EXECUTION COMMITTEE

ACT NUMBER 26-2006

Session 26-2006 celebrated in the *Banco de Guatemala* building located at *séptima avenida número veintidós guión cero uno, zona uno* of this city on Friday, June 23, two thousand six, as of sixteen hours and thirty minutes.

The Coordinator, with the corresponding quorum, for the consideration of the Execution Committee, submitted the project for the Order of the Day.

FIRST: Approval of Project for act number 25-2006, corresponding to the session celebrated on June 16, 2006.
(The project of act 25-2006 circulated.)

SECOND: Market information and monetary variables.

a) Money Market
b) Exchange Markets.
c) Indicative Variables
d) Estimated Monetization Flow

THIRD: Determination of Bidding Quotas for Term Deposits.

FOURTH: Discussion and definition of the guidelines of execution for the Monetary, Exchange rate and Credit Policy.

FIFTH: Other matters.

Not having more observations, the committee approves the order of the day.

FIRST: The coordinator has put to consideration the corresponding project act.

Not having any observations, the committee approved act number 25-2006.

SECOND: Information of markets and monetary variables.

The coordinator requested the following information be provided.

a) The Director of the Department of Monetary Stabilization Operations, regarding the Money market informed that during the period from June 19 to 23 of 2006, with partial data to date, registered an attraction of LTD's for Q2,612.0 million and maturity of Q2,229.1 million, which gave a result of net fund-raising for Q382.9 million, associated to the operations made in bidding (net fund-raising for Q3.3 million), in the Money Electronic Banking Table –MEBD- and in the stock exchange (net fund-raising of Q224.0 million) and at the window (net maturity for Q155.6 million).

Regarding the interest rates applied in fund raising through LTD's, it was indicated that during the period of June 19 to 23, 2006 for the biddings case, the cut interest rates were of: 5.00% for 91 days and of 6.22% for 364 days. On the other hand, in the MEBD and in the stock exchange the fund-raising took place for 7 days, at the leading interest rate of the monetary policy of 4.50% from June 19 to 21 and of 4.75% from June 22 to 23, 2006, according to the increase made to said interest rate for the Monetary Board in its April 21, 2006 session.

As for the weighted average interest rates of total operations of repurchase agreements made in the stock exchange of the country, it was indicated that, during the June 19 to 23, 2006 period, with partial data, the minimum was of 4.57%, observed June 22, 2006, and the maximum of 4.82%, registered on June 23, 2006. It also pointed out that the amounts negotiated were higher with public titles and that the average weighted interest rates during said period were of 4.62% for the public titles and of 5.85% for the titles of the financial sector.

On the other hand, it was informed that during the June 19 to 22, 2006 period, regarding Treasury-Bond operations the fund-raising registered was for Q100.0 million and maturity for US$78.1 million.

As to the long term deposit bidding positions in US dollars convened on June 21 and 23, 2006, it was mentioned that no bids were presented.

b) The Director for the Monetary Stabilization Operations Department regarding the Institutional Market for foreign currency reported that during the period of June 16 to 22, 2006, the average daily operations for purchase were of US$66.1 million and the sale was of US$62.9 million and that the exchange rates in the referred period remained stable. In effect, on Friday, June 16 they were of Q7.60503 per US$1.00 for purchase and of

Q7.62433 per US$1.00 for sale, on Monday, June 19 the rates were Q7.60664 and Q7.63056, on Tuesday, June 20 they were of Q7.60701 and Q7.62743, on Wednesday, June 21 they were Q7.61106 and Q7.62783, and finally, on Thursday, June 22 they were Q7.61321 y Q7.62755.

In the operations of the electronic systems of negotiations of foreign currency administered by the *Bolsa de Valores Nacional, S.A.* (National Stock Exchange, S.A.), for the period of June 19 to 23, 2006, it was commented that the Private Institutional Foreign Currency System –SPID-, the following operations were made: on Monday, June 19 for US$2.0 million, at a weighted average exchange rate of Q7.63100 per US$1.00, on Tuesday, June 20 for US$0.1 million, Q7.62500 and on Thursday, June 22 for US$0.4 million for Q7.62438. Regarding the Electronic Foreign Currency Negotiation System –SINEDI-, expressed that during the period there were no operations and only the *Banco de Guatemala* registered a daily purchase bid for US$10.0 million, with a price of Q7.58000, according to the guidelines of the Execution Committee.

On the other hand, they informed that the Future Foreign Currency Market that is operated by the National Stock Exchange, S.A., during the period of June 19 to 23, 2006, did not close operations. As for the closing price in reference up to Friday, June 23, they indicated that for maturity to settle in December 2006 was of Q7.62000.

c) The Director for the Economic Studies Department informed that on June 22, 2006, the excess of the daily legal reserve of the banking system was located at Q176.7 million, with an average position of Q204.0 million.

The highlights during the period of June 15 to 22, 2006 the main demonetizing factors were the increase in the balance of and the long term deposits constituted in the *Banco de Guatemala* for Q451.3 million and the deposits of the rest of the public sector in the Central Bank for Q107.8 million; and the decrease in the balance of the Net International Reserve –RIN- balance for the equivalent of Q561.6 million; while the main monetizing factors were the decrease in the deposits of the Central Government in the *Banco de Guatemala* for Q953.7 million and the daily legal reserve for Q117.6 million.

Regarding the indicative variables of the Monetary, Exchange Rate and Credit Policy they indicated that with the projection to May 2006, for December 2006 the total expected inflation estimated with a model of ordinary squared minimums is of 7.67% and with a softened exponential model of 7.18%; the simple average of both models is located at 7.43%, which is found within the margin of tolerance (6.0% +/- 1 percentage point), which suggests restricting the monetary policy; and, for December 2007 the total expected inflation, estimated with an ordinary squared minimum model, is of 7.78% and with a softened exponential model of 6.32%; the simple average of both models is at 7.05%, which is over the expected policy goal (5.0% +/- 1 percentage point), which suggests a restrictive monetary policy.

Regarding the expected subjacent inflation for 2006, with data up to May 2006, estimated with an integrated auto-regression model of mobile averages ARIMA was of 6.89%, whereas the estimated with a softened exponential model was of 6.41%; the simple average of both models is of 6.65%, which is within the margin of tolerance for the policy goal (6.0% +/- 1 percentage point), which suggests the monetary policy be moderately restrictive; and, for December 2007 the estimated subjacent inflation with an integrated autoregressive model of mobile averages ARIMA, was of 7.17%, whereas the estimated softened exponential model was of 5.99%.; the simple average of both models is of 6.58%, which is located over the policy goal (5.0% +/- 1 percentage point), which suggests a restrictive monetary policy.

As to the parameter rate, up to June 15, 2006, the lower limit was 3.96%, and the upper limit is 7.91%; while the simple average between the repurchase agreements of 8 to 15 days (4.75%) and the weighted average of the monetary stabilization operations of up to 91 days (4.69%) was situated at 4.72%, which is located within the tolerance margin estimated for the parameter rate, situation that suggests the monetary policy remain invariable. When referring to the parity liable rate, they declared that up to June 15, 2006, the lower limit was 6.38% and the upper limit was 7.96%, and the weighted average rate of long term deposits of the banking system was of 7.04%, which maintains itself within the fluctuation range of the parity liable rate, which advises an invariable monetary policy.

As to primary liquidity it was indicated that monetary issue observed to June 22, 2006, presents a deviation of Q476.5 million regarding the upper limit programmed runner for said variable, which would indicate that there is space available to restrict the monetary policy, as to the behavior of a wide monetary base, to date, we find it below the lower limit of the programmed runner, which suggest relaxing the monetary conditions. The weighted orientation of the deviations for the present week for Q155.2 million would be indicating restricting the monetary policy.

As to the total payment means, the inter-annual growth observed to June 15, 2006, it ascended to 18.7%, locating itself within the tolerance margin estimated range for said variable (17.9% to 19.9%), which advises an invariable monetary policy; in which the econometric estimation for the payment means for the end of 2006 is of 18.0%, which is over the upper limit of the estimated range for December 2006 (13.0% to 15.0%), which would be suggesting a restrictive monetary policy. The average orientation of the deviation of 1.50%, therefore suggests, restricting the monetary policy. Also, up to said date, the inter-annual variation of banking credit of the private sector registered growth of 27.3%, which is over the range estimated for June 15, 2006 (24.4% to 26.4%), which suggests a restrictive monetary policy; on the other hand, the econometric estimation for the end of 2006 of the banking credit to the private sector is of 26.4%, which is over the upper limit of the estimated range (16.0% to 18.0%), which suggests restricting the monetary policy. The average orientation of the deviations for the present week of 4.65%, therefore suggests, restricting the monetary policy.

As to inflation expectations of private analysts, they indicated that according to the poll made in May 2006, for December 2006 an inflationary rhythm of 7.80% is expected, which is above the goal for monetary policy (6.0% +/- 1 percentage point), an aspect which suggests restricting monetary policy; and, for December 2007, the inflation projection is located at 6.87%, which is over the monetary policy goal (5.0% +/- 1 percentage point), which suggests restricting the monetary policy.

Also it was indicated that the variable implied inflation expectations, for May 2006 showed an inflationary rhythm of 6.34%, which is within a tolerance margin of the monetary policy for 2006 (6.0% +/- 1 percentage point), which suggests a moderately restrictive monetary policy.

They mentioned that the Monetary Conditions Index –ICM-, to June 15, 2006, was -2.88 percentage points which is within the fluctuation margin estimated for said variable on that date (-3.71 to -2.11 percentage points), which advises that the monetary policy should remain invariable.

Regarding the Semi-structural Macroeconomic Model (MMS) used for foreseeing the total inflationary rhythm, projected a rhythm of 6.88% for December 2006, conditioned by gradual adjustments in the leading interest rate of the monetary policy until locating itself at the end of the year at 5.47%, which suggests restricting the monetary policy. Also, the prognosis for said model for a mid-term horizon, projects that for December 2007 an inflationary rhythm of 5.13%, conditioned to gradual adjustments in the leading interest rate of the monetary policy until stopping at 3.52%, which would be suggesting restricting the monetary policy.

To conclude, the orientation of the indicative variables was reported, which incorporates the modifications approved by the Monetary Board on June 21, regarding the calculation and interpretation of some of said variables, including the use of new variables. In that sense, according to the relative weight assigned to the indicative variables by the members of the Monetary Board, they indicated that 63.27% of the same advise a restrictive monetary policy orientation; 24.23% suggest an invariable monetary policy orientation; and 12.50% advise a moderately restrictive monetary policy.

Finally, they indicated that regarding the behavior of the nominal exchange rate, the center of the expected runner for the week of June 19 to 23, 2006 was of Q7.664 per US$1.00 and the observed level (calculated as the average of the exchange rates for purchase and sale in the Institutional Market of Foreign Currency for the period between June 19 to 21) was of Q7.618 per US$1.00, which allows inferring that the observed value of the nominal exchange rate is found within the expected fluctuation band, but close to the lower limit, therefore in this light inflationary or deflationary pressures are not foreseen.

d) The Committee took note that the monetizing and demonetizing factors foreseen for the week of June 23 to 29, 2006 indicate an increase in the creation of primary liquidity for Q2, 915.8 million, fundamentally due to the maturity of LTD's. Also, a decrease in the demand for monetary issue for Q503.7 million is foreseen and a daily banking liquidity position for Q25.5 million. Also, monetary issue is deviated in Q659.1 million above the central programmed point for said variable, therefore the excess of aggregate liquidity estimated for the referred period is located at Q3,045.7 million; if these factors are given, the Committee considered that it would be necessary to make the issue offer compatible with the demand programmed, that the LTD's that expire during the period (Q2,836.6

million, according to registries to June 22, 2006) have to be relocated; and, also, have additional fund raising for around Q209.1 million.

THIRD: Determination of the bidding quotas for the term deposits.

Regarding the determination of quotas for the biddings in the following week, the information provided by the daily monetization flow was taken into account, estimated for the following week, in which a monetary issue demand increase is foreseen for around Q504.0 million, and on the other hand, the adopted measures of the previous week regarding the reduction of quotas and the number of weekly biddings; as well as alternating the bidding terms. Based on the above, the Committee agreed that the fund-raising quota for the 182 and 364 day terms to be convened on Monday, June 26, 2006 to be established at Q10.0 million and Q30.0 million, respectively.

Regarding the convening to bidding of LTD's in US dollars, the Committee took into account the foreseen maturity of Treasury Bonds expressed in US dollars and considered that for the week of June 26 to 29, 2006, it is necessary to convene biddings in LTD's in said currency on Wednesday June 28, to the 91 day and 364 day, for an amount of up to US$30.0 million.

FOURTH: Discussion and Definition of the execution guidelines of the Monetary, Exchange rate and Credit Policy

a) Discussion:

The Committee was informed of the result of the bids convening of LTD's in US dollars, agreed to in the previous session, when taking into account the existing important maturity of the Treasury Bonds expressed in US dollars with residents, therefore agreed to make two biddings (Wednesday June 21 and Friday, June 23), adding the 182 day terms that were being offered (91 days and 364 days), and without a predetermined quota. In that regard, it was reported that no bids were presented for that offer, therefore the biddings were declared deserted.

The Committee was informed that, of the Treasury Bonds Payments made during the week of around US$113.0 million, the holders of most of the totality of said amount (US$106.4 million) were banking institutions and that, the majority of said entities requested funds transfers to accounts constituted in branch banks abroad, which allowed inferring that said resources would not pressure the exchange market, since the banking entities would prefer pursuing profits in international financial markets.

In that context, some members of the Committee declared that the behavior of the nominal exchange rate in the last week is consistent with this reasoning, besides being congruent with the seasonal behavior, and that again makes it relevant that the Central Bank still does not have a current participation mechanism in the exchange market to act in the case of an eventual volatility toward exchange depreciation, therefore it is considered convenient that the Monetary Board retake the discussion of the participation regulation in the exchange market, contained in the Monetary Policy Report to March 2006, since it contains the guidelines that will make the participation of the Central Bank in said market more opportune and transparent.

b) Definition of the guidelines of the execution of the Monetary, Exchange and Credit Policy.

Based on the discussed, the Committee agreed that for the week of June 26 to 29, 2006, it will continue with the execution guidelines of the monetary policy observed during the present week; in other words; continue with operations in the MEBD and in the stock exchange, for fund-raising as well as giving liquidity to the market. The fund-raising operations were made for 7 day terms without quotas, at a leading interest rate of 4.75%, and the bids of liquidity offer in 7 day terms, at a leading interest rate of 7.65%, whose guarantee of said operations will be constituted only by receiving public titles. It is worth indicating that the Committee reiterated the importance of participating in both venues; in other words, keeping simultaneous liquidity giving bids and the retiring of liquidity, considering said participation constitutes a signal of willingness by the Central Bank to moderate the volatility in the short term interest rate.

The Committee taking into account the agreed in matters of coordination with the fiscal policy for the participation in the money market, agreed to convene a bid for the term deposit on Monday, June 26 for the terms of 182 and 364 days, with a fund-raising quota for Q10.0 million and Q30.0 million, respectively. The interest rates will be determined according to the conditions of the market, reflected in the bids received.

On the other hand, the Committee agreed to continue fund raising directly at the window, with the official and public entities. In the case of the public entities, that the fund raising continue to be according to the prevalent financial conditions; in other words, the interest rate for the 7 day terms will be the one applied by the *Banco de Guatemala* in the MEBD and in the stock exchange and, for the other terms, the interest rate will be the mobile average, for each term, of the weighted average interest rate of the previous four bidding events. As to fund raising for the public, the interest rate for each term, can not be higher than the weighted average of the corresponding bid minus one percentage point.

The Committee agreed to convene bidding for term deposits in United States dollars, on Wednesday, in 91 days and 364 day terms, for an amount of up to US$30.0 million. The bids received will be awarded the reference interest rates of the Treasury Letters of the United States of America in similar terms, without excluding the possibility of receiving higher rates if they merit it, convening a session of the Committee to decide the awarding.

The Committee agreed to continue accepting the constitution of term deposits in United States dollars directly at the window, from public entities, in current terms of (91 days and 364 days) and that the interest rate applied will use the interest rates of the Treasury Letters of the United States of America in similar terms as a reference.

As for the participation of the *Banco de Guatemala* in the exchange market, the Committee agreed to continue participating through the electronic negotiating system of foreign currency, with a bid of US$10.0 million at a price equal to that of the last purchase made by the *Banco de Guatemala* and according to the participation regulations established for the effect.

FIFTH: Other matters.

Not having any other matter to discuss, the session ends at seventeen hours, in the same place and on the same date indicated, all who attended sign in agreement.