) connected therewith. If any Note which has matured or is about to mature shall become mutilated or defaced or be apparently destroyed, lost or stolen, the Republic may pay or authorize payment of the same without issuing a substitute Note.

(b) Upon the terms and subject to the conditions set forth in the Fiscal Agency Agreement, and subject to Section 9(e) below, a Note or Notes may be exchanged for a Note or Notes of equal aggregate principal amount, but in such different authorized denominations as may be requested by the holder, by surrender of such Note or Notes to the office of the Registrar, or to the office of any transfer agent, together with a written request for the exchange.

(c) Upon the terms and subject to the conditions set forth in the Fiscal Agency Agreement, and subject to Section 9(e) below, a Note may be transferred in whole or in part (in the principal amount of US$10,000 and integral multiples of US$1,000 in excess thereof) by the holder or holders surrendering the

Note for registration of transfer at the office of the Registrar or at the office of any transfer agent, duly endorsed by, or accompanied by a written instrument of transfer in form satisfactory to the Republic and the Registrar or any such transfer agent, as the case may be, duly executed by, the holder or holders thereof or such holder's or holders' attorney-in-fact or attorneys-in-fact duly authorized in writing.

(d) The costs and expenses of effecting any exchange or registration of transfer pursuant to the foregoing provisions, except for the expenses of delivery by other than regular mail (if any) and except, if the Republic shall so require, the payment of a sum sufficient to cover any tax or other governmental charge or insurance charges that may be imposed in relation thereto or, in connection with Section 9(a) above, the fees and expenses of the Registrar or Fiscal Agent, will be borne by the Republic.

(e) The Registrar may decline to register the transfer or exchange of Notes for a period of 15 days preceding the due date for any payment of principal of or interest on the Notes.

10. Negative Pledge. (a) Negative Pledge. So long as any Note remains outstanding (as defined in the Fiscal Agency Agreement), the Republic will not create or permit to subsist any Security (as defined herein) upon the whole or any part of its present or future revenues, property or assets to secure any present or future Public External Indebtedness (as defined herein) of the Republic without at the same time or prior thereto securing the Notes equally and ratably therewith or providing such other security for the Notes as shall be approved by the holders of a majority of the aggregate principal amount outstanding of the Notes.

(b) Exceptions. The following exceptions apply to the Republic's obligations under subparagraph (a) above:

(i) any Security upon property to secure Public External Indebtedness of the Republic incurred for the purpose of financing the acquisition of such property and any renewal or extension of any such Security which is limited to the original property covered thereby and which secures any renewal or extension of the original secured financing;

(ii) any Security existing upon property to secure Public External Indebtedness of the Republic at the time of the acquisition of such property and any renewal or extension of any such Security which is limited to the original property covered thereby and which secures any renewal or extension of the original secured refinancing;

(iii) any Security in existence as of the date of the Fiscal Agency Agreement or any renewal or extension thereof which secures only the renewal or extension of the original secured financing;

(iv) any Security securing Public External Indebtedness incurred for the purpose of financing all or part of the costs of the acquisition, construction or development of a project or any renewal or extension of such Security, provided that (A) the holders of such Public External Indebtedness expressly agree to limit their recourse to the assets and revenues of such project or the proceeds of insurance thereon as the principal source of repayment of such Public External Indebtedness and (B) the property over which such Security is granted consists solely of such assets and revenues; and

(v) any Security or Securities in addition to those permitted pursuant to clauses (i) through (iv) above, and any renewal or extension thereof, provided that the aggregate amount of Public External Indebtedness secured by such additional Security or Securities shall not exceed the equivalent of US$25,000,000.

(c) Definitions. For the purposes of this Note:

(i) "External Indebtedness" means any Indebtedness which is issued pursuant to agreements or evidenced by instruments subject to Chapter XII of the Commerce Code of the Republic.

(ii) "Indebtedness" means any obligation (whether present or future, actual or contingent) for the payment or repayment of borrowed money or arising from bonds, debentures, notes or other similar instruments.

(iii) "Person" means any individual, company, corporation, firm, partnership, joint venture, association, organization, state or agency of a state or other entity, whether or not having a separate legal personality.

(iv) "Public External Indebtedness" means any External Indebtedness which is in the form of, or represented by, bonds, notes or other securities which are or are intended to be or are securities which are commonly quoted, listed or ordinarily dealt in on any stock exchange, automated trading system, over-the-counter or other securities market (including, without limiting the generality of the foregoing, securities eligible for resale pursuant to Rule 144A under the Securities Act), and which has an original maturity of more than one year or is combined with a commitment so that the original maturity of one year or less may be extended at the option of the Republic to a period in excess of one year.

(v) "Security" means any mortgage, pledge, lien, hypothecation, security interest or other charge or encumbrance including, without limitation, any equivalent created or arising under the laws of the Republic.

11. Covenants. So long as any Note is outstanding, the Republic will:

(a) Ranking: ensure that its obligations under the Notes will at all times constitute direct, general and unconditional obligations of the Republic ranking at all times *pari passu* without any preference among themselves and at least equally with all other present and future unsecured and unsubordinated Public External Indebtedness of the Republic; and

(b) Listing: use reasonable efforts to maintain the listing of the Notes on the Luxembourg Stock Exchange.

12. Modifications, Amendments and Waivers. (a) At any meeting of Noteholders duly called and held as specified in the Fiscal Agency Agreement, upon the affirmative vote, in person or by proxy thereunto duly authorized in writing, of the holders of not less than 66⅔% in aggregate principal amount of the Notes then outstanding represented at such meeting, or with the written consent of the holders of not less than 66⅔% in aggregate principal amount of the Notes then outstanding, the Republic and the Fiscal Agent, upon agreement between themselves, may modify, amend or supplement the terms of the Notes or the Fiscal Agency Agreement, in any way, and the holders of Notes may make, take or give any request, demand, authorization, direction, notice, consent, waiver or other action provided by the Fiscal Agency Agreement or the Notes to be made, given or taken by Noteholders; provided, however, that no such action may, without the consent or affirmative vote, in person or by proxy thereunto duly authorized in writing, of the holders of not less than 75% in aggregate principal amount of the Notes then outstanding, (i) change the due date for the payment of the principal of (or premium, if any) or any installment of interest on any Note, (ii) reduce the principal amount of any Notes, the portion of such principal amount that is payable upon acceleration of the maturity of such Notes, the interest rate thereon or the premium payable upon redemption thereof, (iii) change the coin or currency in which payment with respect to interest, premium or principal in respect of Notes is payable or the place or places in which any such payment is required to be made, (iv) shorten the period during which the Republic is not permitted to redeem the Notes, or permit the Republic to redeem the Notes if, prior to such action, the Republic is not permitted to do so, (v) reduce the proportion of the principal amount of Notes the vote or consent of the holders of which is necessary to modify, amend or supplement the Fiscal Agency Agreement or the terms and conditions of the Notes or to make, take or give any request, demand, authorization, direction, notice, consent, waiver or other action provided hereby or thereby to be made, taken or given, (vi) change the obligation of the Republic to pay additional amounts, if any, pursuant to the Notes, (vii) amend the definition of "Outstanding" in Section 1.1 of the Fiscal Agency Agreement, (viii) change the governing law provisions of the Notes, (ix) change the Republic's appointment of an agent for the service of process, the Republic's agreement not to raise certain defenses with respect to its sovereign immunity or the Republic's agreement to submit to arbitration in respect of disputes relating to or arising under the Fiscal Agency Agreement or the Notes, each as set forth in Sections 17 and 18 of the Fiscal Agency Agreement and in the Notes, (x) change the ranking of the Notes as set forth in Paragraph 1(b) hereof or (xi) in

connection with an offer to acquire all or any portion of the Notes where the consideration consists of either cash, new securities to be issued by the Republic, or any combination of the foregoing, amend any Event of Default. Any such modification, amendment or supplement shall be binding on all Noteholders.

(b) The Republic and the Fiscal Agent may, upon agreement between themselves, without the vote or consent of any Noteholder modify, amend or supplement the Fiscal Agency Agreement or the Notes for the purposes of curing any ambiguity, or curing, correcting or supplementing any defective or inconsistent provisions contained therein or in any manner which the Republic and the Fiscal Agent may deem mutually necessary or desirable that will not adversely affect, in any material respect, the interests of the Noteholders.

13. Notices. All notices to holders of Notes will be valid if (a) given in writing and mailed to the holders of Notes at their respective addresses shown in the Note register and (b) (so long as the Notes are listed on the Luxembourg Stock Exchange and the rules of such Exchange so require) published in a leading newspaper having general circulation in Luxembourg (which is expected to be the *Luxemburger Wort*) or in such other publication or city or cities as specified in the Fiscal Agency Agreement. Any such notice shall be deemed to have been given (x) on the date of mailing, in the case of mailed notice, and (y) on the date of such publication or, if published more than once, on the first date on which publication is made, in the case of published notice.

14. Prescription. All claims against the Republic for payment of principal of or interest on or in respect of the Notes shall be prescribed unless made within five years from the date on which such payment first became due.

15. Governing Law. These Notes are governed by, and construed in accordance with, the law of the State of New York, except that all matters concerning authorization and execution by the Republic, as well as the bringing of any actions and the enforcement of any judgment against the Republic in the courts of the Republic, will be governed by the laws of the Republic.

16. Arbitration. Any dispute, controversy or claim arising out of or relating to the Notes (other than any action arising out of or based on the United States federal or state securities laws), including the performance, interpretation, construction, breach, termination or invalidity thereof shall be finally settled by arbitration in accordance with the Arbitration Rules of the United Nations Commission on International Trade Law (excluding Article 26 thereof) as in effect on the date of the Fiscal Agency Agreement (the "UNCITRAL Arbitration Rules"). The number of arbitrators shall be three, to be appointed in accordance with Section II of the UNCITRAL Arbitration Rules. The appointing authority shall be the Chairman of the International Court of Arbitration of the International Chamber of Commerce. The third arbitrator may be (but need not be) of the same nationality as any of the parties to the arbitration. The place of arbitration shall be New York, New York. The language to be used in the arbitration proceedings shall be English. Any arbitral tribunal constituted under this paragraph shall make its decisions entirely on the basis of the substantive law of the State of New York.

The decision of any arbitral tribunal shall be final to the fullest extent permitted by law, and a court judgment may be entered thereon by any Salvadoran court lawfully entitled to enter such judgment. In any arbitration or related legal proceedings for the conversion of an arbitral award into a judgment, the Republic will not raise any defense that it could not raise but for the fact that it is a sovereign state. The Republic has not consented to the jurisdiction of any court outside El Salvador, in connection with actions arising out of or based on the Notes or in connection with the enforcement of any judgment arising out of such actions, nor has the Republic appointed an agent for service of process outside El Salvador. The Republic waives any *forum non conveniens* defense in any proceeding in El Salvador.

No arbitration proceedings hereunder shall be binding upon or in any way affect the right or interest of any person other than the claimant or respondent with respect to such arbitration.

The Republic's consent to arbitration shall not preclude a holder of any Note from instituting legal proceedings against the Republic in the courts of El Salvador.

17. Sovereign Immunity. The Republic represents and warrants that it has no right to immunity on the grounds of sovereignty or otherwise, from the execution of any judgment in El Salvador, or from the execution or enforcement in El Salvador of any arbitral award (except, in each case, for the limitation on alienation of public property) in respect of any proceeding or any other matter arising out of or relating to its obligations contained in the Notes. The enforcement by a Salvadoran court of a foreign arbitral award is subject to recognition by the Supreme Court of Justice of the Republic, which will recognize such award if all the required formalities are observed and the award does not contravene Salvadoran national sovereignty, public policy and "good morals." The public property (*bienes de uso público*) of the Republic located in El Salvador is not subject to execution or attachment, either prior or after judgment. The execution of a judgment against El Salvador in El Salvador is only available in accordance with the procedures set forth in Article 450 et seq. of the Salvadoran Civil Procedure Code, which envisions registration of the judgment for inclusion in the budget for payment in a subsequent fiscal year of the Republic.

The Republic hereby irrevocably waives, to the fullest extent permitted by law, any requirement or other provision of law, rule, regulation or practice which requires or otherwise establishes as a condition to the institution, prosecution or completion of any action or proceedings (including appeals) in El Salvador arising out of or relating to the Notes, the posting of any bond or the furnishing, directly or indirectly, of any other security.

18. Judgment Currency. All payments required to be made hereunder by the Republic shall be in US dollars, regardless of any law, rule, regulation or statute, whether now or hereafter in existence or in effect in any jurisdiction, which affects or purports to affect such obligations. The obligation of the Republic in respect of any such amount due hereunder shall, notwithstanding any payment in any other currency (whether pursuant to a judgment or otherwise), be discharged only to the extent of the amount of US dollars that any of the Agents may, in accordance with normal banking procedures, purchase with the sum paid in such other currency (after any premium and costs of exchange) on the Business Day immediately following the day on which any of the Agents receives such payments. If the amount in US dollars that may be so purchased for any reason falls short of the amount originally due, the Republic shall pay such additional amounts, in US dollars, as may be necessary to compensate for such a shortfall. Any obligation of the Republic not discharged by such payment shall be due as a separate and independent obligation and, until discharged as provided herein, shall continue in full force and effect.

SUBSCRIPTION AND SALE

Citigroup Global Markets Inc. (the "Manager") has, pursuant to a Subscription Agreement dated September 14, 2004 (the "Subscription Agreement"), agreed with the Republic to subscribe and pay for the Notes in the following amounts:

Manager	Aggregate Principal Amount
Citigroup Global Markets Inc.	US$286,458,000
Total	US$286,458,000

The Subscription Agreement provides that the obligations of the Manager are subject to certain conditions precedent, and that the Manager are committed to take and to pay for all of the Notes if any are taken. The Republic has agreed to indemnify the Manager against certain liabilities in connection with the offer and sale of the Notes, and to contribute to payments which the Manager may make in respect thereof.

The Notes have not been and will not be registered under the Securities Act and may not be offered or sold within the United States or to, or for the account or benefit of, United States persons except to qualified institutional buyers in reliance on Rule 144A and to certain persons in offshore transactions in reliance on Regulation S. In addition, until 40 days after the date of delivery of the Notes, an offer or sale of any of the Notes within the United States by a dealer (whether or not participating in the offering) may violate the registration requirements of the Securities Act if such offer or sale is made otherwise than pursuant to Rule 144A.

The Manager proposes to offer the Notes to certain persons in offshore transactions in reliance on Regulation S and in accordance with applicable law, and proposes to offer the Notes to qualified institutional buyers in the United States pursuant to Rule 144A. The Manager has agreed that, except as permitted under the Subscription Agreement, it will not offer, sell or deliver the Notes within the United States. Terms used in this paragraph have the meanings given to them by Regulation S. Transfer of the Notes will be restricted as described under "Transfer Restrictions."

Although application is being made to list the Notes on the Luxembourg Stock Exchange, the listing does not assure that a trading market for the Notes will develop. The Manager intends to make a secondary market for the Notes. However, it is not obligated to do so and may discontinue making a secondary market for the Notes at any time without notice. No assurance can be given as to how liquid the trading market for the Notes will be.

As the offering of the Notes has not been cleared by CONSOB (the Italian Securities Exchange Commission) pursuant to Italian securities legislation, the Manager has represented and agreed that it will not offer, sell or deliver Notes, nor distribute copies of the Offering Circular nor any other document relating to the Notes in the Republic of Italy, except:

(i) to professional investors *("operatori qualificati")*, as defined in Article 31, second paragraph, of CONSOB Regulation No. 11522 of 1(st) July, 1998, as amended;

(ii) in circumstances which are exempted from the rules on solicitation of investments pursuant to Article 100 of Legislative Decree No. 58 of 24(th) February, 1998 and Article 33, first paragraph, of CONSOB Regulation No. 11971 of 14(th) May, 1999, as amended; or

(iii) to an Italian resident who submits an unsolicited offer to purchase the Notes.

The Manager also represents and agrees that the Notes shall not be placed, sold and/or offered in the primary market to retail individuals residing in Italy.

The Notes shall not be placed, sold and/or offered either in the primary or in the secondary market to individuals residing in Italy.

The Manager represents, warrants and agrees that it has complied and will comply with all applicable provisions of the Financial Services and Markets Act 2000 with respect to anything done by it in relation to the Notes in, from or otherwise involving the United Kingdom.

Each purchaser of Notes must comply with all applicable laws and regulations in force in any jurisdiction in which it purchases, offers or sells Notes or possesses or distributes this Offering Circular or any part of it and must obtain any consent, approval or permission required by it for the purchase, offer or sale by it of Notes under the laws and regulations in force in any jurisdiction to which it is subject or in which it makes such purchases, offers or sales and neither the Republic nor the Manager shall have any responsibility therefor.

The Manager may engage in over-allotment, stabilizing transactions, syndicate covering transactions and penalty bids in accordance with Regulation M under the U.S. Securities Exchange Act of 1934 (the "Exchange Act"). Over-allotment involves sales in excess of the offering size, which creates a short position for the Manager. Stabilizing transactions permit bids to purchase the underlying security so long as the stabilizing bids do not exceed a specified maximum. Covering transactions involve purchases of the Notes in the open market after the distribution has been completed in order to cover short positions. Penalty bids permit the Manager to reclaim a selling concession from a dealer when the Notes originally sold by such dealer are purchased in a stabilizing transaction or a covering transaction to cover short positions. Such stabilizing transactions, covering transactions and penalty bids may cause the price of the Notes to be higher than it would otherwise be in the absence of such transactions. Stabilizing transactions, if commenced, may be discontinued at any time.

It is expected that delivery of the Notes will be made against payment therefor on or about the date specified on the cover page of this Offering Circular, which will be the fifth business day following the date of pricing of the Notes (this settlement cycle being referred to as "T+5"). Under Rule 15c6-1 under the Exchange Act, trades in the secondary market generally are required to settle in three business days, unless the parties to any such trade expressly agree otherwise. Accordingly, U.S. purchasers who wish to trade Notes on the date of pricing or the next succeeding business day will be required, by virtue of the fact that the Notes initially will settle in T+5, to specify an alternate settlement cycle at the time of any such trade to prevent a failed settlement. Purchasers of Notes in other countries who wish to trade the Notes on the date of pricing or the next succeeding business day should consult their own advisor.

BOOK-ENTRY SETTLEMENT AND CLEARANCE

Global Notes

The notes will initially be issued in the form of two registered notes in global form, without interest coupons, as follows:

- notes sold to qualified institutional buyers in reliance on Rule 144A under the Securities Act will be represented by a global note (which we refer to in this Offering Circular as the "Restricted Global Note"); and

- notes sold in offshore transactions to non-U.S. persons in reliance on Regulation S will be represented by a global note (which we refer to in this Offering Circular as the "Regulation S Global Note").

Upon issuance, each of the global notes will be deposited with the Fiscal Agent (as defined in "Terms and Conditions of the Notes") as custodian for DTC and registered in the name of a nominee of DTC.

Ownership of beneficial interests in each global note will be limited to persons who have accounts with DTC (which we refer to in this offering memorandum as the "DTC participants") or persons who hold interests through DTC participants. The Republic expects that under procedures established by DTC:

- upon deposit of each global note with DTC's custodian, DTC will credit portions of the principal amount of the global note to the accounts of the DTC participants designated by the Manager; and

- ownership of beneficial interests in each global note will be shown on, and transfer of ownership of those interests will be effected only through, records maintained by DTC (with respect to interests of DTC participants) and the records of DTC participants (with respect to other owners of beneficial interests in each global note).

Investors may hold their interests in the Regulation S Global Note directly through Euroclear or Clearstream Banking, if they are participants in those systems, or indirectly through organizations that are participants in those systems. Investors may also hold their interests in the Regulation S Global Note through organizations other than Euroclear or Clearstream Banking that are DTC participants. Each of Euroclear and Clearstream Banking will appoint a DTC participant to act as its depositary for the interests in the Regulation S Global Note that are held within DTC for the account of each of these settlement systems on behalf of its respective participants.

Beneficial interests in the global notes may not be exchanged for notes in physical certificated form except in the limited circumstances described below.

Each global note and beneficial interests in each global note will be subject to restrictions on transfer as described under "Transfer Restrictions."

Exchanges between the Global Notes

Beneficial interests in one global note may generally be exchanged for interests in another global note. Depending on whether the transfer is being made during or after the 40-day restricted period, and to which global note the transfer is being made, the Fiscal Agent may require the seller to provide certain written certifications in the form provided in the Fiscal Agency Agreement (as defined in "Terms and Conditions of the Notes").

A beneficial interest in a global note that is transferred to a person who takes delivery through another global note will, upon transfer, become subject to any transfer restrictions and other procedures applicable to beneficial interests in the other global note.

Book-Entry Procedures for the Global Notes

All interests in the global notes will be subject to the operations and procedures of DTC and, if applicable, Euroclear and Clearstream Banking. The Republic provides the following summaries of those operations and procedures solely for the convenience of investors. The operations and procedures of each settlement system are controlled by that settlement system and may be changed at any time. Neither the Republic nor the Manager is responsible for those operations or procedures.

DTC has advised that it is:

- a limited purpose trust company organized under the laws of the State of New York;
- a "banking organization" within the meaning of the New York State Banking Law;
- a member of the U.S. Federal Reserve System;
- a "clearing corporation" within the meaning of the Uniform Commercial Code; and
- a "clearing agency" registered under Section 17A of the U.S. Securities Exchange Act of 1934.

DTC was created to hold securities for its participants and to facilitate the clearance and settlement of securities transactions between its participants through electronic book-entry changes to the accounts of its participants. DTC's participants include securities brokers and dealers, including the Manager; banks and trust companies; clearing corporations; and other organizations. Indirect access to DTC's system is also available to others such as banks, brokers, dealers and trust companies; these indirect participants clear through or maintain a custodial relationship with a DTC participant, either directly or indirectly. Investors who are not DTC participants may beneficially own securities held by or on behalf of DTC only through DTC participants or indirect participants in DTC.

So long as DTC's nominee is the registered owner of a global note, that nominee will be considered the sole owner or holder of the Notes represented by that global note for all purposes under the Fiscal Agency Agreement. Except as provided below, owners of beneficial interests in a global note:

- will not be entitled to have Notes represented by the global note registered in their names;
- will not receive or be entitled to receive physical, certificated notes; and
- will not be considered the owners or holders of the Notes under the Fiscal Agency Agreement for any purpose, including with respect to the giving of any direction, instruction or approval to the fiscal agent under the Fiscal Agency Agreement.

As a result, each investor who owns a beneficial interest in a global note must rely on the procedures of DTC to exercise any rights of a holder of Notes under the Fiscal Agency Agreement (and, if the investor is not a participant or an indirect participant in DTC, on the procedures of the DTC participant through which the investor owns its interest in the Notes).

Payments of principal and interest with respect to the Notes represented by a global note will be made by the Fiscal Agent to DTC's nominee as the registered holder of the global note. Neither the Republic nor the Fiscal Agent will have any responsibility or liability for the payment of amounts to owners of beneficial interests in a global note, for any aspect of the records relating to or payments made on account of those interests by DTC, or for maintaining, supervising or reviewing any records of DTC relating to those interests.

Payments by participants and indirect participants in DTC to the owners of beneficial interests in a global note will be governed by standing instructions and customary industry practice and will be the responsibility of those participants or indirect participants and DTC.

Transfers between participants in DTC will be effected under DTC's procedures and will be settled in same-day funds. Transfers between participants in Euroclear or Clearstream Banking will be effected in the ordinary way under the rules and operating procedures of those systems.

Cross-market transfers between DTC participants, on the one hand, and participants in Euroclear or Clearstream Banking, on the other hand, will be effected within DTC through the DTC participants that are acting as depositaries for Euroclear and Clearstream Banking. To deliver or receive an interest in a global note held in a Euroclear or Clearstream Banking account, an investor must send transfer instructions to Euroclear or Clearstream Banking, as the case may be, under the rules and procedures of that system and within the established deadlines of that system. If the transaction meets its settlement requirements, Euroclear or Clearstream Banking, as the case may be, will send instructions to its DTC depositary to take action to effect final settlement by delivering or receiving interests in the relevant global notes in DTC, and making or receiving payment under normal procedures for same-day funds settlement applicable to DTC. Euroclear and Clearstream Banking participants may not deliver instructions directly to the DTC depositaries that are acting for Euroclear or Clearstream Banking.

Because of time zone differences, the securities account of a Euroclear or Clearstream Banking participant that purchases an interest in a global note from a DTC participant will be credited on the business day for Euroclear or Clearstream Banking immediately following the DTC settlement date. Cash received in Euroclear or Clearstream Banking from the sale of an interest in a global note to a DTC participant will be received with value on the DTC settlement date but will be available in the relevant Euroclear or Clearstream Banking cash account as of the business day for Euroclear or Clearstream Banking following the DTC settlement date.

DTC, Euroclear and Clearstream Banking have agreed to the above procedures to facilitate transfers of interests in the global notes among participants in those settlement systems. However, the settlement systems are not obligated to perform these procedures and may discontinue or change these procedures at any time. Neither the Republic nor the Fiscal Agent will have any responsibility for the performance by DTC, Euroclear or Clearstream Banking or their participants or indirect participants of their obligations under the rules and procedures governing their operations.

Certificated Notes

Notes in physical, certificated form will be issued and delivered to each person that DTC identifies as a beneficial owner of the related Notes only if:

- DTC notifies the Republic at any time that it is unwilling or unable to continue as depositary for the global notes and a successor depositary is not appointed within 90 days;
- DTC ceases to be registered as a clearing agency under the U.S. Securities Exchange Act of 1934 and a successor depositary is not appointed within 90 days; or
- the Fiscal Agent receives a notice from the registered holder of the global note requesting exchange of a specified amount for individual note certificates following a failure to pay at maturity or upon acceleration of any Note.

TRANSFER RESTRICTIONS

The Notes are subject to the following restrictions on transfer. By purchasing Notes, each prospective investor will be deemed to have made the following acknowledgments, representations to and agreements with the Republic and the Manager:

(1) Each prospective investor acknowledges that:

- the Notes have not been registered under the Securities Act or any other securities laws and are being offered for resale in transactions that do not require registration under the Securities Act or any other securities laws; and
- unless so registered, the Notes may not be offered, sold or otherwise transferred except under an exemption from, or in a transaction not subject to, the registration requirements of the Securities Act or any other applicable securities laws, and in each case in compliance with the conditions for transfer set forth in paragraph (4) below.

(2) Each prospective investor represents that it is not an affiliate (as defined in Rule 144 under the Securities Act) of the Republic, that it is not acting on the Republic's behalf and that either:

- it is a qualified institutional buyer (as defined in Rule 144A) and is purchasing Notes for its own account or for the account of another qualified institutional buyer, and it is aware that the Manager is selling the Notes to it in reliance on Rule 144A; or
- it is not a U.S. person (as defined in Regulation S under the Securities Act) or purchasing for the account or benefit of a U.S. person, other than a distributor, and it is purchasing Notes in an offshore transaction in accordance with Regulation S.

(3) Each prospective investor acknowledges that neither the Republic nor the Manager nor any person representing the Republic or the Manager has made any representation to such prospective investor with respect to the Republic or the offering of the Notes, other than the information contained in this Offering Circular. Each prospective investor represents that it is relying only on this Offering Circular in making its investment decision with respect to the Notes. Each prospective investor agrees that it has had access to such information concerning the Republic and the Notes as it has deemed necessary in connection with its decision to purchase Notes, including an opportunity to ask questions of and request information from the Republic.

(4) Each prospective investor represents that it is purchasing Notes for its own account, or for one or more investor accounts for which it is acting as a fiduciary or agent, in each case not with a view to, or for offer or sale in connection with, any distribution of the Notes in violation of the Securities Act, subject to any requirement of law that the disposition of its property or the property of that investor account or accounts be at all times within its or their control and subject to its or their ability to resell the Notes pursuant to Rule 144A or any other available exemption from the registration requirements of the Securities Act. Each prospective investor agrees on its own behalf and on behalf of any investor account for which it is purchasing Notes, and each subsequent holder of the Notes by its acceptance of the Notes will agree, that until the end of the resale restriction period (as defined below), the Notes may be offered, sold or otherwise transferred only:

(a) to the Republic;

(b) under a registration statement that has been declared effective under the Securities Act;

(c) for so long as the Notes are eligible for resale under Rule 144A, to a person whom the seller reasonably believes is a qualified institutional buyer that is purchasing for its own account or for the account of another qualified institutional buyer and to whom it has given notice that the transfer is being made in reliance on Rule 144A;

(d) through offers and sales that occur outside the United States within the meaning of Regulation S; or

(e) under any other available exemption from the registration requirements of the Securities Act; subject in each of the above cases to any requirement of law that the disposition of the seller's property or the property of an investor account or accounts be at all times within the seller or such account's control.

Each prospective investor also acknowledges that:

- the above restrictions on resale will apply from the closing date of the offering of the Notes until the date that is two years after the later of the closing date and the last date that the Republic or any of its affiliates was the owner of the Notes or any predecessor of the Notes (which we refer to in this Offering Circular as the "resale restriction period"), and will not apply after the resale restriction period ends;

- the Republic and the fiscal agent reserve the right to require, in connection with any offer, sale or other transfer of Notes before the resale restriction period ends under clauses (d) and (e) above, the delivery of an opinion of counsel, certifications and/or other information satisfactory to the Republic and the fiscal agent; and

- each Note will contain a legend substantially to the following effect:

THIS NOTE HAS NOT BEEN AND WILL NOT BE REGISTERED UNDER THE U.S. SECURITIES ACT OF 1933, AS AMENDED (THE "SECURITIES ACT"), OR ANY SECURITIES LAW OF ANY STATE IN THE UNITED STATES OF AMERICA, AND MAY NOT BE REOFFERED, RESOLD, PLEDGED OR OTHERWISE TRANSFERRED EXCEPT AS PERMITTED BY THE FOLLOWING SENTENCES. THE HOLDER HEREOF, BY ITS ACCEPTANCE OF THIS NOTE, REPRESENTS, ACKNOWLEDGES AND AGREES THAT IT WILL NOT REOFFER, RESELL, PLEDGE OR OTHERWISE TRANSFER THIS NOTE EXCEPT (A) IN COMPLIANCE WITH RULE 144A UNDER THE SECURITIES ACT, TO A PERSON WHOM THE SELLER REASONABLY BELIEVES IS A QUALIFIED INSTITUTIONAL BUYER (AS DEFINED IN RULE 144A) PURCHASING FOR ITS OWN ACCOUNT, OR FOR THE ACCOUNT OF A QUALIFIED INSTITUTIONAL BUYER WHOM THE SELLER HAS INFORMED, IN EACH CASE, THAT THE REOFFER, RESALE, PLEDGE OR OTHER TRANSFER IS BEING MADE IN RELIANCE ON RULE 144A; (B) IN THE UNITED STATES, PURSUANT TO AN EXEMPTION FROM REGISTRATION UNDER THE SECURITIES ACT PROVIDED BY RULE 144 THEREUNDER (IF AVAILABLE AND UPON DELIVERY OF AN OPINION OF COUNSEL IN A FORM SATISFACTORY TO THE REPUBLIC); OR (C) OUTSIDE THE UNITED STATES IN COMPLIANCE WITH RULE 904 OF REGULATION S UNDER THE SECURITIES ACT; IN EACH CASE IN ACCORDANCE WITH ANY APPLICABLE SECURITIES LAW OF ANY STATE OF THE UNITED STATES AND ANY OTHER JURISDICTION. TERMS USED IN THIS PARAGRAPH HAVE THE MEANINGS GIVEN TO THEM BY REGULATION S OR RULE 144A, AS APPLICABLE, UNDER THE SECURITIES ACT.

Each prospective investor acknowledges that the Republic, the Manager and others will rely upon the truth and accuracy of the above acknowledgments, representations and agreements. Each prospective investor agrees that if any of the acknowledgments, representations or agreements such prospective investor is deemed to have made by its purchase of Notes is no longer accurate, it will promptly notify the Republic and the Manager. If any prospective investor is purchasing any Notes as a fiduciary or agent for one or more investor accounts, such prospective investor represents that it has sole investment discretion with respect to each of those accounts and that it has full power to make the above acknowledgments, representations and agreements on behalf of each account.

TAXATION

El Salvador Taxation

The following is a general discussion of Salvadoran tax considerations. The discussion is based upon the tax laws of El Salvador as in effect on the date of this Offering Circular, which are subject to change. Prospective investors should consult their own tax advisers with respect to Salvadoran tax consequences of the investment. This summary does not discuss the effects of any treaties that may be entered into by, or be effective with respect to, El Salvador.

Under current Salvadoran law, payments of interest on the Notes to residents and non-resident taxpayers of the Republic are subject to taxation in the Republic. Holding a Note will not by itself subject a Noteholder to any tax in El Salvador. Payments of principal and interest on the Notes are not subject to income or withholding tax in El Salvador to non-resident non-taxpayer Noteholders. In addition, gains realized on the sale or other disposition of the Notes are not subject to income or withholding tax in El Salvador provided the transaction takes place outside El Salvador or, if within El Salvador, through a Salvadoran stock exchange by an individual. There are no Salvadoran transfer, inheritance, gift or succession taxes applicable to the Notes.

United States Taxation

The following summary of certain United States federal income tax consequences to original purchasers of the Notes of the purchase, ownership and disposition of the Notes is based upon existing United States federal income tax law, which is subject to change, possibly with retroactive effect. This summary does not purport to discuss all aspects of United States federal income taxation which may be relevant to a particular investor in light of that investor's individual investment circumstances, such as investors whose functional currency is not the United States dollar or certain types of investors subject to special tax rules (*e.g.*, financial institutions, insurance companies, dealers in securities or currencies, certain securities traders, regulated investment companies, and tax-exempt organizations and investors holding Notes as a position in a "straddle," "conversion transaction," or "constructive sale" transaction). In addition, this summary does not discuss any foreign, state, or local tax considerations. This summary only applies to investors that hold Notes as "capital assets" (generally, property held for investment) within the meaning of the United States Internal Revenue Code of 1986, as amended (the "Code"). Prospective investors should consult their own tax advisors regarding the U.S. federal, state, and local, as well as foreign income and other, tax considerations of investing in the Notes.

For purposes of this summary, a "US Holder" includes an individual who is a citizen or resident of the United States, a corporation or partnership (including an entity treated as a corporation or partnership for United States federal income tax purposes) created or organized in or under the laws of the United States, any state of the United States or the District of Columbia (other than a partnership that is not treated as a United States person under any applicable Treasury regulations), an estate whose income is subject to United States federal income tax regardless of its source or a trust if a court within the United States is able to exercise primary supervision over the administration of the trust and one or more United States persons have the authority to control all substantial decisions of the trust. Notwithstanding the preceding sentence, to the extent provided in Treasury regulations, certain trusts in existence on August 20, 1996, and treated as United States persons under the Code and applicable Treasury regulations prior to that date, that elect to continue to be treated as United States persons under the Code or applicable Treasury regulations also will be US Holders. As used herein, the term "non-US Holder" means a holder of a Note that is not a US Holder.

Payments of Interest and Additional Amounts

Payments of interest on a Note (including Additional Amounts, if any) generally will be taxable to a US Holder as ordinary interest income at the time it is received or accrued, depending on the US Holder's regular method of tax accounting. Interest on the Notes will constitute income from sources outside the

United States but, with certain exceptions, will be treated separately, together with other items of "passive income" or "financial services income," for purposes of computing the foreign tax credit allowable under the U.S. federal income tax laws. If any foreign taxes were to be paid or withheld in respect of payments on the Notes, a US Holder might be eligible, subject to a number of complex limitations, for a foreign tax credit.

Sale, Exchange or Retirement of a Note

A US Holder will generally recognize taxable capital gain or loss upon the sale, exchange, retirement or other disposition of a Note (including payments as a result of an acceleration) in an amount equal to the difference between the amount realized upon that sale, exchange, retirement or other disposition (other than amounts representing accrued and unpaid interest) and that US Holder's adjusted tax basis in the Note. A US Holder's adjusted tax basis in a Note generally will equal that US Holder's initial investment in the Note. That gain or loss will generally be long-term capital gain or loss if the Note is held for more than one year, and generally will be U.S. source income or loss for U.S. foreign tax credit purposes. Under current law, net capital gains of individuals may be taxed at lower rates than items of ordinary income. The ability of a US Holder to offset capital losses against ordinary income is limited.

Non-US Holders

Subject to the discussion below of special rules that may apply to certain non-US Holders and the discussion below of "backup" withholding, payments of interest and any Additional Amounts on the Notes are currently not subject to U.S. federal income tax, including withholding tax, if paid to a "non-US Holder," whether or not that non-US Holder is engaged in a trade or business in the United States, unless:

(i) the holder is an insurance company carrying on a U.S. insurance business to which the interest is attributable, within the meaning of the Code, or

(ii) the holder has an office or other fixed place of business in the United States to which the interest is attributable and the interest is derived in the active conduct of a banking, financing or similar business within the United States and certain other conditions exist.

In addition, (i) subject to the discussion below of special rules that may apply to certain non-US Holders and the discussion below of backup withholding, a non-US Holder will not be subject to U.S. federal income or withholding tax on any gain realized on the sale or exchange of a Note, and (ii) the Notes will be deemed to be situated outside the United States for purposes of the U.S. federal estate tax and will not be includible in the gross estate for purposes of that tax in the case of a non-US Holder who was not a citizen of the United States at the time of death if income on the Notes would not have been effectively connected with a United States trade or business at the time of the holder's death.

Special rules may apply in the case of non-US Holders (i) that are engaged in a U.S. trade or business, (ii) that are former citizens or long-term residents of the United States, "controlled foreign corporations," "foreign personal holding companies," corporations which accumulate earnings to avoid U.S. federal income tax, and certain foreign charitable organizations, each within the meaning of the Code, or (iii) certain non-resident alien individuals who are present in the United States for 183 days or more during a taxable year. Such persons are urged to consult their U.S. tax advisors before purchasing Notes.

Backup Withholding and Information Reporting

In general, information reporting requirements will apply to payments of principal of and interest and any Additional Amounts on the Notes to non-corporate US Holders if those payments are made within the United States or by or through a custodian or nominee that is a United States Controlled Person, as defined below. Backup withholding tax will apply to those payments if such a US Holder fails to provide an accurate taxpayer identification number or, in the case of interest payments and the accrual of interest,

fails to certify that it is not subject to backup withholding or is notified by the Internal Revenue Service that it has failed to report all interest and dividends required to be shown on its United States federal income tax return. Payments of principal and interest to beneficial owners who are non-US Holders generally will not be subject to information reporting and backup withholding, but those holders may be required to establish their exemption from information reporting and backup withholding by certifying their status on United States Internal Revenue Service Forms W-8BEN.

The payment of proceeds of a sale or redemption of Notes effected at the U.S. office of a broker will generally be subject to the information reporting and backup withholding rules described above. In addition, the information reporting rules will apply to payments of proceeds of a sale or redemption effected at a foreign office of a broker that is a United States Controlled Person, unless the broker has documentary evidence that the holder or beneficial owner is not a US Holder or the holder or beneficial owner otherwise establishes an exemption.

Under U.S. Treasury regulations, a payment to a foreign partnership is treated, with some exceptions, for backup withholding purposes as a payment directly to the partners, so that the partners are required to provide any required certifications. Investors who hold a Note through a partnership or other pass-through entity should consult their own tax advisors regarding the application of these regulations to their own situation.

A "United States Controlled Person" is:

- a United States person (as defined in the United States Treasury regulations);
- a controlled foreign corporation for United States federal income tax purposes;
- a foreign person 50% or more of whose gross income is derived for tax purposes from a U.S. trade or business for a specified three-year period; or
- a foreign partnership in which United States persons hold more than 50% of the income or capital interests or which is engaged in a U.S. trade or business.

Any amounts withheld under the backup withholding rules from a payment to a holder of a Note generally will be allowed as a refund or a credit against the holder's United States federal income tax liability as long as the holder provides the required information to the Internal Revenue Service.

European Union Directive on Taxation of Certain Interest Payments

The Council of Economic and Finance Ministers of the European Union (the "EU") has adopted a new directive regarding the taxation of savings income. Subject to a number of important conditions being met, it is proposed that EU member states ("Member States") will be required from July 1, 2005 to provide to the tax authorities of other Member States details of payments of interest and other similar income paid by a person to an individual in another Member State, except that Austria, Belgium and Luxembourg will instead impose a withholding system for a transitional period unless during such period they elect otherwise. Where any obligation to withhold amounts in respect of payments on the Notes arises as a result of this directive, there will be no obligation of the Republic to pay Additional Amounts. Holders should consult their own tax advisors regarding the implications of the directive in their particular circumstances.

VALIDITY OF THE NOTES

The validity of the Notes will be passed upon on behalf of the Republic by Lic. Belisario Amadeo Artiga Artiga, the *Fiscal General* ("Attorney General") of the Republic and by Rodriguez, Zelaya & Asociados, Salvadoran counsel to the Republic, and by Arnold & Porter LLP, U.S. counsel to the Republic. The validity of the Notes will be passed upon on behalf of the Manager by Francisco Armando Arias, Salvadoran counsel to the Manager, and by Cleary, Gottlieb, Steen & Hamilton, U.S. counsel to the Manager. As to all matters of Salvadoran law, Arnold & Porter LLP will rely on the opinions of the Attorney General and Rodriguez, Zelaya & Asociados, and Cleary, Gottlieb, Steen & Hamilton will rely upon the opinion of Francisco Armando Arias.

GENERAL INFORMATION

1. The Regulation S Global Note has been accepted for clearance through Euroclear and Clearstream, Luxembourg and the Restricted Global Note has been accepted for clearance through DTC. The initial CUSIP numbers for the Regulation S Global Note and the Restricted Global Note are P01012 AM 8 and 283875 AM 4, respectively. The initial common codes for the Regulation S Global Note and the Restricted Global Note are 020163232 and 020163186, respectively, and the initial International Securities Identification Numbers for the Regulation S Global Note and the Restricted Global Note are USP01012AM84 and US283875AM40, respectively.

2. The Republic has obtained all necessary consents, approvals and authorizations in the Republic of El Salvador in connection with the issue and performance of the Notes. The issue of the Notes is authorized under Legislative Decree No. 349 (as published in the *Diario Oficial* on June 17, 2004) of the Republic's Legislative Assembly.

3. Neither the Republic nor any Ministry of the Republic is involved in any litigation or arbitration proceedings which are material in the context of the issue of the Notes nor, so far as the Republic is aware, are any such litigation or arbitration proceedings pending or threatened.

4. Application has been made to list the Notes on the Luxembourg Stock Exchange. So long as any of the Notes are listed on the Luxembourg Stock Exchange and the rules of such stock exchange shall so require, the Republic will maintain a paying agent and transfer agent in Luxembourg.

5. Copies of the following documents may be obtained on any business day (Saturdays, Sundays and public holidays excepted) at the office of the Paying Agent in Luxembourg so long as any of the Notes are listed on the Luxembourg Stock Exchange:

(a) the Fiscal Agency Agreement incorporating the forms of Global Notes and Note Certificates;

(b) copies of the Constitution of the Republic, and the Legislative Decrees of the Republic referred to in paragraph 2 above (in Spanish); and

(c) copies of the Republic's consolidated public sector fiscal accounts for the last calendar year (as and when available in English).

6. Other than as disclosed herein, there has been no material adverse change in the financial condition of the Republic which is material in the context of the issue of the Notes since December 31, 2003.

ISSUER

Republic of El Salvador
Ministry of Finance
Boulevard Los Héroes No. 1231
Edificio Ministerio de Hacienda
San Salvador
El Salvador

FISCAL AGENT, PRINCIPAL PAYING AGENT, REGISTRAR AND TRANSFER AGENT

Citibank, N.A.
5 Carmelite Street
London EC4Y OPA
United Kingdom

UNDERWRITER

Citigroup Global Markets Inc.
390 Greenwich Street, 4th Floor
New York, New York 10013
United States

LEGAL ADVISORS TO THE REPUBLIC OF EL SALVADOR

As to United States Law
Arnold & Porter LLP
399 Park Avenue
New York, New York 10022
United States

As to Salvadoran Law
Lic. Belisario Amadeo Artiga Artiga
Fiscal General de la República
Pasaje El Rosal, No. 1-B
Final 51 Avenida Sur
Colonia El Rosal
San Salvador
El Salvador

As to Salvadoran Law
Rodriguez, Zelaya & Asociados, S.A.
Calle Sisimiles
Colonia Miramonte No. 2956
San Salvador
El Salvador

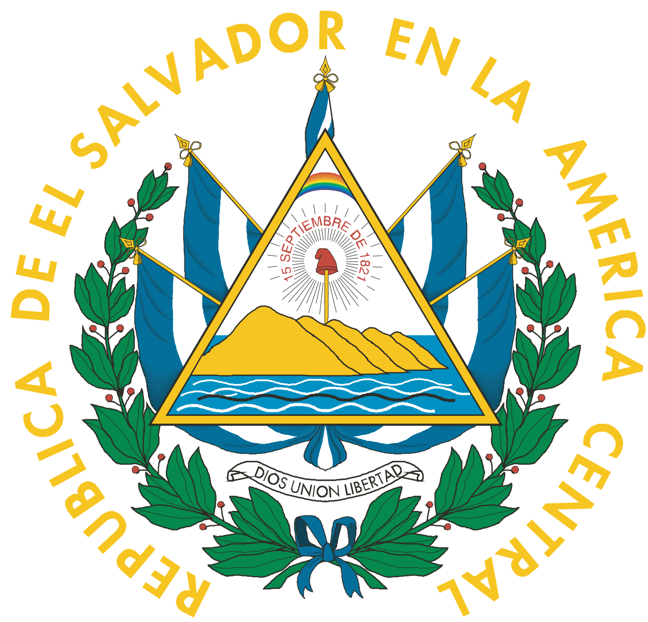
LEGAL ADVISORS TO THE MANAGER

As to United States Law
Cleary, Gottlieb, Steen & Hamilton
One Liberty Plaza
New York, New York 10006
United States

As to Salvadoran Law
Francisco Armando Arias
85 Ave. Nte. #825
Colonia Escalón
San Salvador
El Salvador

LUXEMBOURG TRANSFER, LISTING AND PAYING AGENT

Kredietbank S.A. Luxembourgeoise
43 Boulevard Royal
L-2955 Luxembourg
Luxembourg


REPUBLICA DE EL SALVADOR EN LA AMERICA CENTRAL
15 SEPTIEMBRE DE 1821
DIOS UNION LIBERTAD