

Country

Ecuador

Primary Analyst: Whitney Kane Gomez
949 760-2441
Morgan Stanley & Co. Incorporated

Country Update

April 21, 2005

Latest Developments

Politics

Events are still developing in Ecuador, though protests seem to have ended today. There are three stories to keep an eye on: Gutierrez, congress and Bucaram.

1. **Gutierrez.** Our understanding is that former President Gutierrez has left the Brazilian Embassy and is with the military. He is apparently weighing his options: either try to re-take power or depart the country. The most important factor for Gutierrez at this point appears to be what the Organization of American States determines about yesterday's events in Quito. Indications from the OAS that they believe something unconstitutional or improper occurred yesterday could give new wind to Gutierrez's sails, though at this point it is hard to envision him reestablishing himself as Ecuador's leader. Further, discussions in the OAS on this issue appear to be delayed until tomorrow, making it harder for Gutierrez to re-gain any kind of momentum.

2. **Congress.** The other developing situation is in congress. Recall that protesters this week and last were calling for all politicians, not just Gutierrez, to leave power. We understand that three members of congress have resigned from their positions in order to comply with what they viewed as the will of the people. Further resignations or additional protests calling for congress to dissolve itself could significantly complicate the outlook. If congress does resign, we believe the likelihood of earlier than scheduled (October 2006) presidential and congressional elections increases.

3. **Bucaram.** We have not been able to find any information on Abdala Bucaram's whereabouts. We believe that it is possible that he is en route to his home in Panama.

Scenarios

Despite the lack of clarity on the outlook, we see three possible scenarios playing out:

1. **Palacios establishes himself and remains in office until Gutierrez's term ends in January 2007.** In this scenario we do see risk to the economic policy outlook, particularly fiscal. Of significant note are comments that Palacios made this morning about making debt restructuring a top priority.
2. **Political pressure on President Palacios continues, and events related to congress and/or additional protests lead to early elections.** In this scenario we would expect to see economic policy remain on hold, with limited damage to the fiscal situation or resources safeguarded in the FEIREP.
3. **A continuation of the political uncertainty of earlier this week, caused by an attempt by former President Gutierrez to re-take power.** Given the slow pace at which the OAS is likely to rule, we see this as a very low probability scenario.

The only clearly bondholder-friendly scenario that we see is the second one (new elections). Though the economic policy outlook appears likely to change considerably, we continue to see Ecuador with significant local financing sources (this month's tax filings, the FEIREP and pension funds). Despite S&P's placing of Ecuador on watch for downgrade of its B-rating, we do not anticipate any external-debt related payments pressures. On the back of the large move we have seen in bonds already, we maintain our Overweight recommendation until there is more clarity on the political outlook.

The Primary Analyst(s) identified above certify that the views expressed in this report accurately reflect his/her/their personal views about the subject securities/instruments/issuers, and no part of his/her/their compensation was, is or will be directly or indirectly related to the specific views or recommendations contained herein.

This report has been prepared in accordance with our conflict management policy. The policy describes our organizational and administrative arrangements for the avoidance, management and disclosure of conflicts of interest. The policy is available at www.morganstanley.com/institutional/research.

Please see additional important disclosures at the end of this report.

Emerging Markets

A Palacios Administration

Given the difficulties that Palacios faced in the first hours of his presidency (lack of military support for multiple hours and still significant protests), we thought he might move slowly and tread carefully. The announcement this morning on restructuring debt indicates that he is likely to maintain a populist stance and could attempt to take aggressive action.

It is still very early, but we are seeing some signals from President Palacios on what his team could look like. He has named Mauricio Gandara as Interior Minister.

Gandara has government experience and is considered to be a centrist. He is perceived to be someone who can negotiate with groups from both ends of the political spectrum. We view this as a positive. Palacios also had advisers yesterday that are considered to be rather conservative and right wing. So while the statements from Palacios seem to indicate that he wants to bring new blood and the younger generation to government, he does seem to be relying on the counsel of more established, experienced people. This is somewhat positive, in our view.

Local consultants in Quito appear to believe that economist Rafael Correa could be named to head the finance ministry. Correa is US-educated and holds a PhD in economics. He hails from Guayaquil and has been supportive in the past of Palacios' views on loosening fiscal policy and reworking how the FEIREP is distributed. If

Correa is named, he is likely to find that the challenges of running the country's fiscal affairs are quite different from his experience in academia. We could find that he moves at a more measured pace in changing economic policy than his background may suggest. Instead of Correa, Palacios could also choose a more experienced figure to head up his economic policy. Again, the key issue for bondholders at this point is whether the new government moves ahead with today's idea of restructuring debt.

Critical to the outlook in Ecuador is the multilateral financing (\$600 million) that we expected the government to receive this year. While Palacios is likely to be open to the social development and project financing, it is less clear whether he will be open to following policy recommendations from the multilaterals. It is very possible that multilateral financing declines significantly on the back of this change in administration. The good near-term news is that the country's tax filings will take place this month and we expect the government to find itself with sufficient liquidity to manage the coming few months. Still, we find this morning's comments on debt very worrisome.

Ecuador's representatives at the FTA negotiations in Lima have asked to remain on as observers. While Palacios has said that he supports the idea of the FTA, he is likely to take a stronger stance on certain issues. We believe this likely means additional delays for Ecuador on this front.

Emerging Markets Rating Distribution Table*(as of April 1, 2005)*

Rating	Coverage Universe		Investment Banking Clients (IBC)		
	Count	% of Total	Count	% of Total IBC	% of Rating Category
Overweight	8	30%	4	57%	50%
Equal-weight	11	41%	1	14%	9%
Underweight	8	30%	2	29%	25%
Total	27		7		

Coverage includes all Emerging Market issuers that we currently rate. Investment Banking Clients are companies from whom Morgan Stanley or an affiliate received investment banking compensation in the last 12 months.

Analyst Ratings Definitions

Overweight (O) Over the next 6 months, the fixed income instrument's total return is expected to exceed the average total return of the relevant benchmark, as described in this report, on a risk adjusted basis.

Equal-weight (E) Over the next 6 months, the fixed income instrument's total return is expected to be in line with the average total return of the relevant benchmark, as described in this report, on a risk adjusted basis.

Underweight (U) Over the next 6 months, the fixed income instrument's total return is expected to be below the average total return of the relevant benchmark, as described in this report, on a risk adjusted basis.

More volatile (V) The analyst anticipates that this fixed income instrument is likely to experience significant price or spread volatility in the short term.

Local Markets Portfolio Model Portfolio*(as of April 1, 2005)*

FX	No. of Trades	% of FX Local Markets Portfolio	Interest Rate	No. of Trades	% of Interest Rate Portfolio
Bullish	2	100%	Bullish	5	100%
Bearish	0	0%	Bearish	0	0%
Total	2	100%	Total	5	100%

Important Disclosures on Subject Companies/Issuers

The information and opinions in this report were prepared by Morgan Stanley & Co. Incorporated and/or one or more of its affiliates (collectively, "Morgan Stanley") and the research analyst(s) named on page one of this report.

Issuer Name: Ecuador

Fixed Income Research 12-Month History

Issue Type: Sovereign Bonds

Current Rating: Overweight --as of 10/06/2004

Previous Rating: --as of 06/24/2004 --Equal-weight

Morgan Stanley policy prohibits research analysts from investing in securities/instruments in their MSCI sub industry. Analysts may nevertheless own such securities/instruments to the extent acquired under a prior policy or in a merger, fund distribution or other involuntary acquisition.

Morgan Stanley is involved in many businesses that may relate to companies or instruments mentioned in this report. These businesses include market making, providing liquidity and specialized trading, risk arbitrage and other proprietary trading, fund management, investment services and investment banking. Morgan Stanley trades as principal in the securities/instruments (or related derivatives) that are the subject of this report. Morgan Stanley may have a position in the debt of the Company or instruments discussed in this report.

Other Important Disclosures

The securities/instruments discussed in this report may not be suitable for all investors. This report has been prepared and issued by Morgan Stanley primarily for distribution to market professionals and institutional investor clients. Recipients who are not market professionals or institutional investor clients of Morgan Stanley should seek independent financial advice prior to making any investment decision based on this report or for any necessary explanation of its contents. This report does not provide individually tailored investment advice. It has been prepared without regard to the individual financial circumstances and objectives of persons who receive it. Morgan Stanley recommends that investors independently evaluate particular investments and strategies, and encourages investors to seek the advice of a financial advisor. The appropriateness of a particular investment or strategy will depend on an investor's individual circumstances and objectives. You should consider this report as only a single factor in making an investment decision.

Morgan Stanley fixed income research analysts, including those principally responsible for the preparation of this research report, receive compensation based upon various factors, including quality, accuracy and value of research, firm profitability or revenues (which include fixed income trading and capital markets profitability or revenues), client feedback and competitive factors. Analysts' compensation is not linked to investment banking or capital markets transactions performed by Morgan Stanley or the profitability or revenues of particular trading desks.

This report is not an offer to buy or sell any security/instrument or to participate in any trading strategy. In addition to any holdings disclosed in the section entitled "Important Disclosures on Subject Companies," Morgan Stanley and/or its employees not involved in the preparation of this report may have investments in securities/instruments or derivatives of securities/instruments of companies mentioned in this report, and may trade them in ways different from those discussed in this report. Derivatives may be issued by Morgan Stanley or associated persons.

Morgan Stanley makes every effort to use reliable, comprehensive information, but we make no representation that it is accurate or complete. We have no obligation to tell you when opinions or information in this report change.

With the exception of information regarding Morgan Stanley, reports prepared by Morgan Stanley research personnel are based on public information. Facts and views presented in this report have not been reviewed by, and may not reflect information known to, professionals in other Morgan Stanley business areas, including investment banking personnel.

The value of and income from investments may vary because of changes in interest rates, foreign exchange rates, default rates, prepayment rates, securities/instruments prices, market indexes, operational or financial conditions of companies or other factors. There may be time limitations on the exercise of options or other rights in securities/instruments transactions. Past performance is not necessarily a guide to future performance. Estimates of future performance are based on assumptions that may not be realized.

This report may include research based on technical analysis. Technical analysis is generally based on the study of trading volumes and price movements in an attempt to identify and project price trends. Technical analysis does not consider the fundamentals of the underlying issuer or instrument and may offer an investment opinion that conflicts with other research generated by Morgan Stanley. Investors may consider technical research as one input in formulating an investment opinion. Additional inputs should include, but are not limited to, a review of the fundamentals of the underlying issuer/security/instrument.

The model portfolio is a hypothetical portfolio and is not intended to reflect actual trading performance. As a hypothetical model, the portfolio does not necessarily represent a portfolio of securities that the Firm holds or trades. Any references to losses, gains or positions with respect to the portfolio represent hypothetical not actual losses, gains or positions.

To our readers in Taiwan: Information on securities/instruments that trade in Taiwan is distributed by Morgan Stanley & Co. International Limited, Taipei Branch (the "Branch"). Such information is for your reference only. The reader should independently evaluate the investment risks and is solely responsible for their investment decisions. This publication may not be distributed to the public media or quoted or used by the public media without the express written consent of Morgan Stanley. Information on securities/instruments that do not trade in Taiwan is for informational purposes only and is not to be

construed as a recommendation or a solicitation to trade in such securities/instruments. The Branch may not execute transactions for clients in these securities/instruments.

Certain information in this report was sourced by employees of the Shanghai Representative Office of Morgan Stanley Dean Witter Asia Limited for the use of Morgan Stanley Dean Witter Asia Limited.

THIS PUBLICATION IS DISSEMINATED IN JAPAN BY MORGAN STANLEY JAPAN LIMITED; IN HONG KONG BY MORGAN STANLEY DEAN WITTER ASIA LIMITED; IN SINGAPORE BY MORGAN STANLEY DEAN WITTER ASIA (SINGAPORE) PTE., REGULATED BY THE MONETARY AUTHORITY OF SINGAPORE, WHICH ACCEPTS RESPONSIBILITY FOR ITS CONTENTS; IN AUSTRALIA BY MORGAN STANLEY DEAN WITTER AUSTRALIA LIMITED A.B.N. 67 003 734 576, A LICENSED DEALER, WHICH ACCEPTS RESPONSIBILITY FOR ITS CONTENTS; IN CANADA BY MORGAN STANLEY CANADA LIMITED, WHICH HAS APPROVED OF, AND HAS AGREED TO TAKE RESPONSIBILITY FOR, THE CONTENTS OF THIS PUBLICATION IN CANADA; IN SPAIN BY MORGAN STANLEY, S.V., S.A., A MORGAN STANLEY GROUP COMPANY, WHICH IS SUPERVISED BY THE SPANISH SECURITIES MARKETS COMMISSION (CNMV) AND STATES THAT THIS DOCUMENT HAS BEEN WRITTEN AND DISTRIBUTED IN ACCORDANCE WITH THE RULES OF CONDUCT APPLICABLE TO FINANCIAL RESEARCH AS ESTABLISHED UNDER SPANISH REGULATIONS; IN THE UNITED KINGDOM BY MORGAN STANLEY & CO. INTERNATIONAL LIMITED, AUTHORISED AND REGULATED BY THE FINANCIAL SERVICES AUTHORITY; AND IN THE UNITED STATES BY MORGAN STANLEY & CO. INCORPORATED AND MORGAN STANLEY DW INC., WHICH ACCEPT RESPONSIBILITY FOR ITS CONTENTS. IN AUSTRALIA, THIS REPORT, AND ANY ACCESS TO IT, IS INTENDED ONLY FOR "WHOLESALE CLIENTS" WITHIN THE MEANING OF THE AUSTRALIAN CORPORATIONS ACT. NOT FOR DISTRIBUTION TO PRIVATE CUSTOMERS AS DEFINED BY THE UK FINANCIAL SERVICES AUTHORITY.

The trademarks and service marks contained herein are the property of their respective owners. Third-party data providers make no warranties or representations of any kind relating to the accuracy, completeness, or timeliness of the data they provide and shall not have liability for any damages of any kind relating to such data.

This report may not be sold or redistributed without the written consent of Morgan Stanley.

Morgan Stanley research is disseminated and available primarily electronically, and, in some cases, in printed form.

Additional information is available upon request.

30692 4/21/05 BL

The Americas

1585 Broadway
New York, New York 10036-8293
Tel: (212) 761-4000

Europe

25 Cabot Square, Canary Wharf
London E14 4QA, England
Tel: (44 20) 7425-8000

Japan

20-3, Ebisu 4-chome, Shibuya-ku
Tokyo 150-6008, Japan
Tel: (81 3) 5424-5000

Asia Pacific

Three Exchange Square
Hong Kong
Tel: (852) 2848-5200